Research Review

Fourth Quarter 2024

OVERVIEW

For the calendar year, most major asset classes and sub-asset categories generated positive returns. Gains continued to remain concentrated within domestic equity markets, most notably mega-cap tech stocks. As 2024 ended, the often-observed Santa Claus Rally failed to materialize as broad losses blanketed financial markets. Despite the sharp rally across small cap stocks that immediately followed the U.S. presidential election, upward momentum sharply reversed course in December, with the Russell 2000 Index falling 8.3%.

Bond markets took a hit amid December's spike in interest rates, with rate-sensitive sectors such as core and the relatively long-duration investment grade corporate space underperforming shorter-duration sectors. Real estate investment trusts (REITs) suffered in both December and the fourth quarter, with interest rate headwinds weighing down the sector and leading to underperformance versus competing categories such as energy infrastructure and global listed infrastructure.

ECONOMIC UPDATE

A Year of Gains, Despite Ending on a Low Note

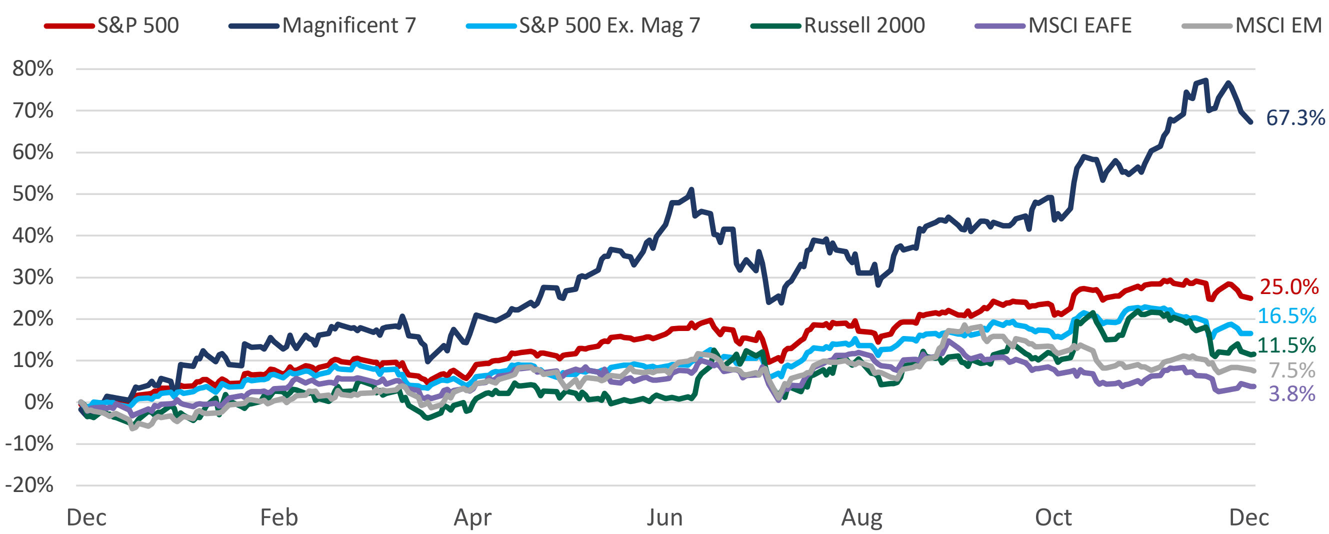
> *"The overarching performance theme across the stock market took on a familiar tone — concentration."*
>
> **MIKE O'CONNOR, CFA**

Global financial markets witnessed a bumpy ending to 2024, as a seemingly countless number of global macroeconomic and geopolitical events were digested. From the U.S. presidential election and a shift in the Federal Reserve's (Fed) policy stance to a swelling list of market-moving international headlines, asset allocators' hands were full in their quest to successfully navigate 2024.

Despite December's pullback, the calendar year story appeared vastly different, rewarding investors. Global equities, led by the U.S., strongly outperformed fixed income and other major real asset sectors for both the fourth quarter and the year. Still, the overarching performance theme across the stock market took on a familiar tone — concentration. One look at the calendar year evolution of global equity performance highlights the persistent dominance of the Magnificent 7[1] mega-cap technology-related stocks, outperforming the broader U.S. large cap market by over 40 percentage points in 2024.

THE MAGNIFICIENT 7 DOMINATED 2024

2024 Cumulative Returns (%)



Source: Bloomberg, L.P.; Data as of 12/31/2024

[1]Alphabet, Amazon, Apple, Meta, Microsoft, NVIDIA, and Tesla

The dominance of these highly successful and innovative darlings of the U.S. corporate world reflects a broader trend that has firmly been in place in the post-pandemic period — U.S. leadership on the global economic playing field. Many of the U.S.'s primary trading partners have grappled with economic headwinds, including lackluster growth, ineffective monetary policy initiatives, volatile currency fluctuations (e.g., Japanese yen carry trade unwind in August), and a highly uncertain near-term path amid President-elect Trump's looming return to the White House. In stark contrast, the U.S. economy has been the envy of the world.

