

# SC Capital Advisors Investor Insights



41-750 Rancho Las Palmas Dr, Ste N-3, Rancho Mirage, CA 92270

Phone: 760-776-1488

Email: info@scadvisors.net

**4th Quarter 2023**

## 2023 4th Quarter in Review & Outlook

*“In Wall Street, the only thing that’s hard to explain is next week.” — Louis Rukeyser*

### Wall Street gets it wrong

Investors who were looking to Wall Street for stock market advice for 2023 may have missed out as consensus estimates proved to be way too conservative with many prominent strategists calling for another down year prior to 2023. According to the New York Times, the average gain predicted for U.S. stocks by Wall Street strategists was 6.2%. (Replace “week” with “year” in the Rukeyser quote above.) Actual capital market returns for 2023 are shown below.

**Asset Class Returns 2023 (12-31-2023)**

	US Large	US Mid	US Small	REITs	Intl Large	Intl Small	Em Mkts	Bonds
Q1	7.5%	3.8%	2.7%	1.6%	8.5%	4.9%	4.0%	3.0%
Q2	8.6%	4.9%	5.2%	2.4%	3.0%	0.6%	0.9%	-0.8%
Q3	-3.2%	-4.2%	-5.1%	-8.6%	-4.1%	-3.5%	-2.9%	-3.2%
Q4	12.0%	11.7%	14.0%	18.0%	10.4%	11.1%	7.9%	6.8%
2023	26.5%	16.4%	16.9%	12.2%	18.2%	13.2%	9.8%	5.5%

Indexes: US Large, Russell 1000; US Mid, S&P MidCap 400; US Small, Russell 2000; REITs, DJ US Real Estate; Intl Large, MSCI EAFE; US Small, MSCI EAFE Small Cap; EM, MSCI Emerging Markets; S&P GSCI TR; Bonds, Bloomberg US Agg Bond. Source: Morningstar.

Almost all broader equity benchmarks shown above registered double digit returns for 2023. Broader U.S. stock market returns were positive 8 out of the 12 months of 2023. The market took a breather for three straight months starting in August after a very strong start. A weak fall for stocks may have been predictable as data from Blackrock shows that September is the only month in the history of the U.S. stock market since 1926 with a negative average return (-0.8%).

The S&P 500 was down 5.8% (Morningstar) for September with many small- and mid-cap indexes trailing further.

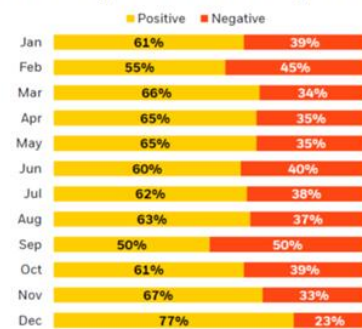
SEPTEMBER IS A TOUGH MONTH FOR STOCKS

### September historically the worst month for stocks

**Avg stock market return by month**  
(since 1926)



**Positive/Negative returns for stocks by month**



Markets seemed to follow history the remainder of 2023 with stocks continuing declines in October, another traditionally weak month historically. However, the last two months of the calendar year have been historically strong, according to Blackrock. Decelerating inflation coupled with robust economic growth and anticipation of Federal Reserve rate cuts in 2024 led to strong returns to close out the last two months of 2023. The S&P 500

Source: Morningstar as of 8/31/23. U.S. stocks are represented by the S&P 500 Index from 1/1/17 to 8/31/23 and the S&P 500 U.S. Eq Stock Index from 1/1/19 to 1/1/17. Unmanaged indices that are generally considered representative of the U.S. stock market during each given time period. Past performance does not guarantee or indicate future results. Index performance is for illustrative purposes only. You cannot invest directly in the index.

was up 14.1% for November and December (Morningstar).

### Shifting themes

It usually makes sense for investors to ignore the themes that come out of Wall Street and circulate through the financial press. Throughout the market selloff of 2022, one prevailing theme to explain the decline in stock prices was that rising interest rates depress the valuations of stocks. This is true in theory as interest rates are used to discount future cash flows in stock valuation models: A larger discount rate yields a lower stock valuation. However, analysts who practice discounted cash flow valuation of companies use long term estimates of interest rates rather than current rates in their models. Thus, a rise in current interest rates to higher modeled rates is just noise.

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*...investors quickly forgot about the “long duration” theme as Artificial Intelligence exploded onto the scene...*

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As growth stocks and technology companies were getting crushed in 2022, the common theme on Wall Street was that “long

duration” stocks, shares of companies whose earnings materialize well into the future, do poorly in rising interest rate environments. So, the markets sell them off. However, included in the sell off were bellwether growth companies that generate huge and current operating cash flows were sold off as well. Companies like Meta, Google, and Salesforce, etc., are hardly long duration stocks, in our opinion. Of course, even as interest rates continued to creep up in the first half of 2023, investors quickly forgot about the long duration theme as Artificial Intelligence exploded onto the scene, promising to boost long term corporate profit margins. Long duration stocks quickly rebounded, and the long duration theme fizzled away.

