

MARKET COMMENTARY - 3Q 2023



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1. 3Q 2023 Market Returns

Global financial markets struggled in the 3rd quarter as corporate profits declined, U.S. long-term debt was downgraded, and the Fed reinforced a higher for longer rate policy.

Asset Class	Index	QTD	YTD	1 Year	3 years	5 Years
Global Equity	MSCI ACWI	-3.4%	10.1%	20.8%	6.9%	6.5%
US Large Cap	S&P 500	-3.3%	13.1%	21.6%	10.2%	9.9%
US Large Cap Growth	Russell 1000 Growth	-3.1%	25.0%	27.7%	8.0%	12.4%
US Large Cap Value	Russell 1000 Value	-3.2%	1.8%	14.4%	11.1%	6.2%
US Small Cap	Russell 2000	-5.1%	2.5%	8.9%	7.2%	2.4%
International	MSCI EAFE	-4.1%	7.1%	25.6%	5.8%	3.2%
Emerging Markets	MSCI Emerging	-2.9%	1.8%	11.7%	-1.7%	0.6%
Commodities	S&P Global Natural Resources	3.4%	-0.5%	17.4%	18.4%	5.8%
Real Estate	CRSP US REIT	-8.6%	-5.4%	-1.3%	2.3%	2.4%
Muni Bonds	Bloomberg Municipal Bond	-3.9%	-1.4%	2.7%	-2.3%	1.0%
Taxable Bonds	Bloomberg Aggregate Bond	-3.2%	-1.2%	0.6%	-5.2%	0.1%
High Yield Bonds	Bloomberg High Yield Bond	0.5%	5.9%	10.3%	1.8%	3.0%

Global equities declined **-3.4%** for the quarter due to a combination of higher interest rates and corporate earnings are expected to decline year over year for the 4th straight quarter (Factset). The last week of the quarter markets were sent lower on fears of a U.S. Government shutdown that was averted at the last minute. U.S. Small Cap stocks were the worst performing asset class declining **-5.1%**.

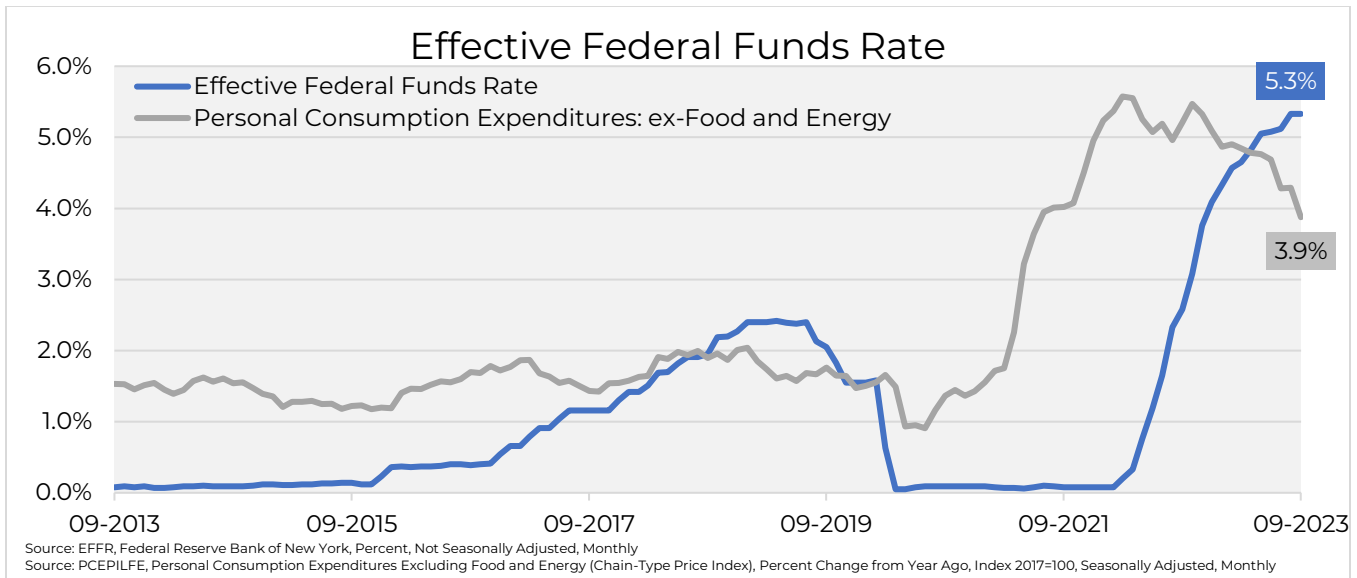
The core bond market returns were negative during the quarter as the Fed confirmed fears of prolonged higher interest rates. Bond yields moved higher, as the 10-year U.S. Treasury bond yield rose over half of a percent and hit 4.5% for the first time since 2007. Corporate and municipal bonds expected return premium over Treasuries fell slightly as new issuance remained low.

