



2024 Outlook:

Rollercoaster-Riding the 2020's

January 5th, 2024

2023 was a banner year for the Stock Market.

It sure didn't start out that way, coming off what was a brutal year for all asset classes in 2022. In many ways, the past 2 annual images were mirrored. Sharp declines were followed by sharp rises in asset prices. What fell the most in '22 rose the most in '23. The reverse was true too.

The Federal Reserve's rate-hiking cycle came to an end as the year concluded. At least, that's the message that was received. The Market exploded with enthusiasm as the year-end rally accelerated. The magic words were rate cuts in 2024. This was a major pivot by the Fed. The central bank was feeling confident about its success in taming inflation and navigating a desired soft-landing. It's far from certain whether that in fact happens. There's also this: The Market is known for false starts.

Rollercoaster Ride

Let's face it, the 2020s have been a rollercoaster ride for investors with wide swings in both directions. New highs were reached in December for the 30-stock Dow, while the S&P and Tech-heavy NAS are still off their all-time highs reached back in 2021. But the strong finish to the year brought 9 consecutive weekly gains, something the S&P had not done since 2004. Would you believe the S&P 500 closed out 2023 almost exactly where it was in 2021? Up and down, down and up; That's exactly what rollercoasters do too. It's been a really wild ride.

The 2020s have been anything but normal. The new decade started with Covid. A global pandemic shut down Planet Earth. Stocks cratered and then soared. 2021 saw supply chains strained with a surge in demand for stuff. Bubbles formed. In 2022, those bubbles burst. Inflation was rampant. 2023 was all about interest rates and Artificial Intelligence (AI). Travel exploded.

Risk: Take and Shake

The Market kept shaking off the growing risks and rallied to close out the year. 2023 was a standout year for risk-taking. The biggest investing risk going into 2024 looks like it will be geopolitics. Traditional relationships and alliances are breaking down, and a more polarized world has given way to structural market risk. It can also be hard to plan for such wildcards, though broad hedging and defensive positioning could play a key part in investing strategy for the new year. But AI remains the greatest growth theme, rivaling the advancement of the internet. It just might be bigger.



2024 is destined to provide many challenges as well as opportunities. Geopolitics have taken center stage with wars, both cold and hot, on the rise. Election will be a dominant theme everywhere. It will start in Taiwan and end in America, with significant elections in India and Russia in between. The results will no doubt shape the landscape for the rest of the decade and beyond.

Protectionism



Protectionism keeps expanding. What started with Brexit in 2016 continued the world over. Elections reflected the spread across continents. It is felt in Europe, Asia and America. Covid exacerbated the issue and the ensuing need for national security. Supply chains got disrupted. Trust was shaken. Borders have been pressed and are under stress. Global alliances are being tested too.

The push toward protectionist trade policies has continued in the United States, regardless of who is in the White House. It's just come under different branding in different administrations. The Trump administration chose tariffs. Biden's White House has chosen subsidies. "America First" and "Make America Great Again" have been replaced with "de-risking," "diversifying" and "leveling the playing field." They've both been inflationary.

The results are often the same and built on platforms that seek to address national security concerns. Atop the list are the loss of manufacturing jobs and supply chain risks. Billions of Dollars in subsidies have even been doled out to American industry to encourage domestic production. Tariffs and quotas remain in place on many imports, and economic sanctions are increasingly being used as a tool to stabilize markets rather than deterrence.

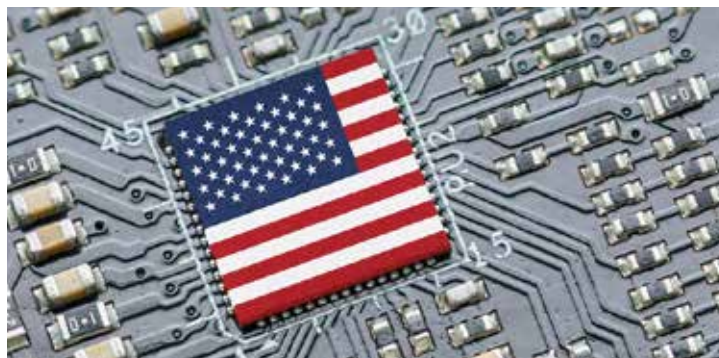
World Order Shifting

The outcome of the 2024 Presidential election will have a profound impact on global markets and global alliances.

