"An investment in knowledge pays the best interest"

~ Benjamin Franklin

As we turn the page on 2024 and enter a new year, the traditional Wall Street predictions for the year ahead are arriving in my inbox. Reflecting on all the scenarios put forward by my peers, I always remind myself that they each have a probability of occurring and that investing in the stock market is much like racing in the Tour de France. Both require careful training and planning, strategic thinking, and the ability to navigate unexpected challenges.

Training and preparation are critical: Professional cyclists undergo rigorous, structured training programs that typically begin at least seven months before the event, focusing on building endurance, strength, and specialized skills. These programs include altitude training camps to improve oxygen utilization, targeted interval training to enhance power output, and specific race simulations to prepare for the varied terrain. Proper preparation also involves meticulous attention to nutrition, recovery, and injury prevention. Without this comprehensive approach to training, riders would be unable to withstand the grueling 21-stage race, which pushes athletes to their absolute limits over thousands of miles.

Strategic adaptation to each stage: Cyclists face various terrains and weather conditions, similar to how investors must adapt to market fluctuations and economic changes. Both endeavors reward those who stay informed, make calculated decisions, and remain resilient in the face of setbacks.

Navigating the unexpected: Just as a cyclist must choose the right moments to push ahead or conserve energy, an investor must decide when to buy, hold, or sell stocks. The race is not won in a single sprint but through sustained effort, much like building a successful investment portfolio over time.

Ultimately, reaching the finish line or achieving financial goals requires patience, perseverance, and a willingness to learn from every twist and turn along the way.

Continued review and realignment with financial goals is critical. Proper diversification, asset allocation, and regular reviews can help safeguard your investments.

Our goal is always to provide you with innovative solutions adapted to the uncertainty of investing, guiding you through an optimal allocation according to your financial goals and risk tolerance. Now for my view on the topics affecting your investments.

A CIO's View

Movement in these areas is monitored daily by our models. We also regularly cover these topics in our monthly Navigator and quarterly Fixed Income Commentary.

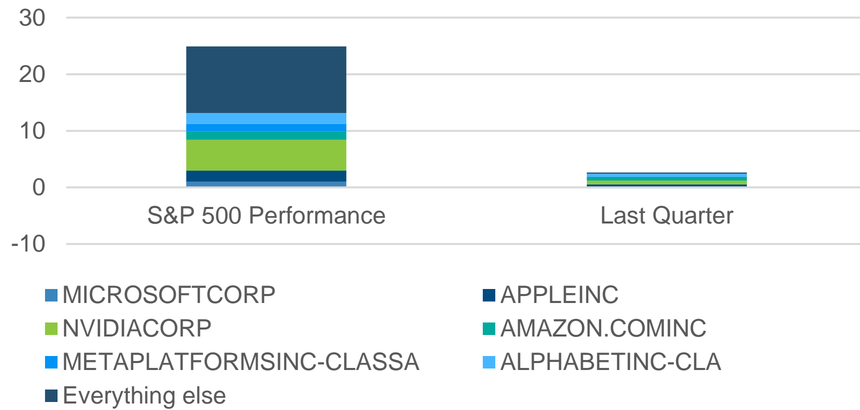
Market Return: A Narrow and Negative Quarter

Last quarter the artificial intelligence gold rush and some technology stocks were showing signs of cooling off. This past quarter was a clear year-end rally of these stocks which contributed to the entire S&P500 Index return and more, as the rest of the index had a negative contribution.

A few statistics: the S&P 500 Index was up 24.5%, for the year, with less than 29% of its stocks beating the index. The average stock return was 12.8% while the top six names (Microsoft, Apple, Nvidia, Amazon, Meta, Alphabet) were up 55% on average, and still disproportionately accounted for more than 13% of the 24.5% annual return (more than half of the performance).

The fourth quarter, the index was up 2.3% and the average stock in the index was down 1.9%, with 36% of the stocks beating the S&P Index (Exhibit 1).