Over the last nine months, Fed policy has started to show signs of increased impact on several important metrics: interest rates have moved higher, the unemployment rate has deteriorated, and the inflation rate has declined. Recently, the 19 Fed Chairmen reinstated their optimism that they will manage to slow inflation to 2% without causing a deep recession.

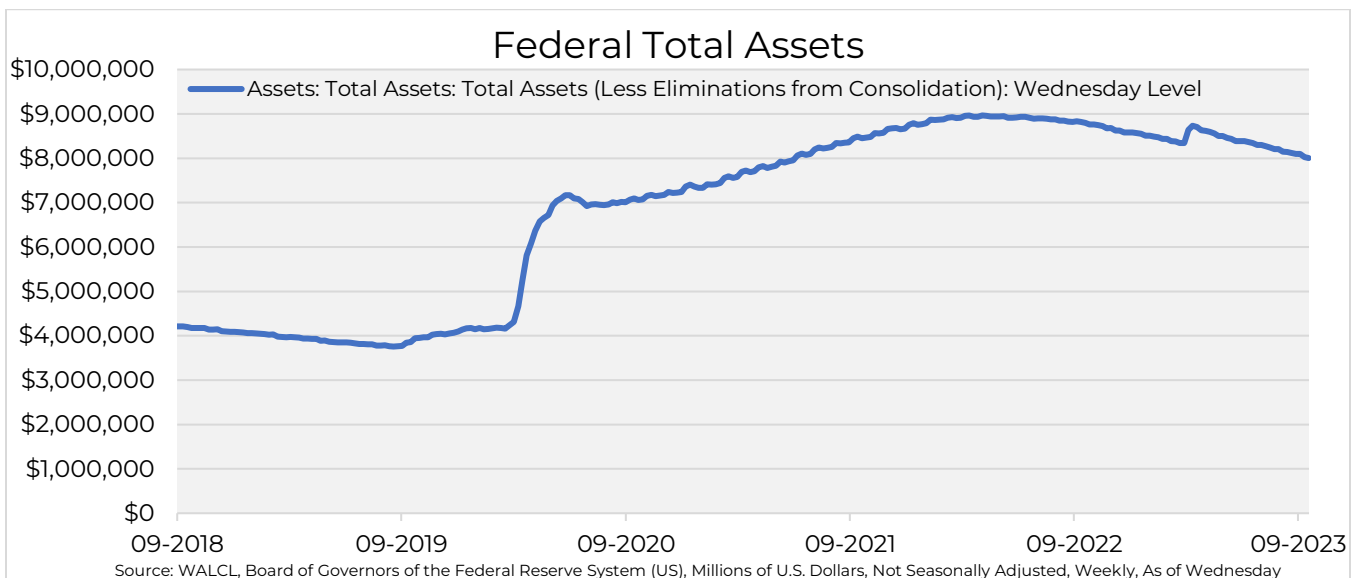
Indicator	Metric	Last	12/31/2022	1Y Ago	3Y Ago	5Y Ago
Yield	10 Year US Treasury	4.59%	3.88%	3.83%	0.69%	3.05%
Fed Funds Rate	Effective Fed Funds	5.33%	4.33%	3.08%	0.09%	2.18%
Unemployment	US Unemployment	3.8%	3.5%	3.5%	7.9%	3.7%
Inflation	Core CPI	3.7%	6.5%	8.2%	1.4%	2.3%
Inflation	Core PCE	3.9%	4.9%	5.5%	1.4%	2.0%

2. The Federal Reserve Indicates Higher for Longer

The Fed Funds rate is currently at 5.33%, the highest reading since 2001. After briefly pausing rate increases on June 14th, the Fed raised rates in July by 0.25%. At the September meeting the Fed left rates unchanged and updated the Fed Dot Plot, which indicates one more potential hike in 2023. After the September Fed meeting, Chairman Powell stated, “*We’re in a position to proceed carefully in determining the extent of additional policy firming.*” Overall consumer inflation fell to its lowest level since late 2021. The Fed’s long-term goal is to achieve a Fed Funds rate that is 0.5% higher than Core PCE: ex-Food and Energy inflation.



