Q4 2024: Post-Election Policy Shifts & Market Impacts

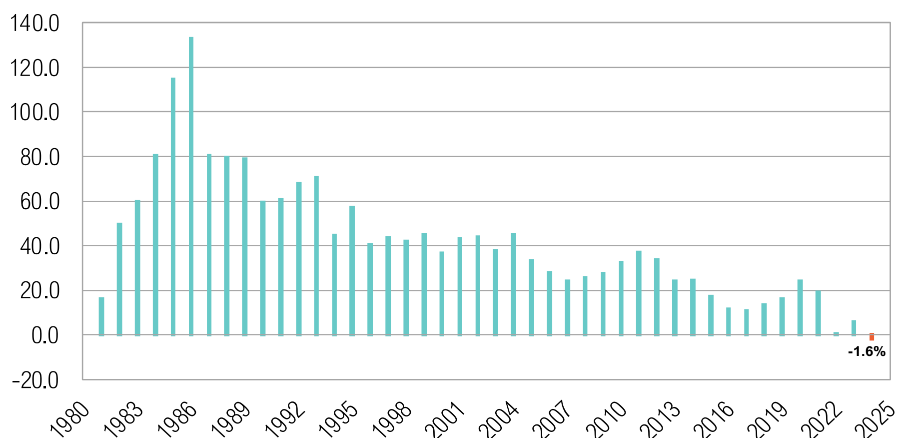
By Peak Trust Company's Chief Investment Officer, Lisa Russell, CFA. January | 2025

HIGHLIGHTS

- U.S. large-cap stocks reached over 50 new all-time highs in 2024, ending the year up 25%. U.S. small-cap stocks gained 11%, and U.S. intermediate-term bonds ended 2024 up 1%.
- Post-election, small business optimism recorded the largest month-over-month increase since July 1980. A comparable shift in sentiment was noted in various CFO surveys.
- Despite sticky inflation and higher interest rates, the U.S. consumer remained resilient while U.S. government spending continued unabated.
- The incoming administration appears focused on the challenging task of bolstering economic growth while reducing the deficit.
- The most critical element of this endeavor will be to curtail the deficit while keeping long-term yields contained to avoid disrupting economic expansion.

