Market Review Commentary

November 2023

Kayne Anderson Rudnick Investment Management

STOCKS AND BONDS RALLY IN NOVEMBER

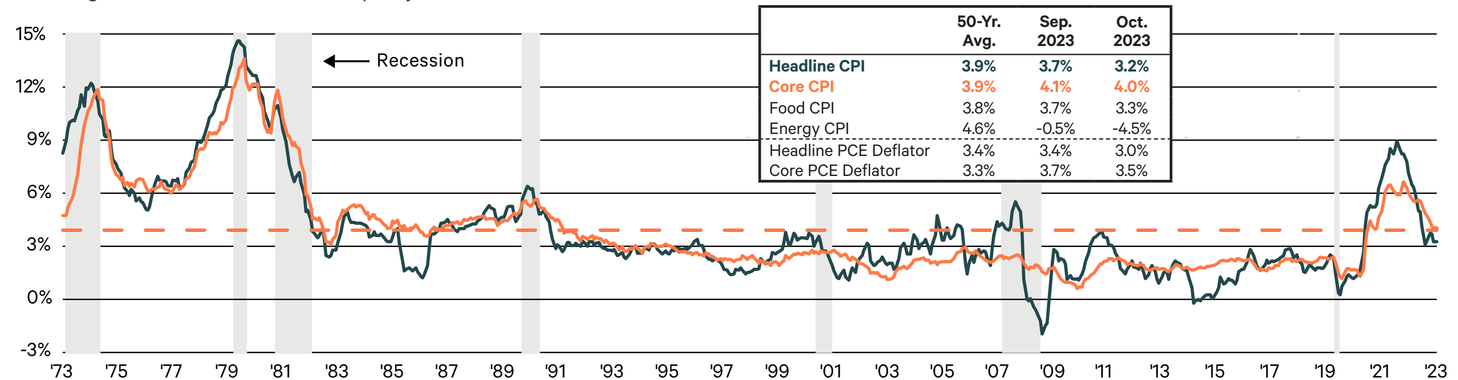
Stocks and bonds rallied in November on the growing belief that the Federal Reserve may be finished raising interest rates. The S&P 500 Index returned 9.13% and posted its best month of the year. Small capitalization stocks, a market underdog, participated in the broad rally and kept pace with larger stocks with a return of 9.05%, as measured by the Russell 2000 Index. Growth stocks outperformed value stocks, aided by enthusiasm for artificial intelligence, and gained 10.90%, as represented by the Russell 1000 Growth Index, versus the 7.54% return for the Russell 1000 Value Index. The 10-Year U.S. Treasury yield moved lower during the month, sliding to 4.36% from a peak of almost 5% a month ago. Lower bond yields also helped drive stocks higher in the month since lower bond yields make equity investments more attractive.

IS THE FED DONE RAISING RATES?

After months of worrying about recession and how high the Federal Reserve would raise interest rates, the Fed kept rates unchanged at the beginning of the month, fueling a strong market rally across stocks and bonds on the belief that the central bank is finished raising rates. The Fed's decision to leave rates in the range of 5.25% and 5.50% continues to be supported with softer inflation data, moving the Fed closer to its preferred inflation gauge of 2%. More good news came on the last day of the month as reports for October confirmed inflation data slowing. Signs of softer inflation appear to signal that the Fed will hold rates steady at its December policy meeting.

FIGURE 1: CPI AND CORE CPI

% Change vs. Prior Year, Seasonally Adjusted



	50-Yr. Avg.	Sep. 2023	Oct. 2023
Headline CPI	**3.9%**	**3.7%**	**3.2%**
Core CPI	**3.9%**	**4.1%**	**4.0%**
Food CPI	3.8%	3.7%	3.3%
Energy CPI	4.6%	-0.5%	-4.5%
Headline PCE Deflator	3.4%	3.4%	3.0%
Core PCE Deflator	3.3%	3.7%	3.5%

Data as of December 4, 2023. Data is obtained from BLS, FactSet and J.P. Morgan Asset Management and is assumed to be reliable. CPI used is CPI-U and values shown are % change vs. one year ago. Core CPI is defined as CPI excluding food and energy prices. The Personal Consumption Expenditure (PCE) deflator employs an evolving chain-weighted basket of consumer expenditures instead of the fixed-weight basket used in CPI calculations. ***Past performance is no guarantee of future results.***

