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Retirement Market Recap

CALMER TIDES

Will lowering rates result in a wave of higher stock prices?

While the equity market continued to rally in the first half of 2024, fixed-income markets struggled to gain ground amid choppy, volatile trading. However, the third quarter of 2024 finally gave bond investors room to breathe a massive sigh of relief as the rally they desperately needed took hold, with the Bloomberg US Aggregate Bond Index gaining 5.20%.[1] At the September Federal Open Market Committee meeting the Federal Reserve (the Fed) announced an aggressive, 50-basis-point interest rate cut, citing favorable economic data with a trendline of moderate, but not sweltering, growth.

Despite the prospect of additional cuts from the Fed (generally seen as a favorable outcome for financial markets), it is difficult to ignore the non-economic drivers moving behind the scenes in 2024; a historically contentious U.S. election, elections in over 50 countries and the most heightened period of geopolitical instability since the Cold War. As a result, alternative safe havens such as gold have experienced historically strong performance year-to-date.

The equity market remained resilient in Q3, extending this year's gains with the S&P 500 advancing 5.89% despite a short-lived but aggressive sell-off in early August. While large cap equities continue to be one of the top-performing asset classes the last two years, Q3 saw a shift down the market capitalization spectrum, with the Russell 2000 Total Return Index (small cap gaining 9.27% during the quarter and over 10% in July.[2] International equities continued their strong performance, with the MSCI EAFE gaining 7.26% and the MSCI Emerging Markets gaining 8.72%.

Emerging markets, an asset class that has proven difficult for many investors in the previous decade, provided a welcomed diversifying return stream for portfolios, many of which are overweight U.S. large cap growth technology stocks. For example, in September the MSCI Emerging Markets Index outperformed other major equity indices by well over 4.50%. The index is up 16.86% in 2024 and expectations for the asset class remain positive. Elijah Oliveros-Rosen of S&P Global anticipates, "monetary policy easing in the United States to positively impact emerging markets especially those with strong economic growth fundamentals like Brazil and Vietnam."[3]

Fixed income markets had a notably positive quarter to coincide with equities. As mentioned, the Bloomberg U.S. Aggregate Bond Index gained over 5% for the quarter, driven by the dovish shift in the Fed's guidance, capped off by the first of what may be several interest rate cuts this year.

In previous quarters, high-yield bonds have been the highlight of investors' fixed-income exposure, primarily driven by such bonds' higher sensitivity to equity markets. But in Q3, long-duration, high-grade bonds shined with the anticipation and announcement of rate cuts. The Bloomberg Long Term Treasury Index (Bloomberg US Long Government/Credit Index), which measures U.S. government debt with more than 10 years to maturity, gained 7.82% on the quarter and is up 15.43% since this period last year.

2024 has seen strong performance in various asset classes coupled with the prospect of lower interest rates, but the political and global landscape continues to be uneasy and top of mind. The trend of identity politics has led many Americans to fear a severe market pullback if their favored candidate does not win. However, as Eshe Day of *Bloomberg* explains, "Election years have generally been good for the U.S. stock market. The S&P 500 Index has risen in almost every election year since 1960. The exceptions were 2000 and 2008, which were marred by the dotcom bust and the great financial crisis, respectively. The record looks even better for recent election cycles. In the three election years since 2008 — 2012, 2016, 2020 — the benchmark index rose at least 10%."[4]

[1] All index performance figures attributable to YCharts.
[2] YCharts. Russell 2000 Total Return Index Fundamental Chart.
[3] Oliveros-Rosen, Elijah. "Emerging markets Q4 economic outlook". *CNBC*. Web. Retrieved from https://www.cnbcafrica.com/media/6362549582112/emerging-markets-q4-economic-outlook-/
[4] Day, Eshe. "Here's What the Trump-Harris Showdown Means for Stocks." *Bloomberg*. https://www.bloomberg.com/news/articles/2024-09-09/harris-vs-trump-how-the-2024-presidential-race-impacts-the-us-stock-market

Statistics are attributed to Morningstar.

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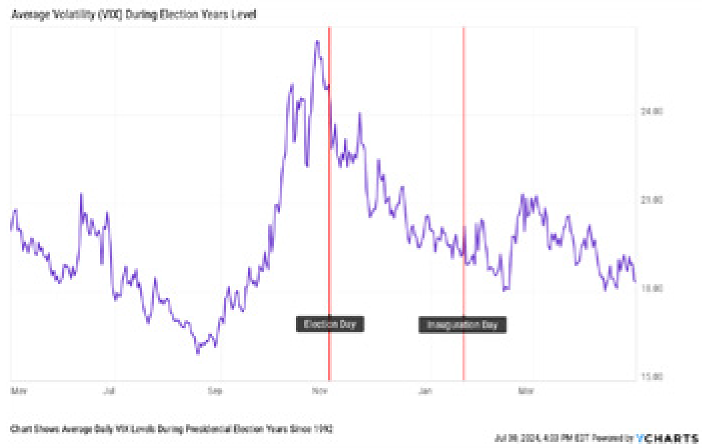
Given the uncertainty leading up to an election, it is unsurprising that volatility increases. However, average volatility (measured by the VIX) tends to decline after Election Day through the lame duck/transition period, as seen in Figure 1.[5] With today's unstable geopolitical climate, unforeseen geopolitical events may lead to spikes in volatility.

