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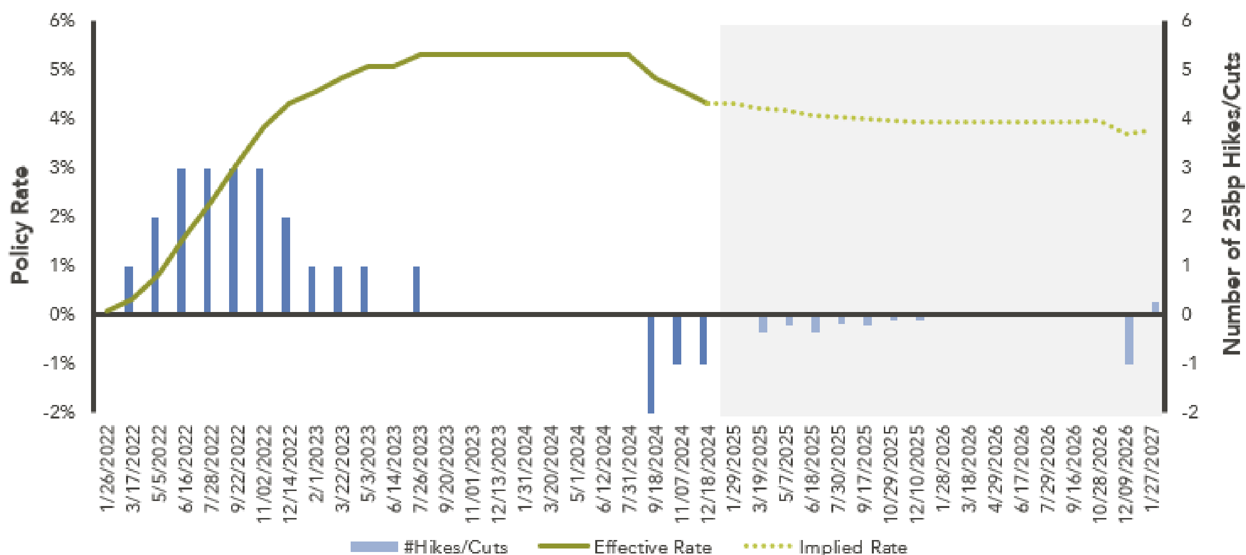
U.S. Economy: Job growth was much stronger than expected in December, likely providing the Federal Reserve less incentive to cut interest rates in 2025. Nonfarm payrolls surged by 256,000 for the month, up from 212,000 in November and above the figure forecasted by economists. Job growth came from the familiar sources of health care (+46,000), leisure and hospitality (+43,000), and government (+33,000). The retail space also saw a sizeable gain (+43,000) after losing nearly 30,000 jobs in November heading into the holiday shopping season. The unemployment rate has edged down to 4.1%, slightly lower than expectations. An alternative measure that includes discouraged workers and those holding part-time positions for economic reasons moved down to 7.5%, a slight decrease and the lowest since June 2024. Average hourly earnings increased 0.3% in December, which was in line with forecasts, but the 12-month gain of 3.9% was slightly below the outlook and indicative that wage inflation is becoming less of a concern. At its December meeting, Fed officials deemed the labor market mostly healthy though slowing and lowered its key borrowing rate by 25 basis points (while indicating a slower pace of reductions ahead). To that point, markets expect the Fed to hold pat at its meeting in January, with futures pricing after the jobs report swinging to the expectation of just one cut this year. Central bankers have expressed concern lately with the pace of inflation, which has held above the Fed's 2% target largely because of stubbornly high housing costs as well as some goods prices. As measured by CPI, inflation rose 2.7% on an annualized basis in November.



Source: Bloomberg as of January 8, 2025. Gray shading indicates forecasts.

Fixed Income: The fourth quarter was a reversal of fate and a paradox for fixed income markets. The Federal Reserve continued to cut interest rates, but rates faded out the curve on fears of reinflation and increased deficits. The bellwether Bloomberg U.S. Aggregate Bond Index gave back most of its 3Q gains in 4Q, bringing its full 2024 return down to 1.3%. Spread sectors were tighter for most of the quarter before paring gains in the second half of December. Valuations remain rich as credit fundamentals have proved resilient. In addition, strong technical factors as a result of high all-in yields are keeping a lid on spreads. Fixed income continues to be an attractive asset class with starting yields near 5%. Spreads are tight across sectors and will likely hold at similar levels until they are shocked wider, meaning it is important to remain diversified across sectors. It is very uncommon for the Fed to be cutting its policy rate while rates are rising. In addition, there is significant uncertainty regarding the new Trump administration's economic policies. Finally, there are heightened geopolitical threats that could result in economic disruptions, which could pose challenges to fixed income markets.

