Market Flash Report

December 2024

Key Takeaways

- US Dominance: The S&P 500's modest -2.4% monthly decline in December masks a significant divergence from global markets, as US equities continued to outperform international peers across market caps and styles. While developed international markets fell -2.3% for the month, their quarterly decline of -8.1% highlights the sustained strength of US market but also the strength of the US dollar.
- Growth Leadership: Large Cap Growth stocks demonstrated remarkable resilience with a 0.9% monthly return for December and 7.1% gain for Q4, dramatically outperforming Value's -6.8% monthly and -2.0% quarterly declines. This performance gap underscores the ongoing market preference for strong growth prospects as rates stay high.
- Small Cap Struggle: Small cap stocks faced significant headwinds with a sharp -8.3% monthly decline, though managing a slight 0.3% quarterly gain, highlighting the challenging environment for smaller companies. Investors are conflicted and thought we would see a more significant rotation into small caps as rates were cut. Policy uncertainty caused the long-end of the yield curve to rise, cutting expectations for these firms.
- Fixed Income Pressure: The fixed income market reflected ongoing rate uncertainty, with long-term Treasury bonds declining -6.4% in December and -9.7% for the quarter, as the 10y Treasury yield moved from 3.9-4.6% during the quarter. Bond returns for the year were more muted than expected given the high starting point for yields and the 10y Treasury yield will start 2025 higher than at the start of 2024.

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Index Performance (as of 12/31/2024)

Equity	Q4 2024	One-Year	Three-Year
U.S. Large Cap	2.4%	25.0%	8.9%
U.S. Small Cap	0.3%	11.5%	1.2%
Developed Non-U.S.	-8.1%	4.3%	2.2%
Emerging Markets	-7.8%	8.1%	-1.5%
Real Assets			
Real Estate	-8.2%	4.9%	-4.3%
Infrastructure	-5.5%	10.5%	3.0%
Fixed Income			
Core Plus			
U.S. High Yield Debt	0.2%	8.2%	2.9%
Emerging Market Debt	-1.5%	6.6%	-0.5%
Core Bonds			
U.S. Aggregate Bonds	-3.1%	1.3%	-2.4%
U.S. Treasuries	-3.1%	0.6%	-2.9%
U.S. Municipal Bonds	-0.9%	0.9%	0.1%

Month-End Values/Yield	Current	Prior Month	One-Year
CBOE Volatility Index	17.4	13.5	12.5
10-Year Treasury Yield	4.6%	4.2%	3.9%

Sources: Bloomberg, Pathstone, as of 12/31/2024

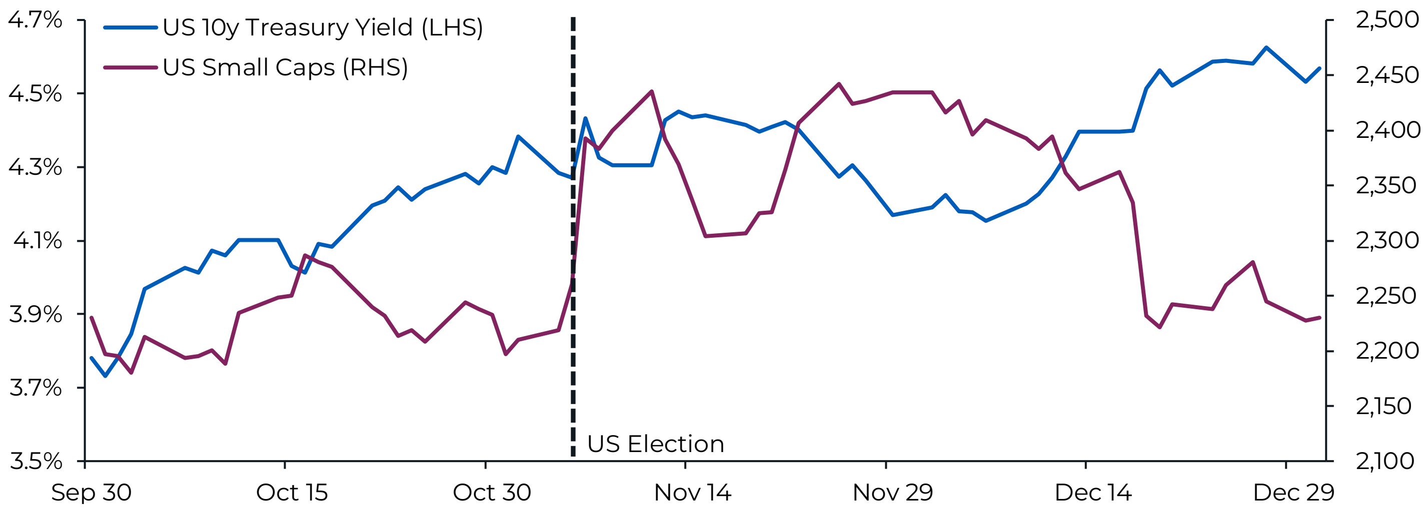
You cannot invest directly in an index; therefore, performance returns do not reflect any management fees. Returns of the indices include the reinvestment of all dividends and income, as reported by the commercial databases involved. Returns over one year have been annualized. Details of all indices reflected are described in the Disclosure page.

