PAPAMARKOU WELLNER PERKIN

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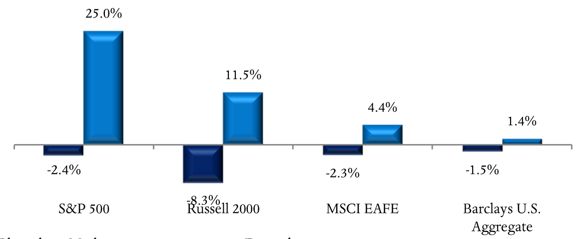
2024 Year-in-Review

2024 was an impressive year for risk-assets. US stocks were broadly higher, with the major equity benchmarks posting double-digit returns, amidst a positive backdrop of strong economic activity, robust corporate earnings growth and easing monetary policy. The S&P 500 index rose +25.0% in 2024, registering its best two-year return (+57.8%) in more than 25 years. The bellwether benchmark was propelled higher from another stellar year by the "Magnificent Seven" technology stocks which rose +67.3%, representing a little over half the index's 2024 return. The top performing sectors were Communication Services (+40.2%), Information Technology (+36.6%), Financials (+30.5%), and Consumer Discretionary (+30.1%). At the other end of the spectrum were Materials (-0.04%), Healthcare (+2.6%), and REITs (+5.2%). Smaller stocks performed well on an absolute basis with the S&P Midcap 400 (+13.9%) and Russell 2000 indices (+11.5%) registering double-digit gains, but underperforming on a relative basis. Overall, large-cap growth (+33.4%) performed meaningfully better than small-cap growth (+15.1%), as well as large-cap value (+14.3%), and small-cap value (+8.0%).

Overseas stocks produced positive results, to varying degrees, in 2024. The large-cap MSCI EAFE developed market equity index rose a modest +4.4%. In Europe, the Stoxx 600 benchmark added a more respectable +9.6%, aided by a recovering economy and lower interest rates, which led to Euro currency depreciation against the US Dollar, to the weakest level in two years. In Asia, Japanese stocks increased a strong +21.3% on the back of corporate reforms and a weaker Yen. The Shanghai composite rallied +18.1%, breaking a multi-year losing streak, aided by government stimulus measures and monetary liquidity injections. Emerging market stocks rose +8.0%, hindered by lackluster returns from Latin America.



Source: Bloomberg Markets

US fixed income markets saw dramatic shifts in Federal Reserve monetary policy and interest rate expectations during 2024. Investors entered the year anticipating seven 25 basis point (bp) rate cuts, but hawkish central bank sentiment through early-May reduced expectations to just one reduction. Then, a mid-year economic softening prompted the Fed to moderate its stance and follow-up with 100bps of cuts across three meetings (September 50bps, November and December 25bps each). Bond yields went on a roller-coaster ride in 2024, with the 10-year U.S. Treasury Note starting off at 3.88%, rocketing higher to 4.73% by April, then falling as low as 3.61% in September, only to finish the year at 4.57%. In the end, the US Aggregate Bond index produced a lackluster annual return of +1.4% (including coupons). To the upside, equity-sensitive high yield bonds produced a solid +8.1% return for the year.

The past year saw dramatic swings in commodity markets. Precious metals reached record highs across multiple currencies, with gold rising +27.2%, reacting to profligate government spending. Energy markets diverged sharply; natural gas surged +65% while WTI crude oil declined -3%. Economically sensitive commodities were affected by weak Chinese demand, offset by AI and green energy initiatives. Agricultural commodities saw some remarkable gains, driven by arid conditions. Coffee jumped +80% and cocoa topped the sector with a +160% increase. Overall, the S&P GSCI Commodity index rose +9.2% in 2024.

Geopolitics

2024 marked an unprecedented year of political transformation, with national elections across more than 60 countries, encompassing nearly half the world's population. Major democracies including India, France, and the UK underwent leadership transitions, while the US saw shifting candidates, legal challenges, and even assassination attempts on the road to a Trump presidential victory and Republican sweep of Congress. Sovereign and corporate leaders increased their understanding and governance of generative AI and other key technologies in an effort to gain competitive advantage. Global climate change seemingly intensified with floods, earthquakes, fires, and extreme weather wreaking havoc and leaving indelible marks on communities worldwide. Though the world managed to gather for the Paris Olympic Games, in celebration of peace and unity, geopolitical tensions persisted through ongoing conflicts in Ukraine and the Middle East, including the collapse of the Assad regime in Syria.

United States

The US economy was resilient in 2024, producing strong GDP growth (2.7% est.), still-low unemployment (4.2%), increased consumer spending (+3.7%), and decelerating inflation (core-PCE +2.8%). In defiance of the skeptics, the recession fears that lingered from the prior year's interest rate hiking cycle (+525bps) proved to be unfounded. While inflation has yet to reach the Federal Reserve's 2% threshold, its declining trend provided the FOMC enough cover to pivot from its restrictive policy, with three rate cuts totaling 100bps. Looking ahead, while the monetary liquidity and fiscal austerity prospects are hazy, the US is attempting to re-industrialize. The necessary reshoring will necessitate a reshaping of domestic manufacturing and industry, driving shifts in global supply chains, as well as advances in automation and AI.