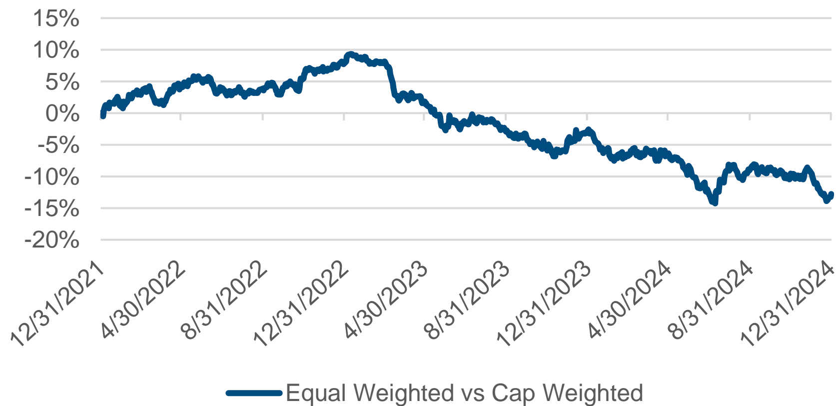
Exhibit 1: S&P Performance Q4 and FY 2024



Source: Bloomberg.

We like to measure the notion of market breadth by comparing the performance of the equal-weighted S&P 500 Index versus the cap-weighted index performance. You can see below that there was a strong 2022, followed by a challenging 2023, Q1/Q2 2024, a strong comeback in Q3 2024, which was given back in Q4 (Exhibit 2). For a longer term perspective on this important notion, please refer to our paper: https://21355211.fs1.hubspotusercontent-na1.net/hubfs/21355211/DoesSizeMatter_Commentary.pdf

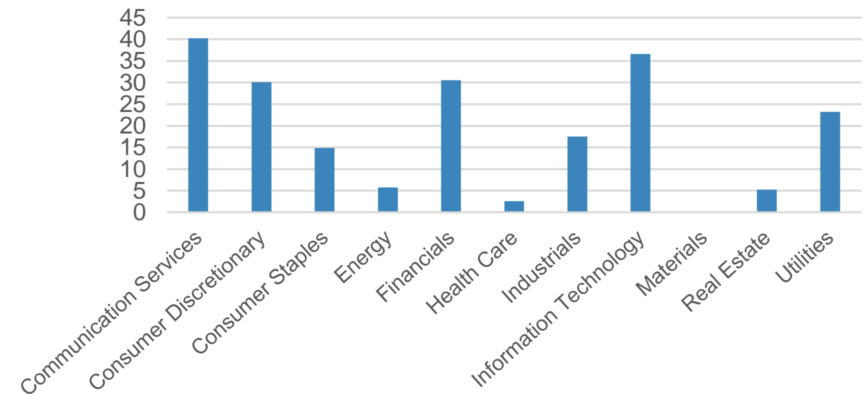
Exhibit 2: S&P500 Cap-Weighted vs. Equal-Weighted Performance



Source: Bloomberg.

We have stressed over the past quarters the importance of diversification. While the S&P 500 has extended its year-to-date gains to nearly 24.5%, the communication services sector gained 40.2%, technology gained 36%, and financial and consumer goods gained 30%. The laggards were utilities at 23%, industrials at 17%, consumer staples at 15%, energy and real estate at 5%, and materials at 0%. This sector perspective underscores the value of a well-diversified portfolio and a broadening of the 2024 rally that we had been expecting (Exhibit 3).

Exhibit 3: 2024 Sector Returns



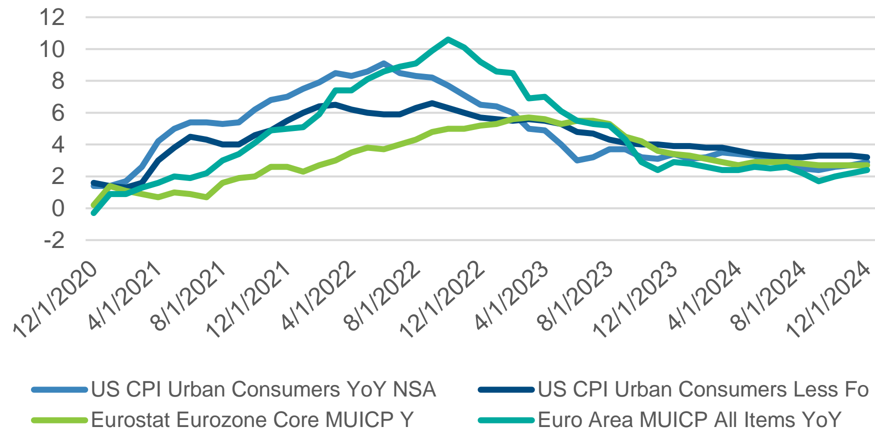
Source: Bloomberg.

