Research Review

November 2024

OVERVIEW

Following the U.S. presidential election on November 5, performance across the financial markets reflected the view that the second Trump presidency would overwhelmingly favor domestic-oriented sectors, particularly small businesses. This could come at the expense of the already beleaguered international sectors, which have faced economic and financial market headwinds in recent years.

Risk-on sentiment during the month appeared most evident in smaller capitalization domestic equities. The Russell 2000 Index posted double-digit total returns, easily outperforming the mid-single-digit gains of U.S. large cap stocks. Overseas, performance spanning international developed and emerging market equities meaningfully lagged U.S. stocks.

In the bond markets, a modest monthly decline in interest rates and a further compression in credit risk premiums drove broad-based positive returns across most major fixed income sectors despite renewed worry regarding a potential second wave of inflation. Not surprisingly, the monthly decline in interest rates helped support the rate-sensitive real estate sector in November, with U.S. real estate investment trust securities (REITs) posting a solid monthly gain. Similarly, double-digit total returns were realized across the energy infrastructure sector.

ECONOMIC UPDATE

A Risk-On Rally Ensues

> *"The anticipation of a potentially more supportive business environment – from the combination of anticipated corporate tax cuts and deregulation efforts – supported domestic risk asset performance."*
>
> **MIKE O'CONNOR, CFA**

Prospects for a more pro-business presidential administration set to take control of the White House in January helped add fuel to the already red-hot U.S. equity markets in November. The S&P 500 Index ascended to its highest price level on record, and consequently, most commonly-referenced valuation gauges increased to exceptional levels.

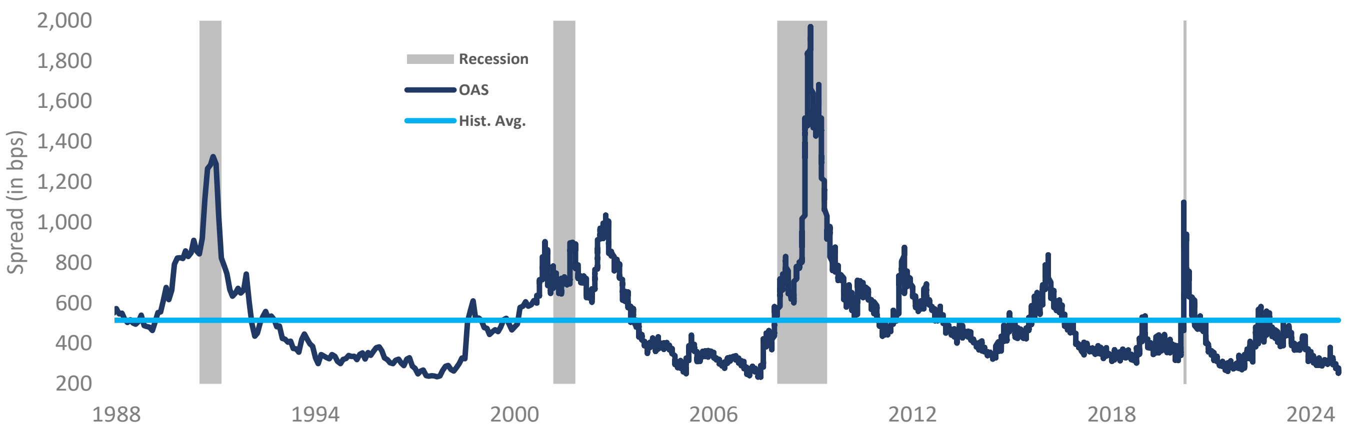
The anticipation of a potentially more supportive business environment – from the combination of anticipated corporate tax cuts and de-regulation efforts – supported domestic risk asset performance. Conversely, stubborn fundamental headwinds plaguing many of the U.S.'s key trading partners and the expectation for a material increase in import tariffs helped drive a significant disparity between international risk asset performance and that experienced in the U.S.

The strong bid for U.S. risk exposure was pervasive and supported strong performance throughout the corporate capital structure. Credit-oriented fixed income sectors enjoyed a continuation of the performance tailwinds in place throughout most of 2024 as risk premiums collapsed.

Of significance, the option-adjusted spread (OAS) of the high yield bond market tightened to a low of 253 basis points (bps) on November 12, a level that not only established a fresh cycle tight in this key metric but also measured near the narrowest observed level in the history of the U.S. high yield bond market. Further, the month-ending spread of approximately 270 bps stood at half its long-run average, a testament to the market's belief that the near-term bias for the economy and corporate America is one of continued strength and positive momentum.

