CETERA® INVESTMENT MANAGEMENT

2023 FOURTH QUARTER OUTLOOK

Bears Peek from Dens as Economy Brightens

At-A-Glance

U.S. Gross Domestic Product (GDP) growth for the second quarter was 2.1% and the first quarter was revised higher to 2%. The Atlanta Fed is estimating third quarter GDP growth to be near 5%, ahead of consensus estimates of near 3%.

The Consumer Price Index (CPI) increased to 3.7% year-over-year in August, but more importantly, Core CPI slowed to 4.3%. Gas prices rose, pushing up headline inflation, but core CPI strips out volatile metrics such as gasoline and food prices.

Rates were increased only 0.25% by the Fed in the second and third quarters, putting the current target range at 5.25% to 5.50%.

After climbing the wall of worry in the second quarter, stock returns have been muted in the third quarter as investors digest better-than-expected economic data, moderating inflation, and the Fed's response to these changes.

Bond yields have climbed higher on better-than-expected economic growth and a Federal Reserve that has not waivered on its stance to keep rates higher for longer. Higher bond yields have helped mitigate bond losses.

Overview

As we enter the last quarter of the year, investors are becoming increasingly optimistic about the future of inflation, the economy and fed policy. The optimism, however, is tempered with some healthy skepticism around overhanging risks to both the economy and the markets.

The third quarter saw relatively flat equity returns (as of this writing) and year-to-date the S&P 500 is relatively close to recovering all of last year's decline. As we pointed out in last quarter's Market Outlook, returns were driven in large part by large growth companies that make up an oversized portion of the index. So far, markets have overcome various possible pitfalls from a few regional bank failures to a debt ceiling debate that theoretically could have caused a default on U.S. Treasuries. Looking ahead, the new overhangs in the fourth quarter will likely include the possibility of a government shutdown in early October.

The good news (and bad news) is that government shutdowns are nothing new; this would be the 22nd shutdown since 1976. With markets largely overlooking the debt ceiling debates, we anticipate markets will take any potential shutdown with a grain of salt. Markets tend to trade down on news of a shutdown but recover quickly.

Another possible pitfall facing investors are rising oil prices, which may eventually feed into inflation figures and catch the attention of the Fed, and thus cause another rate hike before year-end. Additionally, there are high valuations in stocks that make up a large portion of major indexes, as mentioned above.

Aside from these potential overhangs, economic data has been surprising to the upside most of this year. Surveys given to business leaders in both the manufacturing and service sectors appear to be improving, while inflation is moderating. Additionally, the labor market is moderating which is good news because labor market imbalances fueled wage inflation. This is something the Fed is looking at closely in creating Fed policy, so with wage inflation and inflation overall dissipating, it could give the Fed room to pause its rate hikes for the remainder of the year, although one more hike could still be on the table.

So, while economic data is relatively weak in some respects, it is showing signs of improvement, which has many economists changing their projections for a possible recession. If we do see a recession, it would likely not be until next year and likely be mild.

Your financial professional can help you stay on track and keep focused on your personalized long-term plans, helping you navigate a changing economy.

For a more detailed look into what we are thinking and what is happening in the economy and markets, check out the rest of our Fourth Quarter 2023 Market Outlook.

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A diversified portfolio does not assure a profit or protect against loss in a declining market.

Glossary

The **S&P 500** is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The **Citigroup Economic Surprise Index** is a measure of how economic data releases compare to market expectations. It is calculated as the weighted historical standard deviation of data surprises.