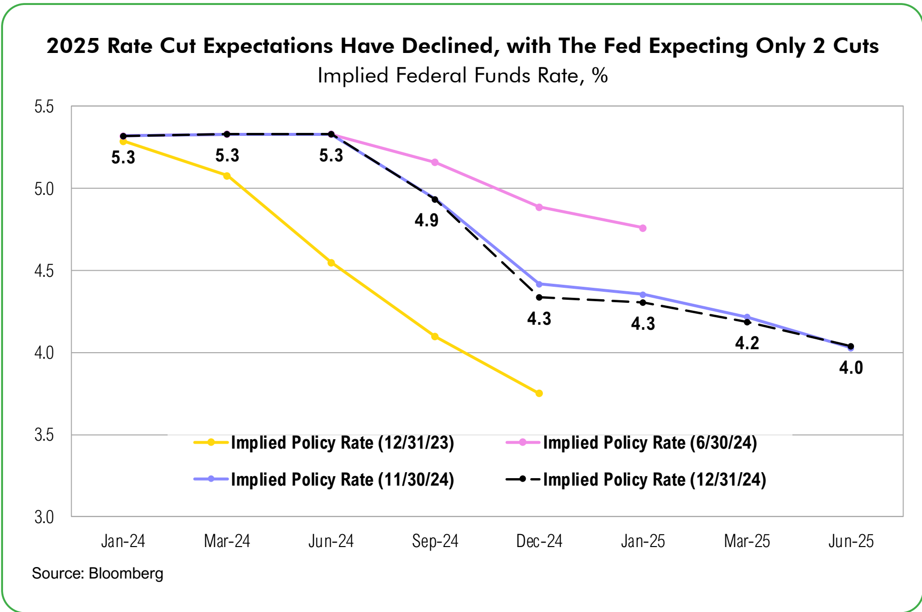
Overview

Markets ended 2024 with mixed results. U.S. large-cap stocks wrapped up the fourth quarter up 2.4% and ended the year up 25.0%. The S&P 500 hit over 50 new all-time highs in 2024. Over the last two years, the S&P 500 has risen a cumulative 53%—the strongest performance since the nearly 66% increase experienced between 1997 and 1998. U.S. small-cap stocks gained 11.5% over the year after a fourth-quarter gain of 0.3%. In contrast, 2024 was another challenging year for U.S. intermediate-term bonds. After declining 3.1% in the fourth quarter, the Bloomberg U.S. Aggregate Bond Index ended 2024 with a modest increase of only 1.3%. This marks a cumulative decline of 1.6% over the past five years, making it the worst five-year return since at least 1980.



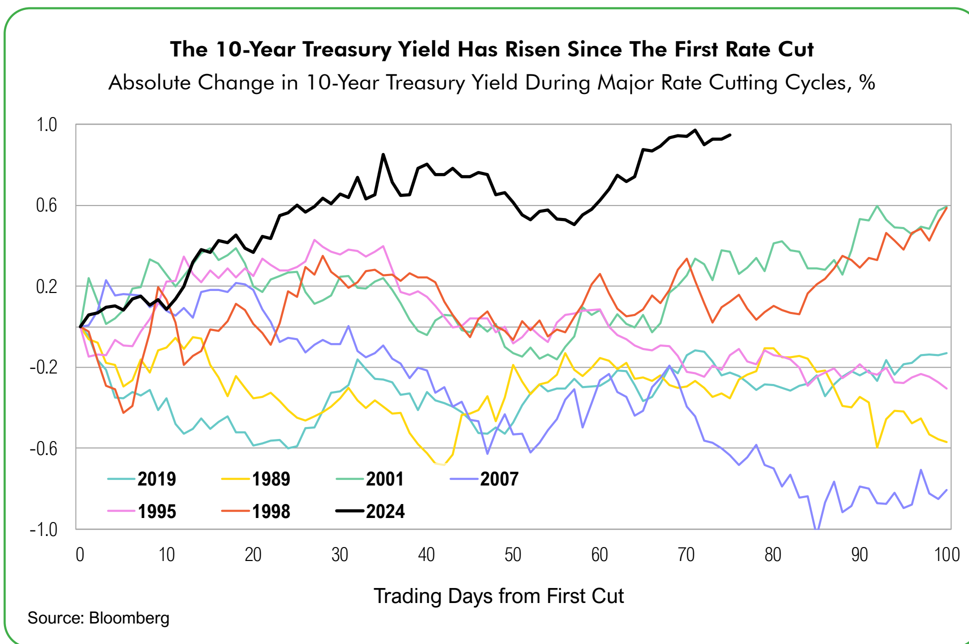
Source: Bloomberg. U.S. intermediate-term bonds proxied by the Bloomberg U.S. Aggregate Bond Index.

After easing to 2.4% year over year in September, headline inflation—measured by the Consumer Price Index (CPI)—ended the year at 2.7%, with housing inflation remaining the key contributor. Core inflation, excluding food and energy, closed 2024 at 3.3% and has stayed above 3% for 43 months. On September 18, with inflation still well above the official 2% target, the Federal Reserve (Fed) began to cut short-term interest rates. In three different meetings in the fourth quarter, the Fed cut interest rates by 1.0%, reducing the year-end rate to 4.25%–4.5%. At the December 18 Federal Open Market Committee meeting, the Fed's economic projections indicated that committee members expected the equivalent of two 0.25% rate cuts in 2025, even though their year-end 2025 inflation expectations rose from 2.1% to 2.5%. The 10-year Treasury yield has increased since the first rate cut in September—a notable shift compared to historical rate-cutting cycles. This uptick pushed 30-year mortgage rates higher, ending December at 7.3%, which is 0.6% above their levels before the initial Fed interest rate cut. By early January, markets anticipated only one 0.25% interest rate reduction for 2025.