Europe

Following a prolonged and broad-based stagnation, the EU economy resumed growth in 2024 (GDP 0.8%) amidst abating inflationary pressures (CPI 2.4%), conditions that appear set to follow-through in 2025. Overall, economic growth in the EU is expected to pick up to 1.5% in the coming year and accelerate thereafter, as consumption and investment are set to rebound from 2024's contraction. These conditions were sufficient for the European Central Bank to cut its policy rate four times, to 3.0%. Economists forecast the union's neutral rate, which neither fuels nor cools growth, to be between 2.0% and 2.5%, which may be achieved later this year. Recent political uncertainties in France and Germany are a brewing concern which may take months to settle and produce economic headwinds.

December 2024 Economic Statistics

	Dec-24	Dec-23	Dec-22
Federal Funds Target Rate	*4.25 - 4.50%*	*5.25 - 5.50%*	*4.25 - 4.50%*
Consumer Confidence Index	*104.7*	*110.7*	*108.3*
Manufacturing PMI Index	*49.3%*	*47.4%*	*48.4%*
Unemployment Rate	*4.2%*	*3.7%*	*3.5%*
JPY/USD	*157.18*	*141.06*	*131.11*
USD/EUR	*1.0353*	*1.1036*	*1.0702*
Gold/oz.	*$2,623.81*	*$2,062.59*	*$1,824.40*
Oil (WTI)/bbl	*$71.72*	*$71.65*	*$80.26*

Sources: see disclosure *

Asia

China's growth and inflation outlook continued to deteriorate over the past year, despite a number of economic stimulus measures announced by President Xi Jinping's government, designed to support consumption, overleveraged local governments and the ailing real estate market. Investor concern of potential deflation is seen in the country's $11 trillion sovereign bond market, where 10-year yields (1.7% at year-end) tumbled to all-time lows. This plunge underscores growing concern that policymakers are unwilling to take the necessary measures to prevent an economic malaise. Financial markets are focused on China given that it contributes approximately 30% to global growth.

Japan's economy exited 2024 on solid footing. Key positive factors include rising wages (large companies agreed to a 5.1% increase) and controlled inflation of approximately 2% (which led the central bank to raise interest rates for the first time since 2007). Continued private consumption and corporate investment are expected to drive economic growth up to 1.5% in the coming year, supported by a tight labor market with 2.5% unemployment. However, two significant risks loom: domestic political uncertainty under Prime Minister Ishiba's minority government facing a summer Upper House election, and a consistently weakening Yen which may trigger tariffs as part of America's new trade policies.

Outlook

Markets are preparing for potentially transformative policy shifts under the incoming Trump administration. The bullish investment case rests on four core elements: strategic trade tariffs, particularly targeting China, to bolster US competitiveness, immigration controls to maintain labor market strength, regulatory rollbacks to stimulate lending and investment, and spending cuts to improve fiscal efficiency. While early executive actions on trade and immigration are likely, broader fiscal reforms may take longer to implement, and regulatory changes likely require significant debate to yield tangible results. Further, investors are eager for greater clarity pertaining to the strategic outcomes of the Russia/Ukraine war and armed conflicts in the Middle East.

Strategists are forecasting US GDP will grow at an above-trend level of 2.1% in 2025. However, given the vast amounts of prior excessive fiscal spending, which now must be curtailed, some prudence is warranted. Side-effects of elevated federal debt include higher longer-term sovereign interest rates and knock-on effects in the credit and mortgage markets (the average 30-year fixed mortgage rate has risen above 7%). Further, with interest rates above that of the rest of the G7, the US Dollar Index has risen to two-year highs. This also amounts to a foreign exchange headwind for multi-national corporations. When combined with the planned fiscal austerity by the Department of Government Efficiency, elevated interest rates and a strong US Dollar could lead to lower than expected economic activity, both domestically and abroad.

Meanwhile, corporate earnings remain strong and are set to accelerate, with the S&P 500 expected to produce fourth quarter earnings growth of 11.9% (the best quarter since Q4 2021), leading to full-year 2024 growth of 9.4%, on revenue growth of 5.1%. Thereafter, the index's 2025 profits are expected to grow by a robust 14.8% on revenue growth of 5.8%. While the S&P 500 index is highly concentrated in high-growth, highly-valued, technology companies, the majority of the remaining constituents are attractively valued, offering compelling prospects for long term investors. Further, international stocks trade at historically large discounts to their US counterparts and offer solid value. Thus, we remain cautiously optimistic.

The Federal Reserve's focus has shifted toward evenly balancing inflation and labor concerns, while acknowledging potential economic impacts of the incoming Republican administration. The Fed's revised projections call for higher 2025 core-PCE inflation and reduced rate cut expectations (from four to two 25bp moves) reflecting a more hawkish outlook. The longer-end of the yield curve has shifted higher, but in our opinion still does not offer sufficiently attractive inflation-adjusted returns to investors. In lieu, we recommend short-dated risk-free bonds as well as higher-yielding credits.

Augmenting our long-bias towards quality equities, we continue to favor select hedge funds and non-market correlated investments which serve to dampen volatility of traditional portfolios. In addition, our research indicates that precious metal miner investments, which have trailed the appreciation of gold and silver bullion, offer attractive potential with reduced correlation to equities. For capital appreciation oriented investors, select software equities, with an activist element, appear to be timely investments. We have also identified innovative private equity funds attempting to disrupt the education and healthcare industries.

We wish you all a Happy, Healthy and Prosperous New Year and thank you for your continued trust and support.

*Sources: Reuters, Bloomberg, Bureau of Labor Statistics, Conference Board, Federal Reserve, Institute for Supply Management, MSCI, Russell, Standard & Poor's, Financial Times and the Wall Street Journal.