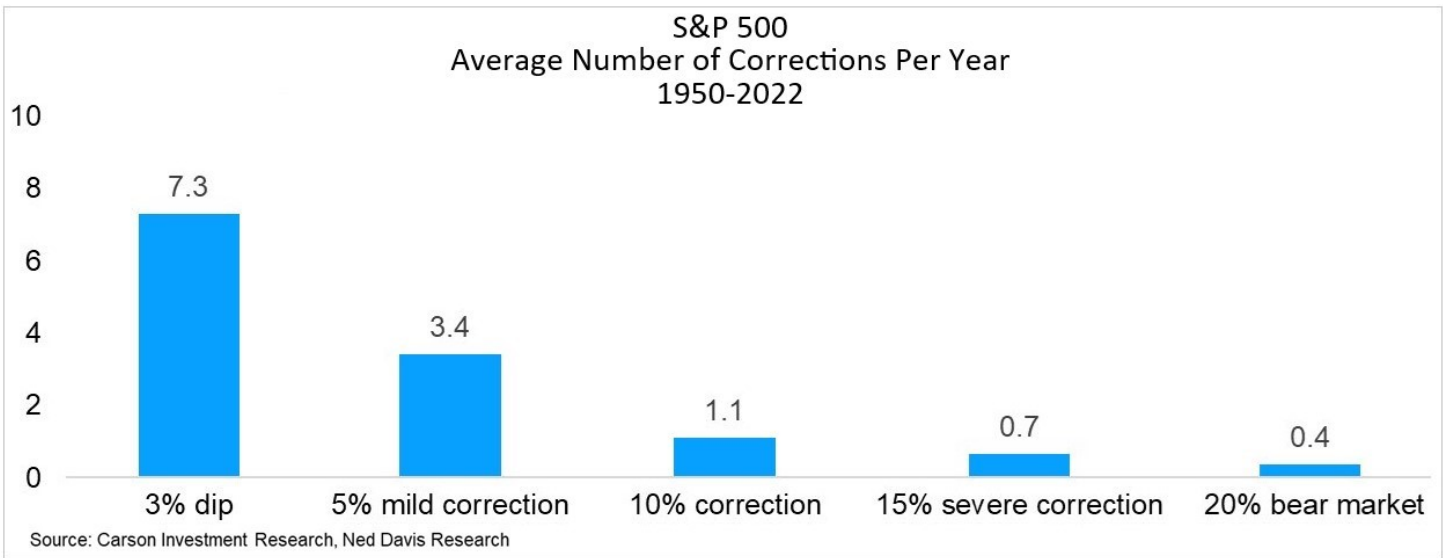
CHART OF THE MONTH

AUGUST 2023



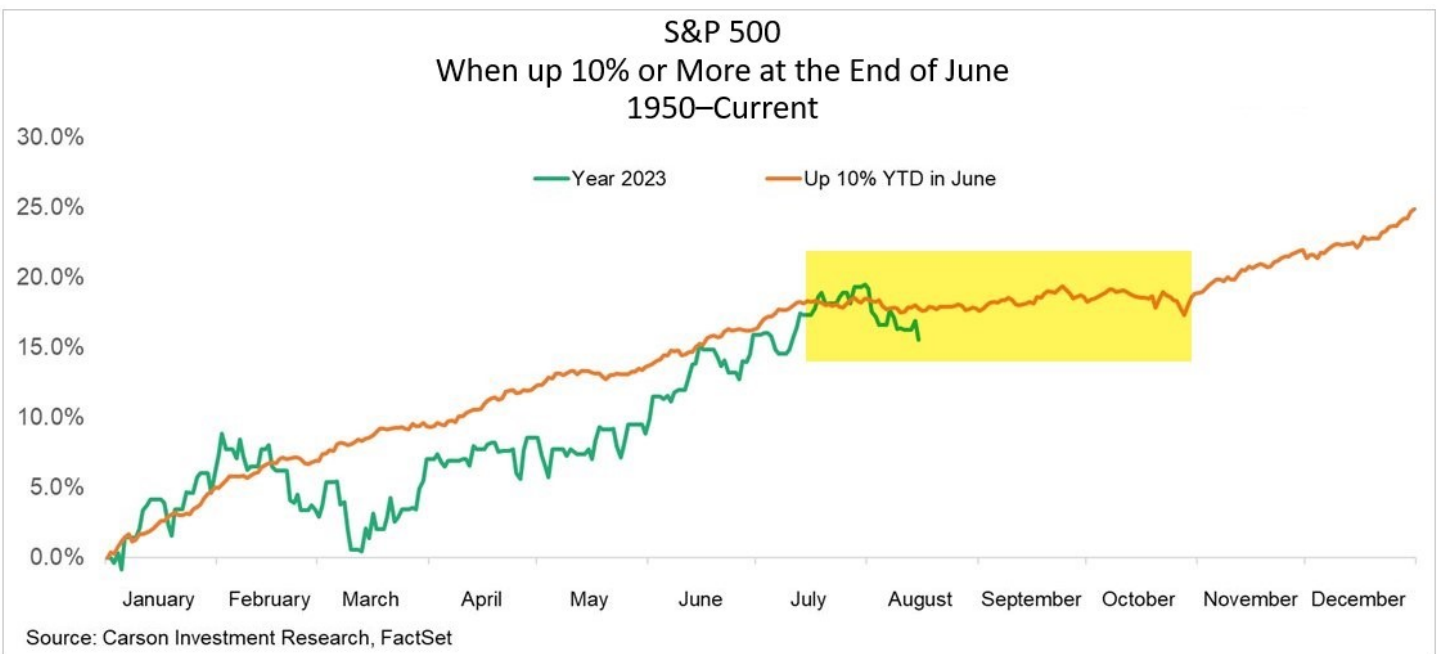
As measured by the S&P 500, the stock market has declined 4.8% from its peak on July 31. Equity prices began to soften when the yield on the 10-year U.S. Treasury rose above 4.0% in early August. The benchmark Treasury has since climbed to 4.23%, a rise of 5.8%, approximating the diminution in stock valuations this month.

The pop in Treasury yields is due to better-than-expected economic data coupled with an increasing supply of government debt owing to the surge in the federal deficit. As it relates to the former, the Atlanta Fed's GDPNow tracking model raised its third quarter real GDP growth rate projection from 4.1% on August 11 to 5.0% on August 15 and to a whopping 5.8% on August 16, defying expectations for a near-term slowdown or recession. Positive economic surprises, however, are bearish for bonds because of the possible negative impact on inflation, which may require further tightening of monetary policy.

Meanwhile, the roughly 5% pullback in stocks should not be a surprise given the gains since the bottom last October. It is important to keep in mind that the market tends to experience adjustments of this magnitude about 3-4 times per year (see graph above). The most recent drawdown in the S&P 500 was 7.8% between February 2 and March 13. The index subsequently advanced 19%. Volatility is the price investors pay to earn potentially higher-than-risk-free rates of return.

As shown below, when the S&P 500 has increased at least 10% in the first half (as it did in 2023), it has tended to consolidate from August through October. August, September, and October have historically been more challenging months but November and December have generally produced stronger-than-normal returns. If the past is prologue, the market may make up for the seasonal weakness and approach or even surpass its interim high on July 31 by the end of the year.

While cautious near term, we remain constructive on the outlook for the economy and the stock market, reminding clients that year three of the presidential cycle has been the strongest of the four years since 1950, generating returns more than twice as high as the others.



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