HIGH YIELD SPREADS HAVE TIGHTENED TO NEAR-RECORD LEVELS

High Yield Option-Adjusted Spreads



Data source: Bloomberg, L.P., NBER; Data as of 11/29/2024
Note: Monthly yield spread vs. 5-Year Treasury used for 1/1987 - 9/2000; Daily OAS used thereafter

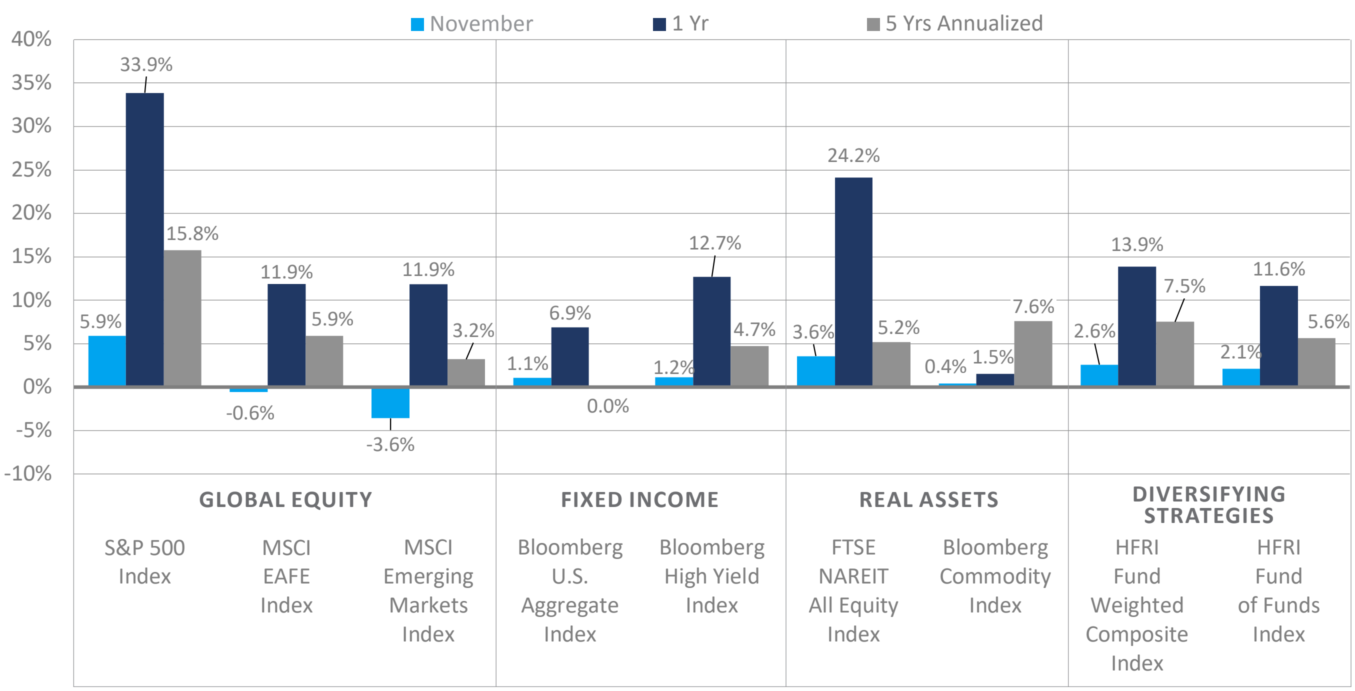
There is, however, a flipside to the well-grounded narrative of a market environment marked by a more significant degree of tailwinds than headwinds. A narrow implied path for future Federal Reserve (Fed) interest rate cuts in the coming quarters could apply an additional layer of incremental support for the U.S. dollar, further weighing on the relative performance between U.S. and non-U.S. financial market returns.

To conclude, while most major asset classes and sub-asset categories witnessed solid monthly total returns in November, the bid for risk assets remained concentrated within U.S. risk sectors. Both international developed and emerging market equities grappled with fundamental challenges, downward currency pressures versus the U.S. dollar, and the expectation for a material increase in tariffs. This could force corporate leaders and politicians alike to reimagine how best to position their respective interests in a second Trump administration.

