A person in a suit and tie

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**JANUARY 2024**

**QUARTERLY COMMENTARY**

**by RANDY GARCIA, CEO**

Last year was filled with a multitude of surprises for economists, Wall Street pundits, and investors, too. Our economy remained stronger than almost anyone expected, including the Fed. On average, the 21 economists and Wall Street strategists who published a 2023 year-end target, followed by Birinyi Research, were looking for a below average stock market gain of 6%. Actual results shocked many who held little optimism and were therefore under invested while large U.S. stocks gained +26%, smaller stocks +17%, and even international advanced +15%. 2023 was the second year in a row where professional forecasts missed actual results by 18%. In other words, they were unable to foresee the down market of 2022 as well as the up market of 2023. This lack of accuracy is not even close enough to place better than last in a game of horseshoes. This is why we repeatedly remind clients that *reacting to market predictions can be misleading and expensive for investors* who choose to follow predictions. Nevertheless, some investors can’t resist listening to predictions and forming investment decisions based on those who purport to have greater insight.

Investors always want to know what headlines will have the biggest influence on the U.S. economy and financial markets. Will it be the Federal Reserve’s interest rate decisions? Some are expecting the Fed to keep rates higher for longer while others are anticipating rapid and deep cuts this year, totaling six quarter-point cuts. Both beliefs go against the traditional market axiom: “It is costly to bet against the Fed,” which has indicated three quarter-point cuts are more likely this year. How about the current wars around the globe or China-U.S. relations? Outcomes are admittedly too hard to predict, even for government leaders. Oil prices can always disrupt domestic and global economies. So, what is this year’s outlook? Impacted by wars, political agendas, elections, weather, and more, there are too many variables to determine future prices and financial market implications in the short-term. Then there is the perpetual question that never stops being asked: Will the U.S. currency be further debased if tax revenues continue to fall short of government spending? The percentage of foreign governments holding U.S. dollars has declined steadily, but not rapidly, over the past 25 years. Because most countries have little choice but to trade in U.S. dollars there appears no near-term danger of the U.S. losing its status as the world’s reserve currency and our ability to borrow at lower interest rates. Although no one country and currency can compete with the relative stability, safety, and liquidity of the U.S. dollar, Russia, China, Middle Eastern and Latin American countries are trading among one another for oil and other commodities.

Of all the questions asked today, the most often cited is what are the potential consequences if the 2024 elections result in an even more divided and polarized government? There have been 24 Presidential elections since 1928, and the S&P 500 has risen 75% of the time for an average gain of 8%. When there has been a change in the political party holding the presidency, the S&P 500 has gained four times and fallen four times. Even if past outcomes leaned convincingly one way or the other, statisticians would argue that the sample size is too small to prove reliable. Although many investors around the globe who expect to be impacted by our elections fear the worst, people are more influenced by perceptions than reality and those misperceptions equate to opportunities.

There is one question overlooked by the media and investors that can have equal or larger consequences. Given Middle Eastern sentiment regarding Israel’s response to Hamas’s terrorist attacks and U.S. involvement, what are the implications if there is a Palestinian refugee mass exodus to other countries? And will the Palestinian casualties lead to a new generation of even stronger hatred for the U.S. inciting even greater security risks to our country and its citizens? Is the U.S. sufficiently prepared to adequately safeguard our citizens from even greater threats? There is no way of precisely knowing the answers to any of these questions.

If history is an indicator, the period before the Fed begins to cut rates has been a good time for the market. In the previous five rate hiking cycles since 1990, the Fed paused an average of 10 months between its last hike and its first cut. On average, stock and bond returns have been higher during the pause period. The median return for stocks was 21% during the pause. After the first rate cut, stocks tend to continue rallying, appreciating another 15% on average. The only exception was between early-2001 and mid-2003. Bonds returned an average +15% in the pause before the cuts and 7% afterward. These are arguments for a strong 2024 posed by veteran investors. Conversely, many are holding much larger amounts than needed in money market funds (almost $9 trillion, $1.4 trillion more than one year ago), chasing 5% annualized yields because of the belief that this decision is a “no brainer.” As reiterated in prior correspondence, they fail to comprehend adequately the meaning and personal financial consequences of “opportunity cost.” Compared to last year when yields approached 5%, money market instruments have returned far less than either stocks or bonds. Furthermore, given the Fed’s plans to cut rates in half as it approaches its lower inflation target, holders of money market instruments will likely be left with less attractive opportunities of lower yields or reinvesting in stocks or bonds at higher prices. Besides, how many people of substantial financial means do you know who have become wealthy by investing in savings accounts?

We do know that disciplined investors who can avoid the traps and habits others find hard to resist come out on top. With stocks outperforming inflation by seven percentage points per year over the last century while money market instruments barely kept pace with inflation, long-term investors have stayed ahead of price increases when consistently applying time-proven, prudent-based investment principles. Our duty is to assist each client, to the best of our ability, without conflicts of interest, to achieve all that is important to them from a financial perspective. We welcome this responsibility and opportunity. Your team at ICC wishes you and yours a prosperous, healthy, and delightful New Year.

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Sincerely,

Randy Garcia

Chief Executive Officer

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