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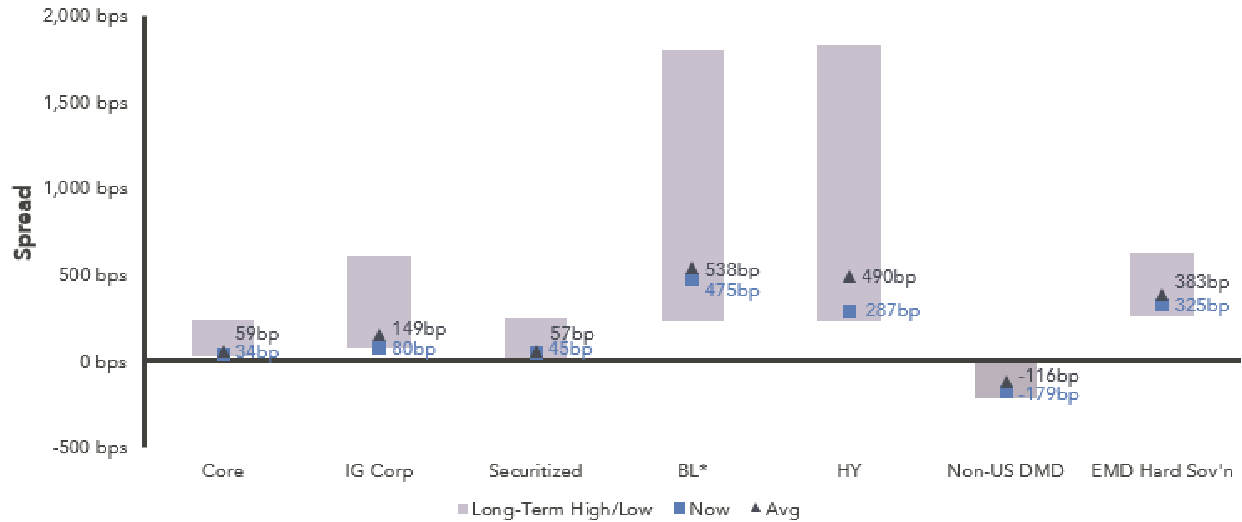
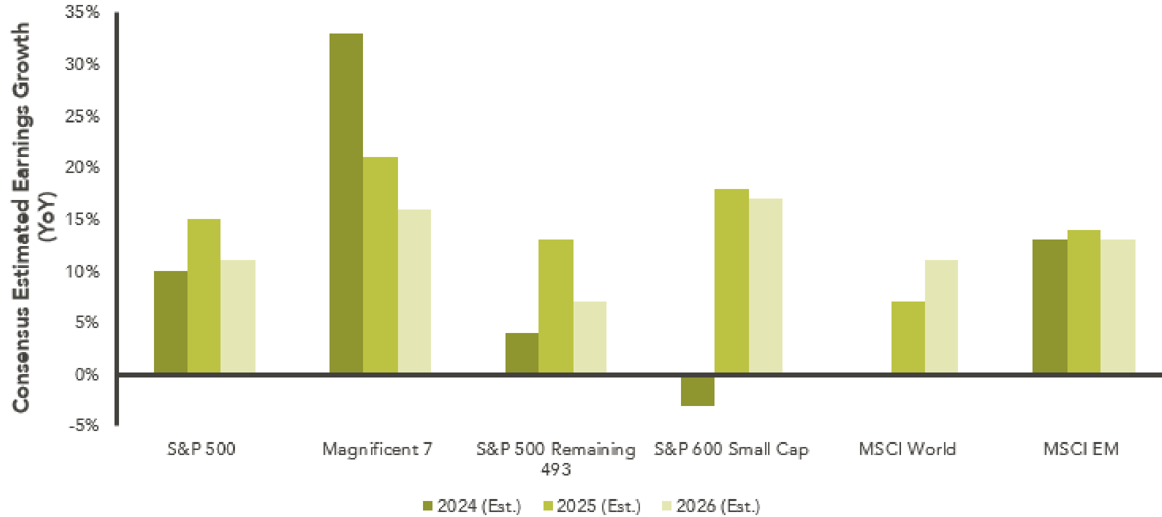