Inflation: Improvements so far but resilience ahead

The January CPI report showed lower-than-expected inflation (Exhibit 4), with core CPI rising 0.2% month-over-month (3.2% year-over-year), mainly due to moderation in lodging prices and motor vehicle fees. The stock market welcomed the data since core CPE had increased 0.3% four straight months.

With this data in mind, the report is making the possibility of a March rate cut palatable and has caused Treasury yields to drop slightly.

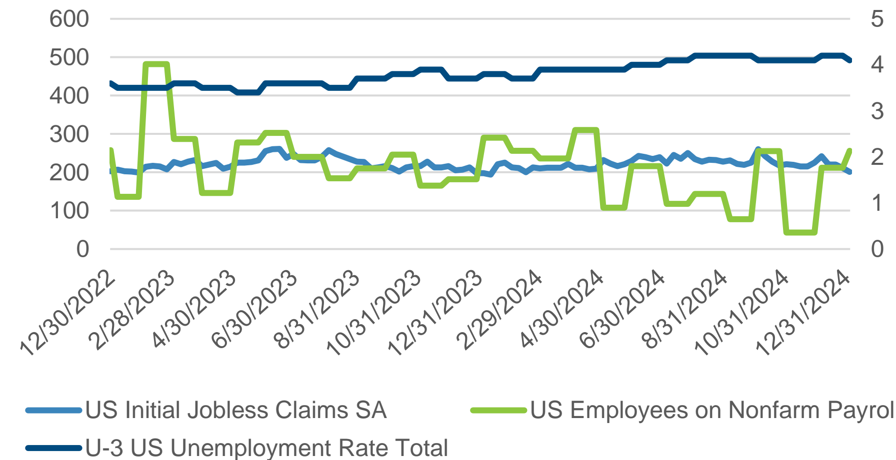
Exhibit 4: US/Europe Core Inflation Rates Ease Slightly



Source: Bloomberg.

In contrast, the labor market was well above expectations, in particular in December with nonfarm payrolls rising to 256,000 versus 165,000 estimated. The unemployment rate also fell to 4.1% (Exhibit 5). This news in isolation decreased the likelihood of the FOMC cuts in 2025 from three 25bps cuts to only two.

Exhibit 5: Unemployment/Nonfarm Payroll Display Resilient Economy



Source: Bloomberg.

FOMC September meeting: Majority Backs a 50bps Rate Cut Amid Cautious Economic Outlook

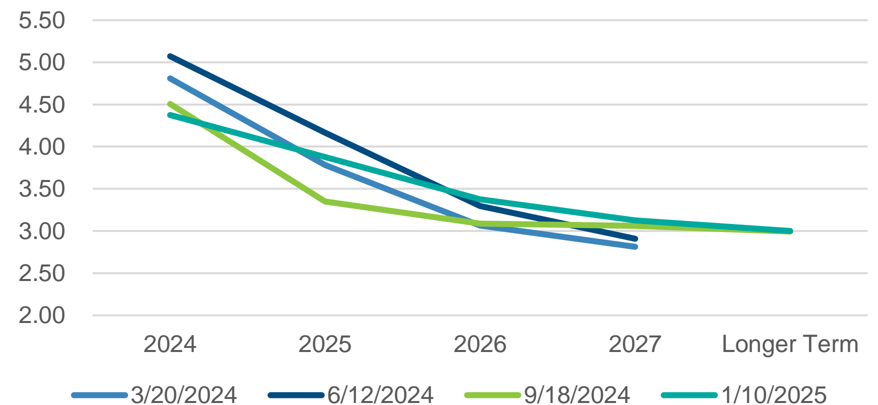
The December FOMC meeting minutes revealed that the Federal Reserve is approaching a point where it may slow the pace of interest rate cuts. Most participants noted continued progress in disinflation, but almost all acknowledged increased upside risks to inflation. The committee decided to lower the federal funds rate by 25 basis points, with a vast majority supporting this move.