Domestically, inflation continues to moderate, the labor market generally remains tight, and real GDP growth has averaged about 3% over the trailing 2 years. The Fed's confidence in this supportive set of economic conditions resulted in the incremental removal of policy restraint through a 100 basis point (bp) reduction in the Fed funds rate through 2024. Moreover, at their final policy meeting of the year, the Fed's updates to their Dot Plot projection table for near-term policy adjustment reflected a further 50 bp reduction to the policy rate in 2025, albeit a lesser revision from their 100 bp expectation at their September meeting.

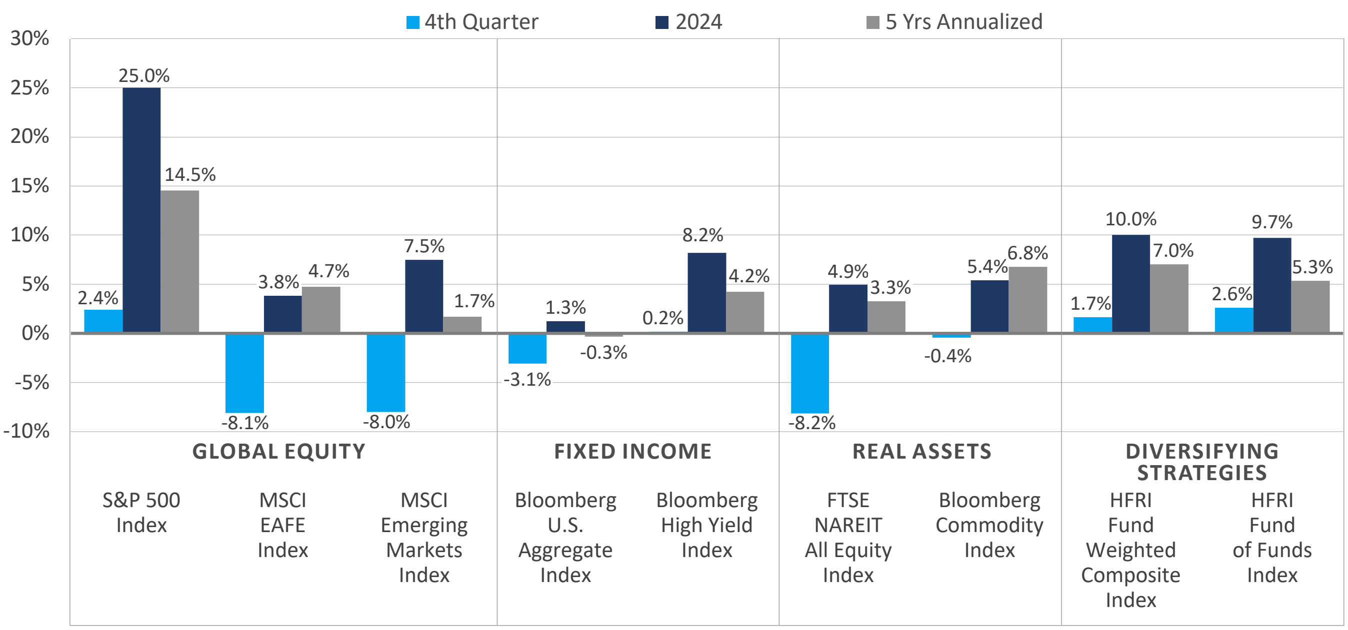
The financial and economic conditions at the end of the year continued to reflect a balanced backdrop. Global equity valuations were at or near their cycle peaks. U.S. large caps measured near historical highs versus a less extreme valuation backdrop abroad. Credit conditions reflected particularly benign market conditions, a dynamic often associated with few near-term fears of a cyclical downturn. Fundamentally, the picture remains mixed, with meaningfully positive domestic fundamentals somewhat counterbalanced by material weakness abroad.

Looking back, 2024 will be remembered as a year full of potentially volatility-inducing macroeconomic events. Markets were buffeted by national elections across the globe, shifting global central bank postures following a multi-year inflation fight, growing geopolitical tensions, and potential possible trade disputes among some of the world's largest economies. Nevertheless, the scenario was one investors have grown familiar with in recent years — significant outperformance by both domestic markets and the broader U.S. economic engine, while broadly positive returns for almost all major asset classes were, of course, a welcomed development.

MARKET SUMMARY

A DISAPPOINTING END TO AN OTHERWISE STRONG YEAR

Total Returns for Key Assets and Markets



Data source: Lipper and Hedge Fund Research

GLOBAL EQUITY

The fourth quarter of 2024 was marked by significant movements in global equity markets, driven by a mix of economic data, central bank policies, and geopolitical events. The quarter began with optimism but ended with volatility as economic resilience gave way to central banks' cautious stances on future rate cuts. U.S. equity markets were buoyed by strong economic data and corporate earnings, while international markets were negatively affected by the strengthening of the U.S. dollar. Emerging markets performance was mixed, with some regions benefiting from economic reforms while others struggled with external pressures such as the continued impact of the nearshoring theme.

