OBSERVATIONS

- Markets were mixed last week with the S&P 500 gaining 1.0%, while small caps (Russell 2000) declined -1.0%, and the yield on the 10-year Treasury fell -2 basis points to end the week at 4.15%.[1]
- The Manufacturing Purchasing Managers Index (PMI) increased in November to 48.4—any number below 50 denotes contracting economic activity—up from October's 46.5 level.[1]
- The Services PMI, in contrast, was below expectations after falling from October's 56.0 figure to 52.1. Despite November's decline, it has remained above 50 for 51 of the past 54 months since mid-2020.[1]
- According to the Job Openings and Labor Turnover Survey (JOLTS), the number of open jobs in the US increased in October to 7.7 million up from September's 7.4 million figure. The number of quits—a barometer of how confident employees are in finding a new job—increased to 3.3 million in October from September's 3.1 million figure.[1]
- Initial unemployment claims came in +9k over expectations registering 224k new claims last week, but they remain low and on par with claims for the same week last year. [1]
- The US economy added 227,000 jobs in November, a stronger showing than October's revised total of 36,000. The November unemployment rate ticked up to 4.2% from 4.1%. Average hourly earnings rose 4% from a year earlier. Economists had expected a gain of 3.9%.[1]
- The University of Michigan's December Index of Consumer Sentiment improved for the fifth consecutive month, rising from November's 71.8 to 74.0, its highest reading in seven months.[1]

EXPECTATIONS

- Q3 earnings reports are wrapped up with 99% of the S&P 500 having reported results. Earnings for the index grew +11.9% in Q3 on a year-over-year (YoY) basis, the highest earnings growth since Q4 2021.[2]
- The Fed Funds Futures market is increasingly pricing in an additional -25 basis point rate cut at the Fed's next meeting in mid-December. As of last Friday, markets suggested an 85% chance of a rate cut, up from roughly a 50% chance in late-November. Several Fed officials recently indicated that current policy was sufficiently restrictive that an additional rate cut this year would still be appropriate.[1]

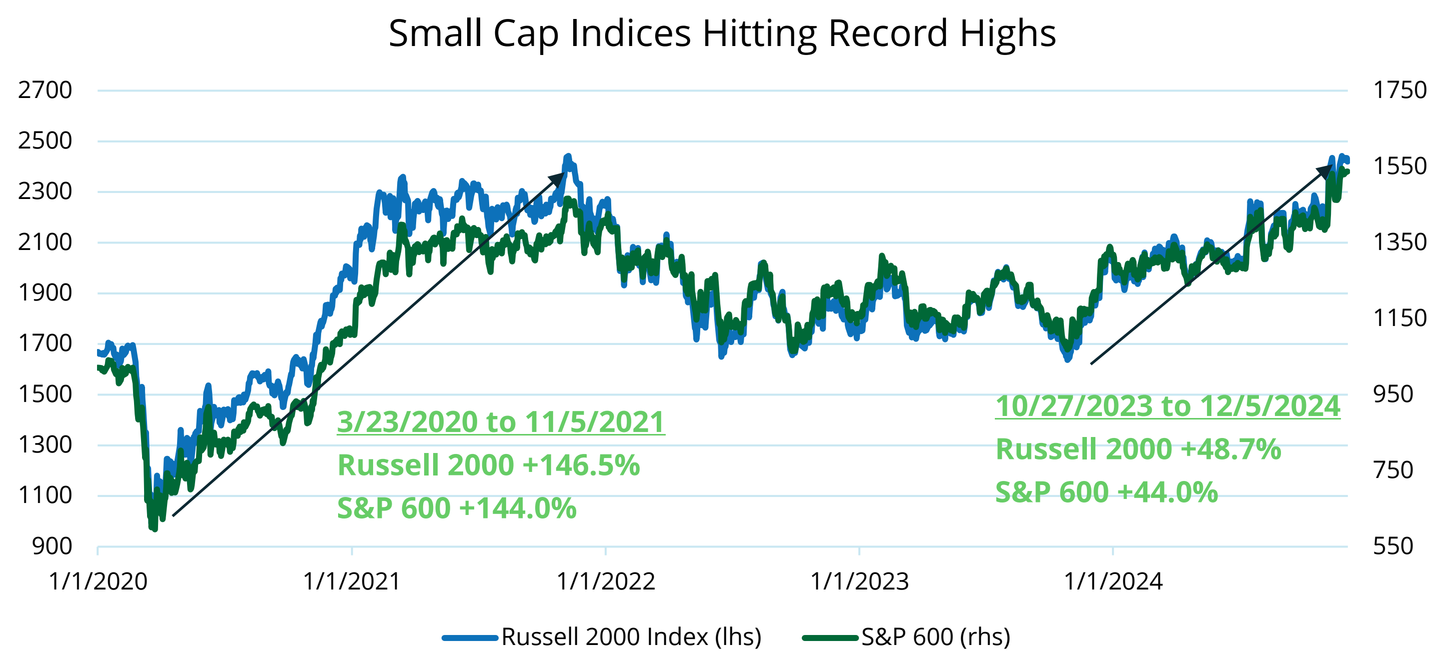
ONE MORE THOUGHT: Small- and Mid-Caps Shine in H2-2024.[1]

