ICR® 4th Quarter Newsletter – January 2025

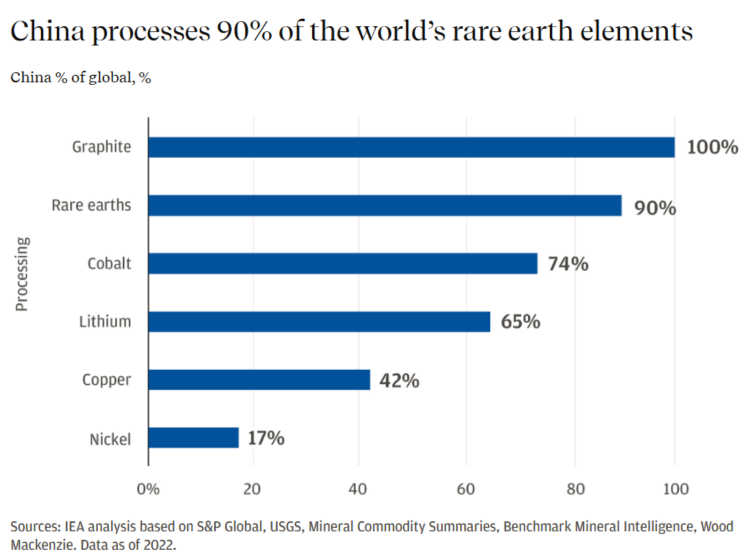
The final quarter of 2024 saw the S&P 500 advance a little over 2%, with most of the gains coming in the days surrounding the election. After that initial bounce, markets were choppy and drifted down a bit in the final weeks of the year. Small cap stocks lagged their larger counterparts, posting a flat performance for the quarter. Sector performance varied widely. The consumer discretionary sector finished up over 14% while the materials and health care sectors both lost over 10%.

Foreign stocks, as measured by the MSCI EAFE index for developed foreign markets, lost 8.4% while emerging markets stocks fell 8.2%, though still finishing the year up about 5%. After large gains in the first part of the year, gold finally registered a flat quarter, still finishing up almost 30% in 2024. The U.S. dollar appreciated substantially in the fourth quarter, particularly in reaction to the election results given the anticipated America-first trade policies of the incoming administration, which we'll get into later.

Despite the Federal Reserve cutting the federal funds rate by 25 basis points twice during the fourth quarter, longer term rates generally rose. The ten-year Treasury yield went from 3.79% to 4.58%, an indication that the markets may be worried about inflation rising again in the coming months. The annualized Consumer Price Index has remained at 3% or less since June, but recently ticked up to 2.9% from its low of 2.4% in September. The economy remains strong, with the unemployment rate still hovering around 4% and GDP growth around 3%, but those could be signals that the Fed doesn't need to continue cutting rates. The consensus had been for a methodical and extended rate-cutting campaign, but that forecast has become cloudy in light of recent data.

Of course, the biggest development during the fourth quarter was the election, which resulted in a supermajority for the Republican party for at least the next two years. In our last newsletter, we pointed out that politics generally only affect the markets at the margin, but a supermajority could potentially make political policy more impactful in this cycle. We're going to use this space to talk about what effects a second Trump administration might have on the economy and the markets.

First, tariffs have been a particularly contentious issue, with President Trump wielding them as a political tool and economists fearing that they will lead to another surge in inflation. Indeed, corporations do pass down the cost of tariffs to consumers, which leads to higher prices, but the exact impact will depend on the scope and breadth of the tariffs enacted. During his first administration, Trump levied tariffs and inflation remained subdued, but it sounds as though he plans significant increases from those levels – especially on China. What has changed somewhat in the last six years, is that China has established itself as a dominant force in parts of the supply chain for a number of industries, most critically technological hardware and rare earth elements, where it processes 90% of the world's supply. These are essential components in batteries and electric vehicles, so tariffs approaching 50% would have a dramatic impact in those industries.



Next, amid growing support for cutting wasteful government spending, Trump created the temporary Department of Government Efficiency, the leaders of which have vowed to cut trillions from the federal budget. If that were to happen, there would undoubtedly be economic pain in the short run. Even wasteful government spending still has a net stimulative effect on the economy, and cutting that dramatically would likely reduce short-term economic growth. In the long run, perhaps it would lead to more growth if resources are allocated more efficiently (though that's a huge "if"). We have our doubts that anything close to the kind of cuts that have been promised will come to fruition for a couple of reasons. First, Trump uses the economy and the stock market as a scoreboard and if drastic spending cuts start to reflect negatively on his presidency, it seems likely that he would pull the plug on further cuts. Second, there is a natural tendency for those in charge – no matter their political party – to still spend more in those areas that they deem important.

Finally, given his outspoken criticism of Fed Chair Jerome Powell, there is growing speculation that Trump will try to pressure him out of the office so that he can appoint a yes-man to the position. When asked whether he would resign if requested by the president, Powell emphatically said he would not and pointed out that it is "not permitted under the law" for the president to fire or demote him. But, if Trump finds a way to force Powell out before his term ends in May 2026, that could bring enormous uncertainty to the markets. For as much second-guessing as Powell has faced, his tenure as Fed Chair is now largely viewed as successful in bringing inflation down without sending the economy into a recession. Plus, the markets tend to favor the devil they know over one they don't, and a Trump appointee could be viewed as a wild card. While Trump originally appointed Powell during his first term, his thoughts on the role of the Federal Reserve and how it should be run seem to have shifted tremendously since then.

These are just a few items to keep an eye on, but the most important thing is to focus on your long-term goals and to have an investment plan that you can stick to. Whether the shifting political and economic environments prove to be headwinds or tailwinds, we're committed to constructing portfolios that are resilient and build long-term wealth for our clients.

Feel free to reach out with any questions or concerns you have and, as always, thank you for your support and the opportunity to serve you.

Sincerely,

James A. Heine James L. Cobb

Market Report (as of 12/31/24)

Index	**2024 (%)**	**3-Year Annualized (%)**	**5-Year Annualized (%)**
S&P 500	23.3	7.3	12.7
Dow Jones Industrial Average	12.9	5.4	8.3
U.S. Aggregate Bond Index	1.3	-2.4	-0.3
MSCI EAFE (Foreign Index)	1.2	-1.1	2.1