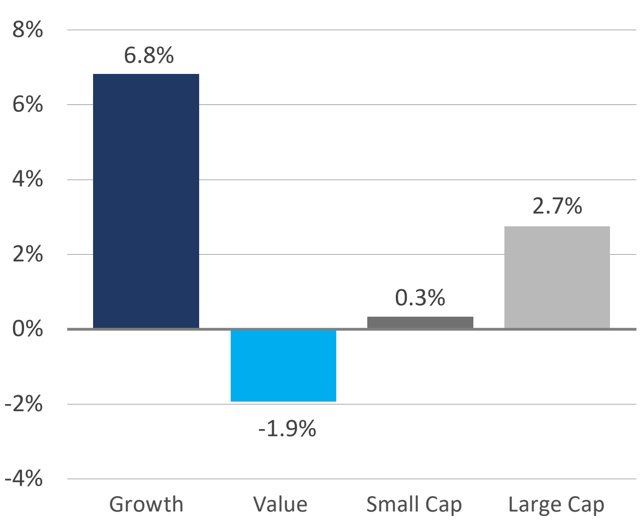
U.S. equity markets had an abnormally weak fourth quarter, first buoyed by the presidential election and then hindered by the lack of a highly anticipated Santa Claus Rally. The Fed's announcement of fewer expected rate cuts in 2025 and the threat of widespread tariffs led to some late-quarter volatility. Despite concerns about renewed inflation, the U.S. economy's resilience and strong labor market data helped maintain investor confidence.

The strengthening of the U.S. dollar was the predominant story for U.S. investors in international markets. Economic weakness internationally has led global central banks to adopt an easier monetary path with lower interest rates relative to the Fed, which supported the value of the U.S. dollar and weighed on international equity returns for U.S. investors.

Japanese equity markets experienced a turbulent quarter, generally rising in local terms but declining in U.S. dollars. The Nikkei 225 Index saw sharp declines in early October, followed by a recovery in late December. Investors began to price in an improved earnings outlook for large cap exporters on the backdrop of a weakening yen. The Bank of Japan's monetary policy decisions, including maintaining real negative interest rates and providing signals of future rate hikes, played a crucial role in market movements throughout the quarter. Despite challenges, Japanese companies continue to make improvements in corporate governance and equity market support. In 2024, share buybacks totaled more than $100 billion, a new record for the third consecutive year.

ELECTION RESULTS BUOYED EQUITY RETURNS

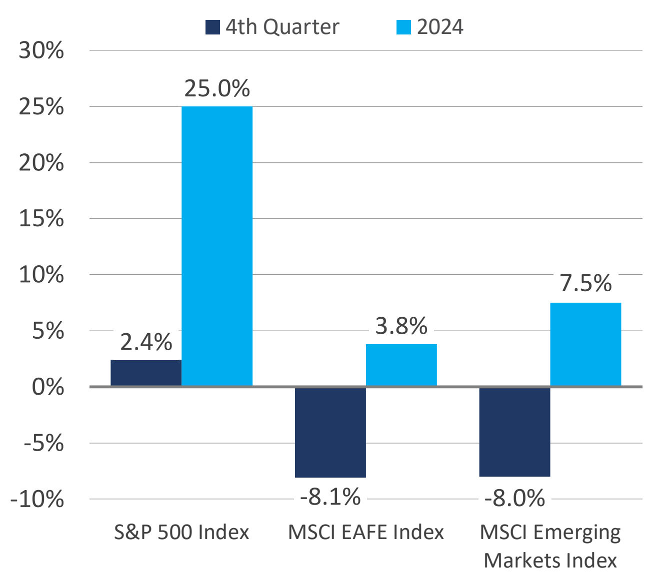
U.S. Equity Returns - Fourth Quarter 2024



Source: FTSE Russell

U.S. MARKETS OUTPERFORMED ON DOLLAR STRENGTH

Global Equity Markets Total Return



Source: S&P and MSCI

Europe ex-UK equity markets faced a challenging quarter. Political instability in key economies like Germany and France, caused by government spending and fiscal budget plan issues, weighed on investor sentiment. The European Central Bank's decision to cut interest rates by 25 bps in October and December provided some relief, but the overall economic outlook remained subdued. Materials, real estate, and consumer staples sectors underperformed, while industrials showed resilience.

In local terms, the UK equity markets showed relative stability in the quarter, supported by strong performance in the financial and healthcare sectors. The resolution of some Brexit-related uncertainties and positive economic data helped improve investor confidence.

A victory for Donald Trump and a GOP election sweep acted as a headwind to emerging markets in the fourth quarter, leaving investors uncertain about the impact of proposed tariffs and the threat of retaliatory action. China's equity markets struggled despite government stimulus measures, as concerns about economic slowdown and regulatory crackdowns weighed on investor sentiment. Brazil's currency plunged to a 30-year low, causing an uncharacteristic cut in government spending. Despite these challenges, some sectors, such as technology, showed resilience amid the broader market downturn.