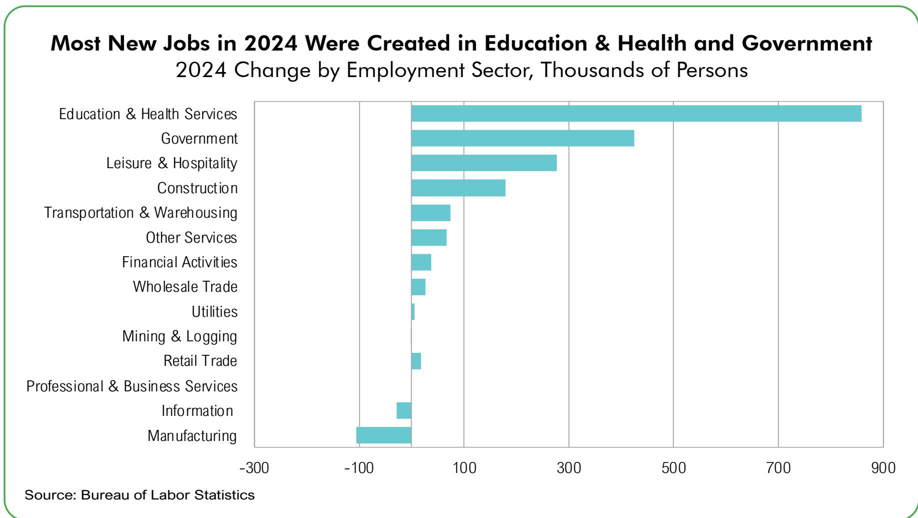
Two key factors have characterized the U.S. economy: the resilience of the U.S. consumer and the alarming rate of government deficit spending. Consumer spending continues to be robust. Over the holiday spending period, online sales increased by a record $241 billion (or 9% year over year). This is despite credit card interest rates nearing record highs at an average of 24% and the personal savings rate standing at 4.4%—well below the historical average of 8.4%.

In the 2024 fiscal year, the U.S. government fiscal deficit reached $1.8 trillion, making it the largest deficit recorded in a non-crisis or non-recessionary year on record. The fiscal deficit for 2025 (which began in October) has already surpassed $620 billion and is projected to reach $1.9 trillion by fiscal year-end. With interest rates still elevated, the interest expense on U.S. public debt rose by 20% over the past 12 months, climbing to $886 billion. This is nearly on par with national defense spending ($928 billion) and spending on health care programs ($926 billion).



The U.S. economy grew at an annualized rate of 3.1% quarter over quarter in the third quarter, with projections for the fourth quarter estimated at 2.3%. The services sector continues to be the main driver of growth. The