The system is changing as the World Order shifts from West to East. Foreign adversaries have been increasingly trying to weaponize the system. Cyber-attacks have become a constant. It's a fact of reality in this Digital Age. Bad actors act bad. It's never been easier to organize crime. Connectivity comes with serious costs.

The United States has implemented massive spending bills like the Inflation Reduction Act, and the CHIPS and Science Act, which poured Billions of Dollars into domestic production. This was a direct response to Russia's invasion of Ukraine and shutting off the energy flow to the EU.

The strategy aims far beyond Europe. The CHIPS and Science Act also provided substantial subsidies and tax benefits to expand domestic semiconductor manufacturing. Export controls were put in place, limiting advanced AI chip access to China. President Xi Jinping seeks advanced chip technology to promote a New World Order for the 21st century. China is behind. China intends to catch up.



Taiwan in the Middle

China wants what the United States and Taiwan have. The island nation off the coast of China represents so much in the Digital Age. The vast majority of advanced semiconductor manufacturing is done in Taiwan. It's literally caught in the middle of the brewing cold war between America and China. Taiwan has a Presidential election early in the year. The results will have a profound impact on the rest of 2024 and beyond.



The Biden administration is considering raising tariffs on certain Chinese goods, including electric vehicles and solar products. The goal is to protect America's green industry and limit dependence on Beijing in the clean energy supply chain. Tariffs are protectionist measures with inflationary forces. They've also caused strains with traditional American allies.

Presidential Cycle

Despite all of the risks around elections, these years have tended to be quite good for investors. The Stock Market has not declined in an election year since 1952. General Dwight Eisenhower defeated Adlai Stevenson in a landslide. Eisenhower was the first Republican elected in 20 years. FDR occupied the White House for 12 of those years. The Cold War was brewing.

The Presidential cycle has a decent track record for the Stock Market. The election year has historically been positive. The thinking is, things are so good, the Market is celebrating 4 more years. Or things are so bad, the Market is celebrating a new regime coming. That said, this time seems quite different. We basically have 2 incumbents running. And polls indicate few Americans are excited about a re-match from 2020.



One of the reasons why stocks did so well in 2023: The most anticipated recession in history never happened. Unemployment remained around 5-decade lows and the American people kept spending. That combination led to an Economy that kept chugging along. That defied the vast majority of economist forecasts. The Job Market has been super strong. Companies still can't find enough workers.

The Fed generally tries to steer clear from interfering in an election year. Of course, politics are everywhere these days. The Fed has been accused of playing politics with its dovish pivot, triggering the Market rally. Pressure comes with the territory. Fed Chair Powell faced tremendous pressure during the Trump years. That didn't seem to affect or influence decision-making at the central bank.

Soft Landing Ahead?

After peaking at 9% in the Summer of 2022, inflation has come down substantially to the 3% range as measured by the CPI (Consumer Price Index). It's highly plausible that a recession merely got pushed out to 2024. Growth has slowed around the globe. High prices have contributed to large debt positions. Credit card debt cleared \$1 Trillion for the first time. The cost to service that debt is over 20%. It's a big problem.



Realistically, there's been a rolling recession in the 2020s. Travel and hospitality faced depressionary forces during the lockdown while demand for stuff soared. Inflation ignited. As things opened up, manufactured goods faced recession as spending rotated aggressively towards activities as America opened up. Inflation rotated towards planes, hotels and restaurants. There's been a recession everywhere but labor.