SANTA WAS NOWHERE TO BE FOUND THIS DECEMBER

December S&P 500 Returns (1980-2024)

Data source: FactSet

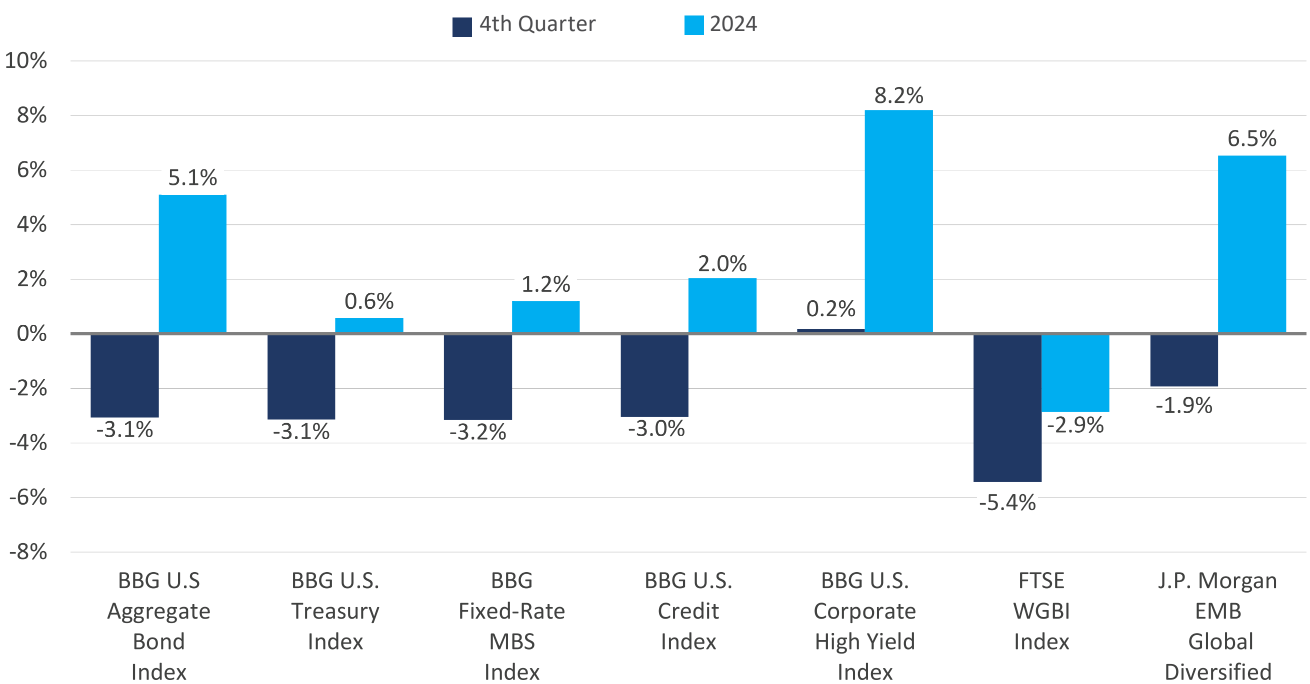
FIXED INCOME

Interest-rate-sensitive bonds sold off as rates rose in response to inflation concerns. President Trump's proposed policies were viewed as boosting growth but also risking inflation. Relatedly, rate cuts by the European Central Bank and Bank of England have outpaced the Fed's easing, which contributed to increased demand for U.S. dollars.

The 10-year Treasury yield increased to 4.57%, and the yield curve structure remained ascending with a 33 bp 10-year to 2-year spread. The Fed made two 25 bp cuts, bringing the Fed funds rate to 4.25%-4.5%, and markets priced in less than a 10% chance of a January rate reduction. It appears the Fed has shifted focus back to prioritizing inflation risks over unemployment, signaling a potential pause in January and possibly an extended break in 2025, to assess and prevent inflationary pressures from reemerging.

