Decatur Capital Management Inc.

Decatur View – Thorns and Roses for 2023 and the Outlook for 2024

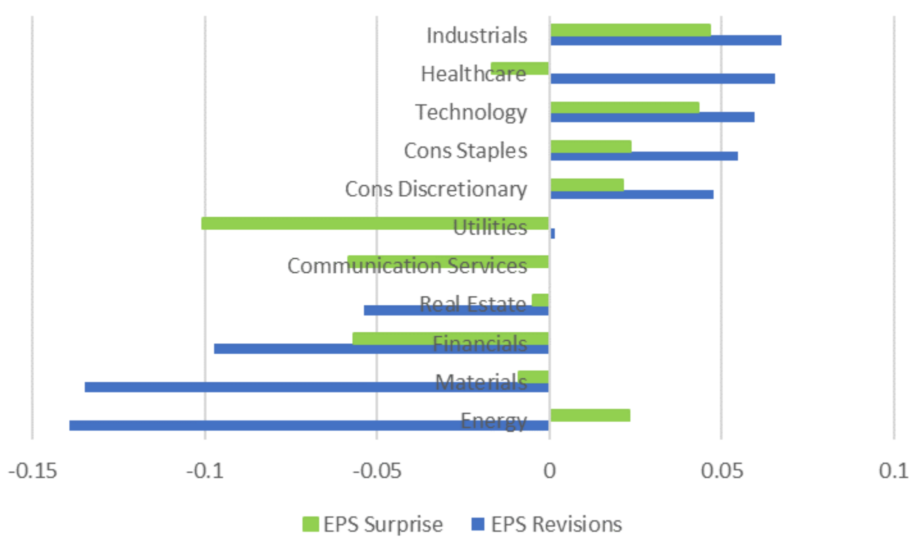
The fourth quarter was positive for equity markets with the S&P 500 gaining a whopping 11.7% for the quarter. This brings the year to date, through December 2023, to 26.3%.

How did our four drivers impact 2023? The drivers, in order of significance, were: 1) earnings expectations 2) the Federal Reserve controlling inflation, 3) continuing strain on banks, and 4) global threats. As we look back, we will assign a 'thorn' if our forecast did not hit the mark and a 'rose' if our forecast was on target.

Expectations - Rose

Earnings and sales expectations continue to forecast positive announcement surprises. In 2023, analysts' were increasing their earnings estimates (blue line) in the technology sector and this sector experienced a positive earnings surprise (green line) relative to the universe of stocks. We underweighted our exposure to materials and the sector experienced negative relative eps surprise.

Chart 1: EPS Revisions and EPS Surprises



Source: Decatur Capital Management, Zacks Investment Research

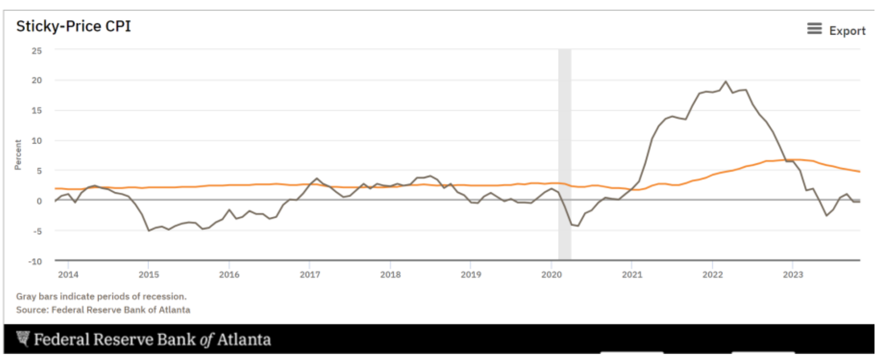
We participated in the upside of the market, but we could have increased our 'risk-on' bet by increasing our technology stocks and reducing our exposure to higher valuation firms such as healthcare stocks. The healthcare sector disappointed with the average healthcare stock experiencing a lower than anticipated surprise.

The Federal Reserve and Inflation - Rose

We were right that the Federal Reserve (Fed) would remain resolute in controlling inflation. Inflation is declining and the market reaction is a soft landing as we finished 2023.

Chart 2 shows the two aspects of inflation, the sticky and flexible Consumer Price Index. The orange line represents the sticky price CPI, which as the name implies, is hard to get rid of and sticks around, such as rents and medical care. The grey line represents the flexible CPI. The flexible CPI includes those costs that may rocket up as inflation builds but are more easily controlled by the Fed, such as hotel rooms costs, entertainment tickets and eating out.