### Cap weight beats equal weight, except . . .

The Morningstar Wide Moat Focus Index (the “Moat Index”) continued its impressive performance through 2023. We use this index’s quality and valuation factors in managing the Core Equity individual stock component of our portfolios. The Moat Index surged by 7.9% in December outpacing the S&P 500 by over 300 basis points during the month, and ended the 2023 calendar year up 32.4%, or 600 basis points above the S&P 500, according to global investment manager VanEck. The performance of the Moat Index is particularly notable this year, as it came amid a top-heavy market where the mega-cap Magnificent Seven was responsible for much of the market’s overall gains. Illustrating this is the S&P 500 Equal Weighted Index which only gained about 14% in 2023. The equal-weight Moat Index outperformed despite this challenging environment for equal-weighted strategies, bearing testament to the moat investing philosophy and the rigorous Morningstar equity research that underpins the index, according to VanEck.

### Bonds rebound big

According to Blackrock, 2022 was the worst year for the bond market since 1926. Poor performance continued for bonds into 2023, until the last two months of the year. Bonds lost money six months in a row in 2023, which had never happened in bond investing history going back all the way to 1926 (below). October turned out to be the month of peak pessimism in the bond market. Bonds rebounded 8.5% in November and December, making it the seventh best two-month window historically dating back to 1926, according to Blackrock. Below, bonds have fared pretty well over the next 12 months after similar two-month bond market rallies.

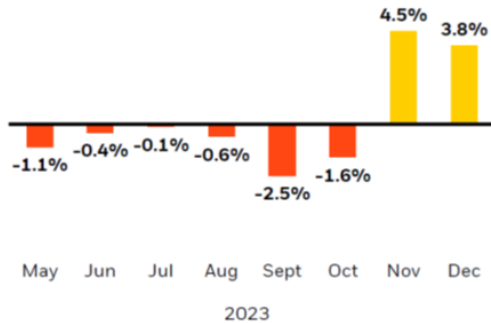
HISTORIC TWO MONTHS FOR BONDS

# November and December was a historic stretch for bonds

After a historic losing streak, bonds rebounded with a historic rally (7<sup>th</sup> best 2-month period since 1926)

### Bonds bounced back after losing money in 6 consecutive months (first time in history)

2023 monthly returns (%)



### Top 10 best 2-month returns for bonds since 1926

Total return (%)

Top 10 best bond months	Return	1 Year Later
Apr-May 1980	16.6	-3.1
Oct-Nov-1981	14.9	25.2
Mar-Apr 1981	11.4	-2.1
Jul-Aug-1982	10.0	16.4
Aug-Sept 1982	9.7	15.6
Sept-Oct 1982	9.6	10.1
<b>Nov-Dec 2023</b>	<b>8.5</b>	<b>?</b>
Apr-May 1985	7.4	18.2
Feb-Mar 1986	7.2	8.7
Nov-Dec 2008	7.1	5.9

Morningstar as of 12/31/23. U.S. bonds represented by the IA SBBI US Gov T Index from 1/1/76 to 1/3/89 and the Bloomberg U.S. Agg Bond TR Index from 1/3/89 to 12/31/23. Past performance does not guarantee or indicate future results. Index performance is for illustrative purposes only. You cannot invest directly in the index.

## Election year chaos?

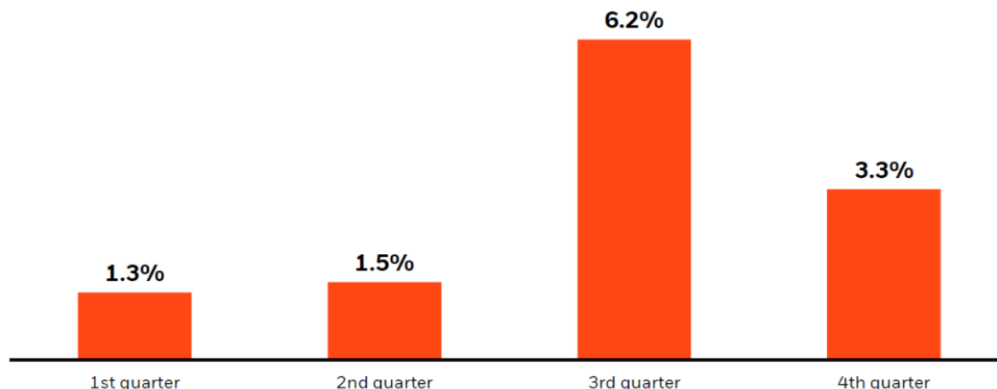
2024 is a presidential election year, and it should be an interesting one. Polls show the public is extremely unenthused about a rematch between Joe Biden and Donald Trump, yet those two are looking to be the respective party nominees at this point. Biden is facing age, health, immigration, and inflation issues while Trump is facing numerous legal investigations and lawsuits unprecedented for a presidential candidate. However, it seems to be only helping him with his base. People tend to be overly worried about elections and investment returns, but history shows they should not.

