# Quarterly Investment Review – Q3 2023

| Asset Class | 3rd Quarter 2023 Return | Year to Date Return |
|---|---|---|
| **Large U.S. Stocks:** S&P 500 Index | -2.1 | 13.1% |
| **Small U.S. Stocks:** Russell 2000 Index | -4.8 | 2.5% |
| **Developed International Stocks:** MSCI EAFE Index | -3.3 | 7.1% |
| **Emerging Market Stocks:** MSCI Emerging Markets Index | -2.6 | 1.8% |
| **Bonds:** Bloomberg Barclays U.S. Aggregate Index | -2.9 | -1.2 |
| **Cash**: Bloomberg 1-3 Month Treasury Bill Index | 1.3% | 3.6% |

The third quarter of 2023 was a step back for global equity investors after a strong start to the year. Early in the quarter, markets continued to march higher as better news on the inflation front and strong earnings reports from U.S. corporations led the market to the highs of the year. In August, however, concerns about continued rising interest rates put a dent in the enthusiasm and downward market action continued through September. Equity market weakness of the last two months has been mild and orderly as we head into the fourth quarter of the year. Furthermore, as we take a step back, 2023 is shaping up as an ordinary year for stock investors as most global markets are delivering returns, but of course not in a straight line.

In fixed income, interest rates resumed their ascent, with bond investors showing losses for the quarter. While the Federal Reserve has slowed down the pace of raising short-term interest rates through the Federal Funds rate, longer-term interest rates are now at fifteen-year highs. The Federal Reserve has direct control over bonds with a maturity of 0-2 years, whereas bonds with a 10 to 30-year time to maturity are typically impacted by various macroeconomic factors. Investors are contemplating a regime of higher inflation and higher supply of U.S. Treasuries in conjunction with larger deficits in the United States, which has lifted interest rates for longer term bonds. We continue to view the changing interest rate environment as healthy and a positive for investors with a time horizon longer than a couple of years. Mathematically, it is the best time to be a bond investor since the early 2000's and positive returns are ahead despite 2023shaping up to be another disappointing year for the asset class.

While various sources of media continue to paint a story of doom and gloom, the unemployment rate in the United States remains at near a fifty-year low and GDP growth is trending just north of 2%, which is similar to the slow and steady pace we have seen over the last ten years. The most recent headline Consumer Price Index (CPI) number in the United States is 4%, somewhat higher than the Federal Reserve's goal of 2%. However, we are seeing progress in achieving the price stability our economy needs to function properly. The U.S. Dollar continues to appreciate to year-to-date highs despite proclamations of the death of the dollar. While this has affected returns in international markets, it will be helpful in the fight against inflation as goods are cheaper in dollar terms. Headlines about striking workers locally here in Detroit or nationally in Hollywood have real impact and should not be dismissed. Nonetheless, labor strikes are not a new phenomenon and in the long term these issues should dissipate. Considering all these points, we are optimistic on the direction of the U.S. economy as recent macroeconomic data remains solid.

As we head into the final stretch of 2023, financial markets are on pace to produce a typical year with returns and volatility around historical averages. Looking ahead, equity valuations, particularly for international and value-oriented sectors appear attractive and bond investors are poised to generate mid-single digit returns over the long term—both factors give us optimism despite a tougher couple of months for portfolios. The end of the year also typically brings about various planning items, particularly for those with Required Minimum Distributions (RMDs). Please reach out to your advisor or our office if you have any questions.

Wishing everyone a tremendous start to the fall season!

*Diversified Portfolios, Inc.*