The Gorton Wealth Management Group of Wells Fargo Advisors

2023 Annual Review
January 2024

An update of performance, trends, research, and topics for the long-term investor

Relevant rates of return a/o 12/31:	2023	vs.	2022
Russell 1000® Growth Index: Stocks within this index include: Apple, Microsoft, Amazon, Alphabet A, Tesla	+42.7%		-29.1%
Russell 1000® Value Index: Stocks within this index include: Berkshire Hathaway B, Exxon, Chevron Johnson & Johnson, JP Morgan	+11.5%		-7.5%
Bloomberg U.S. Agg Bond Index:	+5.5%		-13.0%
S&P 500 Index:	+26.3%		-18.1%
S&P 500 Equal Weighted Index:	+11.5%		-13.1%
Russell 2000® Value Index:	+14.6%		-14.5%
MSCI EAFE® Index:	+18.9%		-14.0%

Long Term Historic Returns, compounded annually (1970-2021)[1]

- Small Value +13.9%
- Large Value +10.5%
- Small Growth +9.7%
- Large Growth +9.7%

Growth and value stocks in this example are represented by the Ibbotson Associates Growth and Value Indexes for 1970–1997 and the Morningstar Style Indexes thereafter. The Ibbotson Associates Growth and Value Indexes are calculated based on data from CRSP US Stock and Index Databases, the Center for Research in Security Prices (CRSP®) and the University of Chicago Booth School of Business. Used with permission.. The data assumes reinvestment of income and does not account for transaction costs or taxes.

Celebrating Excellence: Forbes Best-in-State Wealth Management Teams 2024

The Gorton Wealth Management Group is honored to be recognized by Forbes as one of the Best-in-State Wealth Management Teams of 2024. As a team, we pride ourselves on putting our clients first and helping them achieve their goals and dreams. A big thank you to our clients for their trust and confidence. We look forward to supporting them and future generations as we continue to build and grow our team to help serve our clients for decades to come.

The Forbes Best-in-State Wealth Management Teams award rating algorithm is based on the previous year's industry experience, interviews, compliance records, assets under management, revenue, and other criteria by SHOOK Research, LLC. Investment performance is not a criterion. Self-completed survey was used for rating. This rating is not related to the quality of the investment advice and based solely on the disclosed criteria.[2]

Navigating 2024 with Insight and Discipline

After three days of hurtling through the inky abyss of space, the crew of Apollo 8 entered lunar orbit for the first time in history. As they rounded the dark side of the moon, they saw earth rise on the horizon, a bright and beautiful blue and green orb.

"I began to think that, you know, we often say that I hope to go to heaven when we die. In reality, we go to heaven when we're born."

— Jim Lovell, Astronaut, Apollo 8[3]

Happy New Year! As we step into 2024, we're here with the annual newsletter to reflect on 2023 and provide insights into the geopolitical landscape, market trends, and key issues that we feel could potentially shape the year ahead. In this edition, we will revisit 2023's key events, touch again on Artificial Intelligence, the US's Hegemonic role and discuss what could define 2024 markets.

2023 in Review

- Interest rates increased - in theory making the economy less favorable as borrowing and operating become more costly.
- Global conflicts persisted, notably in Ukraine and Israel/Gaza.
- Along with smaller conflicts like Azerbaijan/Armenia.
- We were "on the brink of recession" the entire year - first predicted to start Q3 2022.
- Three major regional banks failed in the early part of the year creating fear of a contagion in the banking /financial industry, which was brought on by the quick spike in interest rates.
- Q3 earnings were down for the 4th straight quarter (Q4 has not been reported yet.)

So, why did the market go up? (and a lot!)

- Inflation came down by one-half in 2023 and two-thirds from the 2022 peak, the fastest retreat since the Korean War - meaning price increases slowed. Some dropped significantly, like lumber prices, while others like rents remained stubbornly high.
- Corporate earnings, though varied, often outperformed expectations.
- AI optimism propelled to historic highs, what the press has termed "the Magnificent 7," far outpacing the general market.
- Labor shortages boosted wages for many while savings from the Covid lockdowns allowed people to continue to spend, creating healthier spending than had been forecast.
- The Federal Reserve hinted at potential interest rate cuts in 2024.

