

KEY TAKEAWAYS

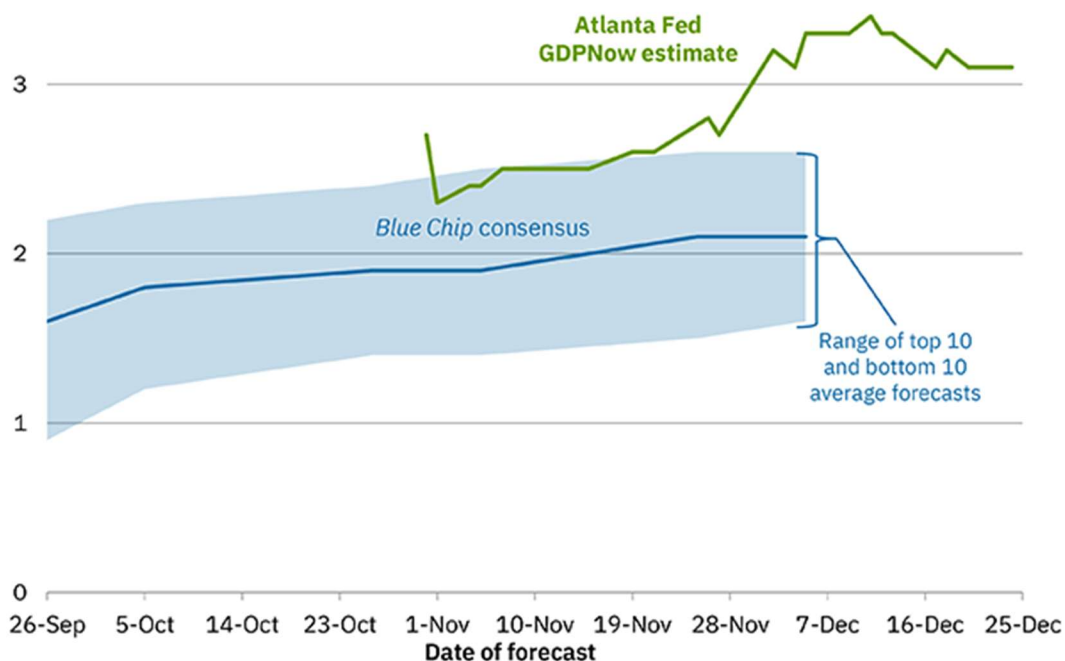
- The equity markets continued the late November rally into early December, but the move higher in yields ended the rally and the market fell to near the lows of the month.
- The U.S. 10-year Treasury Yields hung around the 4.20% mark, but then had a steady march higher into year-end pushing past 4.5%, which helped derail equities as noted above.
- Crude oil again traded in a tight range around \$70 but ended at the highs of the month.

The U.S. Economy

The final reading of 3rd quarter GDP came in at 3.1%, up from previous reports of 2.8%. Core PCE, the imbedded inflation measure, edged higher to 2.2%, from the previous report of 2.1%. The estimates for 4th quarter GDP, from GDPNow, continues to look like the 3rd quarter at around 3.1% with the Blue-Chip consensus forecast moving above 2%, as shown in the chart below. Economic activity remains steady, and the PCE deflator is almost down to the sweet spot of “2%” inflation. It continues to look like a soft-landing, goldilocks scenario, and the market is now pricing in fewer Fed rate cuts for 2025.

Evolution of Atlanta Fed GDPNow real GDP estimate for 2024: Q4

Quarterly percent change (SAAR)



Sources: Blue Chip Economic Indicators and Blue Chip Financial Forecasts

Note: The top (bottom) 10 average forecast is an average of the highest (lowest) 10 forecasts in the Blue Chip survey.