Market returns are increasingly being impacted by Fed action after the pronounced bull run in the first half of 2023. A new twist impacting the markets is a potential government shutdown currently scheduled to occur in November 2023. Another important factor impacting markets is the continued balance sheet shrinking by the Fed. The balance sheet has been reduced by over \$900MM since 4/2022, allowing \$95B of bonds to roll off each month rather than re-investing.

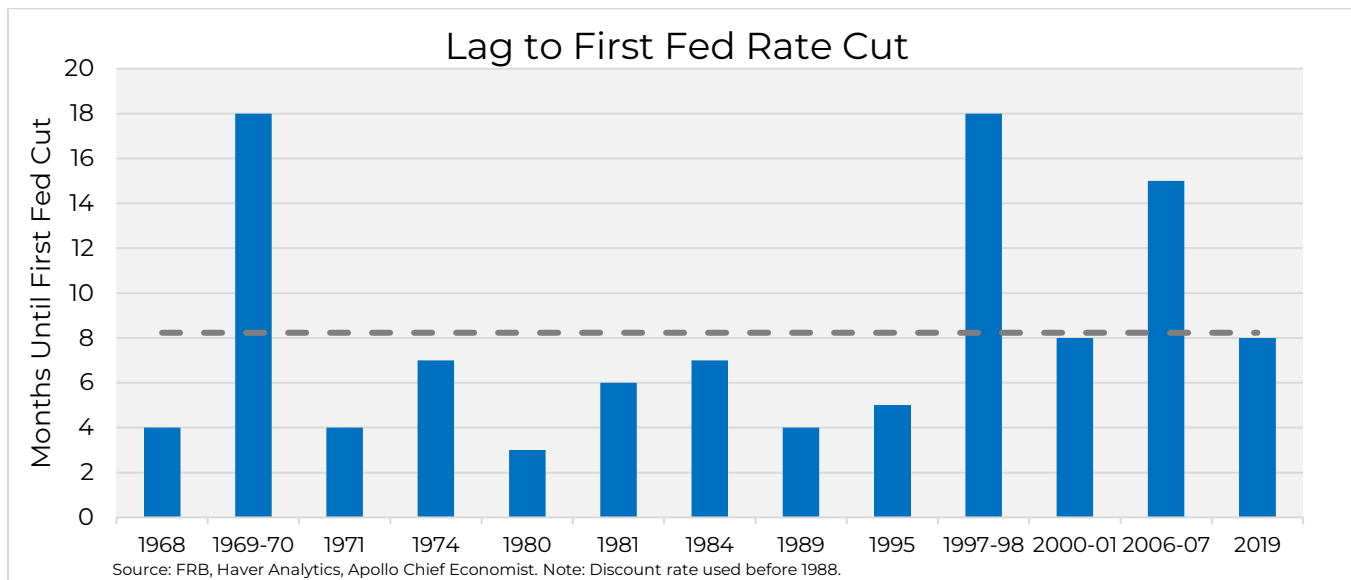


3. Yield Curve Shifts and Opportunities

As outlined in the chart below, the yields on intermediate to long-term U.S. Treasury Bonds rose sharply in Q3. Resilient US economic data has raised concerns of rates staying higher for longer as supported by the Federal Reserve Summary of Economic Projections (released on 9/20/23). The yields have also increased on investment grade bond ETFs that include Treasuries, corporate and securitized bonds.

Name	9/30/2023	3M Ago	6M Ago	12/31/2022	1Y Ago	2Y Ago	3Y Ago	5Y Ago
2 Year Treasury Rate	5.0%	4.9%	4.1%	4.4%	4.2%	0.3%	0.2%	2.8%
5 Year Treasury Rate	4.6%	4.1%	3.7%	4.0%	4.0%	1.0%	0.3%	2.9%
10 Year Treasury Rate	4.6%	3.9%	3.6%	3.9%	3.8%	1.6%	0.6%	3.1%
20 Year Treasury Rate	4.9%	4.1%	3.9%	4.1%	4.0%	2.0%	1.2%	3.1%