Within the geopolitical environment, it is difficult to ignore the potential widening of conflicts in the Middle East and Eastern Europe. Recent escalations have had an extreme humanitarian impact, but it is difficult to quantify the effect of geopolitical events on markets. Research conducted by JPMorgan Private Bank of 80+ years of data found, "Geopolitical events usually have no lasting impact on large cap equity returns. However, geopolitics can have profound market impacts at the local level."[6]

While events themselves may have little lasting impact on large-cap equity returns, the snowball effect of geopolitical shocks can occur, leading to environments that are unfavorable for capital markets, such as a world with reduced globalization marred by widespread political instability. This is a concern for investors, as seen by the flight to gold in recent months. Gold, an asset that is often seen as a hedge to geo and political instability, has performed very well in 2024, gaining over 28% YTD and reaching a record high price of $2,685 per troy ounce on Sept. 26.[7] It is reasonable to think gold will continue to perform well if a further divide between the Western nations and BRICS+ nations develops.

As the third quarter of 2024 ends, the long-awaited first interest rate cut by the Fed has come at last. The prospect of further rate cuts should continue to provide rising tides for various asset classes, notwithstanding a faster-than-expected softening of the economy. Despite the possibility of consecutive years 20% gains for the S&P 500, non-economic data and factors will continue to play a disproportionate role in shaping the last quarter of 2024. However, with what appears to be a clear trendline of declining inflation, the Fed may have effectively succeeded in a soft landing.

FIGURE 1



[5] "How Do Presidential Elections Impact the Market?" *YCharts*. https://go.ycharts.com/hubfs/How_Do_Presidential_Elections_Impact_the_Market/Election_Guide.pdf
[6] "How do Geopolitical Shocks Affect Markets?" *JPMorgan Private Bank*. Web. Retrieved from https://privatebank.jpmorgan.com/nam/en/insights/markets-and-investing/how-do-geopolitical-shocks-impact-markets
[7] *YCharts*. Gold Fundamental Chart.

EQUITY AND RETIREMENT INDICES	3 MO	YTD	1 YR	3 YR	5 YR	10 YR
S&P 500 TR USD	5.89%	22.08%	36.35%	11.91%	15.98%	13.38%
Russell 3000 TR USD (Broad Market)	6.23%	20.63%	35.19%	10.29%	15.26%	12.83%
Russell 1000 TR USD (Large Cap)	6.08%	21.18%	35.68%	10.83%	15.64%	13.10%
Russell Midcap TR USD	9.21%	14.63%	29.33%	5.75%	11.39%	10.19%
Russell 2000 TR USD (Small Cap)	9.27%	11.17%	26.76%	1.84%	9.39%	8.78%
MSCI EAFE NR USD (Int'l Equity)	7.26%	12.99%	24.77%	5.48%	8.20%	5.71%
MSCI Emerging Markets NR USD (E.M. Equity)	8.72%	16.86%	26.05%	0.40%	5.75%	4.02%
S&P United States REIT TR USD (Real Estate)	16.09%	15.69%	34.24%	5.04%	5.49%	7.66%
Morningstar Lifetime Mod. TR 2020	6.18%	9.88%	19.61%	1.79%	5.51%	5.54%
Morningstar Lifetime Mod. TR 2040	7.21%	14.06%	26.49%	4.80%	8.91%	7.94%

FIXED INCOME INDICES	3 MO	YTD	1 YR	3 YR	5 YR	10 YR
ICE BofA 3M US Trsy Note TR USD	1.31%	3.96%	5.39%	3.49%	2.34%	1.67%
ICE BofA 1-3YR US Trsy TR USD	7.82%	2.42%	15.43%	-8.36%	-4.28%	1.09%
BBgBarclays Long Term US Trsy TR USD	-1.81%	-5.01%	-5.61%	-10.49%	-4.26%	0.60%
BBgBarclays US Aggregate Bond TR USD	5.20%	4.45%	11.57%	-1.39%	0.33%	1.84%
BBgBarclays US Treasury US TIPS TR USD	2.48%	4.80%	7.53%	2.55%	3.60%	2.42%
BBgBarclays High Yield Corp TR USD	5.28%	8.00%	15.73%	3.10%	4.72%	5.04%
BBgBarclays Global Aggregate TR USD (Global Bond)	6.98%	3.60%	11.99%	-3.06%	-0.83%	0.57%

ICE BofAML – Intercontinental Exchange Bank of America Merrill Lynch; BBgBarc – Bloomberg Barclays; S&P 500 – Standard & Poors; MSCI – Morgan Stanley Capital International
Sources: Morningstar as of Sept. 30, 2024

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