MARKET SUMMARY

PERFORMANCE TAILWINDS CONTINUED

Total Returns for Key Assets and Markets



Data source: Lipper and Hedge Fund Research

GLOBAL EQUITY

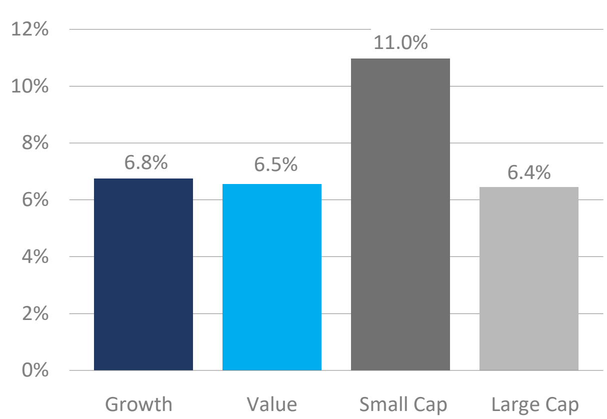
November was a dynamic month for global equity markets, with U.S. equities achieving notable gains, while performance in other regions showed mixed results. Along with the election, the strong U.S. dollar and investor sentiment played crucial roles in shaping market performance. Emerging markets faced challenges, including continuing economic struggles in China and fluctuating commodity prices. Overall, the month highlighted the interconnectedness of global markets and the impact of U.S. political developments on global investor sentiment.

The S&P 500 logged its highest intraday return of the year on November 6. After the election, small cap stocks delivered an impressive double-digit gain following a sharp beta rally. This surge aligns with historical trends, showing that small cap stocks often outperform large cap stocks after the Federal Reserve implements an initial rate cut.

In Japanese equity markets, the TOPIX Total Return Index ended the month down slightly by 0.5% in yen terms, while the Nikkei 225 fell 2.2%. The initial optimism that followed the U.S. election was tempered by concerns over potential tariffs and trade restrictions, particularly those affecting export-intensive industries such as autos and technology. The yen experienced higher-than-usual volatility, initially depreciating but later reversing course against the U.S. dollar as expectations of further rate hikes by the Bank of Japan rose. Supported by the stronger yen and expectations of increasing net interest margins, financial stocks, especially banks, performed relatively well.

SMALL CAP STOCKS SURGED IN RESPONSE TO ELECTION RESULTS

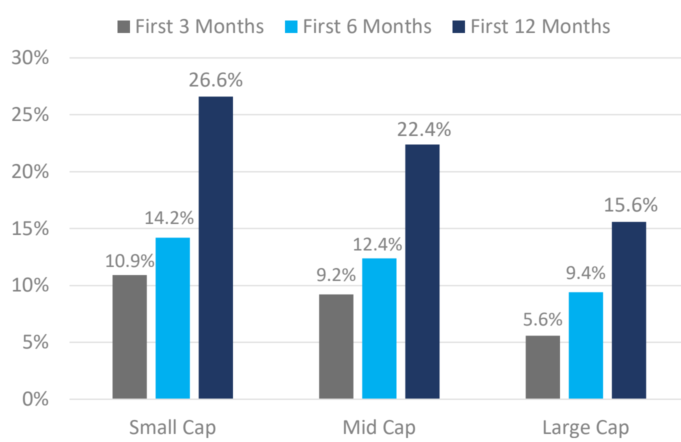
U.S. Equity Returns - November 2024



Source: FTSE Russell

RATE CUTS HISTORICALLY BENEFIT SMALL CAPS

Performance by Market Capitalization



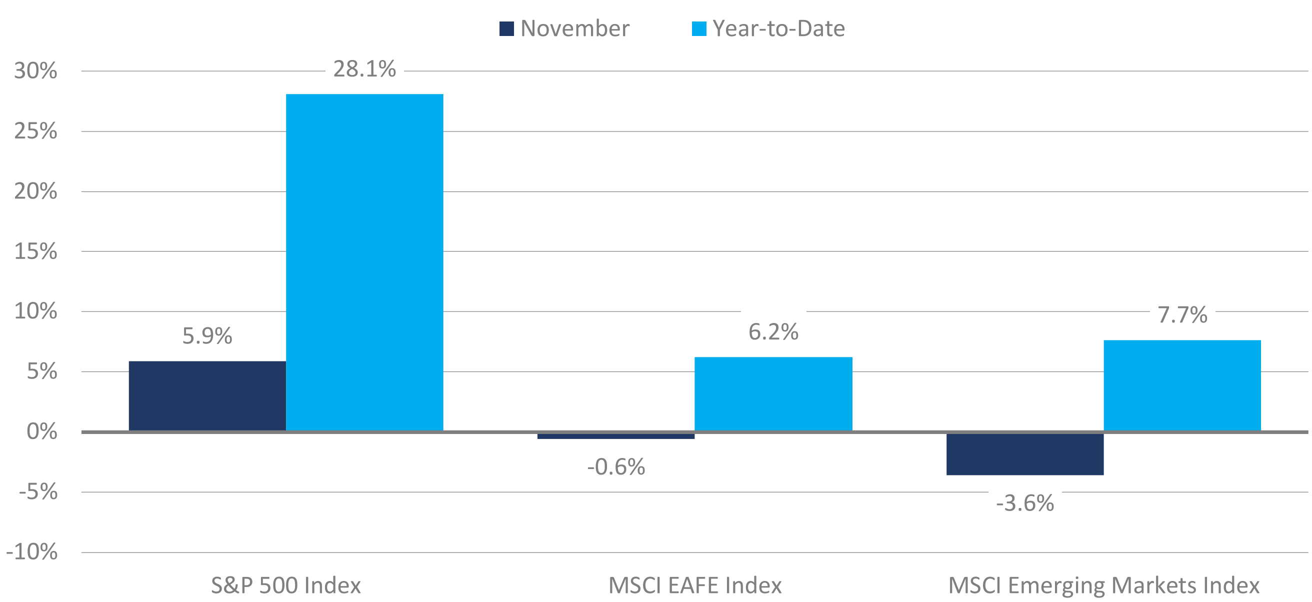
Source: Federal Reserve, Haver Analytics, FactSet

