

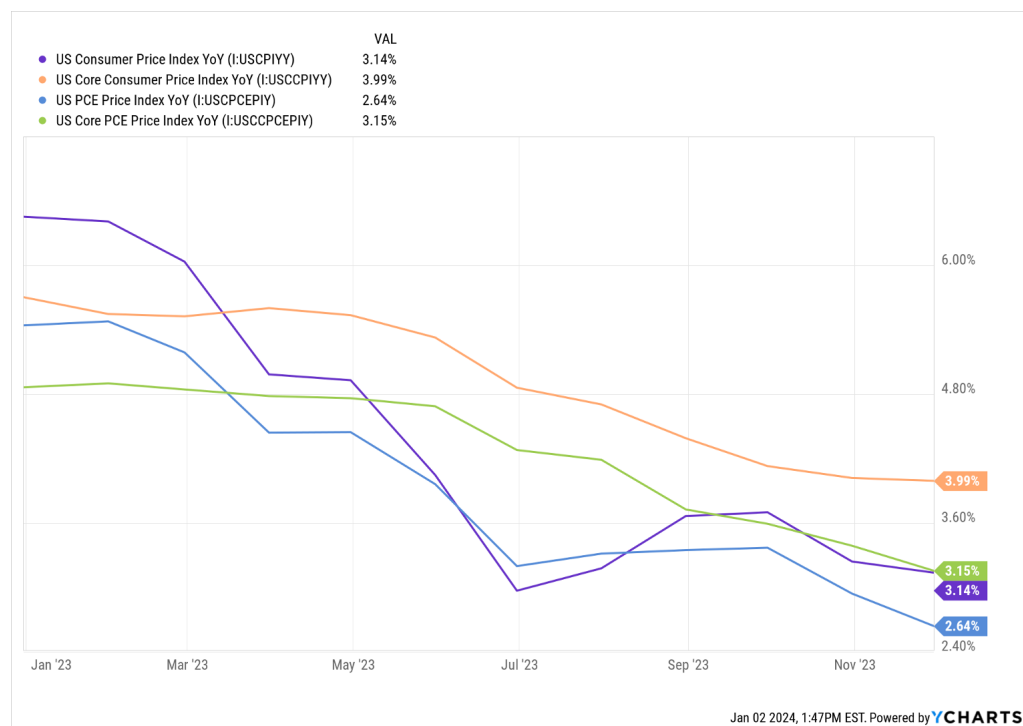


## A Lot Went Right by Robert Sokolowski

2023 will be remembered as a good year and a nice rebound from an abysmal 2022 (the third-worst year ever for a 60/40 portfolio). The S&P 500 notched a 26.3% total return, and the US Aggregate Bond index returned 5.7%. This culminated with both the Dow and the S&P reaching all-time total return highs in late December. However, things weren't as cut and dry as those headline numbers suggest- a lot had to go right. So, without further ado- let's take at the biggest positive stories we saw in 2022.

### Inflation

The inflation rate fell dramatically throughout the year with very few setbacks. In fact, CPI, the most widely used measure of the inflation rate, fell by 3.3 percentage points- a 51% drop! There was substantial fear throughout the year that inflation would begin to reaccelerate and thankfully those fears did not materialize.



Inflation appears to be poised for further forward progress. Looking at the last six months of the core PCE Price Index data (the Fed's preferred measure of inflation), we are running at just a 1.9% annualized inflation rate. This is below the Fed's target of 2% and well below the long-run average of 3.2%. November core CPI data showed prices rising 0.28% month over month with housing, used and leased vehicles, and auto insurance contributing +0.33% to that number. This means the report would have shown 0.05% month-over-month deflation in November without housing and autos.

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### SPECIAL POINTS OF INTEREST

- Our office will be closed the following days for market holidays this quarter:
  - Monday, January 15th, 2024
  - Monday February 19th, 2024
- You still have time to make IRA & HSA contributions for 2023!
- If you would like to schedule a meeting for planning or portfolio questions don't hesitate to contact us!

Shelter costs feed into inflation data with an enormous lag. They paint a more accurate picture of what was happening 6-12 months ago than what's happening today. Furthermore, this shelter component probably overstates what most people are experiencing- especially those who have fixed-rate mortgages or own their homes outright. There are two main points here: 1) These numbers have probably overstated inflation in housing all along, and 2) the lag in the data should provide a tailwind to the inflation fight going forward.