Rate Cuts

Inflation is expected to fall to 2.1% in 2024, reflecting softer labor markets and slower increases in rents. It is expected to tick back up to 2.2% in 2025. The CBO also expects real GDP growth to slow to 1.5% in 2024 amidst a slowdown in consumption, investment, and exports. This scenario would allow for the Fed to start cutting rates to loosen the chokehold and provide more breathing room for the US Economy to function. Stocks like that scenario.

The Market priced in an 88% chance of a rate cut as soon as the March meeting. It sees total rate cuts of 1.5% in 2024. That seems overly optimistic. In fact, for the Fed to cut that aggressively would likely mean the Economy is falling fast into recession and they're trying to chase. Careful what you wish for.

The Market seems ahead of itself. It's too early to declare victory in the fight against inflation. The Fed has made it clear the data is going to drive rates. The Market has been ignoring the Fed's words for a while, rallying in anticipation of aggressive rate cuts ahead. It's hard to imagine the Fed cutting aggressively with the unemployment rate at 50-year lows. That's basically full employment.

The only thing that saves the Fed is high productivity. Innovation drives that. Artificial Intelligence is the big driver today and tomorrow. But the Fed has a dual mandate. Maximum employment has been achieved. Price stability has not. Prices have stopped increasing at those rampant rates. To be clear, prices are not coming down. It's the rate of increase that has. There's plenty of risk that reverses. Oil prices have fallen substantially. That has provided significant relief to prices at the pump. But there are multiple scenarios that could send energy prices higher again.

The World Still Runs on Crude



West Texas Intermediate Crude Oil fell 22% to end the year. The rise from the invasion in Ukraine and the attacks on Israel completely evaporated. The average price of gasoline fell to an average of \$3.21 a gallon across the country. It came as the United States pumped crude at a record rate. The United States surpassed Russia and Saudi Arabia as the largest producer. It happened with a Democrat in the White House, something few would have predicted.

OPEC (Organization of Petroleum Exporting Countries) was forced to respond to the record American production. The Saudis slashed their output by over 1 Million barrels per day. The deeper cuts did nothing to stop the price slide. In fact, it backfired by causing rifts within the organization. 75% of Middle Eastern Oil goes to Asia. China and India like lower prices. OPEC+ is highly dependent on Oil revenue. These nations want higher prices. Who would've thought a new war in the Middle East would lead to lower Oil prices?

Risks in the Middle East



Iran sees America's influence in the Middle East on the run. That belief cemented its alliance with Russia and China. Iran is believed to be behind not just the Hamas attack on Israel, but also the violent activity in the Red Sea. Houthi rebels in Yemen, supported by Iran, have been launching repeated drone and missile attacks on shipping vessels navigating this important route. The Red Sea is a crucial shipping passage that sees one-sixth of world trade pass through daily. Crude Oil is among it.

Ships have been forced to take longer routes. That has added to the cost and delivery times. Global shipping rates jumped 4x, as shippers wanted to be compensated for the risk. The US Military had to step in. This will likely be an issue well into the new year. A direct engagement with Iran is one of the biggest risks for 2024.

Expanded War Possible

Israel is reportedly getting fed up with Hezbollah. It continues to exchange cross-border fire with the powerful Iran-backed Lebanese militant group. Hezbollah has close ties to Hamas. According to our sources, time for a diplomatic solution is running out.

Israel has indicated that an invasion of Lebanon is not off the table. The Israeli military and Hezbollah have regularly traded fire since Hamas attacked Israel. What makes things more complicated: Lebanon currently has no President. It hasn't had a functioning government for over a year. It also has limited money and resources. Hezbollah is more powerful than the official Lebanese army.



Global Economic Order



The Global Economic Order has become multi-polar. It's pitted East versus West. The United States and China have been staring down a new type of Cold War. The good thing is trade relations between these economic powers are still strong. In fact, 2023 saw the largest trade volume in history between the two nations. The Chinese and Americans depend on each other for daily economic activity. And Europe wants access to both the US and China markets.

The US and China are back to having daily military communications. This came off the Biden-Xi summit in San Francisco. One cannot underestimate the importance here. The United States still has the most powerful military in the world. It's the only nation that can send soldiers and supplies anywhere on the planet. There's been a surge in orders for defense contractors as geopolitical tensions continue to ramp higher. A hot war between the US and China is in nobody's interest.