PERFORMANCE TAILWINDS PERSISTED IN THE FOURTH QUARTER

Fixed Income Index Returns

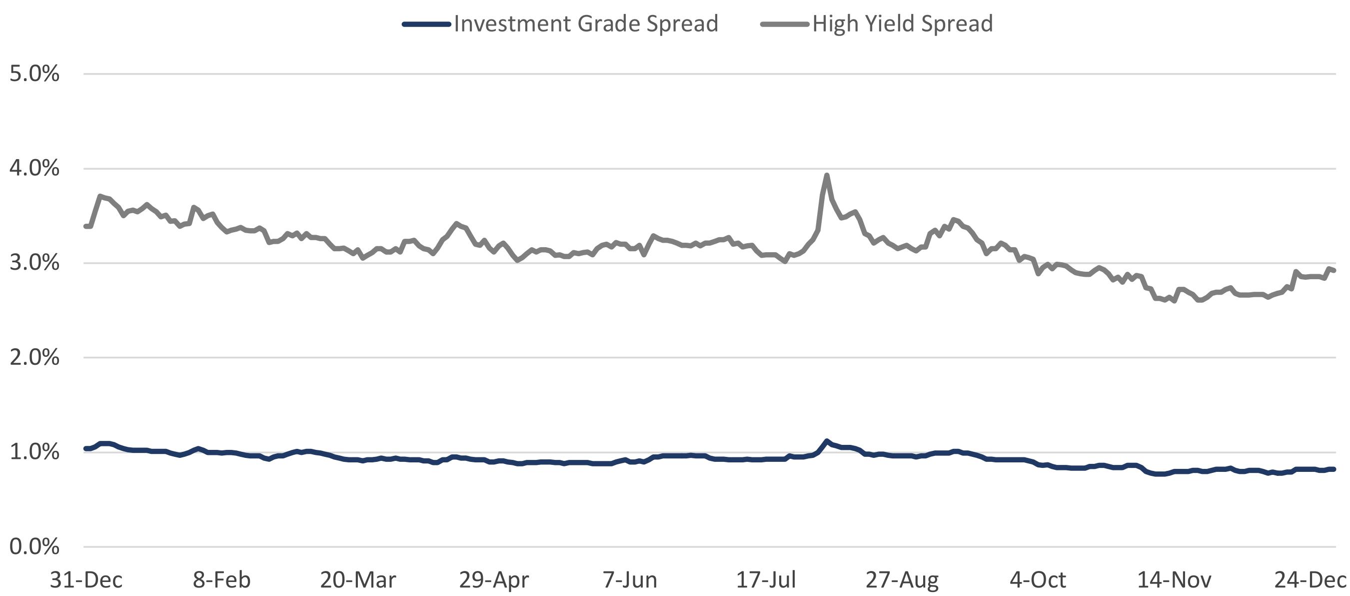


Data sources: Bloomberg, FTSE, J.P. Morgan

Credit spreads tightened, supported by signs of strength and stability in the U.S. economy. High yield (HY) spreads narrowed to below 3% by year-end, the tightest levels since the years before the Great Financial Crisis. Investment grade (IG) spreads also reached multi-decade lows. U.S. institutional loan activity surged as speculative-grade borrowers took advantage of favorable credit conditions. Primary market loan activity climbed to $400 billion as the same speculative-grade borrowers took advantage of the highly accommodating credit conditions. This was the second highest level on record, just shy of the $405 billion peak in the second quarter of 2024.

INVESTMENT GRADE AND HIGH YIELD BONDS SPREADS REMAIN TIGHT

U.S. Corporate Bond Spreads



Data source: Federal Reserve Bank of St.Louis (FRED)

REAL ASSETS

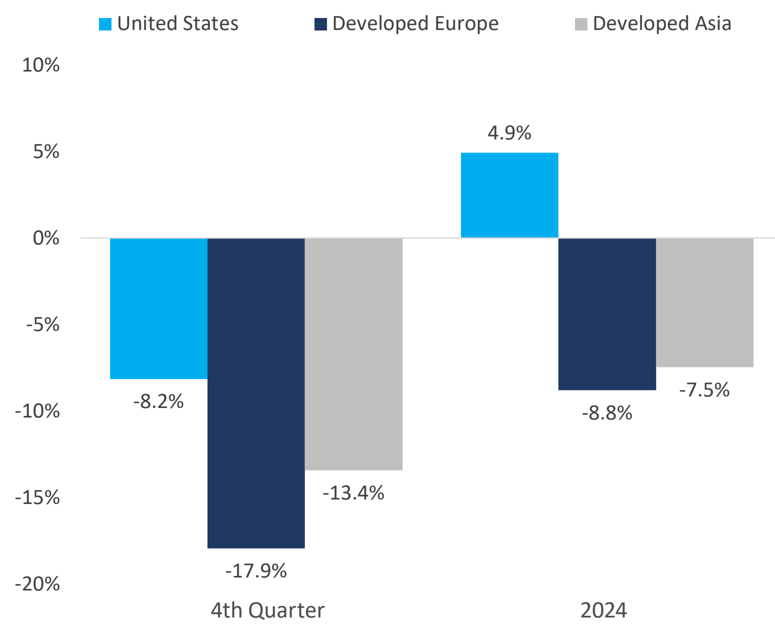
REAL ESTATE

December saw U.S. Real Estate Investment Trusts (REITs) post their worst monthly performance of 2024, falling more sharply than the broader market and erasing much of the year's gains. Listed real estate was weighed down by hawkish commentary from the Fed, which signaled the possibility of only two rate cuts in 2025, fewer than the market had anticipated. Global REITs also fell, but fared better than the U.S. due to smaller declines in developed European and Asian markets.

In the U.S., the retail sector, particularly regional malls, was a standout performer over the trailing one-year period. This strength was supported by limited new construction in recent years and increased traffic to neighborhood retail centers, as flexible work schedules allowed workers to spend less time in downtown metro areas.