Chart 2: Sticky and Flexible Price CPI 12 month Rolling



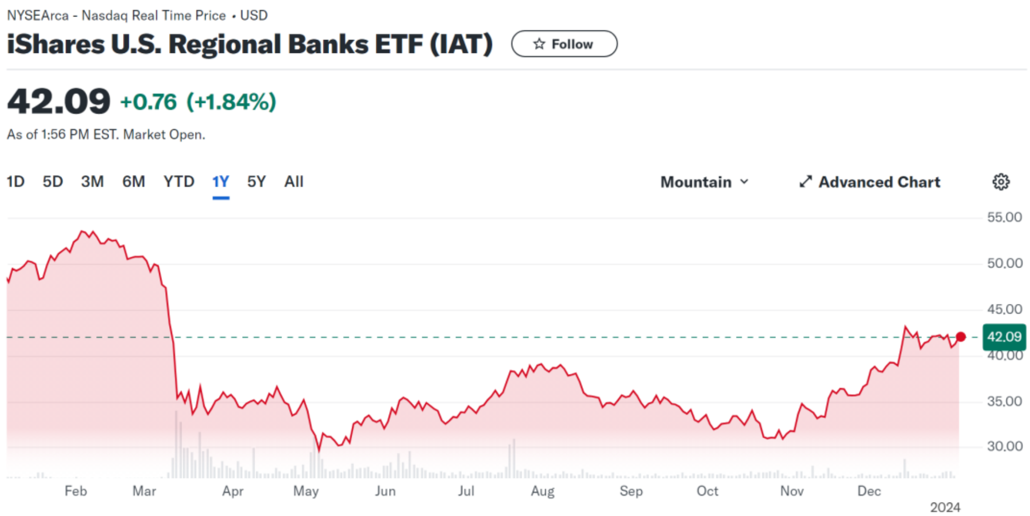
The Federal Reserve increased the Fed Funds rate a historic eleven times in 2022 and 2023 to bring inflation down and now they are evaluating the impact by pausing the last few meetings. The equity markets surged during fourth quarter based on inflation declining to the point that the Fed did not have to increase rates higher.

Credit Contraction – Banks - Thorn

We missed the regional bank rally in fourth quarter. We reduced our exposure to regional banks during 2023, only to see them surge back during the fourth quarter.

The year of 2023 experienced the closing of several regional banks; however, by fourth quarter, the regional banks segment had recovered. We forecasted that banks would continue to suffer with challenges from declining deposits, underwater debt portfolios, and defaulting commercial office building loans. Well, all of the gloom and doom we anticipated did not occur and the regional banks' stock prices are recovering. In the fourth quarter, our underweight to regional banks resulted in missing the rally.

Chart 3: Regional Bank Performance



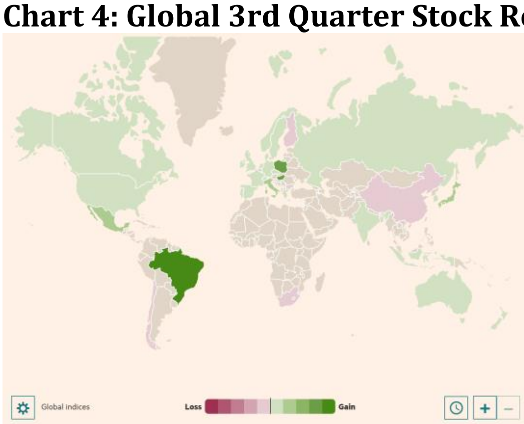
Source: Yahoo Finance

Global Threats - Rose

We correctly forecasted that the global threats would not be factor in global capital markets. We maintained our 'risk on' approach to our global portfolios.

At the beginning of the year, we were concerned with the Russia-Ukraine War and China's impact on global markets. The Russia-Ukraine War has moved into a stalemate with no immediate resolution at hand. In addition, China and the U.S. have toned done the saber rattling. The Israel-Hamas War has had minimal impact on capital markets

Chart 4: Global 3rd Quarter Stock Return Map



https://markets.ft.com/data/world

Chart 4 shows the relative global performance during the year. As world economies fight inflation, most major markets were positive except for China. India is benefiting from manufacturing opportunities as companies search for alternate manufacturing facilities outside of China. In our All Country World excluding the U.S., our overweight to Latin America, Canada, and India was rewarded with positive performance.

Three roses and one thorn, we will refocus our efforts to improve! We will continue to stay true to our investment discipline.

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