Investing in small- and mid-cap stocks is not without its challenges, but those investors with exposure to this asset class over the past several months have been rewarded. Since July 1st, small cap indices have outpaced their large cap peers. For instance, the Russell 2000 Index—a broad index of small cap stocks—has gained +18.3% and the S&P 600—a narrower index of small caps stocks requiring a level of profitability—has gained +17.3%. The Russell Mid-Cap Index gained +17.5% over this period. Whereas the S&P 500 Index has gained +12.2% and the Russell 1000 Index—a broader index of large cap stocks—has gained +13.3%. Moreover, small cap stocks have finally set new record highs. As the Covid pandemic unfolded, small cap indices plunged over 40% as economies closed down around the world. However, as the pandemic economic outlook brightened small caps began to surge and by Nov-2021, the Russell 2000 Index and the S&P 600 had gained over +145% (Chart of Week) setting numerous record highs along the way. However, the Fed's hiking cycle of 2022-2023, which dramatically increased the cost of borrowing—small caps are generally more levered (indebted) than their large cap peers— attributing to small caps losing about 1/3 of their gains from their peak to their trough in Oct-2023. However, it had become clearer to

[1] *Bloomberg LP 12/6/2024*
[2] *Factset Earnings Insights, 12/6/2024*

markets that the Fed was done hiking rates (last rate hike occurred in late July 2023) and despite the fact the Fed had taken its main policy rate from near zero to over 5%, the US economy was unlikely to enter a recession in 2024. While this economic backdrop helped small caps recover from the 2023 lows, the small cap indices still could not break out to new record highs. This stemmed in part from the fundamentals of the asset class—higher borrowing costs had squeezed margins, sales growth was mixed, and biotech industry remained pressured by the poor M&A environment. The AI boom of the past two years that rewarded large-cap semiconductor firms, did little to help most small cap tech companies which were software oriented. However, the first Fed rate cut this past September gave markets confidence that small cap margins could improve as borrowing cost actually eased and the pro-growth economic agenda of the incoming Trump administration served as catalysts to power small caps to new record highs. The S&P 600 recently peaked on 25-November, while the Russell 2000 Index came within 3 basis points of its November 2021 record high the same day. US equity markets typically enjoy a positive December and the 2025 outlook is generally optimistic, therefore it is reasonable to see small cap indices charting further gains in the weeks and months ahead. Our 2025 outlook will be published in early January.

CHART OF THE WEEK



Source: Clearstead, Bloomberg 12/5/2024

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