Dominating the Digital Age

Semiconductors and critical minerals; Dominating the Digital Age requires both. It's the prize of the 21st century that China and the United States covet. The thing is, Technology is becoming more powerful than governments. Communication. Intelligence. Information. Commerce. It's the brains of the Digital Age. Technology companies have the power.



Competition and a free-market system have long been the path to innovation. Protectionism and national security are causing a snag. There are also moral and ethical issues. Advertising is still the dominant model. Revenues surge with increased activity. Algorithms are designed to hook and trigger emotions. People become the products. They're addicted to their phones. Division turns to hate. Companies and countries have much greater power to influence behavior. It's become quite dangerous.

AI Needs a Referee



Congress met with Silicon Valley leaders in an effort to develop a National AI R&D Strategic Plan. The goal was to outline key priorities and goals for federal investments in AI research and development. All parties agree that AI needs what Elon Musk called a "referee." The select committee emphasizes the importance of a shared vision and collective effort to harness the full potential of AI technology. Proper regulation and collaboration are essential, particularly to limit the use by bad actors. Musk went on to say that the meeting and the initiative were important for the future of civilization. It's that big. And it's just getting started.

The Tech Titans saw their stocks surge an average 75% in 2023. The Top 7 companies alone represent nearly 30% of the S&P 500's total market value. At midyear, they accounted for all of the Stock Market gains. The Q4 rally finally saw some broadening in participation. But the 7 Tech Titans accounted for 76% of the S&P gains, adding a combined \$5 Trillion in market cap.

These Tech Titans are unquestionably leading the charge in the AI revolution. Data drives artificial intelligence. Google, Microsoft, Amazon and Apple have an immeasurable amount of data. They know what we're doing, 24/7. Customers rely on their services and have proven to be very brand loyal. These companies are supremely positioned for the AI revolution. IBM is making a comeback after squandering its lead in AI a decade ago. It's also a leader in quantum computing, which increases the speed of problem-solving. Nvidia is the largest provider of the high-performance chips that power AI. It's like the digital equivalent of the picks and shovels that supplied California's Gold Rush in 1849. Demand is fierce.

Earnings Acceleration?



Earnings for the Tech industry are expected to grow 20% next year. AI is the clear driver as more companies are adopting the technology and recognizing the opportunity for greater speed and accuracy in productivity. The Street expects overall earnings to accelerate. Analysts are modeling a 12% jump in growth for 2024. That's a pretty high hurdle. Tech looks poised to deliver again. Their stocks certainly reflect the strength. But a slowing economy could make it tougher for other industries and companies to keep up.

What's Apple Up To?

Apple has been notoriously quiet with its AI plans. Regardless, the company increased in value alone by \$1 Trillion in 2023. That was a 50% increase. That's never happened before. What's more, it occurred while revenues were flat. There was no growth. There's also never been a \$3 Trillion company. Apple's the one.



So, what's the next big thing for Apple? There's long been talk about an Apple Car, but there's been no noticeable movement yet. There's also rumors of a foldable iPhone, but probably not this year. The company is making a splash in Virtual Reality, but so far, it's a very niche market. Perhaps a new version of a long-time favorite is coming.

Mac turns 40 in January. An AI Mac would definitely generate interest. Artificial Intelligence infused PCs and devices will absolutely kickstart the AI revolution on Main Street. Devices have only incrementally improved of late. AI infused devices would be big. Imagine Siri on steroids. The company increased its Research & Development spending by 14% last year. A replacement cycle is fast approaching. Apple might not be first to market. But when they hit, they usually hit big.

2020s - The Rest of the Decade

The Tech Titans of the Digital Age are reminiscent of those dominant companies of the Industrial Revolution. They were run by men named Rockefeller, Vanderbilt, Carnegie and Morgan. They were driven with conviction.