AI optimism

In our 2023 mid-year newsletter, we discussed AI and also hosted an AI webinar with Wells Fargo Investment Institute's Global Security Research Group. Many people are still concerned that AI will eventually take over and replace humans. We continue to believe this kind of AI remains in the distant future, if ever. Think about the example of the driverless car—they have driven millions of miles to learn how to drive and they are still not ready yet, as a major company recently withdrew their vehicles from the streets of SF. Compare that to a 16-year-old, who learns much quicker. The human brain is very efficient and takes about 20 watts of power to operate. In contrast, a computer doing similar tasks takes many kilowatts of power to do the same calculation. That should improve, but the technology still has a ways to go.

Instead of fearing this developing technology, AI could potentially be a powerful force for good, helping industries improve their efficiency and profitability. Companies from all industries are working to get their hands on AI technology to learn how it can help their business. A few examples:

1) A major US tech company has been working on a generative AI model for nuclear regulatory and licensing processes for the last six months. The company hopes to speed up the long and costly process, which could hinder the proposed small modular reactor (SMR) nuclear developments in the US. As we continue to need more energy, nuclear could provide a clean source in the future.
2) Artificial Intelligence in biotechnology can speed up drug discovery, deliver analytics, accurately diagnose medical conditions, edit gene structures, and develop personalized medicine, among other potential applications.

Where should I be investing my money in AI?

It's likely too early to tell who the winners will be in the AI sector, but there likely won't be just one. When we look at the Gartner hype cycle, we would guess we are around the peak of inflated expectations. Just like the introduction of the Internet, it took years before there was enough infrastructure built for companies to fully understand the benefits and uses of the Internet as a tool. We will continue to watch this sector closely for any early signs of enlightenment as to where we can invest further into this new technology, keeping in mind that technology-related stocks, especially of smaller, less-seasoned companies, tend to be more volatile than the overall market.[4]

Innovation trigger

This marks the beginning of the hype cycle around the disruptive technology There usually is some sort of technology breakthrough that gets people talking. Start-up companies emerge and investments from private companies increase substantially.

Peak of inflated expectations

At this stage, the technology begins to bring in more suppliers and users. Generally, hype begins to build around the technology and media coverage increases. Still, there is limited proof of the technology achieving expectations.

Trough of disillusionment

The original excitement around the technology starts to wear off. Performance issues emerge and investors typically begin experiencing lower-than-expected returns on investment.

Slope of enlightenment

This is when the tides begin to turn. Early adopters start seeing the benefits of the new technology and new opportunities begin to emerge. The technology becomes more widely understood and accepted, notably as new use cases emerge. Enterprises begin to understand how they can implement the technologies within their own organizations.

Plateau of productivity

Mainstream adoption begins to take hold. Businesses and users alike are realizing more and more real-world benefits of the technology. Broad understanding of the technology is paying off; users are experience productivity and efficiency gains.

Source: Gartner, 2023.

2024 outlook: The jungle returns

As the US pulls away from its dominant hegemonic role, it creates room for rogue states and bad actors to reassert themselves, allowing the "jungle to grow back." We have discussed the issue of historical world leadership several times before, and it still affects what we see happening around the world. The US citizens have grown tired of being the world's police, engaging in long wars, carrying a huge fiscal debt, and losing jobs that went abroad. We keep seeing the US withdraw from its global duties, and the world becomes more dangerous.

People were ready to make sacrifices during the cold war to prevent the spread of communism, but people have grown tired. The current practice of Hegemony has resulted in mistrust, job losses, income disparity, the emergence of populism, and the endorsement of isolationism.

We hope that as factories are built, production and manufacturing return to the US, and good jobs are generated that we create more stability and harmony among our population. A hegemons job is never over. If not the US, someone has to be in the leadership role to enable free trade, preserve a stable currency and stop small wars from escalating into large ones.