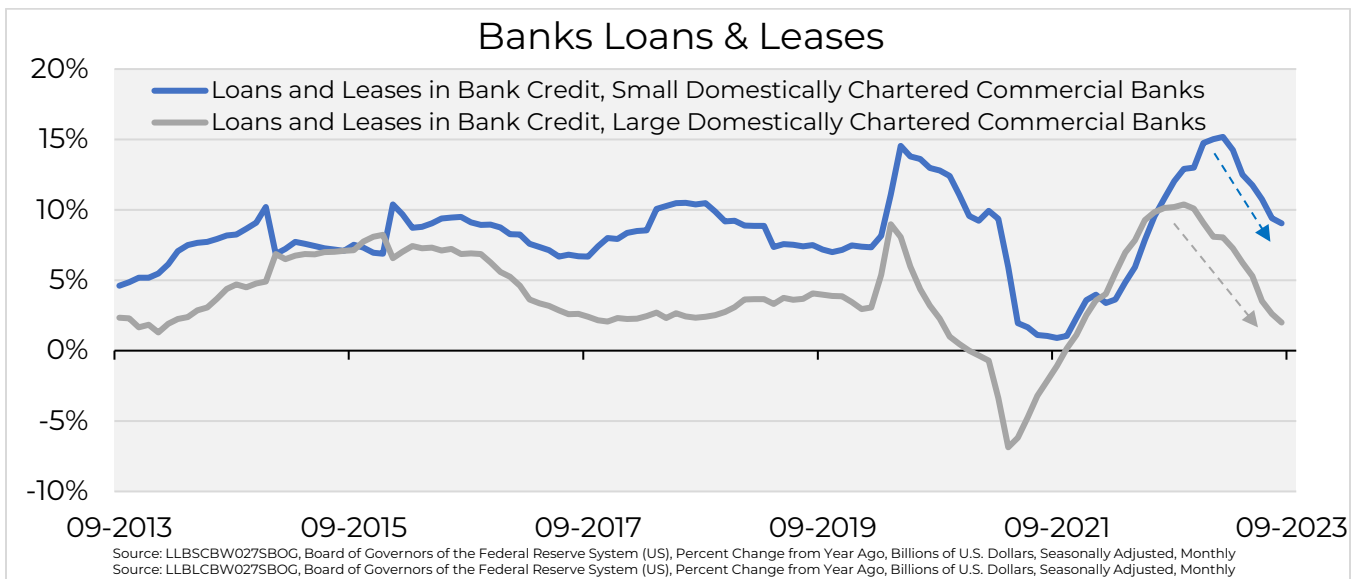
Short-term yields remain temporarily higher than longer term yields, but that phenomenon will eventually dissipate as the Fed continues to target a 2.5% Fed Funds Rate. In the past, there has typically been an average gap of 8 months between the last rate increase and the initial rate reduction. If this pattern holds true in the current economic cycle, the market can anticipate the Federal Reserve to begin making rate cuts in the Spring of 2024. However, it's important to note that a notable distinction in the present circumstances is the persistently elevated inflation, which exceeds the Fed's desired target rate of 2%.



