MONTHLY MARKET REVIEW

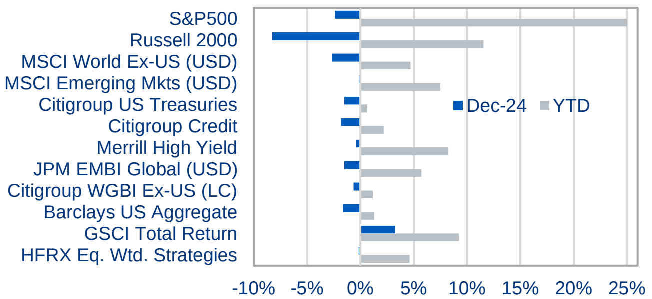
12 2024

Global Market Review

The U.S. equity market gave up some of its earlier strong gains in December holding the return for the year to a mere 25%. Non-U.S. advanced and emerging equity markets also declined in December but rose in 2024, albeit less extravagantly. The Fed's decision to cut its policy rate by 25 basis points in December was widely anticipated, but the hawkish tone of its forward guidance was not, contributing to a steepening U.S. Treasury yield curve and increased policy uncertainty. The prospect that expansionary fiscal policies under the new administration might be met by tighter Fed policy fueled the increase in longer-term yields. This constellation of policies, combined with expectations for an increase in tariffs, also contributed to an appreciation of the U.S. dollar against most major currencies. Oil prices rebounded in December but remained marginally lower for the year. Gold and Bitcoin prices fell in December but were up sharply in 2024 and remained near record highs.

Performance of Major Market Indices

Sources: S&P, MSCI, FTSE Russell, Barclays, Citigroup, Bank of America Merrill Lynch, J.P. Morgan, HFR, Bloomberg.



Despite December's decline, U.S. stocks soared in 2024.

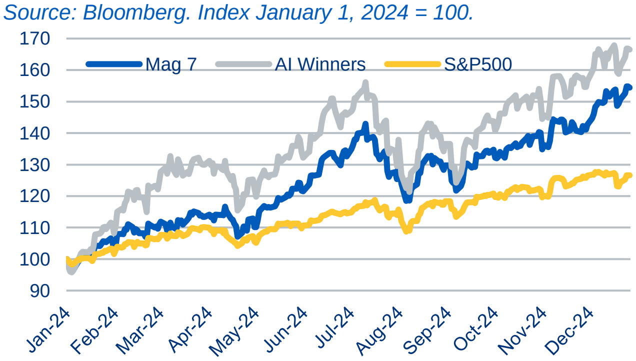
Stellar Year for U.S. Stocks Despite December Decline

December's 2% decline dealt but a glancing blow to an AI-powered U.S. equity market rally that sent the S&P 500 index 25% higher in 2024. December's decline was centered on the value and small cap segments of the market, which fell 6.9% and 8.3%, respectively. For the year as a whole, however, all market segments and sectors generated strong gains, with growth stocks (+32.5%) outpacing value (+14.0%), and large cap stocks (+24.5%) beating small (+11.5%). Across sectors, tech and telecom stocks led the pack by a wide margin, rising 35.7% and 37.7%, respectively.

This pattern of performance reflects hopes that AI will become a transformative technology whose widespread adoption yields a productivity renaissance. An index of 45 stocks judged likely to prosper in an AI revolution rose by 66% in 2024, while the gains of the Magnificent 7 index were more than double that of the S&P 500 (Exhibit 1). NVIDIA rose by 171%.

Exhibit 1. AI Stocks Leads U.S. Equity Market Higher

Source: Bloomberg. Index January 1, 2024 = 100.



By any measure, the valuation of the U.S. equity market is near record highs. Its forward P/E ratio is in the first decile of historical valuations. The valuation spread of the U.S. market over non-U.S. exchanges is at a record peak. The U.S. equity risk premium relative to real U.S. Treasury yields is low. Given these valuation metrics, the forward return potential of U.S. equities appears limited. High levels of market concentration, policy uncertainty, and geopolitical risk further cloud the outlook. Nevertheless, surveys of investor attitudes as well as portfolio flows point to widespread bullish sentiment. The momentum behind the market rally appears strong, at least for the moment.

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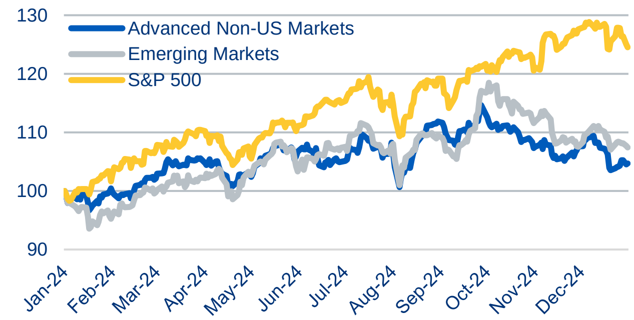
Non-U.S. Equity Markets Continue to Lag the U.S.

The MSCI World ex-U.S. index of advanced economy stocks declined 2.7% in December, bringing its return for the year to 4.7%, well shy of the U.S. market's 25% return (Exhibit 2). Emerging equity markets fell slightly in December but closed the year up 7.5%. Chinese equities, which had been languishing in the face of an incipient debt deflation, have rebounded sharply since September following the announcement of far-reaching stimulus measures. They gained nearly 20% in 2024.

Exhibit 2. Non-U.S. Equity Markets Lag U.S.

Source: Bloomberg. Index January 1, 2024 = 100.