In the UK, domestically focused equities saw gains, recouping some losses from the previous month. The stabilization of long-term government borrowing costs and the Bank of England's decision to cut the Bank Rate by 25 bps contributed to the positive performance. The UK has experienced recent gains in GDP and equity performance, but the country is still recovering from fiscal spending cuts, Brexit, and the COVID-19 pandemic. In Europe, sectors like information technology and communication services performed well, while materials and consumer staples lagged. Economic data from the euro zone indicated continued weakness as the Composite Purchasing Managers Index (PMI) fell to a 10-month low.

Emerging markets faced significant headwinds during the month, leading to underperformance compared to developed markets. The MSCI Emerging Markets Index fell by 3.6%, reflecting concerns over restrictive trade policies expressed by President-elect Trump. China's uneven economic recovery, particularly in the real estate sector, hindered market performance. Additionally, fluctuations in commodity prices, especially oil, impacted commodity-exporting countries. The strong U.S. dollar exacerbated financial strains as dollar-denominated debt became more expensive for emerging markets borrowers. Despite these challenges, some sectors, such as technology, showed resilience amid the broader market downturn.

CONTINUED STRENGTH IN U.S. EQUITY MARKETS

Global Equity Markets Total Return



Data sources: S&P and MSCI

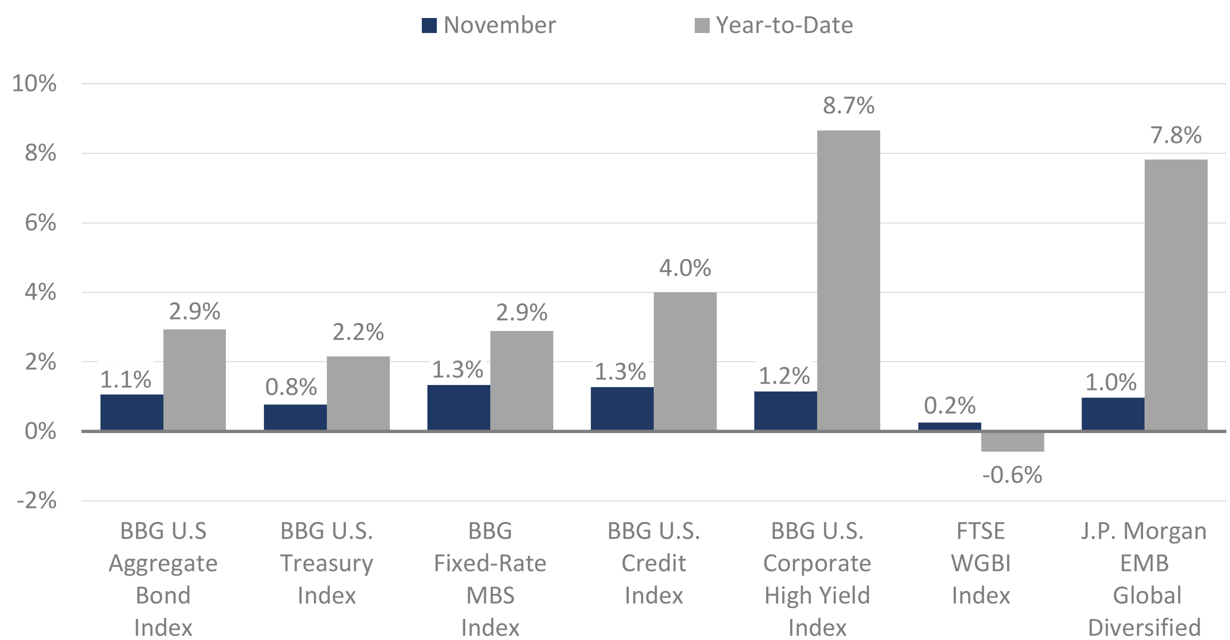
FIXED INCOME

