EDGE
CAPITAL GROUP

THE WEIGHT

2023 Q4 Outlook

Key themes driving the 4th quarter

THE FED

The Fed paused hiking in September but meets in both November and December with the threat of an additional rate hike looming over the markets.

Powell left the door open for another hike if the economic data remains robust but it likely won't happen and that could lift stocks and bonds into year end.

INFLATION

Core inflation is coming down but staying a bit stickier than the Fed would like.

Rising oil prices can trickle throughout the broader economy and negatively impact core inflation.

EARNINGS

Stocks are up this year due to multiple expansion while S&P 500 corporate earnings are flat to down from a year ago.

Earnings appear to have troughed and strong signals for 2024 could boost stocks.

EUROPEAN ECONOMY

Germany, the UK, and other European nations are teetering on recession, likely a bad signal near-term for international equities.

The lack of growth in China is hurting European luxury goods companies, but a turnaround could help stock prices.

POLITICS

A U.S. government shutdown could be a problem, but it's difficult to handicap how it impacts the economy longer term, if at all.

The presidential season heats up as candidates jockey for position ahead of the start of primary season in 2024's first quarter.

Summary of views

◢ 2023 Q3 ◢ 2023 Q4

	FAVORABLE	NEUTRAL	UNFAVORABLE
INVESTMENT GRADE	◢ ◢		
MORTGAGE SECURITIES		◢ ◢	
NON-INVESTMENT GRADE			◢ ◢
U.S. LARGE CAP EQUITIES		◢ ◢	
U.S. MID & SMALL CAP	◢ ◢		
INTERNATIONAL		◢ ◢	
EMERGING MARKETS		◢ ◢	
INFRASTRUCTURE		◢ ◢	
REAL ESTATE		◢ ◢	
ALTERNATIVES	◢ ◢		

Fixed income asset classes

INVESTMENT GRADE
FAVORABLE

RATIONALE U.S. Treasuries remain our most favored opportunity over credit bonds, especially higher-yielding shorter dated maturities. However, high-quality companies with insulated balance sheets do offer some opportunities within the credit space. And tax-exempt municipal bonds continue to offer upside for clients within high tax brackets. All investors should consider their individual long-term goals and risk tolerance.

RISK The Federal Reserve meets twice in the fourth quarter and with strong jobs data and sticky inflation numbers we could see another rate hike. That would favor the short end of the yield curve. If the Fed holds steady and reiterates its position that at some point in 2024 rate cuts will happen that could deliver a rally further out on the yield curve. Credit spreads remain tight so any cracks in the economy could cause spreads to widen and bonds to trade lower.

MORTGAGE SECURITIES
NEUTRAL

RATIONALE While mortgage securities continue to be cheap relative to corporate bonds, the pressure on borrowers is likely to increase as the Fed keeps rates higher for longer and home prices begin to lose some momentum. Investors also need to consider the effect that higher prices have on other borrower costs (e.g. taxes and insurance). To be sure, mortgages have underperformed more recently as the interest curve has steepened and currently offer a yield advantage over corporates. In addition, years of underbuilding and the resulting lack of supply have created a potential soft-landing scenario for housing. However, we would be cautious and opportunistic in adding exposure given the increasing pressure on borrowers and higher for longer Fed.

RISK Multiple risks cloud our view of the MBS market. In addition to further Fed tightening creating supply issues in the near term, the weakness in commercial real estate and further fallout within the banking sector may spill over into other parts of the credit market. This scenario, combined with a more severe economic slowdown, could lead to lower prices for mortgage-backed securities.

NON-INVESTMENT GRADE
UNFAVORABLE

RATIONALE High yield bond spreads have widened more recently alongside an uptick in equity market volatility, although we would still consider them tight by historical standards. We don't believe investors are being compensated for some of the headwinds that come along with higher interest rates and inflation. More specifically, interest coverage ratios are forecast to decrease, and margins are expected to erode, as revenue growth slows and inflation continues to put upward pressure on costs. Net new supply continues to be at the low end of the historical range, providing some near-term technical support. Nevertheless, we would like to see spreads widen before adding to exposure.

RISK An economic scenario where inflation comes down and earnings growth surprises to the upside would likely lead to further spread narrowing and continued strength within non-investment grade credit.

