HCR WEALTH ADVISORS

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December 31, 2024

4th Quarter Market Monitor

Market Commentary

- The Federal Reserve's decision to cut rates by another 50 basis points was a key event in the quarter, leading to a mixed reaction in the markets. The 10-year U.S. Treasury yield soared by over 75 basis points, indicating resistance from the bond market due to concerns of more persistent inflation and uncertainty around the impact of potential policy changes.

- After another positive quarter for U.S. equity markets and a strong 2024, market concentration has continued to grow and so have the risks associated with it. It has historically been difficult for companies to sustain high levels of growth over the long-term, with less than 10% of companies being able to sustain 20% sales growth for more than five years.[1] Even a small reversion of these "Mag 7" stocks (which accounted for over 50% of the S&P 500's return in 2024[2]) may lead to higher volatility in the future.

- The potential for increased volatility remains against the backdrop of increased concentration and high valuations. Our 2025 Market Outlook, Bridging the Divide, brings to light these market nuances within our three key themes of fragility, durability, and the age of alpha.

Fixed Income

- Fixed income markets broadly struggled during the quarter, despite the Federal Reserve's rate cut. The Bloomberg U.S. Aggregate Bond Index returned -3.1% for the quarter. The resilient economy and concerns about persistent inflation pushed interest rates higher with the 10-year Treasury yield rising 77 bps.

- High yield bonds, however, eked out a modest gain, with the Bloomberg U.S. High Yield Index returning 0.2%. There was modest spread compression as fundamentals remain favorable and the asset class continues to attract demand. Spread remain well below long-term average levels, seemingly pricing in perfection.

Equity

- U.S. equities ended the year with modest positive returns in the fourth quarter despite elevated volatility. The S&P 500 returned 2.4% for the quarter, ending the year 25% higher than it began and the first time since 1998 that the index finished back-to-back years above 20%. Strong performance in the technology, communications, and consumer discretionary sectors helped drive results.

- International developed markets, represented by the MSCI EAFE Index, took a large step back, falling 8.1% amid signs of economic weakness, concerns over potential tariffs, and geopolitical uncertainty. Emerging markets also struggled, with the MSCI Emerging Markets Index returning -8.0%.

Real Assets

- Rising interest rates were a significant headwind for REITs in the fourth quarter. The FTSE Nareit Equity REITs Index returned -8.2%, with industrial and self-storage sectors underperforming due to slowing manufacturing and post-pandemic occupancy issues.

- Commodities were modestly negative, with the Bloomberg Commodity Index returning -0.4%, driven by weakness in metals and agriculture. Concerns over tighter supply and geopolitical tensions in the Middle East drove oil prices higher providing a tailwind for the energy sub-sector.

- **Bloomberg Aggregate Bond Index** covers the U.S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities.
- **Bloomberg US Corporate High Yield Index** covers the universe of fixed rate, non-investment grade debt. Eurobonds and debt issues from countries designated as emerging markets (sovereign rating of Baa1/BBB+/BBB+ and below using the middle of Moody's, S&P, and Fitch) are excluded, but Canadian and global bonds (SEC registered) of issuers in non-EMG countries are included.
- **S&P 500 Index** is a capitalization-weighted index designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.
- **Russell 2000 Index** consists of the 2,000 smallest U.S. companies in the Russell 3000 index.
- **MSCI EAFE Index** is an equity index which captures large and mid-cap representation across Developed Markets countries around the world, excluding the U.S. and Canada. The index covers approximately 85% of the free float-adjusted market capitalization in each country.
- **MSCI Emerging Markets Index** captures large and mid-cap representation across Emerging Markets countries. The index covers approximately 85% of the free-float adjusted market capitalization in each country.
- **Bloomberg Commodity Index** is calculated on an excess return basis and reflects commodity futures price movements. The index rebalances annually weighted 2/3 by trading volume and 1/3 by world production and weight-caps are applied at the commodity, sector and group level for diversification.
- **FTSE Nareit All Equity REITs Index** is a free-float adjusted, market capitalization weighted index of U.S. equity REITs. Constituents of the index include all tax-qualified REITs with more than 50 percent of total assets in qualifying real estate assets other than mortgages secured by real property.
- **iShares Conservative Allocation** seeks to track the investment results of an index composed of a portfolio of underlying equity and fixed income funds intended to represent a conservative target risk allocation strategy.

Material Risks Disclosures

- **Fixed Income securities** are subject to interest rate risks, the risk of default and liquidity risk. U.S. investors exposed to non-U.S. fixed income may also be subject to currency risk and fluctuations.
- **Domestic Equity** can be volatile. The rise or fall in prices take place for a number of reasons including, but not limited to changes to underlying company conditions, sector or industry factors, or other macro events. These may happen quickly and unpredictably.
- **International Equity** can be volatile. The rise or fall in prices take place for a number of reasons including, but not limited to changes to underlying company conditions, sector or industry impacts, or other macro events. These may happen quickly and unpredictably. International equity allocations may also be impact by currency and/or country specific risks which may result in lower liquidity in some markets.
- **Real Assets** can be volatile and may include asset segments that may have greater volatility than investment in traditional equity securities. Such volatility could be influenced by a myriad of factors including, but not limited to overall market volatility, changes in interest rates, political and regulatory developments, or other exogenous events like weather or natural disaster.

[1] Goldman Sachs as of October 18, 2024.
[2] Morningstar as of December 31, 2024.