

# Invest Smarter. Live Better.

## Closing Strong

Avalon client portfolios had solidly positive returns in the fourth quarter, as double-digit gains in global equities, gold and US Treasury bonds were more than enough to offset small losses from natural resources. After enduring a difficult third quarter where rising bond yields and a hawkish Federal Reserve drove the markets lower, an end-of-October reversal in yields drove markets higher into the new year.

In our third quarter letter, we noted that historical seasonality of the stock market could both explain a weak Fall and possibly portend a strong close to the year. That seasonality held true as the fourth quarter saw the NASDAQ rise 14.6% while the S&P 500 gained 11.6%. The story was similar outside

of large capitalization growth stocks, as US small capitalization stocks gained 14.0% while US value-oriented stocks rose 9.2%. Internationally, developed market equities rose 10.7% and emerging market stocks gained 8.0%.

One of the reasons for the rally in stocks was the market's more sanguine view on inflation. This also helped fixed income assets. For the quarter, the 20 Year US Treasury Bond index returned 12.9% while the Barclays Aggregate Bond index gained 6.8%. These moves were enough to shift both indices from negative into positive territory for the year. And offered a reprieve from what has been a historically difficult market for fixed income since 2022.

### A Fantastic Rally to Close Out the Year (2023 Full Year Returns)

1) SPDR S&P 500 ETF TRUST	26.19%	
2) ISHARES MSCI EAFE ETF	18.40%	
3) ISHARES US REAL ESTATE ETF	11.93%	
5) ISHARES CORE U.S. AGGREGATE	5.65%	
6) SCHWAB SHORT-TERM U.S. TREASURY	4.31%	
7) ISHARES NORTH AMERICAN NATURAL RESOURCES	3.13%	

## Breadth

With the performance of small capitalization and value-oriented stocks, breadth within the US stock market improved slightly in the fourth quarter. Despite this, 2023 returns were primarily driven by the largest capitalization technology stocks (the Magnificent 7) which account for close to 30% of the S&P 500's value. Behind the full weight of the Magnificent 7 (Apple, Microsoft, Alphabet, Amazon, Nvidia, Meta and Tesla), the market capitalization weighted S&P 500 returned 26.2% for the full year. In comparison, an equal weighted basket of S&P 500 stocks (limiting the impact of these 7 constituents) returned 13.7%.

Improving breadth is a good sign that we will continue to monitor. As we noted in our third quarter letter: *Historically, a lack of breadth indicates a less than healthy market. As breadth narrows, market concentration peaks. And, historically, market concentration has tended to foreshadow equity drawdowns. We are not suggesting an imminent market correction though we would feel much better about equities were breadth to broaden.*

## Portfolio Positioning

In the fourth quarter, we added to client portfolio positions in US Treasury Bonds as well as US equities. Within US equities, we added to large capitalization growth stocks, small capitalization stocks as well as quality

stocks (defined as stocks of companies with sustainable business models and healthy balance sheets). From a valuation perspective, small capitalization stocks are historically attractive relative to their large capitalization peers. And while our analysis would indicate that valuations for both large capitalization growth and quality stocks are fairly priced, these companies have proven the most resilient in periods of economic distress.

## New Additions to the Team + Seeing All of You

We are excited to be adding two talented individuals to the Avalon team early in 2024. And we look forward to introducing them to you once they are onboarded and up to speed. On a technical level, the new team members have impressive experience and domain expertise within the investment and wealth management worlds. And, more importantly, we think both are great cultural fits. Each has known either Clara or Ross for over 15 years. We are thrilled that they are joining us and are confident that they will add to your experience here at Avalon.

Looking forward to a great 2024 and to seeing you soon. We remain grateful for your confidence in us.



Clara Basile



Ross Revenaugh



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