Equity Asset Classes

U.S. LARGE CAP
NEUTRAL

RATIONALE As the third quarter wore on, it became more and more apparent that the Federal Reserve was going to leave interest rates at higher levels for longer to combat inflation. In turn, U.S. large cap stocks sold off under the weight of those increased rates. As we move into earnings season, however, we anticipate strong results that hopefully can push stocks higher especially if companies' guidance for 2024 is also upbeat. Stocks are not overvalued at these levels so good earnings can engender good stock market results.

RISK The market has been trading in a range for much of the last quarter and is looking for clues to break either way. Another hike at the November or December FOMC meeting could really dampen stocks and cause a breakout to the downside as the market remains on edge about higher interest rates throughout 2024. Conversely if corporate earnings are strong and the Fed holds rates steady (which is our base case) that could set the conditions for a year-end rally in equities.

U.S. MID & SMALL CAP
FAVORABLE

RATIONALE Despite ongoing economic growth small cap stocks struggled in the third quarter. Conditions appear favorable for the sector but performance hasn't matched up so far in 2023. We continue to believe that as rates stabilize and economic growth stays positive small cap stocks are well positioned to outperform their large cap brethren.

RISK While valuations are extremely compelling on an historical basis, valuation is a notoriously poor investing tool over the short term. If the economy slows and rates remain high that's a bad sign for smaller companies that are more reliant on capital markets for fund raising. But if we get clarity from the Fed that rates have peaked and the economy stays out of recession, that could be the catalyst the sector needs to climb higher.

INTERNATIONAL
NEUTRAL

RATIONALE Although pockets of Europe are struggling, Japan is proving itself to be a more investible market than it has in decades. That has drawn interest from a number of U.S. investors and helped the sector mute losses in the quarter. However, a rally in the U.S. dollar due to rising rates generated additional headwinds for foreign equity market returns. The dollar was especially strong last quarter as interest rates continued to rise and the hurdle of currency weakness was too high for international equities to overcome.

RISK European luxury companies depend on Chinese consumers to help fuel growth. If China's economy continues to suffer, that'll make for a tough stretch for those luxury firms. If, however, China's economy picks up we could see some ripple effects in the EU. Additionally, stock market performance will depend somewhat on whether the U.S. dollar continues to strengthen or weakens somewhat. If the Fed holds rates steady at both meetings this quarter, we could see the dollar sell off.

EMERGING MARKETS
NEUTRAL

RATIONALE The economic struggles in China continue, causing some to raise the question of the nation's viability as an investment option. That seems a bit melodramatic to us as there is almost always a price that equates to value. But it is a different landscape in China than the tech-driven markets of a few years ago. However, while Chinese companies may be struggling, opportunities do exist within other large nations like India, Brazil and Mexico. We think selectivity is the key to finding values across emerging markets.

RISK A lot of the risk revolves around China and whether the government can engineer a turnaround in the economy or whether the economic malaise will continue. The real estate sector, where much wealth is stored, is suffering. But the government has reignited the growth engine in times past, so perhaps can do it again. The region is out of favor these days so any good news could draw flows and push stocks higher.

Non-core asset classes

INFRASTRUCTURE
NEUTRAL

RATIONALE Due to continued economic and policy headwinds, our views on the asset class have not changed since the prior quarter. Stubbornly high interest rates remain a formidable challenge for an asset class that broadly carries a high level of debt and is dependent on new projects (which require financing) for future growth. In addition, elevated wage inflation will continue to generate expense challenges for many sectors within this broad asset class, especially those without inflation offsets. Despite these obstacles, we have seen a strong bid for energy assets over the summer months as higher crude and natural gas prices should lead to more production volume and incremental fee income for many. Renewables continue to struggle with financing costs and access to raw materials while transportation assets are expected to slow if recessionary clouds develop.

RISK The primary risk for infrastructure assets remains economic growth and whether the US enters a recession in 2024. Valuations remain reasonable but we would expect tougher economic conditions to pressure forward profits and investors may ultimately overpay for these assets. Should interest rates remain at lofty levels for several years, we would expect debt financing to become a significant risk to the broad asset class.

