

GREY COURT

Capital Market Flash Report

December 2023 Equity and fixed income markets ran with any and all signs that the Fed is executing an immaculate soft landing. The market's expectations for rate cuts in 2024 exceeded the Fed's own expectations as investors sought to front-run the news of a complete end to the war on inflation without any real damage to the economy. Softening energy markets, trouble in China, and an expanding US government deficit did not ignite broader concerns. Risk-on sentiment was rewarded for the month and the year.

US EQUITY

Small caps soared with the positive sentiment on rate policy. They reclaimed some lost ground relative to large caps with their strongest outperformance since February 2000. Firms particularly sensitive to interest rates, whether by discounting future growth or financing higher levels of debt, were rewarded. Small-cap healthcare and financials surged by 17.6% and 16.1%, respectively. The rally was also broad-based as the S&P 500 Equal Weight Index generated 6.9%, outpacing the S&P 500 by over two percentage points.

	Month (%)	YTD (%)
S&P 500	4.5	26.3
Russell 1000	4.9	26.5
Russell 1000 Value	5.5	11.5
Russell 1000 Growth	4.4	42.7
Russell 2000	12.2	16.9
Russell 2000 Value	12.4	14.6
Russell 2000 Growth	12.0	18.7

CURRENCIES

The US dollar weakened as the Fed indicated a softer rate policy ahead and the market responded with aggressive expectations for future rate cuts in 2024. The Yen had the most ground to recover and it appreciated as domestic prices and wages appeared to be increasing, providing some indication that Japan's central bank may eventually move off its uniquely strong accommodative monetary policy. Canada's strong linkages with the US economy helped further support their currency despite weakening energy prices.

	Month (%)	YTD (%)
US Dollar	-2.1	-2.1
Euro	1.4	3.1
Yen	5.1	-7.0
Emerging Markets ¹	1.3	4.8
Canadian Dollar	2.4	2.3
Bitcoin	12.6	156.4

NON-US EQUITY

Europe gained with its own potential rate cuts on the horizon. However, slowing global growth, notably in China, and a strengthening yen caused a small loss on a local basis in Japan, while there was a gain on a US dollar basis. Gains in periphery countries in EAFE supported returns. Equities declined in China with Moody's issuing a downgrade warning, while domestic and foreign affairs concerns continued to weigh on foreign investment flows. EM ex-China gained with several central banks in South America leading with rate cuts.

	Month (%)	YTD (%)
MSCI All-Country World ex-US	5.1	16.2
MSCI EAFE	5.3	18.9
MSCI Europe	5.0	20.7
MSCI Japan	4.4	20.8
MSCI Emerging Markets	3.9	10.3
MSCI China	-2.4	-11.0
MSCI Emerging ex-China	6.4	20.6

REAL ASSETS

Strong production and rising storage levels in the US put a damper on crude oil prices. Natural gas prices continued to fall with a warmer winter and robust production leading the Energy Information Administration to cut its price forecast. Industrial metals recovered some of the year's losses. Gold gained ground as it often does between the Fed's last rate hike and first rate cut, offering a safe haven with forestalled competition from rising yields. Declining long-term rates, including mortgage rates, led to an outsized return for REITs.

	Month (%)	YTD (%)
Commodities ²	-2.7	-7.9
Energy	-6.0	-21.6
Industrial Metals	4.0	-9.1
Gold	1.1	12.8
Master Limited Partnerships ³	-2.2	26.6
Real Estate Investment Trusts ⁴	9.9	13.7

FIXED INCOME

The general decline in the mid to long end of the yield curve broadly supported fixed income markets, as the 10-year yield fell essentially to where it started the year. The return on US long-term Treasuries was almost double that of the S&P 500, enabling a positive return for 2023. Investment grade indexes benefited from their duration while high yield bonds gained with a narrowing credit spread. A November rally left municipal bonds relatively expensive coming into the month, limiting gains.

	Month (%)	YTD (%)
U.S. Aggregate	3.8	5.5
U.S. Intermediate Treasuries	2.1	4.3
U.S. Long Treasuries	8.6	3.1
U.S. TIPS	2.7	3.9
Corporate IG Bonds	4.3	8.5
High-Yield Bonds	3.7	13.4
Tax-Exempt Bonds	1.6	4.6

HEDGE STRATEGIES

All hedge strategies generated positive returns for the month. Relative value arbitrage led the way as the Fed's extended pause on rate hikes allowed for mean reversion effects across markets to play out. Macro generated the lowest return with crosscurrents in markets following the Fed's midmonth meeting, and as most equity market indexes generally moved in one direction. Implied volatility for the S&P 500 fell and completed a large decline for the year as the economy remained resilient and equity risk was rewarded.

	Month (%)	YTD (%)
Equity Hedge	1.6	6.9
Equity Market Neutral	0.6	4.2
Event Driven	1.1	0.4
Relative Value Arbitrage	2.1	4.7
Macro	0.4	-1.3
Volatility Index (VIX = 12.45)	-3.6	-42.5

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MSCI returns are gross USD. Currency returns are Simple Price Appreciation (SPA) USD basis. Fixed Income reported on Bloomberg Indices. 1MSCI Emerging Markets Currency Index. 2Bloomberg Commodity Indices. 3Alerian MLP Index. 4MSCI US REIT Index. Hedge Strategies reported on HFRX Indices SPA with a one-day lag. For complete Index Descriptions, see <http://www.greycourt.com/disclosure-of-indices/>. Investing involves risks and you may incur a profit or loss. Past performance is no guarantee of future results.

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