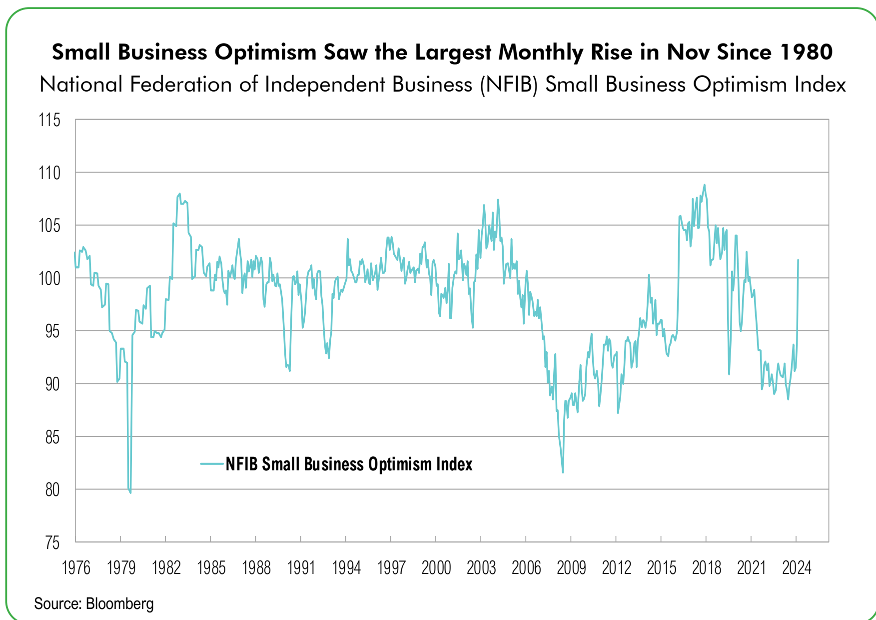
ISM Services PMI has consistently expanded throughout the fourth quarter, finishing December with a reading of 54.1. In contrast, the manufacturing sector has contracted for eight straight months, and the ISM Manufacturing PMI ended 2024 with an improved reading of 49.3—the highest since April. (A reading below 50 indicates contraction in the sector.) The manufacturing sector experienced the largest job losses in 2024, shedding over 106,000 jobs during the year, followed by the information sector, which lost more than 28,000 jobs. In contrast, the education and health services sectors added nearly 860,000 jobs in 2024, while the government sector gained almost 425,000 jobs. Overall, the labor market remained strong throughout 2024, and the unemployment rate concluded the year near record lows at 4.1%.



Post-Election

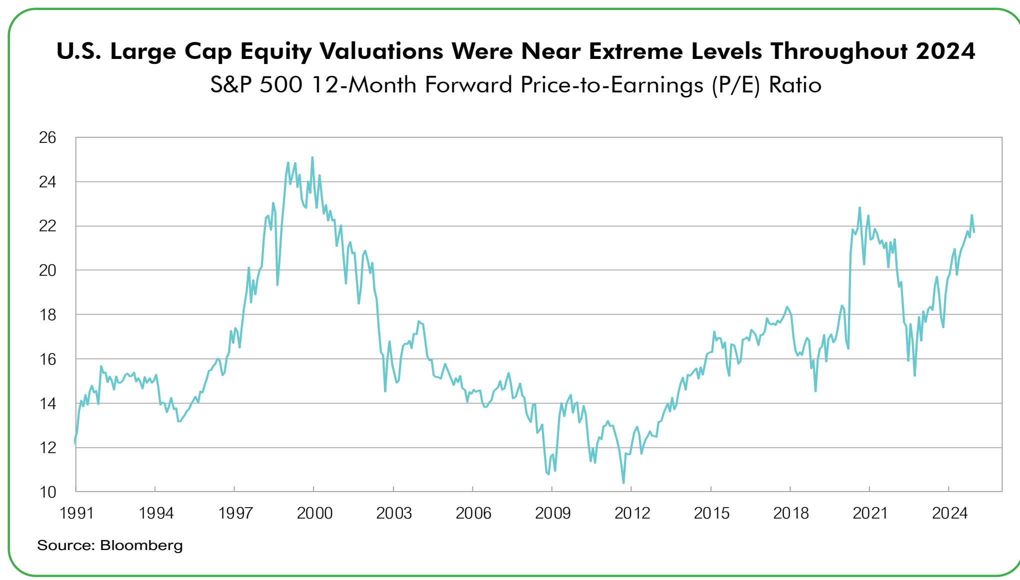
One of the defining events of 2024 was the 60th U.S. presidential election, held on November 5. Following the election, in which the Republican party emerged as the decisive winner, consumer sentiment ticked up from 72 in November to 74 in December. This increase was primarily driven by the 16-point spike in Republican sentiment, which offset the nearly 12-point drop in Democrat sentiment. Similarly, small business optimism jumped by eight points in November—the largest month-over-month increase since July 1980. A similar (7.4 points) spike in small business optimism was recorded in 2016. Following that, the Russell 2000 Index gained 25% over the next 12 months and an annualized 13% over the ensuing four years. The S&P 500 gained 24% over the next 12 months and an annualized 20% over the next four years.