REAL ESTATE
NEUTRAL

RATIONALE For real estate investors, higher for longer interest rates continue to strike fear of compressed profit margins from the increased cost of capital. Ongoing concerns surrounding commercial real estate remain for banks and other property lenders. Office remains the key detractor and focus of risk though other segments like data centers and industrial properties continue to shine. We remain neutral here as risks abound but believe opportunities can be found in the public REIT space for patient investors and within the private markets, especially on the debt side.

RISK If rates remain high, income generating assets like T-bills provide a low-risk alternative to those investing in real estate for income generation. Additionally, as approximately $1 trillion in commercial loans come due over the coming year, those loans will be refinanced at higher rates putting further pressure on owners. Conversely if rates recede, oversold REITs are likely to rebound while private real estate values should stabilize and even rebound.

ALTERNATIVES
FAVORABLE

RATIONALE A higher for longer Fed continues to create a favorable backdrop for managers, as investors become more discerning in security selection and opportunities on the short side arise from tighter financial conditions. Several of the hedge fund strategies we follow had their best three month stretch of the year through August, and early estimates through September indicate continued outperformance vs. broad market indices. While the narrow rally in high growth equities earlier this year led to lagging performance for many of these strategies, the investment thesis did not change. In an environment where greater macroeconomic uncertainty exists, the room for policy error is high, and valuations are difficult to justify across various asset classes. It makes sense for investors to be hedged. The latest focus on growing fiscal deficits is just another reason to stay that way for now.

RISK The risk to more directional strategies is illuminated by a Federal Reserve that is frequently adjusting their assessment of where inflation and rates should be in the future, and therefore, prone to changing course. The risk of government policy error is high, so hedging strategies should take this into account in overall positioning.

Key wealth strategy reminders Q4

As 2023 comes to a close, be mindful of checklist items to tie up “loose ends” so that you can enjoy and celebrate the end of this year and the start of a new one.

Being mindful of deadlines, it is important to take advantage of any income and estate planning items prior to December 31st. Did you make any significant changes this year such as selling a home, business, or property? If so, kindly provide the relevant information to your Edge team. This will enable us to proactively oversee and optimize your portfolio’s tax planning. Be sure to discuss any other tax planning items with your CPA and Edge team as soon as possible. These items include:

- Annual giving to family
- Annual giving to charity
- Tax management in your invested portfolio
- Medicare enrollment and change window
- Health insurance management
- Retirement account management

Key wealth strategy reminders Q4

ANNUAL GIVING- FAMILY

The annual giving limit before a tax filing requirement is $17k per donee ($34k from a married couple if "gift-splitting"). Consider giving during your Thanksgiving meal with family.

An education savings 529 plan is a great gifting vehicle. Talk with your Edge team about "supercharging" gifts, dynasty education trusts, and future Roth IRA possibilities.

If gifting beyond the annual exclusion above, be sure your tax advisor files a timely gift tax return.

ANNUAL GIVING- CHARITY

Consider additional tax benefits of donating appreciated securities or "gift bunching" to charity.

A donor advised fund (DAF) is a great gifting vehicle. You are creating a legacy, and you can make your charitable decisions at a more convenient time.

Process any charitable giving prior to year-end for an income tax deduction in the current year.

TAX PLANNING- PORTFOLIO

Your Edge team is paying particular attention to any upcoming capital gain tax distributions from your mutual fund holdings.

Work with your CPA and your Edge team to prepare for year-end tax loss harvesting and portfolio rebalancing.

After your prior year income tax return is filed, please share a copy with your Edge Team.

MEDICARE DEADLINE

Medicare Open Enrollment OCTOBER 15th- DECEMBER 7th

All adults who are 65 and older must enroll in Medicare to avoid penalty.

If already enrolled, this window is also the time to make any desired changes.

RETIREMENT ACCOUNTS

Work with your Edge team to process your Required Minimum Distribution (RMD) from your retriement account prior to year end to avoid penalty. Consider a Qualified Charitable Distribution (QCD) to fufill the requirement and benefit your favorite charity.

Is this is a good year to process a partial or full Roth IRA Conversion from a tax deferred retirement account? Discuss with your tax advisor and Edge team.

Fund the maximum allowed to your retirement plans. Also fund the maximum allowed to your healthcare savings account (HSA) for triple tax benefits.

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