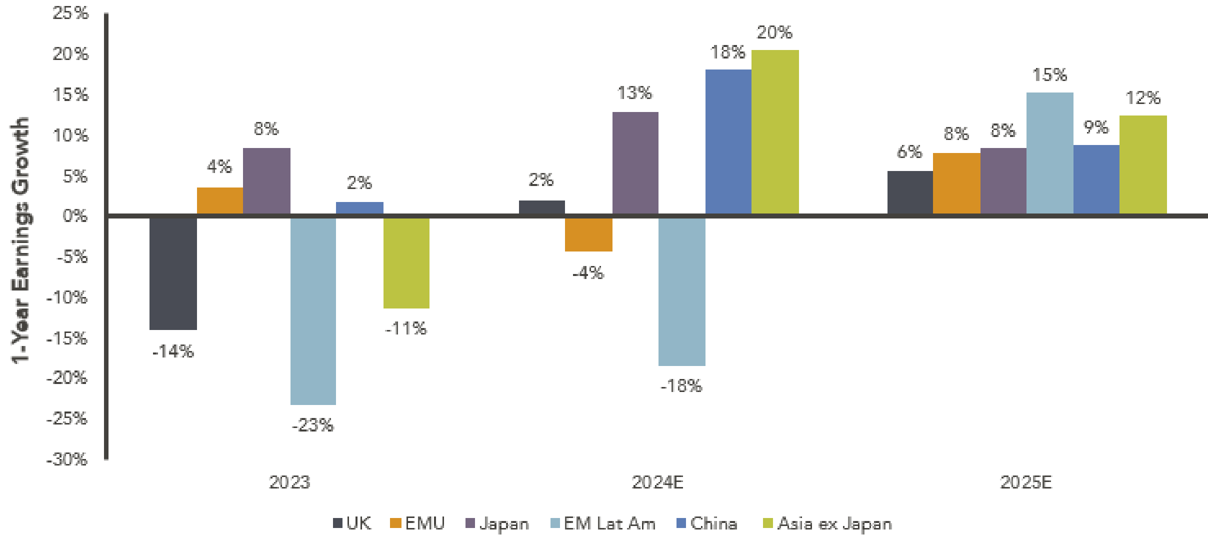
*BL spread over LIBOR, not over Treasuries.
Source: Bloomberg, Credit Suisse, JPMorgan as of December 31, 2024. Long-term high, low, and average based on longest available data for each index.

U.S. Equities: Defying expectations, the U.S. equity market posted its second consecutive year with returns greater than 20%, as the S&P 500 Index advanced by roughly 25% in 2024. Driven by lower inflation, the first Fed rate cut, and the outcome of the presidential election, investors exhibited a brief rotation into small-cap equities, which advanced 11.5% in the year (as measured by the Russell 2000 Index). Market leadership by large-cap growth equities, however, remains the dominant theme, as the Magnificent 7 stocks contributed more than 50% to the calendar year return of the S&P 500 Index. As a result, the U.S. equity market became more concentrated over the course of the year. While this theme is most prevalent within large-cap equities (the top 10 S&P 500 Index holdings now comprise over 37% of the benchmark), mid- and small-cap equity indices also reached historic levels of concentration in 2024. From a style perspective, although growth equities led the U.S. market last year (the Russell 1000 Growth Index outpaced the Russell 1000 Value Index by 19%), seven sectors posted double-digit returns across both cyclicals (e.g., Information Technology, Consumer Discretionary, and Financials) and defensives (e.g., Consumer Staples and Utilities). Pockets of market breadth emerged throughout the year, but concerns about the future path of interest rates, economic data, and geopolitics repeatedly led investors back to mega-cap stalwarts given the strong earnings growth exhibited by these companies. Going forward, although fundamentals are attractive and forward valuations remain near historic lows relative to large caps, small-cap equities must see a rebound in earnings growth to gain persistent favor with investors. Given recent market strength, future returns for U.S. equities may be more muted, though the backdrop for the space remains positive relative to other geographies given a new pro-business presidential administration that may spur economic growth and M&A activity. That said, risks remain within U.S. equity markets, as policy uncertainty, including increased tariffs and immigration reforms, may be inflationary. Any acceleration in inflation, in tandem with structurally higher rates, lofty valuations, and a stronger U.S. dollar, could lead to a market correction in 2025.