The minutes highlighted a careful approach to future monetary policy decisions, given recent economic strength and inflation concerns. Many participants emphasized the need for caution in light of these factors. The committee generally viewed the current policy stance as meaningfully restrictive, allowing time for careful calibration of future changes.

Regarding the labor market, participants observed a gradual easing of conditions but noted that indicators merited close monitoring. The unemployment rate remained low, and there were no signs of rapid deterioration. The Fed staff slightly adjusted their economic projections, expecting slightly slower GDP growth and a marginally higher unemployment rate compared to November's forecast.

The dot plot is now at all forecasted horizons (Exhibit 6).

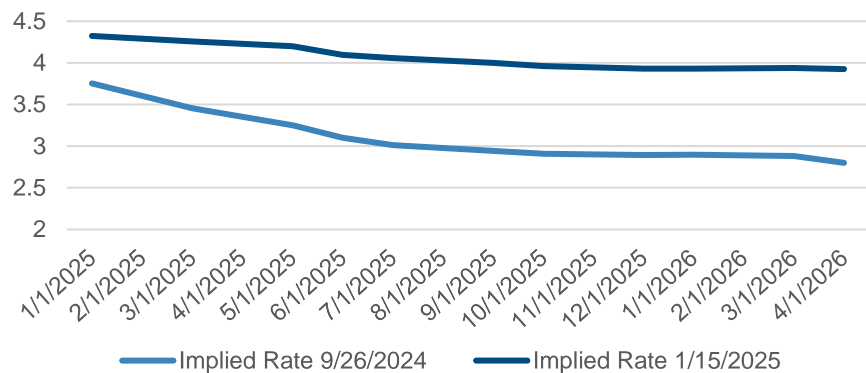
Exhibit 6: FOMC Dot Plots Continue to Signal High Rates for Longer



Source: Bloomberg.

The rates markets have incorporated this information (Exhibit 7) and are pricing in higher rates, optimistically expecting more cuts ahead, showing an implied rate curve higher than the ones of the last quarter.

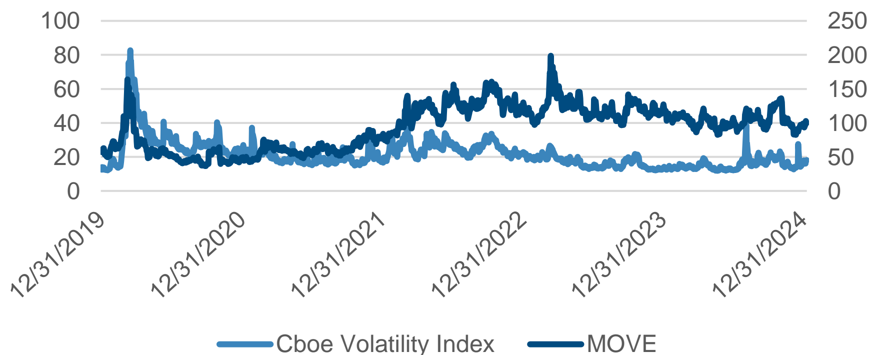
Exhibit 7: Implied Rates Have Significantly Increased in Q4



Source: Bloomberg.

Interest rate uncertainty is still high, as can be seen in Exhibit 8. The MOVE Index (implied volatility of a basket of OTC options on US interest rate swaps) illustrates the uncertain environment we are in. With a continuation of the positive trend this quarter, that uncertainty is a little lower than it used to be, indicating that the “higher for longer” scenario might be sinking in. Meanwhile the VIX (Volatility) Index has rebounded from its lows with a spike on December 18th as the Santa rally was unravelling and erased 3.6% from previous highs.

Exhibit 8: The MOVE Index Indicate Moderating Uncertainty in Interest Rates, while the VIX Index Indicates a Constructive Investment Narrative



Source: Bloomberg.

We continue to see US equities trading at multiples of 24X-27X with some mild signs of economic slowdown in combination with resilient inflation. The prudent thesis makes risk assets seem overbought, exposing vulnerabilities in US equities. The Shiller CAPE (cyclically adjusted price-earnings ratio) is 37, near the highs of the dotcom bubble. In contrast, the Euro Stoxx 50 is trading at 14X-15X multiples, the FTSE 100 Index is trading at 12X-15X, and the S&P TSX Index is trading at 17-28X, offering viable competing alternatives to US equities. Yield spreads continue to compress and are at 10-year lows by historical standards both in the corporate and high yield segments.