REITS STRUGGLE AMID FEDERAL RESERVE SIGNALS

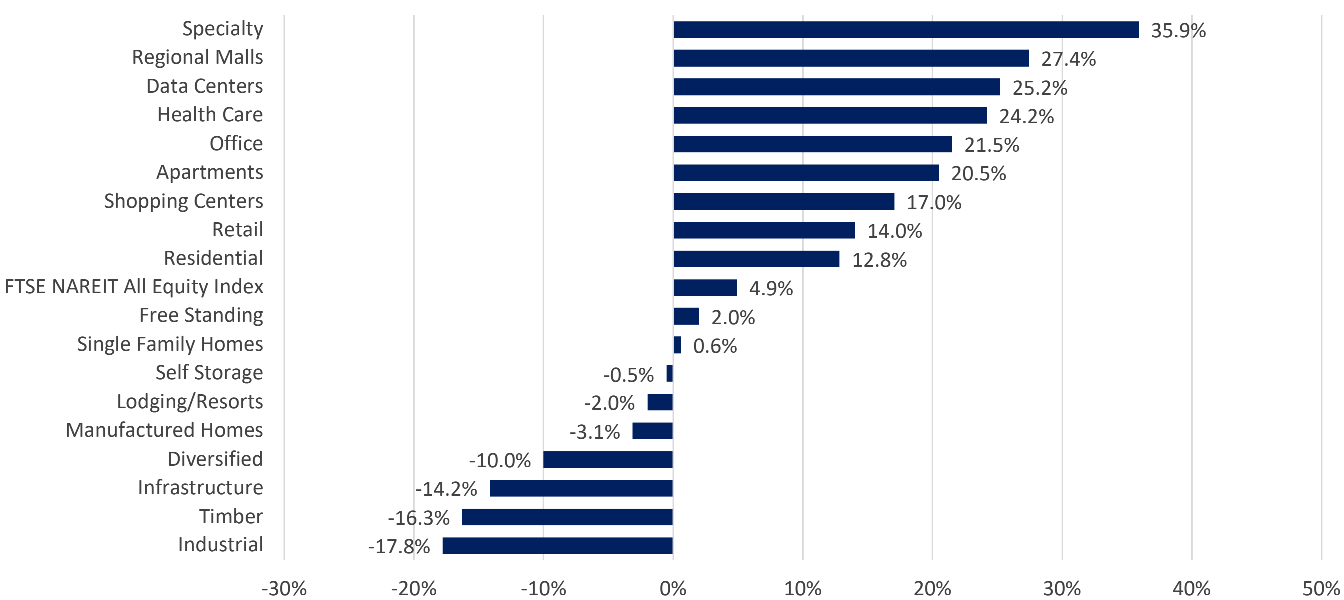
Total Returns for Key Assets and Markets



Data source: FactSet

LIMITED SUPPLY AND FLEXIBLE WORK SUPPORT REGIONAL MALLS

U.S. REIT Trailing Performance by Property Type, Year-to-Date



Data source: FactSet

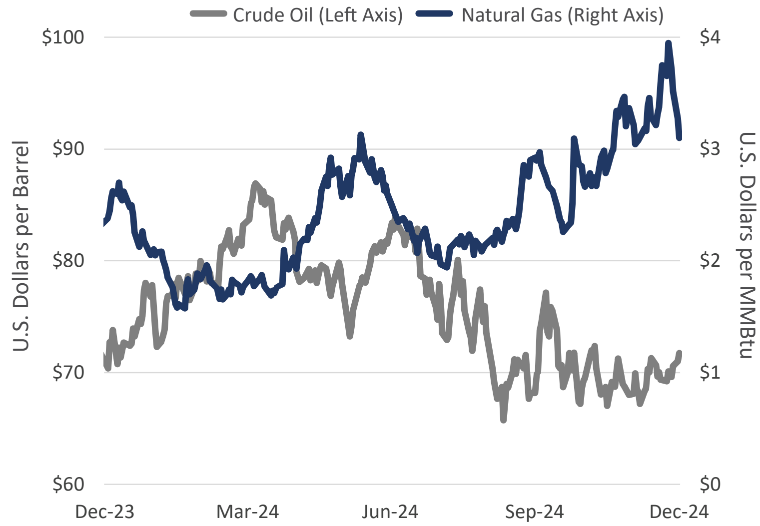
NATURAL RESOURCES

Crude oil prices rose modestly, supported by cold weather, reduced U.S. stockpiles, and expectations of economic stimulus in China. Cold weather in Europe and the U.S. boosted demand for heating oil, while expectations of new policy actions to stimulate growth in China, the world's largest oil importer, supported higher prices. A decrease in U.S. crude stockpiles provided additional price support, with the West Texas Intermediate (WTI) Continuous Contract closing the year higher than November levels.

Although volatile and declining sharply in December, natural gas prices rose through the quarter, rebounding on anticipated winter heating demand despite abundant U.S. storage levels. Prices continued to remain volatile into month-end as extreme cold weather was forecasted in parts of the U.S. and Europe.

