



We are happy to report that stocks continued their strong momentum from the 2nd quarter and bonds joined the party as well. With interest rates dropping, bonds rallied. While large cap growth U.S. stocks remain the leading asset class YTD, up 28.16%, the leaders of the quarter were notably small cap U.S. stocks and REITs, outperforming large cap growth by about 6% and 12%, respectively. This quarter was a strong example of the benefits of diversification – even precious metals stock funds gained an average of 16.8%. As we've noted, the near-perfect scenario and optimism built into valuations of large cap growth stocks leave an opportunity for outperformance by other asset classes in favorable environments.

As recently noted in BARRON'S, it was a great quarter for income-oriented and dividend stock fund investors after several months of lackluster returns. While utilities surged, so did funds in Morningstar's real estate category, up 15.8%; infrastructure funds, up 12.8%; and financials, up 10.8%, all of which pay generally higher-than-average dividends. Utilities, REITs and infrastructure companies are dependent on debt to finance their businesses, so a rate cut lowers their cost of capital.

This was the first quarter in some time when bonds shone for the same reason as dividend stocks. The average long term bond fund surged 7.6%. Bond prices move inversely with rates, and bonds with the longest maturities are the most sensitive to rate moves. Short-term bond funds by contrast, gained 3.2% this quarter.

We have spoken extensively about the Federal Reserve over the last four years. It has been quite a ride since the Fed first cut interest rates in early 2020 because of the COVID-19 slowdown in the economy. After nearly two years of near-zero rates, the Fed began a furious rate rise cycle in early 2022, prompted by spiking inflation. Then last month, the Fed finally pulled the trigger, lowering the Federal Funds Rate (FFR) by .50% to a range of 4.75% to 5.00%. The goal remains for the Fed to execute a soft landing, where they can reduce rates over time without sending the economy into a recession. So far, the economy seems to be cooperating as it added 254,000 jobs in September, well above the 150,000 forecasted.

As we approach the final quarter of the year, investor focus will likely shift toward the trajectory of inflation, central bank policy decisions and corporate earnings reports. The interplay between these factors will be crucial in determining whether markets can sustain the momentum built in the second half of the year or if further volatility lies ahead. Given the elevated uncertainty, especially with the general election looming in November, a balanced approach to portfolio allocation – one that emphasizes diversification – remains prudent as we navigate the evolving market landscape.



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Sources:

1. WSJ: *How Long Can Economy's Goldilocks Moment Last?* 10.05.2024
2. Barron's: *Divided Funds Come Roaring Back*, 10.07.2024
3. Valmark: *VWS Quarterly Update Q3 2024*, 10.15.24

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