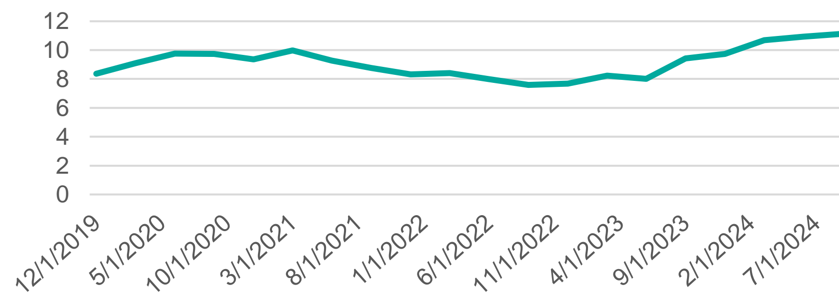
Economy: Resilient with a Moderate Slowdown

Recession risks have continued to inch lower however more recently recession probability has stayed constant over the past few quarters at a low 20%.

For 2025, we are continuing to see some further signs of slowdown which could grow more substantial: for instance, personal savings buffers are lower than post-pandemic which could diminish consumer strength. In addition, fiscal policy is uncertain with the potential lapsing of past policies, the additional labor participation rate looks more challenging, the delayed impact of variable rate debt is likely to be seen in more corners of the economy, political changes, and geopolitical tensions in the Middle East could create additional headwinds.

Relatedly, credit card delinquencies are rising to levels now higher than the 2020 recession (Exhibit 9).

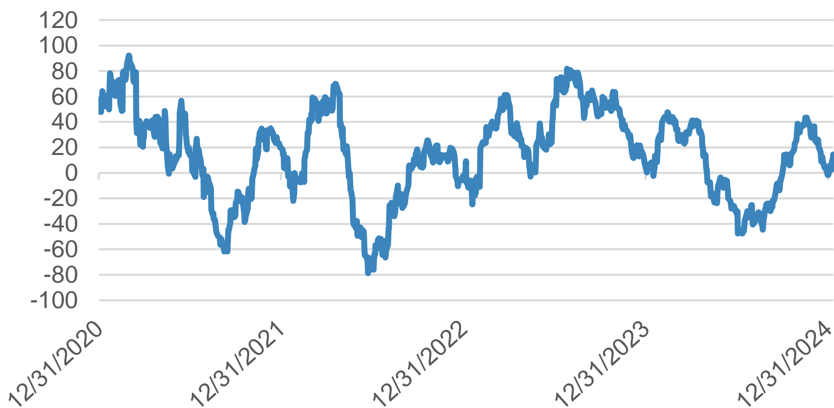
Exhibit 9: Credit Card Delinquencies Starting to Rise (% of balance delinquent 90+ days)



Source: Bloomberg

Another sign of economic slowdown is the Citigroup Economic Surprise Index which despite a rebound last quarter stayed in neutral territory, indicating that while still resilient, the US economy is no longer posting as many strong positive surprises as the majority of 2023 and 2024 (Exhibit 10).

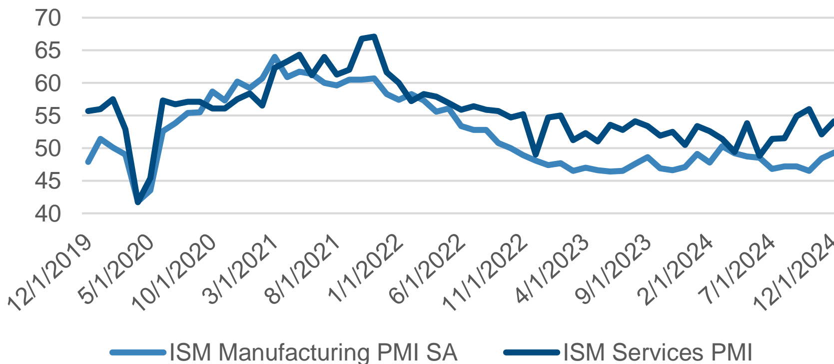
Exhibit 10: The Citigroup Economic Surprise Index Indicates How Economic Data Compares with Consensus Estimates



Source: Bloomberg, Citigroup.