According to the November 2024 National Federation of Independent Business (NFIB) small business survey, 36% of respondents expect the economy to improve, 18% plan to increase hiring, and 28% intend to make capital outlays. CFO surveys of larger companies conducted between October and November 2024 indicate a similar rise in optimism about the U.S. economy, while concerns regarding the health of the economy, company sales, and revenue have declined sharply compared to the survey conducted between August and September 2024. Another area signaling economic optimism is U.S. high-yield credit spreads, which ended December near historical lows at 2.7%, suggesting that the economy may achieve a "soft landing." Furthermore, the November Job Openings and Labor Turnover Survey (JOLTS) report, released in early January, showed signs of stability. Job openings increased for the second consecutive month (the first two-month rising



streak since December 2022), and the total number of job openings surpassed the 8-million mark for the first time since May 2024. Vibes are also shifting among larger businesses as they seek to align themselves with the new administration. Meta recently announced adjustments to the company's moderation policies and practices, citing a shifting political and social landscape and a commitment to embracing free speech.

Even before post-election economic sentiment surveys showed improved optimism, equity valuations remained elevated throughout the year, climbing back to extreme levels akin to the tech bubble. Despite these elevated valuations, U.S. large-cap returns were once again above average. With only 19% of S&P 500 constituents outperforming the broader index over the past year, returns remain substantially driven by a handful of mega-cap technology stocks, including Nvidia (up 171% in 2024), Meta (up 65%), Tesla (up 63%), and Amazon (up 44%). The Magnificent Seven now account for over a third of the S&P 500, an increase from a fifth of the index in 2022. Earnings growth for the S&P 500 is expected to be 15% in 2025. In contrast, earnings growth for the Russell 2000 index is expected to accelerate by 40% in 2025.



With the new administration taking office on January 20, President-Elect Donald Trump has already announced several key nominations for Cabinet positions and White House roles. Among these is Scott Bessent, a former Democratic donor, nominated as Treasury Secretary. Bessent has outlined a "3-3-3" target of achieving 3% economic growth, reducing the federal deficit to 3% of GDP by 2028, and increasing daily energy production by the equivalent of 3 million barrels of oil—approximately a 20% increase from current levels. When asked about his decision to accept the nomination, Bessent remarked: *"This election cycle is the last chance for the U.S. to grow our way out of this mountain of debt…"*

Conquering the mountainous size of the fiscal deficit is daunting; however, there is reason for optimism. In addition to Bessent, Trump has announced the formation of the Department of Government Efficiency (DOGE). Led by Elon Musk, the department's goal is to enhance government accountability and efficiency within federal agencies. While DOGE will be an advisory board, not an official government department, board, it could draw attention to and subsequently ease the U.S. fiscal deficit burden.