U.S. interest rates ended in November roughly where they began, though they were volatile during the intra-month. The 10-year Treasury yield finished the month at 4.13% but peaked at 4.37% in mid-November as inflation concerns met pro-growth policy expectations. Trump's nomination of Scott Bessent for Treasury Secretary, considered a market-friendly voice on economic policy and tariffs, rallied rates. The yield curve flattened, with the 10s/2s spread ending the month at only 0.05%.

The market-implied probability of a 25 bp rate cut by the Fed at its December meeting rose to nearly 90% following guidance from multiple officials. Fed Governor Chris Waller noted that he believes policy is still restrictive, while New York Fed President John Williams expressed confidence in inflation moving lower and suggested moving policy to be more neutral over time. Despite inflation exceeding their 2% target, a December cut was widely anticipated.

BONDS ON TRACK FOR POSITIVE 2024 RETURNS

Fixed Income Index Returns

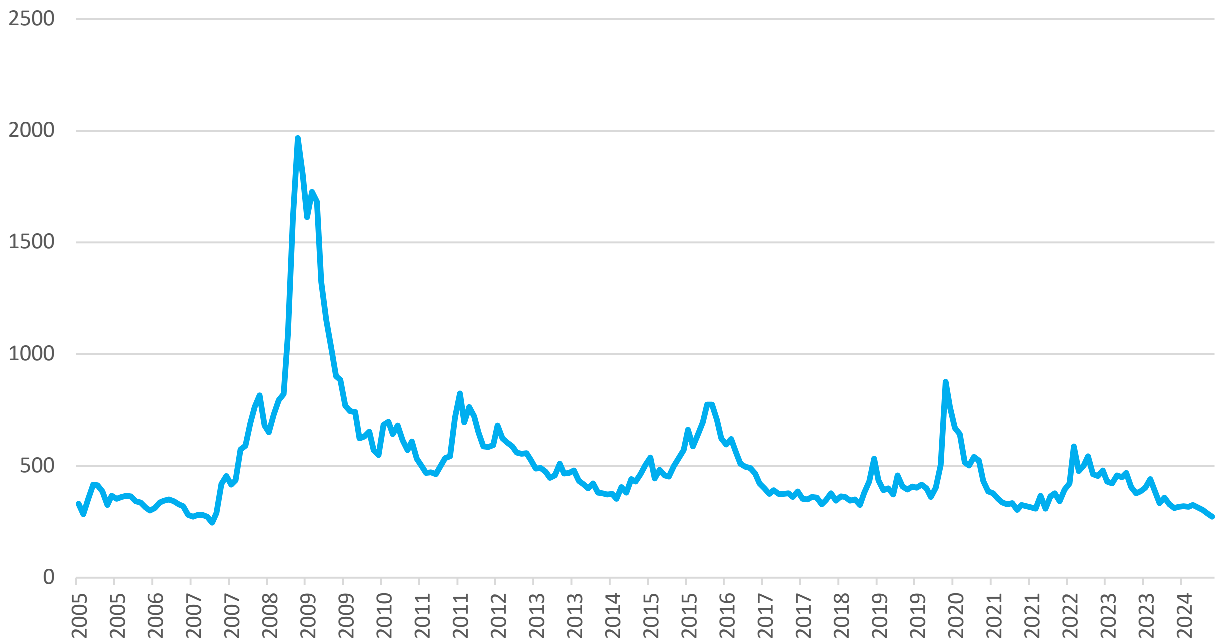


Data source: Lipper

Credit spreads tightened to near a post-global financial crisis record after the election. Investment grade (IG) spreads ended the month at 0.83%, while high yield spreads ended the month at 2.74% and fell below 2.60% mid-month. Credit rallied across the high-yield rating spectrum (i.e., BB, B, CCC) in what was an overall risk-on period for the market. While the quality of the high-yield market has been fundamentally strong relative to history, valuations have been unattractive, given the tightness of spreads. Nevertheless, investor appetite for credit remained strong even as issuance stayed elevated.