Source : <https://www.frbatlanta.org/cger/research/gdpnow>

Stocks and Bonds

The U.S. 10-year Treasury yield started the month holding around 4.2% digesting the fall in yields from 4.5% but the second week of the month started a steady march north of 4.5% to yields near the summer highs. The Fed cut rates again, which continues to drive the markets thinking policy error, i.e. triggering another round of inflation. To the Fed's credit, they are stating that policy is still restrictive and that less rate cuts are likely coming than had been previously forecast. The bond market is not yet convinced, though yields have at least temporarily stalled out in the 4.6% area. There is still a lot of uncertainty regarding the economy, both in the U.S. and globally. Additional uncertainty is, what if any, major policy changes are enacted with Trump's inauguration in a few weeks. The Fed seems to be taking a wait and see approach. So as usual, we will continue to monitor incoming news to ascertain what might be coming next. The sharp increase in yields was a meaningful headwind for High Quality fixed income, which as measured by the iShares US Aggregate Bond ETF decline -1.69% for the month. The U.S. 10-year Treasury bond yield ended the month at 4.57%, up significantly from November's close of 4.18%.

The Dow Jones Industrial Average dropped -5.27%, the S&P 500 fell -2.50%, and the small cap iShares Russell 2000 ETF crashed -8.28%. The international markets traded better than the U.S. markets. The MSCI EAFE iShares Core International Developed Markets ETF Index declined -2.88%, and the MSCI Emerging Markets iShares Core ETF Index eased -1.06%.

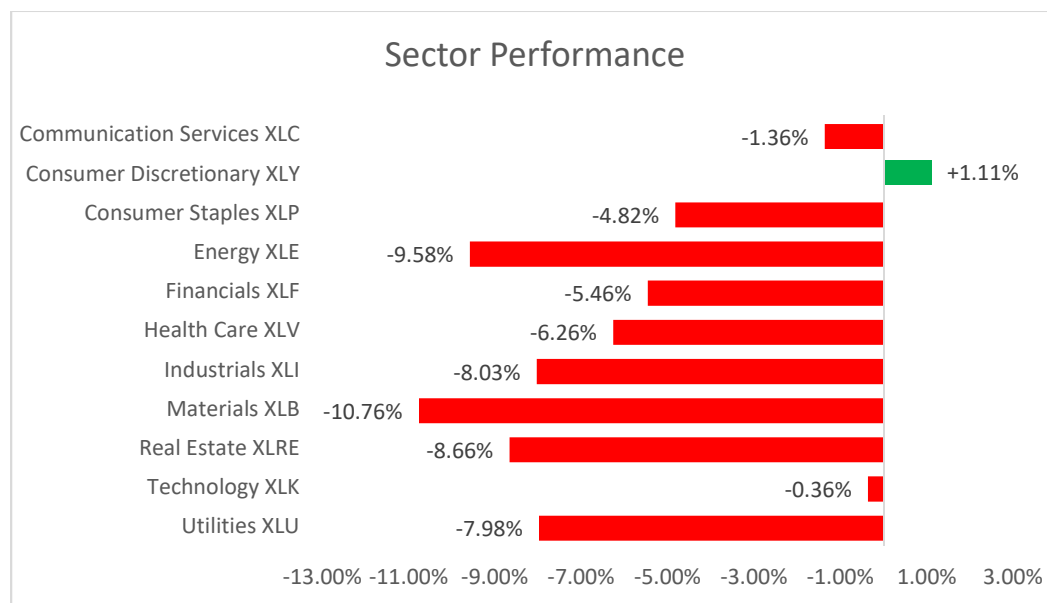
December's sector performance was the opposite of last month with red and very red.

The "best" relative performers were...

- Consumer Discretionary: +1.11%
- Technology: -0.36%
- Consumer Services: -1.36%

The worst performers were...