Further signs of a moderate slowdown can be seen in the leading indicators of the PMI ISM surveys (Exhibit 11). Both indices are hovering around the neutral 50 level. While the declines seem to have stabilized and improved at the last reading they have not shown any clear signs of improvement over the past six months.

Exhibit 11: ISM Manufacturing and Services Indices are in Neutral Territory

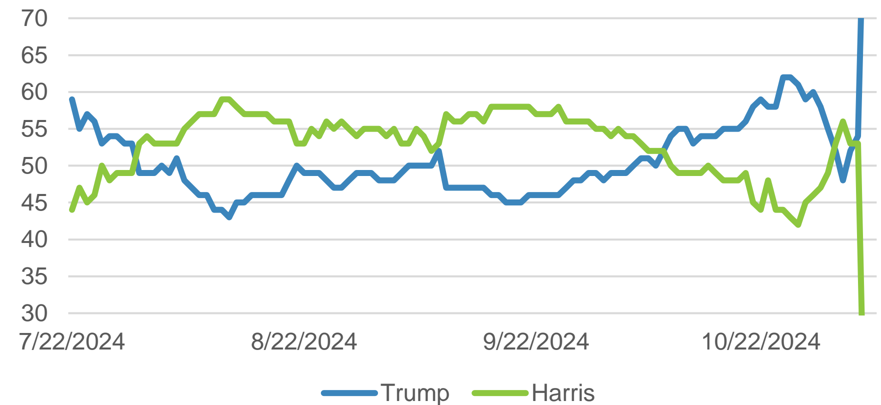


Source: Bloomberg.

US Elections: Uncertainty lifted leading to a relief.

We monitored the election, with some unprecedented developments for both candidates over the past year (Exhibit 12). The outcome of the election can yield significant changes to regulation, fiscal policy, trade policy and foreign policy. Of particular interest are the risks of higher tariffs and increased fiscal spending which could reinvigorate inflation risks. We anticipate some volatility as the year progresses and the agenda become more clearly defined on fiscal, trade, and regulatory policies.

Exhibit 12: Election Betting Odds



Source: Bloomberg, PredictIt

Investment Implications

Investing is like the Tour de France: it's about enduring the climbs, mastering the descents, and knowing when to accelerate, all while relying on our training and preparation. True success doesn't come from a single burst of speed, but from a consistent strategy and unwavering resilience.

By applying these lessons of preparation, diversification, adaptability, risk management, and seeking expert guidance, investors can navigate the complex financial landscape with greater confidence and skill.

Looking forward, while we still do not see any major risks to the upside or the downside, the current return/risk environment does not appear the most favorable, thus our cautious stance to look for higher quality equity and fixed-income segments, repositioning capital from short and long-term fixed income to intermediate maturities, more emphasis towards international

equities as well as a willingness to embrace any trading weaknesses to capitalize on future opportunities.

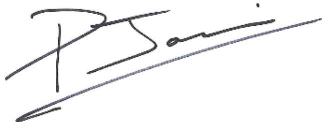
Given the current market conditions we reiterate our recommendations:

- Diversify-Diversify-Diversify: by asset class (bonds, equities, alternatives, options), by investment approach (long, tactical, premium income), by style (active, passive, defined outcome), by benchmark (equal-weighted vs. cap-weighted), by geography (US, international, global). Embrace other scenarios.
- Be realistic and remain cautious and opportunistic in the current environment with active risk management and tactical strategies.
- Follow a systematic and flexible approach and stick with it during episodes of volatility.

I hope this letter finds you and your family happy, healthy, and enjoying the new year. Our thoughts are also with those impacted by the recent LA wildfires, reminding us of the importance of resilience and community during challenging times.

If you have any questions about your portfolio or would like to discuss your current positioning, please contact your advisor at any time. Our team always has your best interests at heart and stands ready to help you meet your goals with the appropriate allocations and proactive financial planning. As always, we thank you for your trust and business.

Warm regards,



Patrick Jamin
President & CIO

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