OIL GAINS AS GAS DECLINES AMID CONTRASTING TRENDS

Price of WTI Crude and U.S. Natural Gas



Data source: FactSet

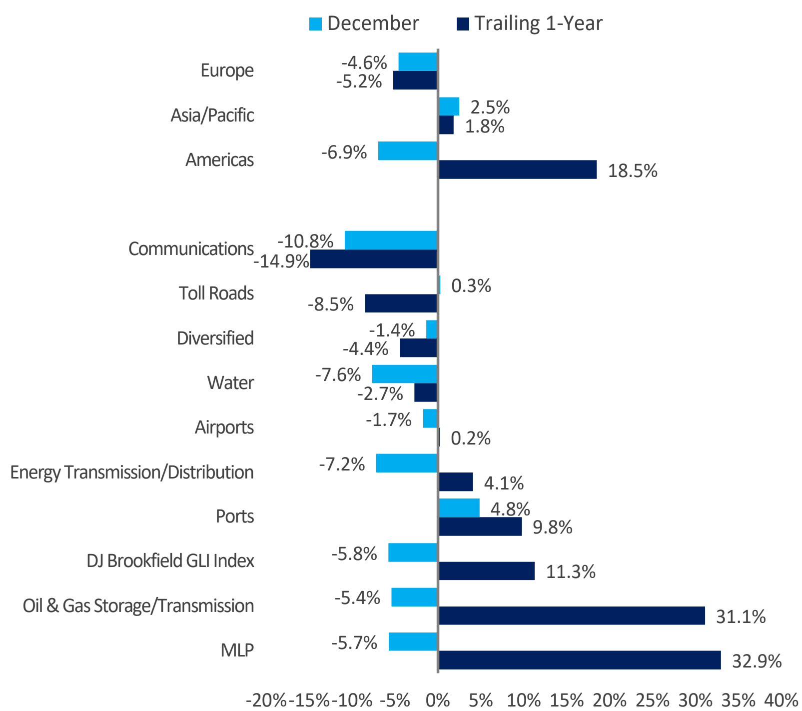
INFRASTRUCTURE

In December, global listed infrastructure stocks experienced a pullback, as measured by the Dow Jones Brookfield Global Infrastructure Index. The rate-sensitive sector declined more than the broader market, driven by the same narrative of hawkish commentary from the Fed and rising interest rates.

The midstream energy sector also suffered during the December pullback. Nevertheless, the sector still ended the year with exceptional performance. Robust oil prices throughout 2024 supported strong cash flows. This enabled companies to maintain disciplined capital expenditure strategies, execute share buyback programs, and strengthen balance sheets by reducing leverage.

RATE SENSITIVITY DROVE DECEMBER DECLINES IN INFRASTRUCTURE STOCKS

Listed Infrastructure Trailing Returns



Data source: FactSet

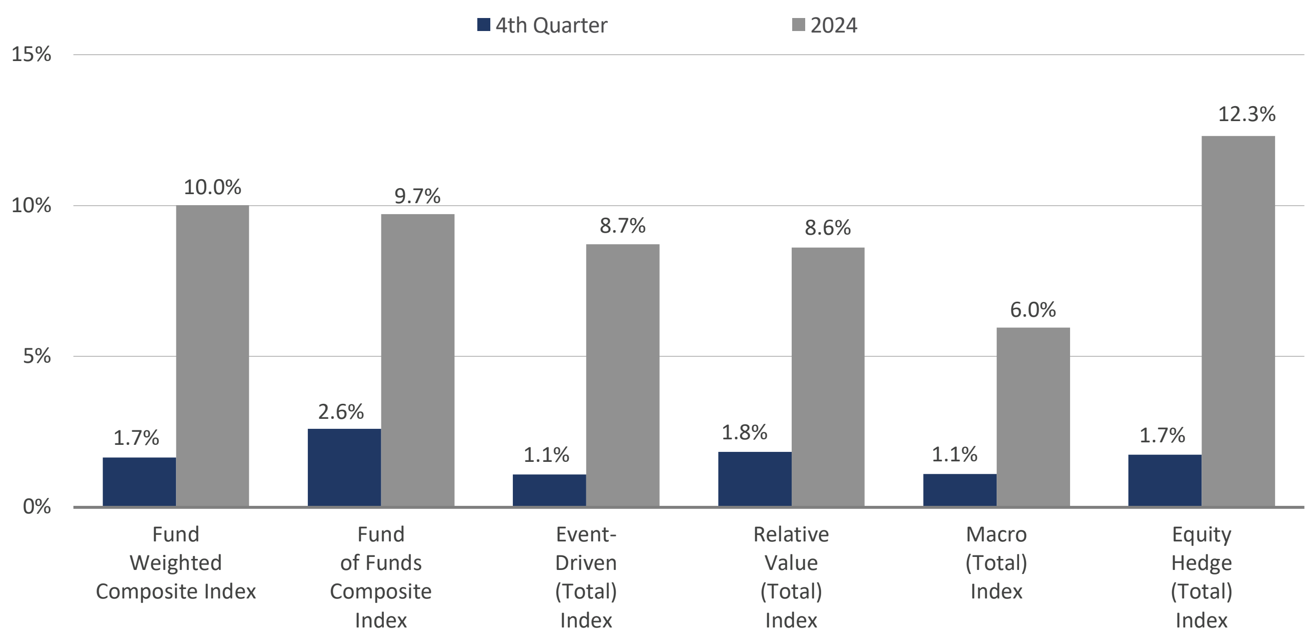
DIVERSIFYING STRATEGIES

Across all major strategies, hedge funds finished the year with a strong fourth quarter. The relative value and hedged equity indices led returns, each gaining nearly 2%. Global macro generated a strong enough quarter to surpass a 5% return for the year. Within hedged equity, technology-focused managers were the leaders for the quarter and the year. The risk-on spirit persisted throughout 2024, with the technology sector being the biggest beneficiary.