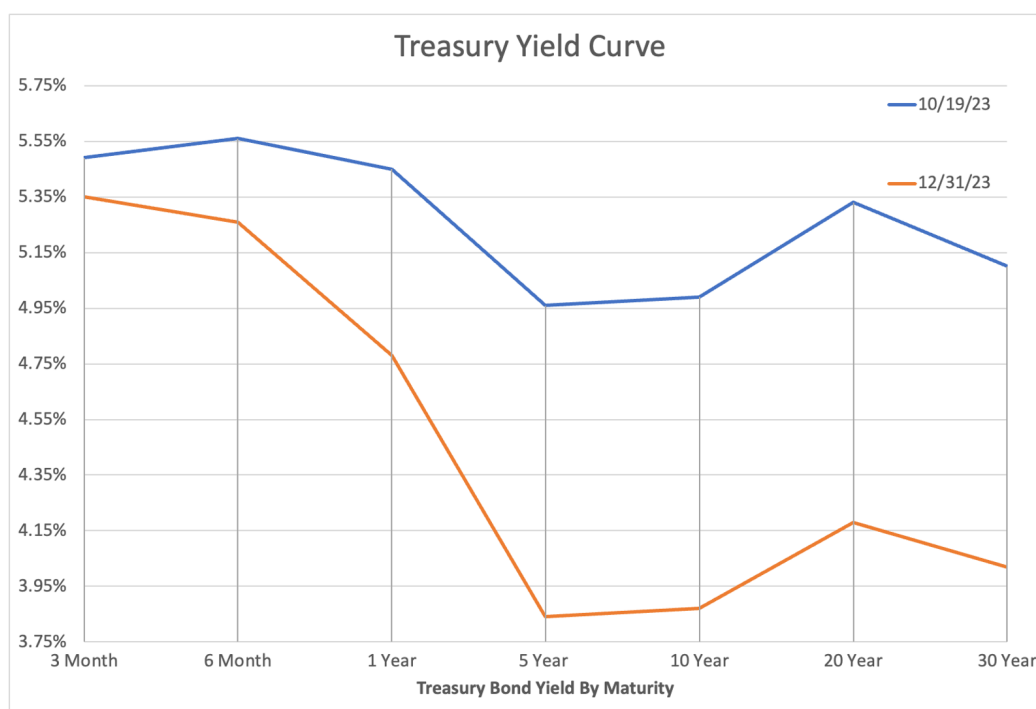
### The End of Year Bond Rally

Rising interest rates were an issue for both the stock and bond markets for most of the year. Rates on longer-term bonds peaked on October 19th while the stock market was experiencing a significant correction. Stocks bottomed just eight days later with the S&P down 10.3% from its July high. Stocks and bonds then rallied 16.2% and 8.1% respectively into year end. Bond prices move inversely to their yields.

There were a few factors that drove this huge rally:

- September and October are seasonally weak months and flipping the calendar to November helps. There isn't a great logical explanation for this phenomenon.
- Mutual funds have fiscal years that end on October 31st and need to book capital losses before that date. There were a higher than usual amount of tax loss candidates this year and this accounting quirk probably drove higher than average selling by mutual funds in October.
- **The Biggest Factor** - At their November 1st meeting, the Fed announced they were not raising interest rates. In the weeks after, Fed officials continued to offer comments suggesting they were more likely to cut rates going forward than raise them. This is no doubt tied to the progress on inflation and the prospects for continued inflation moderation.

Since October 19th, interest rates have plummeted. The following chart shows the treasury yield curve on 10/19 and again at the end of the year. This is a stunning drop in rates in such a short time.



The bond rally since late October prevented what would have been an unprecedented third straight calendar year of negative bond returns. Bonds were tracking for a negative total return for 2023 as recently as November 10th and finished the year up 5.7%!

## US Economic Strength

The US economy showed remarkable strength in the face of some serious headwinds this year, most notably rising interest rates, high inflation, and poor consumer sentiment. However, the economy appears to have expanded by about 2.9% in 2023. This is solid growth in any environment. Furthermore, the labor market strength has continued. There are nearly 1.4 open jobs for each unemployed person and the unemployment rate remains at a very low level. Wage growth has moderated as well which helps businesses control their input costs and therefore the prices of the goods and services they sell. This helps keep a lid on price increases across the economy.

Businesses are starting to show similar strength to the broader economy once again. Corporate profits declined from Q4 2022 – Q2 2023. That earnings recession ended in the third quarter of this year.

## Geopolitics

There was a lot that could have gone wrong geopolitically in 2023 that didn't. The wars in Ukraine and Israel/Gaza could have expanded but remained relatively contained. There has certainly been a tremendous amount of human suffering in these wars, but thankfully they have not yet become more regional or global conflicts. Likewise, China has been threatening to invade Taiwan for years, and that seems to still be a goal of theirs, but we have not seen conflict there yet. The massive supply chain disruptions caused by the Russia/Ukraine war seem to have largely been overcome. These disruptions undoubtedly added to inflation worldwide in 2022.