ELECTION YEARS AND MARKET PERFORMANCE

# U.S. stocks in a presidential election year

### First half of presidential election years tends to be sluggish, followed by a big second half

Average return, 1/1/26 – 12/31/23



Morningstar as of 12/31/23. Stock market represented by the S&P 500 Index from 1/1/70 to 12/31/23 and IA SBBI U.S. large cap stocks index from 1/1/26 to 1/1/70. Past performance does not guarantee or indicate future results. Index performance is for illustrative purposes only. You cannot invest directly in the index.

Generally, presidential election years are slightly better than average for stock market returns, according to Blackrock, above. Going back to 1926, on average, the first half of a presidential election year tends to be sluggish for stocks. The second half tends to be strongest, 6.2% on average in the third quarter and 3.3% in the fourth quarter.

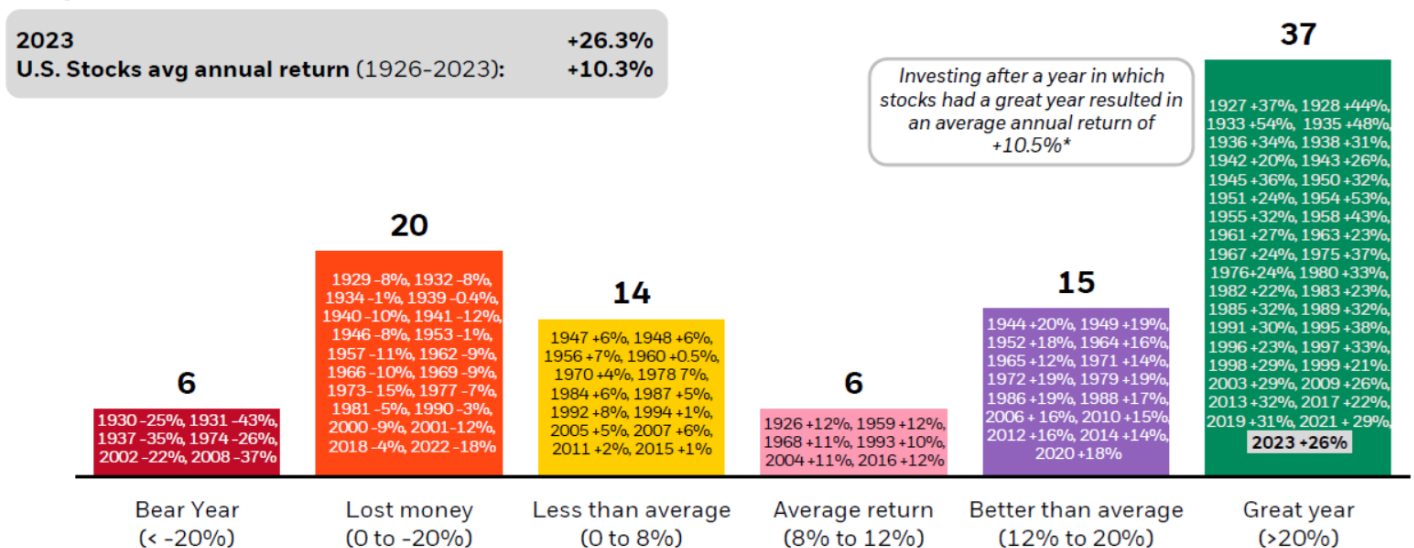
In closing, stocks had a great year in 2023. In the chart below, Blackrock publishes calendar years for stocks going back to 1926. The average annual rate of return for stocks from 1926 to 2023 is 10.3%. However, only six calendar year returns over that entire period came in close to that average return.

# U.S. stocks had a great year in 2023

U.S. stocks average 10% return, but very rarely return their average in a calendar year

## Range of returns for stocks by calendar year

Average annual return, 1/1/26 – 12/31/23



Source: Morningstar as of 12/31/23. U.S. stocks are represented by the S&P 500 Index from 3/4/57 to 12/31/23 and the IASBBI U.S. Lrg Stock Tr USD Index from 1/1/26 to 3/4/57, unmanaged indexes that are generally considered representative of the U.S. stock market during each given time period. Past performance does not guarantee or indicate future results. Index performance is for illustrative purposes only. You cannot invest directly in the index.