Systematic macro managers felt the tailwind of continued uptrends in the U.S. dollar, rallying each month of the quarter. Commodities were another area of strength, led by long positions in cocoa. Their prices hit record highs as West African supply disruptions continued. Short exposures to U.S. Treasuries were also positive contributors as rates rose amid renewed inflation fears.

HEDGE FUNDS FINISHED THE YEAR ON A HIGH NOTE

HFRI Indices Performance Returns (U.S. Dollars)



Data source: HedgeFund Research

INDICES

The Alerian MLP Index is a composite of the 50 most prominent energy Master Limited Partnerships that provides investors with an unbiased, comprehensive benchmark for this emerging asset class.

Bloomberg Fixed Income Indices is an index family comprised of the Bloomberg US Aggregate Index, Government/Corporate Bond Index, Mortgage-Backed Securities Index, and Asset-Backed Securities Index, Municipal Index, High-Yield Index, Commodity Index and others designed to represent the broad fixed income markets and sectors. On August 24, 2016, Bloomberg acquired these long-standing assets from Barclays Bank PLC. and on August 24, 2021, they were rebranded as the Bloomberg Fixed Income Indices. See https://www.bloomberg.com/markets/rates-bonds/bloomberg-fixed-income-indices for more information.

The CBOE Volatility Index (VIX) is an up-to-the-minute market estimate of expected volatility that is calculated by using real-time S&P 500 Index option bid/ask quotes. The Index uses nearby and second nearby options with at least eight days left to expiration and then weights them to yield a constant, 30-day measure of the expected volatility of the S&P 500 Index.

FTSE Real Estate Indices (NAREIT Index and EPRA/NAREIT Index) includes only those companies that meet minimum size, liquidity and free float criteria as set forth by FTSE and is meant as a broad representation of publicly traded real estate securities. Relevant real estate activities are defined as the ownership, disposure, and development of income-producing real estate. See https://www.ftserussell.com/index/category/real-estate for more information.

HFRI Monthly Indices (HFRI) are equally weighted performance indexes, compiled by Hedge Fund Research Inc. (HFX), and are used by numerous hedge fund managers as a benchmark for their own hedge funds. The HFRI are broken down into 37 different categories by strategy, including the HFRI Fund Weighted Composite, which accounts for over 2,000 funds listed on the internal HFR Database. The HFRI Fund of Funds Composite Index is an equal weighted, net of fee, index composed of approximately 800 fund- of- funds which report to HFR. See www.hedgefundresearch.com for more information on index construction.

J.P. Morgan's Global Index Research group produces proprietary index products that track emerging markets, government debt, and corporate debt asset classes. Some of these indices include the JPMorgan Emerging Market Bond Plus Index, JPMorgan Emerging Market Local Plus Index, JPMorgan Global Bond Non-U.S. Index and JPMorgan Global Bond Non-U.S. Index. See www.jpmorgan.com for more information.

Merrill Lynch high yield indices measure the performance of securities that pay interest in cash and have a credit rating of below investment grade. Merrill Lynch uses a composite of Fitch Ratings, Moody's and Standard and Poor's credit ratings in selecting bonds for these indices. These ratings measure the risk that the bond issuer will fail to pay interest or to repay principal in full. See www.ml.com for more information.

Morgan Stanley Capital International – MSCI is a series of indices constructed by Morgan Stanley to help institutional investors benchmark their returns. There are a wide range of indices created by Morgan Stanley covering a multitude of developed and emerging economies and economic sectors. See www.morganstanley.com for more information.

The FTSE Nareit All Equity REITs Index is a free-float adjusted, market capitalization-weighted index of U.S. equity REITs.

Russell Investments rank U.S. common stocks from largest to smallest market capitalization at each annual reconstitution period (May 31). The primary Russell Indices are defined as follows: 1) the top 3,000 stocks become the Russell 3000 Index, 2) the largest 1,000 stocks become the Russell 1000 Index, 3) the smallest 800 stocks in the Russell 1000 Index become the Russell Midcap index, 4) the next 2,000 stocks become the Russell 2000 Index, 5) the smallest 1,000 in the Russell 2000 Index plus the next smallest 1,000 comprise the Russell Microcap Index, and 6) U.S. Equity REITs comprise the FTSE Nareit All Equity REIT Index. See www.russell.com for more information.

S&P 500 Index consists of 500 stocks chosen for market size, liquidity and industry group representation, among other factors by the S&P Index Committee, which is a team of analysts and economists at Standard and Poor's. The S&P 500 is a market-value weighted index, which means each stock's weight in the index is proportionate to its market value and is designed to be a leading indicator of U.S. equities, and meant to reflect the risk/return characteristics of the large cap universe. See www.standardandpoors.com for more information.

Information on any indices mentioned can be obtained either through your advisor or by written request to information@feg.com.

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All data is as of December 31, 2024 unless otherwise noted.

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