- Materials: -10.76%
- Energy: -9.58%
- Real Estate: -8.66%



Source: <https://www.morningstar.com>

Oil Report

Crude Oil continues to trade around \$70 +/- a couple of dollars going on 2+ months. The themes remain similar, demand concerns vs. the ever-expanding list of geopolitical conflicts. The market continues to be comfortable trading this range and has pretty clearly set up \$75 and \$65 as the important lines in the sand. A push and hold of \$75 likely is the start of a larger rally. On the other hand, a drop and remaining below \$65 likely opens up considerably more downside with significant economic weakness the probable driver. The net effect remains a stalemate awaiting further information for a sustained direction. The current NYMEX WTI Crude Oil futures settled at \$71.87 posting a gain of over 5% from the prior month's close of \$68.15 a barrel and nearly the highest level of the last two months. RBOB gasoline was slightly stronger than Crude for the month and popped over 6% vs. November's close. We are in the seasonal lull for the Crude Oil complex for the next few months.

The Rest of the Data

The November ISM Manufacturing Index increased to 48.4 from October's reading of 46.5, remaining below 50. The ISM Services Index decreased to 52.1 in November, from October's print of 56.0. Any reading below 50 generally indicates deteriorating conditions, whereas a reading above 50 generally indicates improving conditions. The prices paid component for Manufacturing eased back to the normal range and Services' prices held at elevated levels. Consumer confidence dropped to 104.7 in December, which compares to an upwardly revised 112.8 in November. The unemployment rate climbed to 4.2%, while the number of jobs added jumped by 227,000 in November, much better than October's report, and beat expectations of 220,000 jobs. It appears that the hurricanes did have a big impact on the October report. The Consumer Price Index for All Urban Consumers (CPI-U) was up +0.3%, breaking the streak of 4 consecutive 0.2% prints, in November, on a seasonally adjusted basis. Over the last 12 months, the All-Items Index rate increased to +2.7% on a non-seasonally adjusted basis. The CPI ex Food and Energy again held at 3.3% over the last year. The economic data remains good, with even employment looking a lot better than last month; the fly in the ointment is that inflation is holding steady over the Fed's target of 2%. The economic reports continue to suggest the economy remains in reasonable shape. The solid jobs report likely keeps the Fed at bay for another rate cut in the short term. We will continue to monitor economic activity, and inflation reports for potential shifts.

Summary

The market had been taking an optimistic view of future economic progress, but the continued increase in interest rates finally got the equity markets attention and equities had some hard drops during the last 3 weeks. It seems with the number of crosscurrents this month, that we likely see continued choppy price action as the markets wait for the new administration. A pullback in interest rates might provide a positive boost. However, if rates move to new highs, we will likely see continued selling pressure. We also may have the occasional tape bomb as the new administration shares potential policy changes. For now, it continues to feel like a Goldilocks scenario, where we are in a happy spot for growth. Given all of that, this is why we focus on understanding your risk tolerance and building an allocation to match that rather than guessing based only on market outlook.

As always, the markets can be emotional, so we retain our focus on what we can control, which is the amount of equity risk that is taken in a clients' portfolio in concert with the clients' risk tolerance and long-term goals. The markets will always face different "worries", today it is inflation/war vs. growth and interest rates, tomorrow it will be something else. We have built our asset allocation models with dynamic features and quarterly rebalancing, both in fixed income and equities.

If you have specific questions about your portfolio or financial situation, we are here to help. Long-term financial planning is designed to deal with uncertainty like those we discussed above. Our portfolio management process is to design a prudent allocation across many asset classes. Equities are for long-term growth and several vehicles that we utilize offer defensive mechanisms to mitigate equity market declines.



Kevin Churchill, CFA®, CFP®
Chief Investment Officer
WaterRock Global Asset
Management



Institutional Asset Management adapted for Private Wealth™

WaterRock Global Asset Management, LLC
Kailua-Kona, HI 96740 & Scottsdale, AZ 85260
(808) 896 – 4957

WaterRock Global Asset Management, LLC. ("WaterRock Global") is a Registered Investment Advisory Firm regulated by the State of Washington and the Securities Exchange Commission under the Investment Advisors' Act of 1940 and in accordance and compliance with applicable securities laws and regulations. Investing in the stock market involves risk, including the risk of principal loss. Information in this newsletter is in no way intended as personalized investment advice and should not be interpreted as such. Past performance is not necessarily indicative of future results.