What we think/worry about this year?

<u>Elections at home and abroad</u>

- Taiwan - will the new president lean towards independence or China?
- Mexico - so close to the US and policies obviously effect the US, drugs and the cartels, immigration, etc. Very important to work well with both Mexico and Canada.
- USA - We said three years ago that we would not have the same two candidates running again for many reasons, but mostly age. And here we are.... Who will be our next leader? It may not be either of the two that ran last time.

<u>Conflicts - so many hotspots challenge US capacity</u>

- The Ukraine war rages on, but you see very little in the media currently. We are afraid that if Ukraine loses support and capitulates, that it may embolden Russia to try and take more land. It also may embolden China.
- China- we see both positives and negatives here.
  - It seems like Xi Jinping, on his last trip to the US, ratcheted down diplomatic and economic tensions as shown by his administration finally approving the VMware/Broadcom merger that they had been holding up. China may be looking to put a floor on trade and investment flows as commerce leaves China and their internal economics deteriorate.
  - Of course, this comes with a "but." China continues to build its military to engage in saber-rattling at sea, and to talk boldly about Taiwan.
- And as we write this letter, the Houthi rebels are continuing to attack commercial ships, disrupting free trade and the movement of goods. Recently the US and UK, after several warnings, have conducted air strikes against the Iran backed Houthis in Yemen in an attempt to send a message.

The unknown factor

- What may blindside us in 2024.

Investing in 2024

- We have not seen 5% yields in over 15 years. For those who need fixed income in portfolios, it may benefit securing these for a longer period. It is expected that the Fed will eventually reduce rates, but perhaps not as soon as this spring. The long treasury market has already responded to this with the 10-year yield dropping from a recent high of 5% down to 4%.[5]
- We would foresee risk assets, such as stocks and bonds, to be more volatile, but predict they will remain beneficial long term.
- As you know, we don't predict markets and continue to favor high quality dividend paying stocks for the core of portfolios.
- If you prefer a less volatile portfolio, look at locking in a laddered portfolio of bonds with maturities ranging from 1 to 10 years.

In 2024, we remain dedicated to guiding you through these dynamic times with the insight and consistency you've come to expect from us. Thank you for your continued partnership and trust. We look forward to seeing you for your annual reviews shortly!

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Dividends are subject to elimination and are not guaranteed.
Investing in fixed income securities involves certain risks such as market risk if sold prior to maturity and credit risk especially if investing in high yield bonds, which have lower ratings and are subject to greater volatility. All fixed income investments may be worth less than original cost upon redemption or maturity.

Description of Indexes

An index is unmanaged and not available for direct investment.
S&P 500 Index - a market capitalization-weighted index, composed of 500 widely held common stocks, including reinvestment of dividends, that is generally considered representative of the US stock market.
S&P 500 Equal Weighted Index is the equal-weight version of the widely regarded S&P 500. The index has the same constituents as the capitalization weighted S&P 500, but each company in the S&P 500 EWI is allocated a fixed weight.
Russell 1000 Growth Index - offers investors access to the large-cap growth segment of the US equity universe. The index is constructed to provide a comprehensive and unbiased barometer of the large-cap growth market. Based on ongoing empirical research of investment manager behavior, the methodology used to determine growth probability approximates the aggregate large-cap growth managers' opportunity set.
Russell 1000 Value Index - measures the performance of those Russel 1000 companies with lower price-to-book ratios and lower forecasted growth values. These stocks are selected from the 1000 largest companies in the Russell 3000 Index.
MSCI EAFE Index - the MSCI EAFE Index is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the US and Canada.
Russell 2000 Value Index - measures the performance of those Russell 2000 companies with lower price-to-book ratios and lower forecasted growth values.
Barclays U.S. Aggregate Bond Index - an index comprised of approximately 6000 publicly traded bonds, including U.S. Government, mortgage-backed, corporate, and Yankee bonds with an approximate average maturity of 10 years.