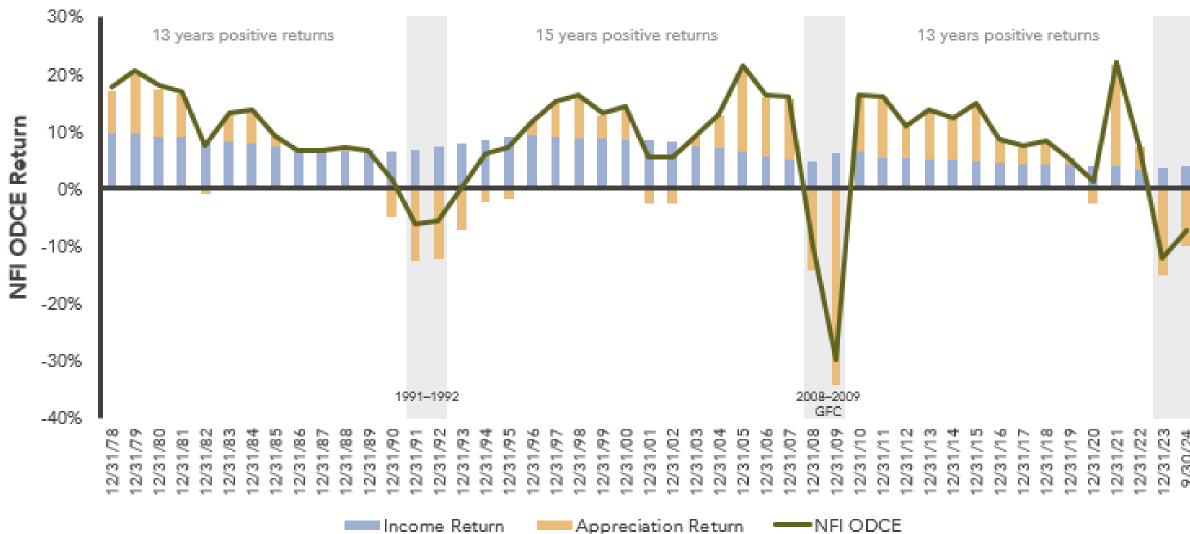
Source: SIT Investments, Bloomberg, and FactSet as of December 31, 2024. MSCI World excludes the U.S. and is expected to notch 0% earnings growth in 2024.

Non-U.S. Equities: Non-U.S. equities ended 2024 by giving back some of the year's gains, with all major indices falling in the fourth quarter. The MSCI Emerging Markets Index returned -8.0% during this period, slightly outperforming its developed counterpart, the MSCI EAFE Index, which returned -8.1%. For the year, EM equities outperformed developed equities (+7.5% vs. +3.8%). Robust performance by EM stocks was supported by China's 3Q rally, which was propelled by positive investor sentiment after Beijing announced stimulus measures and policies to bolster equity markets. Despite this rally, China ended 4Q in the red (-7.7%) as investors remained uncertain about the scale of further government support. Beyond China in emerging markets, Taiwan further benefited from strong semiconductor demand as the AI theme continues to play a significant role in global markets. In India, post-election sentiment remains high due to strong economic and demographic growth prospects, supported by Prime Minister Modi's championed reforms. While India's long-term prospects remain positive, the country underperformed in 4Q as lofty valuations made investors cautious. In developed markets, inflation moderated across Europe in 4Q and is on pace to reach the European Central Bank's goal. However, Europe's economic outlook appears lackluster with growth, political, and trade uncertainty plaguing the continent. Japan's long-running policy of negative interest rates finally ended as expected rate hikes by the nation's central bank materialized. Higher rates and corporate reforms aimed at enhancing shareholder value continue to present opportunities for investors in Japan. In general, global uncertainty persists given the new Trump administration, prompting caution from countries around the world. The impact of future Trump tariffs remains to be seen and along with economic uncertainties in China and Europe could heighten volatility of non-U.S. equities.



Source: FactSet as of January 7, 2025

Real Estate (Lagged): The third quarter of 2024 saw the NFI-ODCE Index achieve a total gross return of roughly 0.3%, driven by 1.1% income growth and offset by a 0.8% decline in appreciation. Similarly, the NPI delivered a total return of around 0.8%, reflecting stabilization in property-level performance after extended declines. These figures mark a turning point and signal the first positive movements in U.S. commercial real estate in over two years, underlining improving market conditions. U.S. commercial real estate values likely bottomed in 2024, and investors expect valuations to consolidate around current levels through 2025. Debt markets have loosened, with lower interest rates halting the rapid increase in cap rates. This stabilization has narrowed bid-ask spreads and stopped the fall in transaction volumes. Elevated barriers to new supply across certain sectors should further support fundamentals, laying the groundwork for a steady recovery. Looking ahead, 2025 appears poised to be an attractive entry point for CRE investment, setting the stage for potentially larger price gains in 2026. With valuations stabilizing, debt markets improving, and property fundamentals strengthening, the market is primed for renewed confidence and activity. Key opportunities lie in structurally driven sectors such as data centers, logistics, and residential properties, which stand to benefit from long-term secular trends. As the industry transitions into recovery, investors entering in 2025 are well-positioned to capitalize on anticipated price gains and income growth in 2026. Chart Source: FactSet as of January 7, 2025



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Prepared by Marquette Associates

180 North LaSalle St, Ste 3500, Chicago, Illinois 60601 PHONE 312-527-5500
CHICAGO BALTIMORE MILWAUKEE PHILADELPHIA ST. LOUIS WEB MarquetteAssociates.com

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