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Investment and Financial Consultants

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2024 ECONOMIC AND FINANCIAL MARKETS REVIEW

The stock market performed very well during 2024, as political and geopolitical concerns took a back seat to positive news about the economy, corporate earnings, and lower interest rates. The economy was generally stronger than expected, with the job market remaining relatively resilient and gross domestic product growing faster than many economists anticipated. Corporate earnings mostly exceeded expectations, as U.S. companies continued to make more money despite uncertainty regarding the economy throughout the year. In September, the Fed began lowering interest rates, which is positive for stocks because it reduces the cost of borrowing for consumers and corporations, and it also makes equities look more competitive versus fixed-income investments. As a result, the S&P 500 Index ended 2024 up 23.31%, while the Dow Jones Industrial Average gained 12.88% last year. Bonds did not fare as well as stocks, as the Bloomberg Intermediate U.S. Government/Credit Bond Index increased by only 3.00% during 2024.

One of the main reasons the stock market performed so well in 2024 was the expectation that the Federal Reserve Board would finally embark on a path of interest rate reductions. The Fed began raising interest rates in 2022 to help reduce inflation. Now that inflation has come down closer to the Fed's target, the Fed has felt comfortable enough to begin lowering interest rates. This helps provide relief to borrowers and thereby facilitates economic growth. However, much of 2024's stock market gains were already pricing in these interest rate cuts, and the key going forward in 2025 might be how frequently and how much the Fed continues to lower interest rates. If inflation does not decline further, the Fed may be more hesitant to continue to lower rates, which would be a negative for stocks.

Although elections typically do not have a long-term impact on the financial markets, a couple of positive things occurred after last year's election. Stock prices rose immediately after the election because investors dislike uncertainty, and going from an unknown to a known outcome provided a sense of relief. Additionally, stock prices, which are based on corporate profits, generally rose based on the prospect of lower taxes and fewer regulations under a Republican Congress and White House.

However, despite some reasons for being optimistic about the markets going forward, it would be unusual to see the gains of recent years continue into the future at a similar pace. Although plenty of stocks have not excelled, the major stock market indexes have performed well in five of the last six years. Therefore, it would not be surprising if stocks experienced more downside volatility this year than in recent years. This is particularly true because market valuations are now relatively high, historically speaking. It will take even better earnings growth this year to support such high stock prices. Also, it remains to be seen what new policies will come to fruition under the new administration, but the potential imposition of tariffs on foreign countries could lead to an increase in inflation in the United States if other economic policies do not offset it. That would create a potential headwind for stocks in 2025.

There are three different types of stock market declines that can occur. The mildest is a brief pullback where the market drops up to 10%. These pullbacks are often short-lived and healthy as they cool

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down an overheated market. The second type is a correction where the market drops 10-20%. Corrections typically last a bit longer than the more frequent pullbacks. The third type of decline is a bear market. Bear markets are declines of over 20% and they can come in short-term “cyclical” cycles or longer-term “secular” cycles, the latter of which can last up to several years. We do not believe that a secular bear market will begin this year. Even if a stock market decline does occur at some point this year, it would hopefully be relatively mild since it would likely come against the backdrop of lower interest rates that would theoretically blunt any such market declines.

Last year, we generally kept our investment philosophy simple by overweighting large-company U.S. stocks and short-term bonds while investing very little in small-company stocks, foreign stocks, emerging markets stocks, and other volatile asset classes. Investing in more volatile parts of the financial markets has not made much sense when the performance of large-company U.S. stocks has generally been more profitable and at relatively lower risk. However, we may look to expand into additional asset classes, such as small company stocks or commodities, if the opportunity presents itself.

As always, we will continue to monitor ongoing economic and financial market conditions. In the meantime, please contact us if you have any questions regarding your portfolio or the financial markets in general.

** Index returns were obtained from the Wall St. Journal and Bloomberg on January 1, 2025.*

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