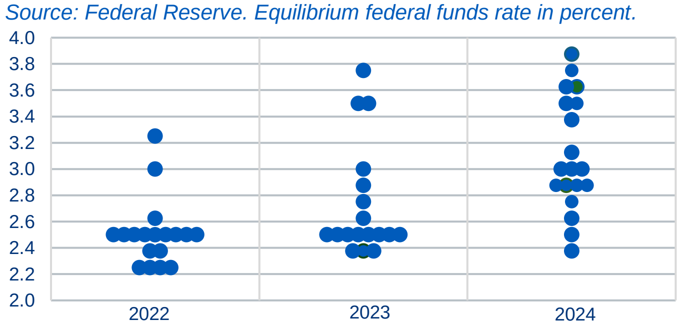
Over the past 10 years, the U.S. equity market has outpaced other advanced economy bourses by a wide margin, generating annual gains of 13% versus 5.2% for non-U.S. advanced markets. Over this period, emerging markets lagged even further behind the U.S., returning 3.7%. Given these trends, U.S. equities represent nearly three-quarters of the MSCI World index and two-thirds of the broader MSCI ACWI Index comprising both advanced and emerging markets.

Fed's Hawkish Forward Guidance Sows Uncertainty

The Fed's decision to cut rates by a further 25 basis points in December was widely anticipated. However, the hawkish tone of its forward guidance was not. The dot plot of each FOMC member's forecast for the long-run equilibrium federal funds rate pointed to a much higher median rate than previous forecasts and increased dispersion in expectations (Exhibit 3).

Exhibit 3. Dot Plot Points to Higher Rates and Uncertainty

Source: Federal Reserve. Equilibrium federal funds rate in percent.



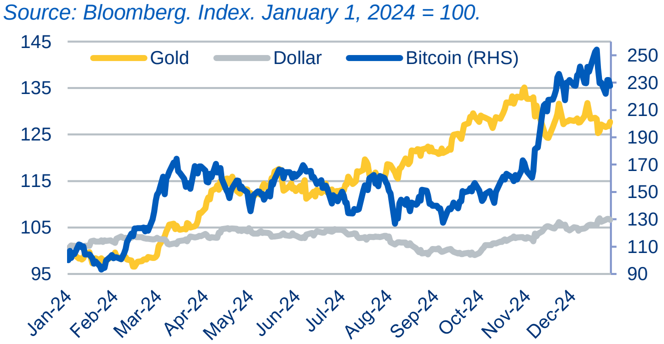
The prospect of a higher equilibrium fed funds rate and increased uncertainty sent longer term U.S. Treasury yields higher in December. The broad U.S. Treasury index fell 1.4% in December and was little changed for the year. The 10+ year maturity segment lost 5.5% in 2024, reflecting the steepening of the yield curve. In the credit markets, investment grade and high yield bonds fell 1.6% and 0.5%, respectively in December but were up 1.4% and 8.4% for the year. Credit spreads remained tight.

Bitcoin Fever Eases but Remains Scalding Hot

Following its 38% gain in November, Bitcoin prices briefly breached $100,000 in mid-December before falling back to $93,687. It rose 220% for the year (Exhibit 4). Speculation that the new administration will actively promote cryptocurrency use was the main catalyst for the latest Bitcoin frenzy. Gold also had a good run in 2024, hitting a record high in November and gaining 26.2% for the year, despite a 1.6% decline in December. Sovereign purchases to diversify central bank reserves, especially by China and Russia, as well as geopolitical concerns were the main drivers of gold's 2024 surge. The gains to Bitcoin and gold came even as the U.S. dollar appreciated against most major currencies. Although Bitcoin and gold grabbed the headlines, the increase in the real effective exchange rate of the dollar (an index of the U.S. dollar versus major trading partners adjusted for inflation differentials) to 30-year highs is the more fundamentally important development. Over the past 10 years, the dollar has had a real appreciation of 24%, while the Chinese RMB had a real depreciation of 12%. A U.S. policy combination of expansionary fiscal policy, contractionary monetary policy, and tariff increases, if it ultimately materializes, is likely to lead to a further appreciation of the dollar, eroding the competitiveness of U.S. exports and contributing to a widening current account deficit. China's export-led growth policy and depreciating currency will only exacerbate these trends.

Exhibit 4. Bitcoin and Gold Surge Despite Strong Dollar

Source: Bloomberg. Index. January 1, 2024 = 100.



Performance of Major Market Indices through 12-31-2024

Sources: MSCI, FTSE, Barclays, Citigroup, Bank of America Merrill Lynch, J.P. Morgan, S&P GSCI, HFR, Bloomberg.

	1-Month	QTD	YTD	1-Year	3-Year	5-Year
S&P500	-2.4%	2.4%	25.0%	25.0%	8.9%	14.5%
Russell 2000	-8.3%	0.3%	11.5%	11.5%	1.2%	7.4%
MSCI World Ex-US (USD)	-2.7%	-7.4%	4.7%	4.7%	1.9%	5.1%
MSCI Emerging Mkts (USD)	-0.1%	-8.0%	7.5%	7.5%	-1.9%	1.7%
Citigroup US Treasuries	-1.5%	-3.1%	0.6%	0.6%	-2.8%	-0.7%
Citigroup Credit	-1.8%	-3.0%	2.2%	2.2%	-2.2%	0.3%
Merrill High Yield	-0.4%	0.2%	8.2%	8.2%	2.9%	4.0%
JPM EMBI Global (USD)	-1.5%	-2.1%	5.7%	5.7%	-0.8%	0.3%
Citigroup WGBI Ex-US (LC)	-0.6%	-0.2%	1.2%	1.2%	-3.2%	-1.8%
Barclays US Aggregate	-1.6%	-3.1%	1.3%	1.3%	-2.4%	-0.3%
GSCI Total Return	3.3%	3.8%	9.2%	9.2%	9.6%	7.1%
HFRX Eq. Wtd. Strategies	-0.2%	0.3%	4.6%	4.6%	1.5%	2.6%