Returns in the year after a calendar year of 20%+ tend to be average or about 10.5%. The most important lesson in the chart above is market timing does not work. Thirty seven out of 98 calendar years were great, 20%+. The other categories of returns other than “great” tend to wash themselves out. The lesson for investors who practice market timing, when you miss the great years, results suffer.

So, what’s in store for 2024 from Wall Street? For what its worth, according to Forbes, the consensus estimate among Wall Street strategists is for an 8.5% return for the S&P 500 for 2024, on average. (Perhaps Wall Street is privy to the Blackrock data above.) We will take the predictions with our usual grain of salt. Rather than prognosticate, we will do as usual: Let the market do its thing while monitoring asset valuations, and taking advantage of opportunities as they come along.

Please let us know if you have any questions. We look forward to talking with you soon.

—Dana L. Crosby, CFA, CFP®

**ETF Returns**

For the period ending 12-31-2023

Name	Ticker	YTD	1 Month	3 Months	12 Months	3 Year	5 Year	10 Year
<b>U.S. Large Cap</b>								
iShares Russell 1000	IWB	26.41	5.00	12.07	26.41	8.87	15.35	11.67
iShares Edge MSCI USA Momentum Factor	MTUM	9.16	4.76	12.57	9.16	0.38	10.82	11.47
iShares Edge MSCI USA Quality Factor	QUAL	30.89	4.69	12.06	30.89	9.72	15.66	11.87
PowerShares S&P 500 Low Volatility ETF	SPLV	0.53	2.33	7.33	0.53	5.88	8.40	8.94
Vanguard High Dividend Yield ETF	VYM	6.57	5.62	9.12	6.57	10.21	10.93	9.38
<b>VanEck Vectors Morningstar Wide Moat</b>	<b>MOAT</b>	<b>31.88</b>	<b>7.84</b>	<b>12.88</b>	<b>31.88</b>	<b>12.23</b>	<b>16.96</b>	<b>12.91</b>
<b>U.S. Mid Cap</b>								
SPDR® S&P MidCap 400 ETF	MDY	16.09	8.63	11.53	16.09	7.83	12.36	8.99
PowerShares S&P MidCap Low Volatil ETF	XMLV	1.85	4.90	8.66	1.85	5.39	5.83	8.62
PowerShares DWA Momentum ETF	PDP	20.88	5.91	11.17	20.88	-0.56	12.32	9.18
PowerShares High Yld Eq Div Achiev™ ETF	PEY	7.30	8.82	12.00	7.30	11.51	10.72	10.27
<b>U.S Small Cap</b>								
iShares Russell 2000	IWM	16.84	12.13	13.99	16.84	2.10	9.88	7.13
PowerShares S&P SmallCap Low Volatil ETF	XSLV	1.34	9.36	12.72	1.34	4.93	3.17	6.03
<b>REITs</b>								
iShares US Real Estate	IYR	11.93	8.99	17.98	11.93	4.97	7.03	7.31
<b>International Large Cap</b>								
iShares MSCI EAFE	EFA	18.40	5.36	10.71	18.40	4.17	8.21	4.18
iShares Edge MSCI Intl Momentum Factor	IMTM	13.91	3.54	10.08	13.91	0.34	8.97	-
PowerShares DWA Developed Mkts Mom ETF	PIZ	17.97	5.49	11.18	17.97	-0.39	8.25	3.28
iShares Edge MSCI Intl Quality Factor	IQLT	18.76	6.09	12.88	18.76	4.39	10.40	-
PowerShares S&P Intl Dev Quality ETF	IDHQ	18.79	4.89	10.76	18.79	1.81	9.69	6.08
iShares Edge MSCI Min Vol EAFE	EFAV	12.55	4.16	7.61	12.55	0.81	3.61	4.18
iShares International Select Dividend	IDV	10.38	6.18	11.70	10.38	5.03	6.09	2.69
<b>International Small Cap</b>								
iShares MSCI EAFE Small-Cap	SCZ	13.01	7.16	11.13	13.01	-0.66	6.42	4.61
WisdomTree International SmallCp Div ETF	DLS	15.32	7.82	11.87	15.32	2.11	5.13	3.66
<b>Emerging Markets</b>								
iShares MSCI Emerging Markets	EEM	8.99	3.60	8.00	8.99	-5.85	2.91	1.83
PowerShares S&P Em Mkts Low Volatil ETF	EELV	8.86	4.03	8.29	8.86	6.68	4.92	2.03
PowerShares DWA Emerging Markets Mom	PIE	13.74	3.94	6.47	13.74	-2.52	7.12	2.66

Data source: Morningstar

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