Ironwood Investment Counsel, LLC

Ironwood Investment Counsel, LLC constructs and manages customized investment and wealth management programs designed to meet our clients' unique goals and objectives. Our distinctive process maximizes performance through return enhancement, risk reduction, tax efficiency, and cost containment.

Your Ironwood Team
14646 North Kierland Boulevard
Suite 135
Scottsdale, Arizona 85254
480-609-4700
Fax 480-609-4725
www.ironwoodic.com

Second Quarter 2023 Market Commentary

In many ways, the second quarter of 2023 proved the market's resilience in the face of economic calamity — contrived or otherwise. From Wall Street's prediction of an impending recession, which has become the most widely anticipated recession in history (and which also has yet to materialize), to future Federal Reserve Open Market Committee (the "Fed") policy decisions in the wake of persistent inflation, the quarter was defined by seemingly manufactured fear that failed to make a recognizable impact.

Coming off of a challenging year in 2022, markets resumed their upward trajectory from the first quarter. As the second quarter came to a close at the end of June, the S&P 500 posted an 8.74% return. This milestone was cheered by investors. However, while the S&P 500 is rallying, the narrowness of this advance should be recognized, as much of it has been driven by a small number of stocks. The Dow Jones Industrial index also ended the second quarter on a high note, finishing with an overall return of 3.97% for the period.

Overall, second quarter performance was strong for other equity benchmarks as well. The Russell 2000 Index ended the three-month period with an advance of 2.31%, a positive for smaller companies across the country. In addition, the MSCI EAFE Index, which tracks a broad group of publicly traded businesses domiciled outside of the U.S., closed out the quarter with a 3.19% return.

Fixed income investors, however, had slight declines for the quarter as interest rates resumed their slow march higher. The Bloomberg U.S. Aggregate Bond Index closed down -0.84% under the weight of a Fed Funds rate hike in May. Tax-free bonds suffered similar middling performance, with a total loss for the quarter of -0.41%.

Despite investors' continued focus on inflation, commodity prices fell again during the second quarter. The S&P Goldman Sachs Commodity Index fell -5.85% over the three-month period, bringing total declines to -11.41% for the year and almost -25% over the last twelve months. Crude oil was especially hard hit during the quarter, declining nearly -10%.

Over the second quarter, multiple themes made an impact on the markets. Below, we highlight some of the defining topics:

Recession Concerns Abating

Economists were quite convinced that recession would strike in 2023. They were joined by business leaders and investors in anticipating a slowdown and ultimately negative growth. However, the U.S. economy and jobs market proved less sensitive to higher interest rates than previously thought. In fact, U.S. economic activity rose during the second quarter to the highest level in 13 months, driven by a continued rebound in the service sector. While growth forecasts are lower, they are not yet negative. To this point, the World Bank now projects growth to be 2.1% for 2023, a revision higher than January's estimate of 1.7%.

Employment Resilience

Over this latest economic cycle, there have been more jobs than people to fill them. The consensus expectation is that this ratio should begin to equalize; however, the numbers held steady throughout the quarter. The consensus may yet prove to be right, though. Shortly after quarter-end, the Labor Department reported that there were a seasonally adjusted 9.8 million open job positions in the U.S., down from 10.3 million in the prior month. In May, employers added 339,000 jobs, bringing the total number of jobs added this year to nearly 1.6 million. Further, the Inflation Reduction and CHIPS Acts may have helped ignite a manufacturing boom in the U.S., as evidenced by a doubling of manufacturer's construction spending over the last year.

Federal Reserve Policy

After 10 consecutive interest rate increases, the Federal Reserve Open Market Committee (the "Fed"), paused and did not take action on June 15th, leaving the Fed Funds rate unchanged. While the Fed indicated that they may resume interest rate increases later this summer, the pause was welcome news for investors and future borrowers. The Fed has two mandates, price stability and full employment. With regard to price stability, the Labor Department reported that the Consumer Price Index slowed in June to 3% from a year earlier. While the most recent inflation report is promising, CPI still resides above the Fed's target of 2%.

Debt Ceiling

Over the month of June, Congress was able to come together to lift the debt ceiling after a contentious period. Despite concerns of the debt ceiling overhang becoming a real risk to the market, investors have chosen to ignore the negative implications of this situation thus far. With rising interest rates, the cost of debt service will also rise, and nowhere will this be felt more sharply than with the U.S. government. U.S. government interest payments have doubled from over $1 billion per day in 2022 to almost $2 billion per day in 2023.

Season of Artificial Intelligence (AI)

The second quarter also saw AI-related stocks shoot to the moon. Perhaps not entirely comparable to the 1990s "dot-com" era, AI seems to be creating a similar level of enthusiasm whether or not it is warranted. Shares of tech darling, NVIDIA, increased by over 24% in one day, adding over $180 billion in market value on positive earnings news and hopes of future AI growth. It is too early to tell whether the attention surrounding AI is yet another "flash in the pan" or just the tip of the iceberg of how it could impact the economy of the future.

Broader Market Opportunity

As it relates to the second half of the year, there are positives on the horizon including the fact that many stocks have not meaningfully participated in the 2023 rally. Though performance in the market has largely been driven by seven companies thus far, there are many attractively valued, high quality securities that we expect to catch up. Earnings growth has been somewhat challenged in the near term; however, we expect to see a positive earnings recovery in 2024.

Despite the many predictions of volatility in 2023, we feel it is important to stay the course through the “doom and gloom” forecasts. At Ironwood, we have found the optimal way to manage client portfolios is to focus on quality investments and to follow value while not placing too much emphasis on predictions. We are constantly re-evaluating the companies from which we buy equity and that we lend to, ensuring they still demonstrate the quality we initially found. Carefully selecting companies that are insulated from the “disaster of the day” while avoiding overconcentration and the latest fads, we recognize that, most importantly, each of our client’s needs are highly individualized. We aim to work together with you to meet and exceed your long-term objectives and make careful, calculated decisions that can not only weather the storm but allow you to prosper in good markets and challenging ones.

We are honored that you have entrusted us with your capital. This is a privilege and responsibility we do not take lightly. Please contact us if you wish to set up an appointment to review your portfolio and wealth management objectives. We look forward to speaking with you.

Ironwood Investment Counsel, LLC