SPREADS NEAR RECORD LOWS

High Yield Option-Adjusted Spread (bps)



Data source: Lipper

REAL ASSETS

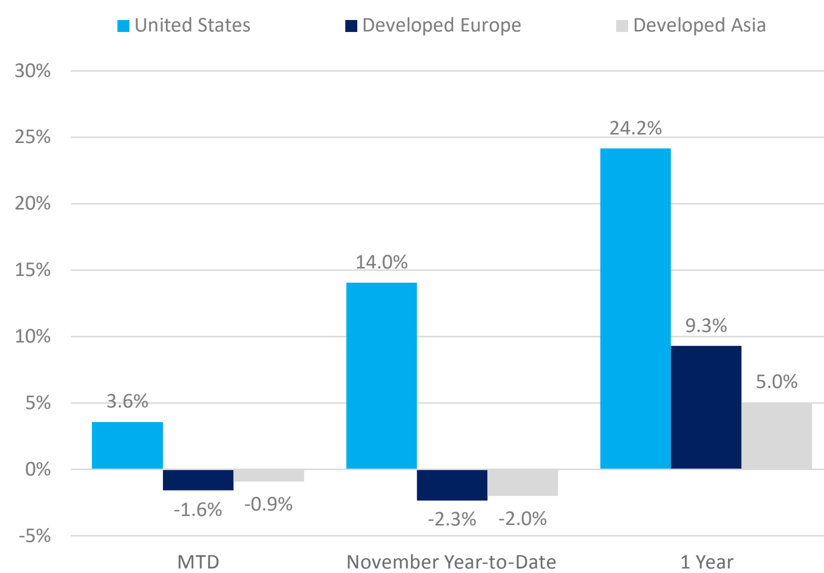
REAL ESTATE

U.S. Real Estate Investment Trusts (REITs) regained some lost ground in November. However, performance for the fourth quarter through November remained subdued as the end of the year approached. Global REITs have continued to underperform their U.S. counterparts, primarily driven by weakness in developed European and Asian markets.

Most property sectors have delivered positive returns year-to-date. Industrial REITs are the notable exception, as they faced headwinds from an oversupply of new developments, with construction completions exceeding net absorption levels. In contrast, the office sector has achieved an impressive year-to-date and trailing one-year recovery, even as vacancy rates remain at record highs.