## Looking Ahead

In speaking with clients recently, the election is already something people are thinking about. I'll concede that no one knows what will happen this year, but I wanted to share two of the findings from a study conducted by Vanguard on markets during election years.

- There is no statistical difference between the performance of a 60/40 portfolio in election versus non-election years. (Though statistically insignificant, the edge in actual returns went to election years at an 8.7% return versus 7.7% in non-election years.)
- Volatility has historically been lower in the 100 days before and after presidential elections than for all other periods.

Elections aside, the economy and corporations seem to be on much more solid footing than a year ago. Substantial progress has been made on inflation, the corporate earnings recession has ended, interest rates have eased significantly in the past few months, and the Fed is signaling they are willing to cut rates if necessary. Overall, this is a constructive position for stocks and the economy.

Market Index	Q4 Total Return	YTD Total Return	1 Year Total Return
S&P 500	11.7%	26.3%	26.3%
DJIA	12.9%	15.4%	15.4%
Nasdaq Comp	13.8%	44.6%	44.6%
MSCI EAFE	10.9%	18.0%	18.0%
Russell 2000	14.0%	16.9%	16.9%
US Aggregate Bond	6.8%	5.7%	5.7%



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Estate planning may be one of the most important things that people never want to discuss. It helps your loved ones swiftly settle your estate and know that they are abiding by your wishes. It can help end family disagreements before they happen. However, estate planning is not a one-and-done task. It needs to be continually monitored and updated. So, even if you have recently crafted your estate plan, take the time now to check a few things that may need updating.

**Beneficiary Designations:** The new year is a great time to check your beneficiary designations on accounts and life insurance policies. If you have any major life changes in 2023 you may need to update beneficiaries. It is also a good idea to check your beneficiaries' contact information. They may have moved or changed phone numbers recently and getting that updated will help financial institutions track them down.

**Trusted Contact:** Schwab encourages all clients to have a trusted contact on file. This is a person that Schwab or Metis Wealth could contact in the event we couldn't reach you. This person will not have access to your accounts or be able to make any changes on your behalf like a Power of Attorney could. They would however be able to help Schwab or us get in contact with you. For clients over 60, we recommend listing someone younger than you, if possible, rather than a spouse or anyone of similar age.

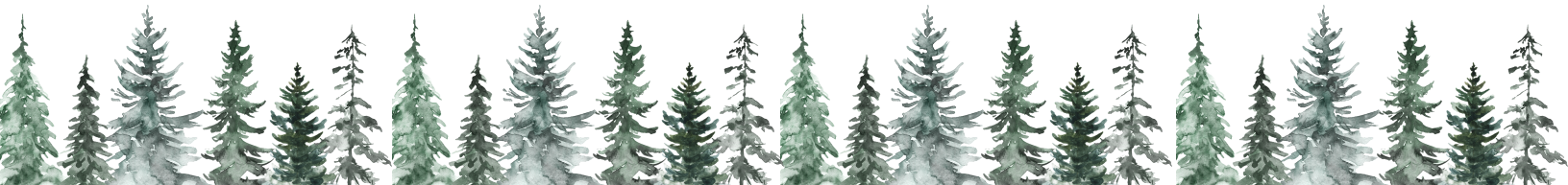
**Power of Attorney (POA):** There are different kinds of POAs including financial and health care. There are also different ways to structure your POA including when they have power and what type of power they have. If you do not have a POA, you can add it to your list of New Year resolutions. If you do have one, now is a good time to revisit it and ask yourself if that person is still the best choice and to consider if you need to make any changes to the power itself. Also, make sure that person knows they are your POA and where to find necessary information that they may need to act as your POA.

**Will:** Do you have a will? If not, then this is your top priority. Everyone needs a will. Laws vary from state to state, but people are often surprised to learn that things may not transfer as simply as they think. For example, in South Carolina, if you pass intestate (without a will) half of your estate goes to your spouse, and the other half is split among your children!

If you have a written will in place, I would recommend that you pull it out and make sure it is still accomplishing what you would like and that no changes are needed. Any life changes that occurred in 2023 may warrant an updated will.

**Executor:** Do the people you have named executor and alternative executor know that they have been assigned these roles and are they comfortable with them? This is not something that someone wants to be caught off guard with after a death, so be sure they are aware. Although no one wants to have that conversation, it is also a good idea to let them know where they can find important estate documents, passwords, contact information, and lists of accounts.

Estate attorneys typically don't charge too much for estate plan updates if you already have documents in place. If you're unsure about whether your estate documents will achieve your intended goals, it's worth it to have an estate attorney read through them for you. We are also available to provide as much help as we can!



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