MARKETS POSITIVE ON INTEREST RATE DIRECTION

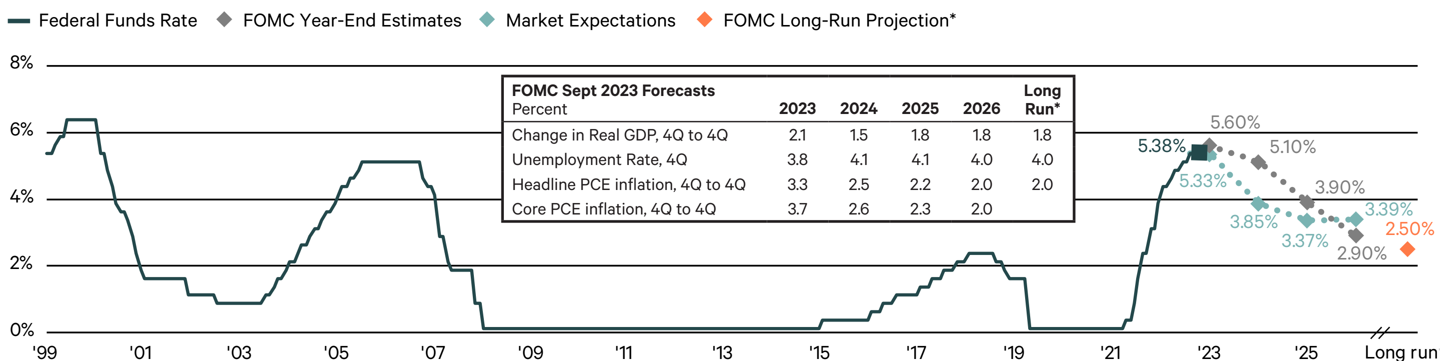
With growing optimism that rate hikes are behind us, the market narrative has pivoted from potential recession to a soft landing, where inflation is declining and the economy is continuing to grow and unlikely to tip into a recession. As inflation data is materially lower than a year ago and on the decline, this clarity on interest rates is what the market has been hoping for and helps strengthen the health of the stock market. The cost of capital (borrowing) is pegged to interest rates, and lower rates are obviously better for borrowing than higher rates. In particular, small-cap stocks experienced a strong

rebound from the outlook of lower inflation and possible rate cuts in 2024. Smaller, growing companies generally perform better in an improving economy and benefit from lower borrowing costs to finance growth.

While monthly data will continue to be key in gauging inflation and interest rates, the market conversation of “higher rates for a longer period of time” quickly reversed this month to the federal funds futures market pricing in rate cuts by the end of 2024, assuming continued better inflation data along the way. It appears we are on a path to lower inflation, but caution is warranted. Recall the consistent story of this rate tightening cycle is that investors have been wrong in anticipating the Fed’s moves. In fact, Fed Chair Jerome Powell signaled to the market at a speech at the end of the month that the central bank would “tighten policy further if it becomes appropriate to do so.”

FIGURE 2: FEDERAL FUNDS RATE EXPECTATIONS

FOMC and Market Expectations For the Federal Funds Rate



FOMC Sept 2023 Forecasts Percent	2023	2024	2025	2026	Long Run*
Change in Real GDP, 4Q to 4Q	2.1	1.5	1.8	1.8	1.8
Unemployment Rate, 4Q	3.8	4.1	4.1	4.0	4.0
Headline PCE inflation, 4Q to 4Q	3.3	2.5	2.2	2.0	2.0
Core PCE inflation, 4Q to 4Q	3.7	2.6	2.3	2.0	

*Data presented is as of December 1, 2023 and is obtained from Bloomberg, FactSet, Federal Reserve and J.P. Morgan Asset Management and is assumed to be reliable. Market expectations are based off of USD Overnight Index Swaps. *Long-run projections are the rates of growth, unemployment and inflation to which a policymaker expects the economy to converge over the next five to six years in absence of further shocks and under appropriate monetary policy. Forecasts are not a reliable indicator of future performance. Forecasts, projections and other forward-looking statements are based upon current beliefs and expectations. They are for illustrative purposes only and serve as an indication of what may occur. Given the inherent uncertainties and risks associated with forecasts, projections or other forward-looking statements, actual events, results or performance may differ materially from those reflected or contemplated.* ***Past performance is no guarantee of future results.***

That said, a scenario of a stable economy with declining rates is likely to help many depressed market sectors experience a rebound. Investors who have a chunk of their investments in cash may find suitable opportunities among a broader range of equity investments and longer-term fixed income strategies.

Douglas S. Foreman, CFA

Co-Chief Investment Officer

Douglas S. Foreman, CFA is Co-Chief Investment Officer, Portfolio Manager, and a member of the Executive Management Committee. He has approximately 37 years of investment experience.

Julie Biel, CFA

Chief Market Strategist

Julie Biel, CFA is Chief Market Strategist, Portfolio Manager, and Senior Research Analyst with primary research responsibilities for the small and mid-capitalization information technology and health-care sectors.

Large-capitalization stocks are represented by the S&P 500® Index which is a market capitalization weighted index which includes 500 of the largest companies in leading industries of the U.S. economy. Growth stocks are represented by the Russell 1000® Growth Index which is a market capitalization-weighted index of growth-oriented stocks of the 1,000 largest companies in the Russell Universe, which comprises the 3,000 largest U.S. companies. Value stocks are represented by the Russell 1000® Value Index which is a market capitalization-weighted index of value-oriented stocks of the 1,000 largest companies in the Russell Universe, which comprises the 3,000 largest U.S. companies. Small-capitalization stocks are represented by the Russell 2000® Index which is a market capitalization-weighted index of the 2,000 smallest companies in the Russell Universe, which comprises the 3,000 largest U.S. companies. This report is based on the assumptions and analysis made and believed to be reasonable by Advisor. However, no assurance can be given that Advisor’s opinions or expectations will be correct. This report is intended for informational purposes only and should not be considered a recommendation or solicitation to purchase securities. ***Past performance is no guarantee of future results.***