EUROPEAN AND ASIAN MARKETS LAG U.S. REAL ESTATE

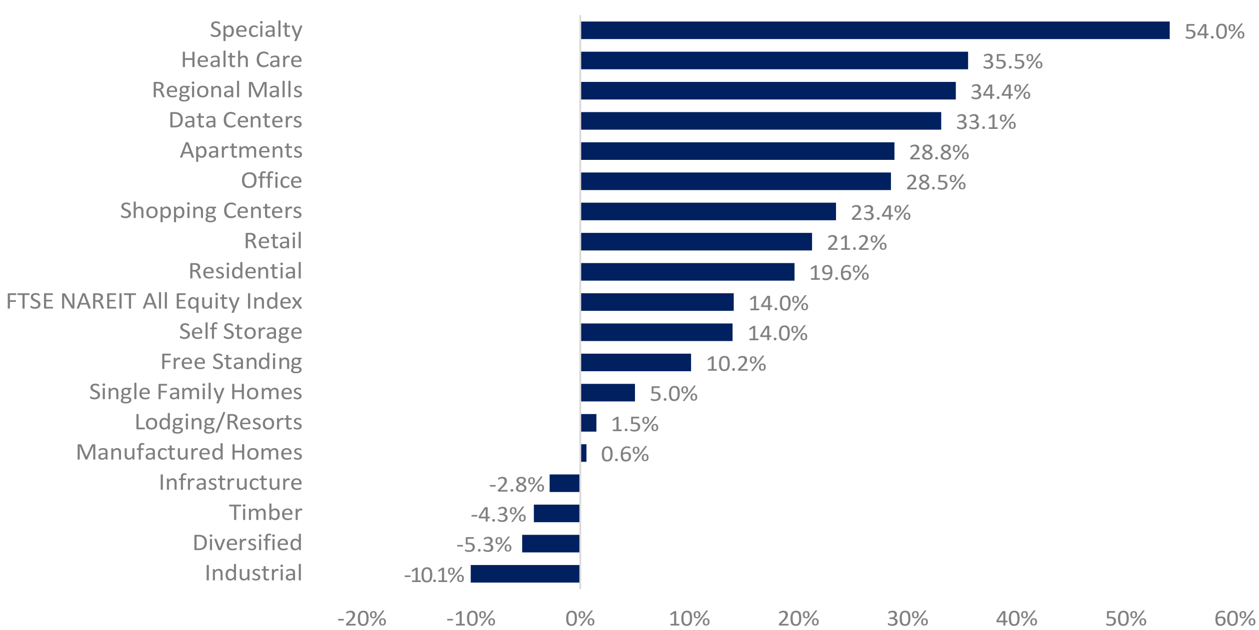
Trailing REIT Performance by Geography



Data source: FactSet

OFFICE REIT SECTOR AMONG TOP SECTORS DESPITE RECORD VACANCIES

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



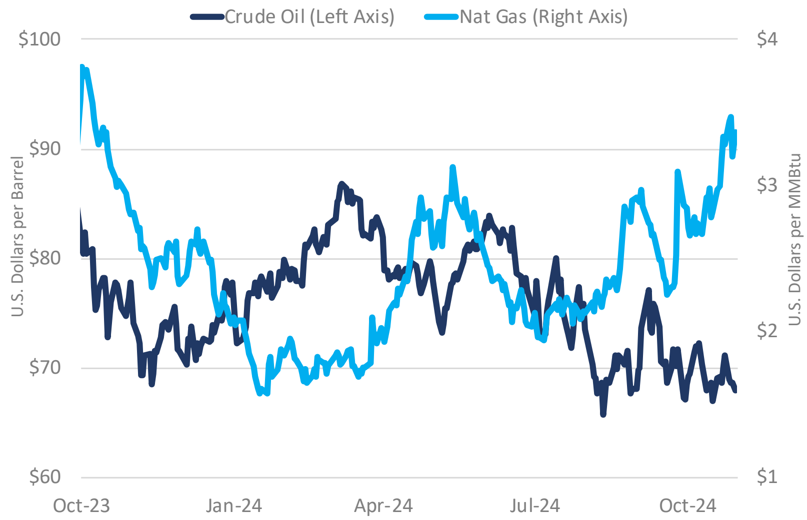
Data source: FactSet

NATURAL RESOURCES

Crude oil prices remained rangebound in November, with the West Texas Intermediate (WTI) Continuous Contract closing the month at around $68 per barrel. In early December, OPEC+ announced their decision to delay the initiation of oil production increases until April 2025 and extend the complete unwinding of output cuts an additional year, extending to the end of 2026, as the group seeks to address rising non-OPEC production. Meanwhile, natural gas prices experienced a significant increase of around 24%, as measured by the Henry Hub Continuous Contract, driven by forecasts of colder winter weather and producer production curtailments.

CRUDE OIL RANGE BOUND AMID SPARE CAPACITY AS NATURAL GAS JUMPS

Price of WTI Crude and U.S. Natural Gas



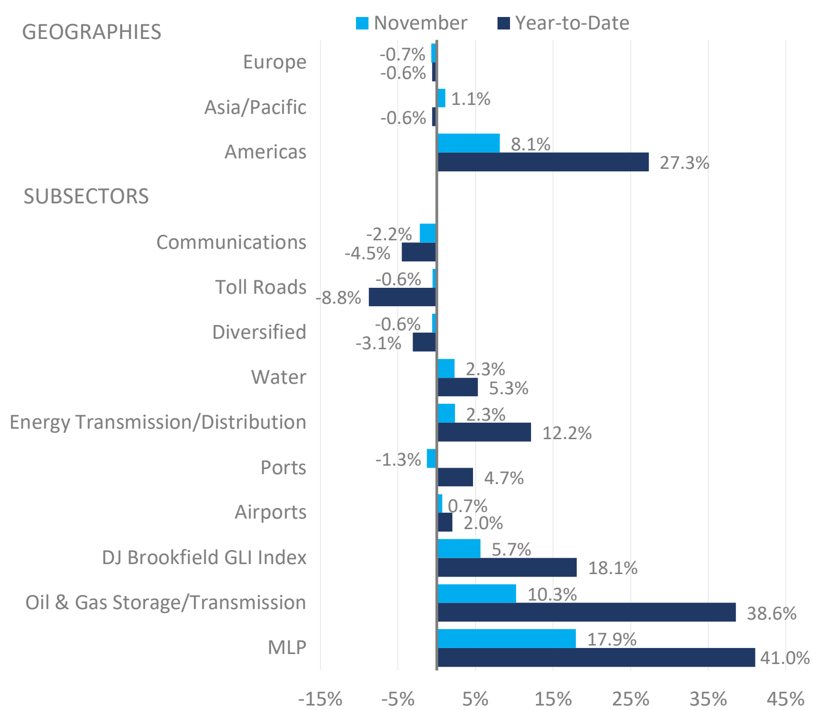
Data source: FactSet

INFRASTRUCTURE

In November, global listed infrastructure stocks rose by 5.22%, as measured by the Dow Jones Brookfield Global Infrastructure Index. The midstream energy sector has experienced an exceptional year, supported by robust oil prices that have fueled strong cash flows. This has enabled companies to adopt disciplined capital expenditure strategies and strengthen balance sheets by reducing leverage. Additionally, midstream energy was viewed as a beneficiary of the "Trump Trade" around the election, with the sector positioned to potentially gain from regulatory easing and more efficient project approvals under his administration.