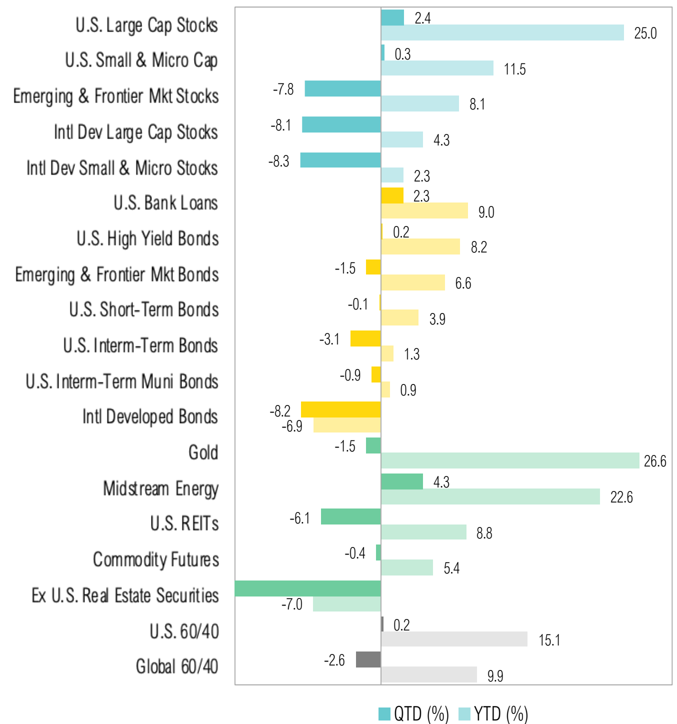
Markets

U.S. equity markets outperformed their international counterparts in the fourth quarter. U.S. large-cap stocks rose by 2.4%, while international developed large-cap stocks fell by 8.1%. Likewise, U.S. small-cap stocks finished the quarter unchanged, gaining only 0.3%, whereas international developed small-cap stocks dropped by 8.3%. Emerging and frontier market stocks closed the fourth quarter down 7.8%. The U.S. dollar ended the month at its highest level since November 2022. Fixed-income markets showed similar trends: while U.S. intermediate-term bonds ended the fourth quarter down 3.1%, international developed market bonds finished the quarter down 8.2%.

Despite ending the fourth quarter down 1.5%, gold finished 2024 up 26.6%, setting over 30 new record highs. This is un-

precedented, given the strong dollar and rising rates. Is this increase fueled just by Foreign Central Bank purchases or is there something more to this move? Either way, it warrants watching. After reaching a one-year low of $65.8 per barrel on September 10, West Texas Intermediate (WTI) crude oil ended the year at $71.7 per barrel. Despite rising oil prices, U.S. national average gasoline prices reached a three-year low of $3.02 on December 12.

In September, the People's Bank of China announced a series of economic stimulus measures, including interest rate cuts, increased government spending, and relaxed property market restrictions aimed at revitalizing sluggish growth in the face of a weak real estate sector and declining consumer confidence. However, progress has been underwhelming, and further announcements have been delayed as authorities appear to be waiting for greater clarity on tariffs and the policies of the incoming Trump administration. On December 20, a week after the Chinese government announced its first loosening of monetary policy in 14 years, short-term Chinese sovereign bond yields fell to 0.92%—the lowest level since the Global Financial Crisis. The MSCI China Index ended the fourth quarter down 7.7%.



In global fixed-income markets, 10-year Japanese government bond (JGB) yields reached their highest level since 2011 at 1.18% in early January. Similarly, in early January, UK 10-year Gilt yields climbed to their highest level since August 2008, hitting 4.76%. Furthermore, 30-year UK Gilt yields reached their highest level since August 1998 in early January, rising to 5.3%.

Looking Forward

The incoming administration appears focused on bolstering economic growth while reducing the deficit. Curtailing the deficit while keeping longer-term yields contained will be the most critical elements of this endeavor.

While the Federal Reserve can dictate short-term interest rates through policy decisions, it has less control over longer-term rates. Since the first rate cut in September, longer-term yields have moved higher than in other rate-cutting cycles. That's not to say that a rise in bond yields is inherently bad. However, unless driven by higher long-term growth prospects that translate to higher corporate earnings, rather than fiscal irresponsibility or other perceived policy errors, increased bond yields could negatively impact risky asset valuations. It is now up to fiscal policymakers to thread this needle. If they succeed, it will allow the continuation of government policies that support economic growth, which are critical for supporting equity and credit markets.

About Lisa

Lisa Russell started with Peak Trust Company in 2003 and currently serves as Chief Investment Officer. Lisa brings over 25 years of investment experience to the Peak team. She specializes in designing unique investment programs for high-net-worth clients and trust accounts. She is highly attuned to the tax consequences of investment actions.

Lisa holds a Master of Business Administration in Finance from Emory University and a Bachelor of Science in Business Administration from the University of Southern California. Lisa holds the designation of Chartered Financial Analyst (CFA), and is a member of the CFA Institute and the CFA Society of Seattle.

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