Visionaries named Jobs, Gates, Bezos and Musk all shared characteristics: hyper-smart and hyper-competitive. Losing is not an option for them. They can't rest, for someone else might out-think them. Microsoft and OpenAI caught Google off guard. It sped up the process. The race was on. Google responded. Others are going all in too. Start-ups are born daily with AI.



Silicon Valley companies have every incentive to be there. The prize is dominating the Digital Age. It's still very early days. One issue is the global infrastructure, in many ways, is still tied to the 20th century and fossil fuels. Society is not quite ready for it. Building out the infrastructure takes time, massive amounts of energy and a ton of money. It's happening now.

What does it mean for us in the future? The key is to be what's referred to as "AI adjacent." AI will speed up results and accuracy. We need to evolve and grow with the technology. We need to understand how to use it. AI will replace many jobs and functions. If you're not using artificial intelligence to enhance your productivity, you will be left behind by others who are.

Mountain of Debt

There's still that nagging issue of debt. America has a mountain of it; \$34 Trillion tall. Fitch downgraded the United States credit rating to AA+ from AAA last Summer. You may recall, S&P knocked America's AAA status back in 2011 after a different government fight over the growing debt burden. It was \$16 Trillion then, less than half it is today.



Not only does the US have more debt, but it's more expensive too. We are now paying \$1.1 Trillion annually in interest alone. That's more than defense and medical spending, and just shy of Social Security. The cost to service the Federal debt spiked last year as the Fed raised rates. The Market is finally paying attention and showing signs of stress in the system. Yields fell to end the year. But the days of free money are over. Responsibility and financial discipline have returned.

"Repo" contracts for US Treasuries, jumped to 5.452% to end the year. That is the highest level since 2019. Shrinking bank reserves sent the cost of overnight loans as high as 10%. The Federal Reserve was forced to intervene. Repurchase contracts, Repos, allow investors and companies to borrow against Treasury securities and other collateral to make payments. A spike in the price for repos can be a sign that cash is getting scarce.

Yield Curve Movement



The widely watched yield curve has been inverted for the better part of 2 years. It's become increasingly less inverted. That's generally a good sign, under normal circumstances. Interest rates should be higher for longer maturities to reflect the additional risk.

Demand for short-term Treasuries is quite strong. It's the safest asset on the Planet. We still really like short-term Treasuries. But investors are requiring higher yields for longer-dated Treasuries as the federal debt balloons. Foreign countries have been moving away from Dollars and Treasuries. In fact, 20% of global commodity trading is done outside of Dollars. That's new.

Gold Shines

The weaker Dollar and lower interest rates sent the price of Gold higher. We see that continuing. Fed rate cuts with a slowing economy ahead of a contentious election should show Gold as a coveted asset to own in 2024. We're there and we like it.

We see the yield curve steepening in 2024 as the Fed cuts on the front-end while the Market forces yields higher on the back-end because Congress does nothing to address the mountain of federal debt. Fiscal deficit was 3.7% of GDP in 2022. It could be twice that in 2024. And that's when the Economy has been growing. Normally, that's the time to show fiscal discipline and reduce debt. Not this Congress. Not today's Washington. The Bond Market is awakening. The Bond Vigilantes have returned.



Opportunities Overseas

We've ventured back into international investments. The weaker Dollar is generally good for Emerging Markets. Rate cuts ahead should fuel these faster-growing foreign stocks. China's challenges are opportunities for the rest of Asia. Major infrastructure spending in India, Indonesia and Vietnam will have a lasting impact on global growth. It's already working.

Mexico has benefitted from increased manufacturing in response to the supply chain strains experienced during Covid. Having stable supplies closer to home has proved essential. Brazil is experiencing a recovery, driven by increased energy

production. Brazil provides an alternative to Russia and Ukraine for both food and fuel. Brazil is a large commodity producer so increased demand for agricultural items is good for the South American nation.