MIDSTREAM ENERGY BENEFITS FROM AN EASING REGULATORY OUTLOOK

Listed Infrastructure Trailing Returns



Data source: FactSet

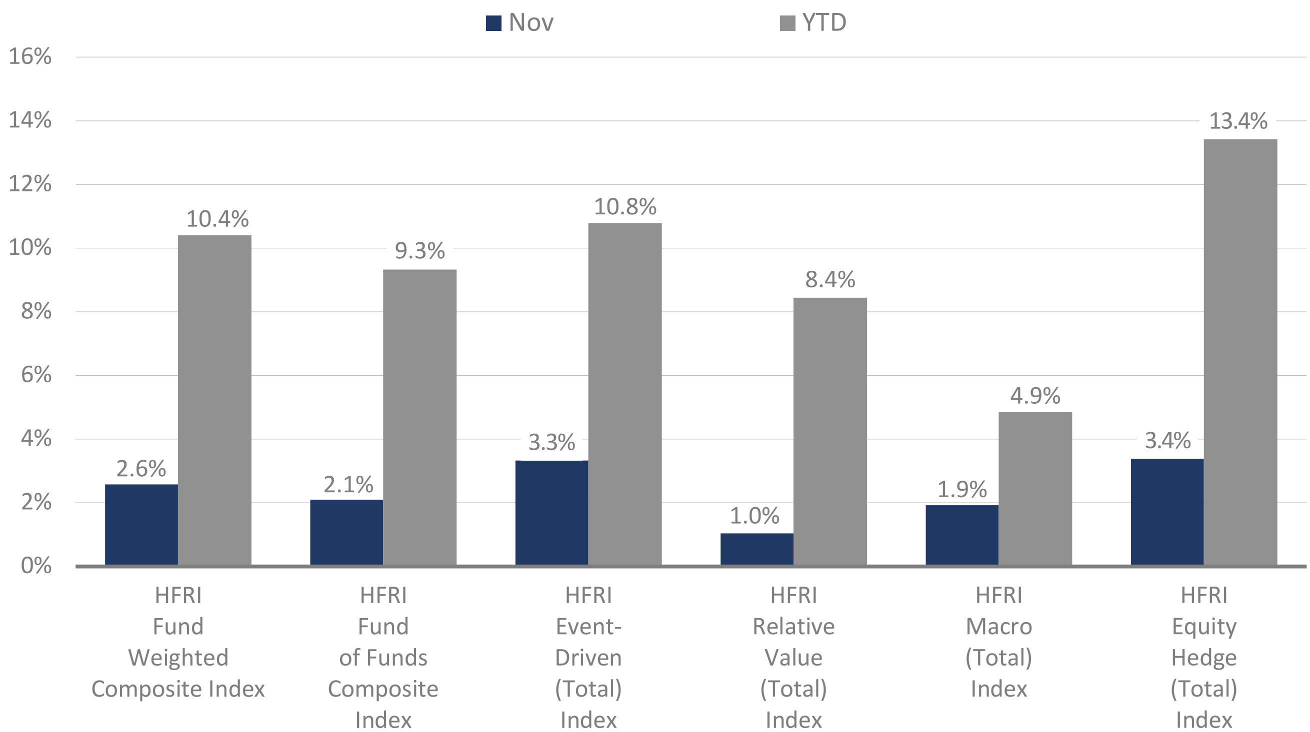
DIVERSIFYING STRATEGIES

Hedge funds surged in November following the election. Markets took the results as a strong tailwind to many hedge fund strategies, especially merger arbitrage. The new administration is anticipated to be much more business-friendly, allowing a significant backlog of deals to come to market.

Unsurprisingly, hedged equity and event-driven were the biggest beneficiaries. The more directional equity and event-driven strategies tended to outperform. Systematic trend-following strategies also generated gains, with extended trends across currencies, equities, and agricultural commodities. Longer-term trend-followers were able to exploit those trends more than shorter-term systematic macro. Funds did see some slight losses in energy and precious metals.

HEDGE FUNDS SURGE ON ELECTION OUTCOME

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.

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All data is as of November 30, 2024 unless otherwise noted.

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