Solid Economic Growth and Rate Cuts Power Stocks to an Historic Return

The S&P 500 rose to an all-time high in the fourth quarter and extended 2024 gains as the election results raised expectations for tax cuts and other pro-growth policies in 2025, while the economy remained on solid footing and the Fed continued to cut interest rates. The S&P 500 logged a modestly positive return for the fourth quarter and an annual return greater than 20% for the second straight year.

While the fourth quarter was positive for most of the market, it didn’t start that way as anxiety over the election and an increased focus on the fiscal state of the U.S. weighed on sentiment in October. Presidential polls tightened materially in October and left the race too close to call, increasing political and policy uncertainty. Additionally, much of the financial media’s focus in October was on the potentially negative fiscal consequences of both candidates’ policies. Specifically, a Wall Street Journal article focused on possible large future increases in the deficit and national debt that could cripple future economic growth. Those fiscal concerns, along with stronger-than-expected economic data, pushed Treasury yields higher and the 10-year Treasury yield rose from 3.75% at the start of October to over 4.20% by Halloween. That rise in yields combined with political and policy uncertainty pressured stocks and the S&P 500 finished October with a modest decline, falling 0.91%.

Those headwinds on stocks were short-lived, however, as Donald Trump convincingly won re-election while Republicans took control of both houses of Congress, completing a “Red Sweep.” Reminiscent of 2016, the Trump and Republican victories proved to be bullish catalysts as investors embraced the idea of future tax cuts, deregulation, and a pro-business administration. That helped the S&P 500 rise above 6,000 for the first time. Shortly following the election, however, investors were reminded of the volatile nature of a Trump presidency, as the president-elect nominated several unorthodox supporters to prominent cabinet positions. These surprises caused investors to contemplate policy risks to the pro-growth agenda and stocks dipped mid-month. However, the withdrawal of Attorney General nominee Matt Gaetz and the nomination of Scott Bessent as Treasury Secretary helped to calm investor nerves about the president-elect’s cabinet and stocks resumed their rally in late November and closed the month near all-time highs.

In December, renewed focus on the potential economic benefits of an incoming Trump administration combined with the "Goldilocks" economic environment of solid growth and continued Fed rate cuts to send the S&P 500 to yet another all-time high near 6,100. However, that rally stalled mid-month as President-elect Trump doubled down on his support for other unorthodox cabinet nominations and lobbed tariff threats at major trade partners including Canada, Mexico and China. Market volatility increased as the Federal Reserve cut interest rates at the December meeting but also reduced the number of expected cuts in 2025 to just two (from four). That sparked a sharp selloff in stocks that continued into year-end, causing the S&P 500 to finish slightly negative for the month, but well off the highs.

In sum, 2024 was a very strong year for the broad markets as the Fed seemingly achieved a soft economic landing and aggressively cut interest rates, while foreign and domestic political risks and drama failed to derail the rally.

Q1 and 2025 Market Outlook

Markets begin 2025 with great expectations as anticipation of tax cuts and pro-business deregulation, a continued economic soft landing and ongoing Fed rate cuts helped propel stocks higher throughout 2024 and the S&P 500 completed the best two-year run since the late 1990's.

Starting with politics, investors are eagerly awaiting the implementation of pro-growth policies from the Republican Congress and Trump administration, which includes an extension of the 2016 Tax Cuts and Jobs Act and possible additional corporate and personal tax cuts, along with sweeping deregulation. If executed, those policies should result in increased corporate earnings, personal incomes, and spending (all of which are positive for stocks).

On growth, the Federal Reserve appears to have achieved the elusive economic soft landing, as economic activity is solid, unemployment is historically low, and inflation has declined substantially. That allowed the Federal Reserve to aggressively cut interest rates in 2024 and investors expect rate cuts to continue in 2025 and to further support continued economic growth.

Finally, geopolitical tensions remained high in 2024 but investors finished the year with hopes for progress on ceasefire agreements between Israel and its antagonists (Hamas and Hezbollah) and between Russia and Ukraine.

And, if all these expectations are realized, we should all expect another strong year of returns in the markets.

However, as we all know, nothing in the markets is guaranteed and while the outlook is positive as we begin 2025, there are significant risks to the outlook we must acknowledge.

Politically, Republicans hold small majorities in the House and Senate and large, complicated tax cut bills could easily be delayed (or derailed). Additionally, while investors have focused on potential positives of pro-growth policies, increased trade tensions and possible tariffs could create unanticipated market and economic headwinds.

On growth, the economy remains in a "sweet spot" with solid, but not spectacular, growth and the Fed can claim a soft landing has been achieved. However, growth can still slow as rates remain historically high and elevated stock valuations imply complacency in the markets regarding the possibility of an economic slowdown.

Geopolitically, while hope for progress on resolution of major global conflicts is high, nothing is guaranteed, and the possibility exists that both conflicts spread in 2025.

Finally, global bond markets are expected to have a bigger influence on stock returns in 2025 and if bond investors think aggressive tax cuts or fiscal spending will dramatically increase the deficit or national debt, bond yields will likely rise and present a headwind on stocks (as we saw in 2022).

Bottom line, while the outlook for markets is positive as we start the year, we won't allow that to create a sense of complacency because as the past several years have shown, markets and the economy don't always perform according to Wall Street's expectations.

As such, while we are prepared for the positive outcome currently expected by investors, we are also focused on managing both risk and return potential because the past several years demonstrated that a well-planned, long-term focused and diversified financial plan has the potential to withstand virtually any market surprise and related bout of volatility, including multi-decade highs in inflation, historic Fed rate hikes, and geopolitical unrest.

At ACM, we understand the opportunities and risks facing both the markets and the economy, and we are committed to helping you effectively navigate this challenging investment environment. Successful investing is a marathon, not a sprint, and even intense volatility is unlikely to alter a diversified approach set up to meet your long-term investment goals.

Therefore, it's critical for you to stay invested, remain patient, and stick to the plan, as we've worked with you to establish a personal allocation target based on your unique financial position, risk tolerance, and investment timeline.

We thank you for your ongoing confidence and trust and please rest assured that our entire team will remain dedicated to helping you successfully navigate this market environment.

Please do not hesitate to contact us with any questions, comments, or to schedule a portfolio review.

Sincerely,

Laura N. Christofferson, CFP®, CDFA®

Matthew B Wigren CFP® CIMA®

RAYMOND JAMES®

ALDEN CAPITAL MANAGEMENT LLC

An Independent Registered Investment Adviser

310-120th Avenue N.E. // Suite 200 // Bellevue, WA 98005 // 425-451-8508

AldenCapital@RaymondJames.com

WEBSITE EMAIL

Linked in