Convergence Commentary
December 2024 Market Recap

Quick Hits:

- Federal Reserve adjusts 2025 guidance
- Stocks digest a higher interest rate outlook
- A look at the Santa Claus rally

Market-Moving Highlights

A narrow stock market rally throughout the first half of December turned into a broad-based selloff to end the year.

The action was sparked in large part by a hawkish outlook from the Federal Reserve following their mid-December decision to cut interest rates by another 0.25%. Every quarter, the FOMC (the Fed's interest rate decision-making body) publishes a Summary of Economic Projections (SEP) that details members' expectations. Back in September, when the Fed was just kicking off the easing cycle, most officials believed inflation was well on its way to their 2% annual target. After a resurgent labor market and stubbornly high inflation readings over the past few months, though, they've lost some confidence. With inflation stubbornly hanging above target, there's no longer much impetus for further easing in the near term.

That's what's being reflected in the market now. After the Fed's first interest rate cut in September, futures markets implied an expected policy rate below 3% by the end of this year. Today, consensus expectations are for a policy rate nearer to 4%.

Index Performance

Index	1 Month	2024 Return	5 Year
S&P 500	-2.63%	25.02%	14.31%
Nasdaq Composite	-0.41%	29.57%	17.15%
Russell 2000	-8.25%	11.54%	7.42%
MSCI ACWI ex US	-2.17%	5.53%	3.95%
Bloomberg US Aggregate Bond	-1.70%	1.25%	-0.32%

The reset in rate cut expectations hit small cap stocks the hardest. After leading the market higher in November, the Russell 2000 index dropped more than 8% in December. That trimmed calendar year gains for the small caps to 11.5% - less than half of the gain experienced by large cap indexes like the S&P 500 (+25%) and NASDAQ Composite (+29.6%).

Still, that double-digit pace of growth for the Russell 2000 was much healthier than what happened outside the United States in 2024. Pressured by lackluster economic growth and widespread political uncertainty, international stocks rose just 5.5% for the year.

Even worse were bonds, where returns continue to be hampered by rising interest rates.

S&P 500 Sector Highlights & Commentary

Best-Performing Sectors		Worst-Performing Sectors	
Communication Services	2.0%	Materials	-10.7%
Consumer Discretionary	1.3%	Energy	-8.8%
Information Technology	0.1%	Real Estate	-7.8%

Just 3 of the 11 S&P 500 sectors closed higher in December. The Communication Services, Consumer Discretionary, and Information Technology are home to each of the mega cap growth stocks that dominated the market in 2024, known colloquially as the ‘Magnificent 7’. That group was especially strong during the first few weeks of the month, when they were driving the indexes to new all-time highs.

On the flip side, shifting Fed policy caused interest rates to rise and the US Dollar to strengthen. Rising rates pushed Real Estate stocks down nearly 8% and erased close to all of that sector’s 2024 gains. Dollar strength, meanwhile, was a headwind for the two sectors most exposed to commodity prices: Materials and Energy.

What to Watch in January

Click here to read our reference guide for economic indicators.

1/10 – BLS Jobs Report - December
In November, the US economy added an impressive 227,000 jobs. That followed an unusually weak October that was marred by temporary factors like labor strikes and severe weather. This latest update on the employment situation will give us insights into how sustainable November's bounce back was.

1/15 – Consumer Price Index - December
Progress on price inflation stalled in the back half of 2024, and that's a big reason the Fed was forced to adjust their policy outlook for 2025. In November, headline CPI index rose to 2.7% year-over-year, up from the prior month's 2.6% reading. Core CPI, which tends to be a better measure of future prices, held steady at 3.3%. Both are hanging above the Fed's 2% annual inflation target. On the bright side, shelter inflation in November fell to the lowest level in several years.

1/16 – Retail Sales – December
Retail sales are what keep the US economy churning, and no time is more important for retail sales than the holidays. November sales were healthy, if not awe-inspiring, but the homestretch of the holiday season is where the rubber meets the road. Given widespread concerns about affordability issues and the health of consumer balance sheets, this report is one to keep a close eye on.

1/29 – FOMC Interest Rate Decision
The Federal Reserve is unlikely to cut interest rates again this month and they won't be updating their economic outlook again until March. However, Fed Chair Jerome Powell will still have plenty of time to adjust forward guidance at his post-meeting press conference.

1/30 – GDP – Q4
Just one day after the Fed decision, the Bureau of Economic Analysis will provide a first estimate of how economic activity fared in the final quarter of 2024. GDP isn't the most timely of economic measures, but it is the broadest.

Market Wrap

The ‘Santa Claus rally’ is a phenomenon documented by Yale Hirsch in his 1972 edition of the Stock Trader’s Almanac. Media pundits often dilute the meaning of the Santa Claus rally to include the entire month of December, but Hirsch’s observation was more specific: he looked at a 7-day period that included the final 5 trading days of one year and the first 2 trading days of the next. What he found was that returns during that 7-day stretch were far better than average.

The stock market is full of historical anomalies like that, but they have a tendency to vanish as soon as they garner widespread attention. The magic of Christmas, however, is harder to kill. In the 50-plus years since Hirsch’s initial publication, S&P 500 returns during the Santa Claus period have been nearly 5x an average 7-day stretch.

S&P 500 Since 1972		
	Santa Claus Periods	Average 7-Day Period
Average Return	1.21%	0.25%
% Positive	75%	57%

It’s good information to have, and sometimes even better information comes from when the market doesn’t follow those seasonal tendencies.

If Santa Claus should fail to call, bears may come to Broad and Wall.

That warning has proved especially true since the turn of the century: Since the year 2000, market returns have been negative more often than not following a negative Santa Claus period.

Sources

Bureau of Economic Analysis
Bureau of Labor Statistics
Census Bureau
BlackRock
Market performance data sourced from Bloomberg Finance L.P.

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