Making Sense of Finance

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Fourth Quarter 2024 Review

STOCK MARKET

Markets in the US rose in the fourth quarter with another positive return by the S&P 500 index. Although December returns were in the red, the S& P 500 index closed out the quarter and year with gains of over 2% and 23%, respectively. The last time the index had two back-to-back years of 20% plus returns was in 1998. (In contrast an equal weighted, not market cap weighted, S&P 500 index had a significantly smaller return of 11% in 2024). The Federal Reserve continued to slash interest rates as the Fed Fund rate was reduced by 25 basis points twice last quarter. However, the December sell-off in stocks was due in large part to indications that future rate cuts won't be as numerous as previously expected due to the stickiness of inflation. The tech laden Nasdaq returned to its leading performer position in the fourth quarter with an increase of 6% and finished the year with a gain of 28%, while the Dow lagged in performance with a less than 1% gain in the fourth quarter and a solid but a comparably lesser increase of 13% for 2024. Given an economy that has proved resilient as denoted by US GDP growth of 3.1% in the most recent quarter for which we have data, many companies were able to realize strong cash flows, and record profits and net profit margins. A part of this cash generated was used by numerous companies to buy back stock in 2024. Last year set a record for the highest dollar amount of buybacks ever in the U.S. Stock buybacks lead to a support for higher stock prices in the short term and are a form of companies returning capital to shareholders as is also done with dividends.

Large cap stocks regained their dominance again in the fourth quarter, beating the smaller companies that had outperformed in the third quarter. Consumer discretionary, technology, communication services and financial stocks were among the best performing sectors last quarter as they were for the year. These sectors were the only positive stock categories in the fourth quarter. The worst performing stock sectors among the losers in the fourth quarter were materials and healthcare. Although these two stock categories had positive returns in 2024, they had the smallest gains. The large weightings of a very small number of stocks have

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Everyone and their neighbor has an opinion. At Karagosian Financial Services, we have a combined 40 plus years of investment experience. We have seen the markets at their highest highs and lowest lows. Through this newsletter we attempt to convey our opinions on current events in the investment world and their likely outcomes. Forecasting is inherently difficult and our advice is geared toward making sensible and prudent choices based on logic and experience, and not based on emotion.

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driven the stock market performance over this past year. For the second consecutive year, less than 30% of stocks outperformed the index, which is below the average of 49% since the year 2000.

Foreign stock markets' performances trailed the US stock market last quarter, as measured by the MSCI EAFE Index of developed countries. In US dollar terms, that index reported a loss of over 8% as the strength in the US dollar compounded the slight index loss measured in local currencies. European stock markets were weak partially due to political instability in Germany and France and the overall weakness in the economies in Europe. Although posting a loss for the quarter, the index was still positive for the year. The Japanese market was positive in yen terms in the fourth quarter and the Japanese Nikkei Index closed out 2024 with its highest year end finish since 1989! The strong dollar also took its toll on emerging market stocks. The MSCI Emerging Market Index measured in US dollar terms declined by over 8% last quarter while up slightly for the year. Tariff concerns may be partially the issue, causing steep declines in the Chinese market last quarter. South Korean stocks were also affected by their country's political instability. Taiwan's stock market was one of the few emerging markets posting positive returns in the fourth quarter.

BOND MARKET

Despite the two previously mentioned Fed Fund rate cuts in the fourth quarter, bond prices in general declined (yields rose) over the last three months. The Bloomberg US Aggregate Bond Index, which is a measure of intermediate term investment grade corporate bonds, lost over 3% last quarter and had a total return of only 1% in 2024. A reasonable assumption by many is that bonds should have performed well given the Fed rate cuts. However, not all bonds perform alike. Longer term rates are set in the global bond market. The Fed Fund rate has an effect on ultra short-term fixed income items such as money market rates and short-term Treasury bills. Intermediate and long-term bond yields actually rose in the fourth quarter as noted by a 2 Year Treasury yield rising from 3.66% to start the quarter and ending the year at 4.25%. The same can be said for the 10 Year Treasury yield in that same time period rising from 3.81% to 4.58%. The 10 Year Treasury yield has a bearing on mortgage rates which have risen approximately a full percentage point in the last quarter. It is more "normal" to have a steepening yield curve, meaning investors require higher rates of return on holding longer term instruments. Some reasons these yields may be driven higher are the expectations of future inflation, a stronger economy, increased government debt and monetary policy.

High yield lower grade bonds were the only bond sector with a positive return last quarter, and they outperformed investment grade bonds all year. Credit spreads tightened to historical lows due to strong demand for any bonds paying higher rates, even if credit quality was questionable as investors believe in the continuation of a solid domestic economy. Shorter term bonds overall performed better than longer term bonds.

OUTLOOK

We are optimistic about the domestic economy over the next year, however, with the Trump Administration, results may be very choppy. The financial markets react poorly to and often excessively to unexpected announcements, something the new President is known for.

The equity markets do seem a bit frothier than historically, with price to earnings ratios being in the mid- 20s, versus about 15x over the long haul, still valuations have little to do with the future direction of the markets near term.

We advise staying the course, given that forecasts are mostly unreliable. Some general trends in certain industries will likely continue, such as bricks and mortar retail facing continued headwinds and large tech companies pushing equity indexes higher.

A key issue that may have helped Trump win the Presidency is the relatively soft consumer confidence levels despite, solid macro-economic data A boost in this area could lead to overall greater consumption and thus more robust GDP growth. Suffice it to say, the Fed and the new administration have many levers they can pull to keep the economy humming.