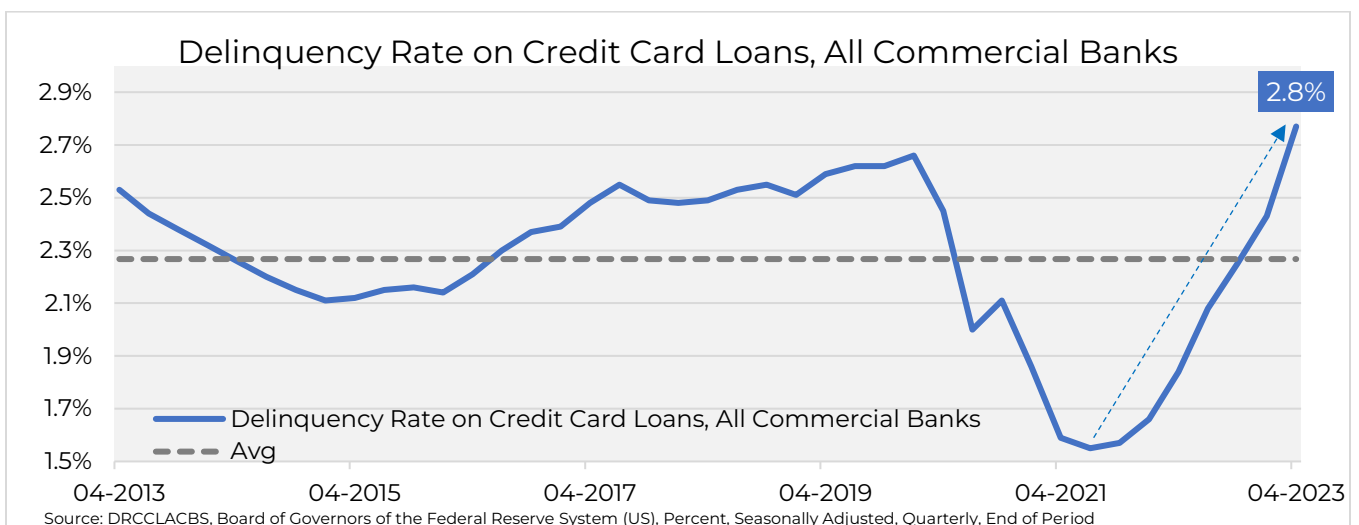
4. Macro-Economic Environment Slowdown

The recent actions of the Federal Reserve in raising interest rates have had notable repercussions on the lending landscape and the broader economy.

In the wake of these rate hikes, banks loans and lease underwriting has decreased sharply over the past year. This stance is manifesting in the form of increased difficulties for businesses restructuring debt and individuals seeking new credit cards, auto loans, and mortgages. Higher interest rates result in diminished borrowing capabilities and demand from households. In addition, a massive shift by consumers out of traditional bank savings accounts to high-yielding money market funds has reduced their ability to offer new loans because of a lower deposit base that serves as required reserves.



Consumer credit card usage has reached a concerning milestone as Americans have depleted their savings and are relying on credit cards to cover their expenses. In the second quarter of 2023, credit card debt surged past the unprecedented threshold of \$1 trillion for the first time in history. Indicators suggest that consumers may be nearing the point of exhausting their available credit limits as delinquencies rise.



5. Equity Rally Stalls

U.S. Large Cap Growth remains the best performing equity asset class in 2023, still led by the Magnificent Seven stocks (Alphabet, Amazon, Apple, Meta, Microsoft, Nvidia, Tesla). In the third quarter the U.S. Large Cap Growth asset class has given back **-3.1%** while global equities have fallen by **-3.4%**. All equities experienced a significant uptick in July but have given back those gains as global equities dropped by **-6.8%** in August and September.

6. GSIS 2023 Allocation Positioning

The GSIS model allocation is structured to protect assets, reduce market volatility, increase cash flow yield, and generate long-term inflation-adjusted growth.

- The **Private Credit** portfolios were positive during the quarter, each outperforming core bonds by 4-5%. The portfolios benefit from the high-quality senior secure structures that primarily feature floating rate components. This asset class should be able to produce high single-digit returns as the Fed's near-term path remains uncertain.
- **Private Real Assets** as a group produced positive returns during the quarter despite poor returns from public markets. The managers' vast data platforms provide insight into the secular shifts to build high quality portfolios. The industrial and data center exposures continue to be the top performing asset classes in these portfolios. The portfolios have very little commercial office and retail exposure, which continue to be under pressure.
- The **Private Equity** strategies continue to perform well as a group. The higher quality, later stage growth and buyout exposures outperformed public markets during the quarter. Secondary purchases continue to be a return driver in 2023.
- Within **Core Public Fixed Income**, the Bloomberg Aggregate and Municipal indexes posted sub **-3.0%** due to the overall rise in yields and credit concerns. The short duration tilt in our client portfolios significantly outperformed in Q3 2023.
- In **Global Public Equities**, global equities all fell during the quarter, whereas buffered equity ETFs were able to navigate the 3rd quarter without similar losses.

Our active strategic allocation continues to remain diversified with a goal of protecting and participating in public and private markets returns. The portfolio tilts and manager selection produced significant excess performance in the 3rd quarter relative to policy and public benchmarks.

Thank you for your Trust and Confidence.



Nick Botticelli

Chief Investment Strategist
nbotticelli@gsisus.com



Matt Underwood, CFA®, CAIA®

Director of Research & Portfolio
Management
munderwood@gsisus.com



Phone: 480-935-2136
Email: info@gsisus.com
www.gsisus.com

