

January 2, 2024

*“To be prepared is half the victory”  
-Miguel De Cervantes*

Perhaps the most significant investment theme in 2023 was the fight to curtail inflation. The Fed successfully balanced lowering inflation while also avoiding a recession. Bonds prices declined, yields rose, and stock indices advanced. Looking forward into 2024 we worry that investor consensus is overestimating the aggressiveness with which the Fed will lower rates in the face of resilient economic growth and that without broader market participation the indices will struggle to advance.

Entering 2023, most strategists forecasted that the stock market decline of 2022 would persist. Our expectation was that the Federal Reserve’s tightening cycle would conclude, and the market would likely end the year higher. We were mostly correct, but we did not foresee the market advance being so narrow. Specifically, seven stocks representing 30% of the S&P 500 market capitalization advanced 75%, while the remaining 493 stocks in the index were up on average 12%. The valuation of the “Magnificent 7” is much higher than the S&P 500, with the group commanding a P/E of 47x and enterprise value to cash flow of 30x versus the S&P 500’s P/E of 21x and EV/EBITDA of 14x. We think that for the stock market to advance in 2024, broader participation of stocks with attractive valuations must occur.

Our investment strategy focuses on owning quality companies generating free cash flow that management deploys in shareholder friendly activities. We believe the lopsided performance of a few stocks in 2023 creates opportunities for stock pickers in 2024. Earnings estimates for the companies comprising the S&P 500 is projected to grow 13% compared to flat earnings in 2023. We will monitor economic data carefully as any slowing in the GDP will impact when the Federal Reserve may begin lowering rates. Longer term, we think the bond yield curve will steepen as investors demand higher returns for longer time horizons, and as the Federal deficit continue to rise. Perhaps the most positive long-term development we can wish to see is the emergence of a consensus among our political leaders aimed at addressing the federal deficit that now exceeds \$34 trillion. That would be a holiday miracle!

We wish you much happiness in 2024 and we are truly grateful for our relationship with each of you.

Sincerely,

JM Sam Nevin, Jr  
Managing Partner

W. Joseph Ryan III  
Partner

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