Quarterly Commentary

- Labor Market: The US labor market showed remarkable resilience in November, with nonfarm payrolls increasing by 227,000 jobs, exceeding economist expectations of 200,000 and marking a substantial recovery from October's hurricane and strike-affected numbers. This strength was further evidenced by job openings rising to 7.7 million in October, with voluntary quit rates increasing, suggesting workers remain confident in their ability to find new employment. While the unemployment rate edged up slightly to 4.2%, the overall labor market dynamics continue to demonstrate fundamental strength despite higher levels of interest rates.
- Consumer Spending: The American consumer demonstrated exceptional strength during the holiday shopping season, shattering previous spending records across both traditional retail and online channels during the critical Thanksgiving period. This surge in consumer activity, which significantly exceeded expectations across multiple shopping days and categories, suggests that despite some economic headwinds, American shoppers remain confident and willing to spend.
- Inflation: The Consumer Price Index reached 2.7% in November, building on October's uptick and remaining stubbornly above the Federal Reserve's 2% target. Core CPI, which excludes volatile food and energy prices, registered at 3.3% annually, while the Fed's preferred measure, PCE inflation, rose to 2.4% in November. Persistent inflationary pressure coupled with policy uncertainty are influencing the Federal Reserve's approach to monetary policy as we head into 2025.
- Monetary Policy: The Federal Reserve responded to these economic conditions by implementing its third consecutive quarter-point rate cut, bringing the benchmark rate to 4.25-4.5%. However, the central bank's more hawkish messaging regarding future rate cuts has sparked significant market reactions, including a surge in the 10y Treasury yield and the US dollar along with increased equity market volatility. The Fed's cautious stance reflects ongoing concerns about inflation persistence and suggests a more measured approach to monetary easing in 2025 than previously anticipated.
- US Budget: The government debt market is showing signs of stress, with major investment managers like Pimco reducing exposure to long-term US government debt due to sustainability concerns and inflation risks. The 10-year Treasury yield climbed to a high of 4.62% in December, its highest level in over six months, reflecting market participants' adjustment to the Fed's more conservative rate cut projections and broader concerns about fiscal dynamics.
- Looking ahead, the economic landscape presents a complex picture of resilience and risk. While labor market strength and consumer confidence provide a solid foundation, persistent inflation, higher rates, and policy uncertainty suggest potential challenges ahead. The Federal Reserve's more measured approach to rate cuts reflects this delicate balance, emphasizing the need for continued vigilance in navigating the current market environment.

Markets Stumble Near Year-End as Policy Questions Mount

US Small Caps = Russell 2000 Index, 9/30/2024-12/31/2024



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