We're invested in India with the fastest growing economy in the world driven by young demographics and a new embracement of global markets. With 1.4 Billion people, India is now the most populated nation. It's a huge, growing market. Importantly, India's government has invested heavily in infrastructure and has benefitted mightily from western desires to reduce dependence on manufacturing in China. It's early days for India's economy. It's very investable.



The Space Race Accelerates

The future of space travel is now. Nations know how important it is to secure a position in the next frontier. Worsening relations on Earth have made it more critical to have a stronghold beyond. The Space Economy has begun.

In the lead has traditionally been the United States and Russia. China has been playing catch-up. They're not alone. India surprised the world last Summer when it became the first nation to land near the south pole of the moon. India became just the fourth country to make a lunar landing.

Technological innovation is making it happen. Investments have been made. More are coming. Elon Musk and Jeff Bezos are high-profile early leaders. SpaceX and Blue Origin are their orbital brands. A SpaceX spinoff of satellite company Starlink with an IPO would likely trigger another burst of investor activity in 2024.



NASA has partnered with private companies to access capital and the entrepreneurial spirit. Lockheed Martin is a big player here. Amazon is too. Amazon's answer to Starlink, Project Kuiper, passed an important test in 2023 and is expected to launch in 2024. Amazon claims data travels 30% faster in space via satellite than it does through cables on Earth. The company anticipates data to double its speed by the end of the decade. Investments are getting returns.

Olympic Creed

2024 is another Olympic year. With all the contentious activity on Planet Earth, it will be refreshing to have a stark reminder of what really matters this Summer. The Olympics are about competition and sportsmanship. The Olympic motto is "Citius, Altius, Fortius," which translates from Latin to English as Faster, Higher, Stronger. Perhaps more important today are the 3 core Olympic values. They are: Excellence, Respect and Friendship. They constitute the foundation on which the Olympic movement builds its activities to promote sport, culture and education with a view to building a better world.

Perhaps lost in the games, like so many other things that have become so commercialized and political, is the Olympic spirit. We mustn't forget the Olympic Creed: The most important thing in the Olympic Games is not to win but to take part. Baron Pierre de Coubertin, who revitalized the Ancient Olympic games in the 19th century, said it best: "The most important thing in life is not the triumph, but the struggle." Let's hope the 2024 games can unite the people of America and the people of the world to a greater cause.



Back to the Market

With all the challenges and opportunities ahead, we see this rollercoaster ride continuing in 2024. Among them all, the biggest issue will most likely be the Presidential election in November. It's going to be significant in every way. All polls indicate few are excited about the prospects for a 2020 rematch. One thing seems clear: It's not going to be smooth sailing.



Did the year-end rally price the Market to near perfection? In aggregate, that looks very plausible. But when you consider the median stock was up 8% last year and trades at a significant discount to the overall S&P, it looks like there are many fairly and perhaps undervalued investment opportunities ahead.

Only 3 sectors outperformed the S&P 500 in 2023. What's more, there were 3 sectors that were actually down on the year. The Tech Titans dominated. Those top 7 stocks might be due for a breather while the remaining 493 could take flight. International stocks and Small Caps have underperformed US Large Caps for years. The spread has seldom been this wide. Both came to life to close out 2023. A mean-reversion seemed ripe. The set-up is there for continuation in the new year.

Bulls and Bears

There's nothing like price to change sentiment. Investor sentiment rallied with the Stock Market in 2023. It ended the year with the Bulls tracking at 52%. That was the high on the year. The previous high was in July. You might remember that was also the previous high for the Stock Market before the 10% decline in August and September. Sentiment switched to 50% Bearish in October, just before the year-end rally.

Sentiment is always a contrarian signal on Wall Street. Investors prove time and again their emotions. They tend to get excited at Market tops and panic at lows. That's been the way for decades. Investors can be analytical and emotional. The Market is practical yet cynical. It focuses on facts. The Market is driven by revenues and earnings. We will learn a lot when Corporate America submits their report cards. This environment is stacked with both challenges and opportunities. Navigating will continue to be difficult. We are confident that this Rollercoaster of the 2020s will continue in 2024. We'll get through it. Hang on for the ride.



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