MARKET MINUTE
WITH McGAREL

Dave McGarel, CFA, CPA
Chief Investment Officer

January 2024

"Santa Claus is Coming to Town" is a great Christmas hit. Yet no one ever wrote a song called "Santa Claus is Leaving Town"...and for good reason. Reality sets in that there is a lot of work to do after a big celebration and the big man won't be back for a whole year. The Santa Claus rally in the equity markets the last two months of the year was a wild celebration. The S&P 500® Index more than doubled its return from the first ten months of the year (10.7%) by adding another 14% in just 41 trading days to end the year with a massive annual return of 26%. The much maligned Russell 2000® Index of small cap stocks did even better since October 31st. Down 4.5% through the first 10 months of 2023, the Russell 2000® Index rallied 22% in the final two months and finished up 17% on the year.

In the November Market Minute, we wrote about staying in stocks even as risk-free rates were attractive... "we believe not owning equities is the greater risk...rallies often come swiftly and being out of the market can greatly impact your long-term returns." But we certainly didn't expect this type of swift response!

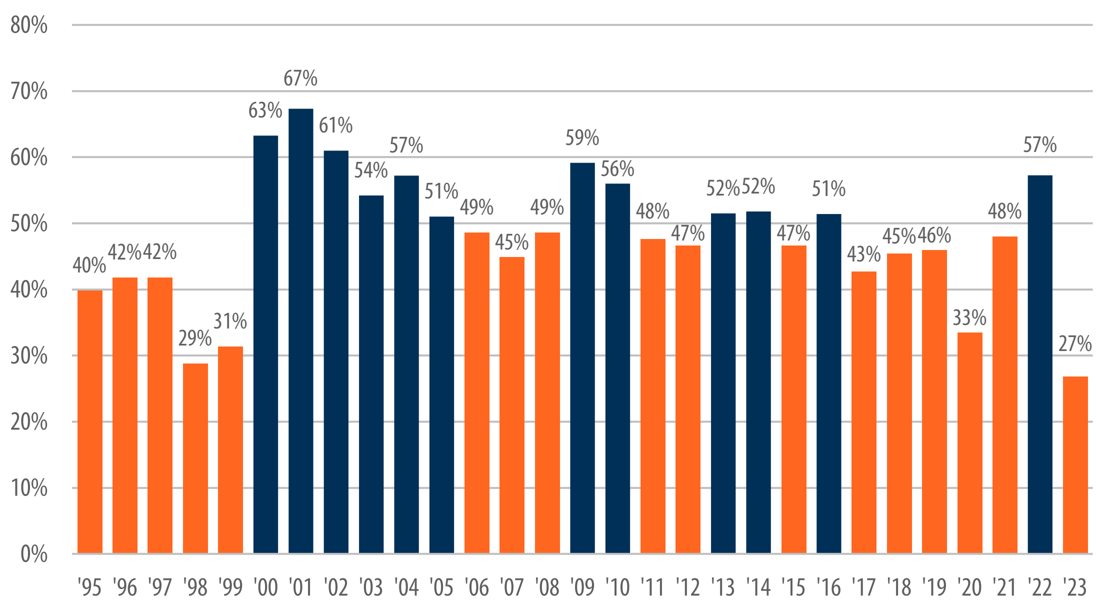
As we continue to advocate maintaining equity exposure, we believe the market rally resulted from investors signaling belief that multiple interest rate cuts will materialize sometime next year and earnings growth will reaccelerate to an above average increase of 10% or more. For the market to go higher from here, the story will have to stay intact and GET BETTER during the year. More rate cuts and bigger earnings growth extending into 2025 is needed to justify further stock gains. None of this is a certainty by any means.

We do know this. Forecasting annual returns doesn't work. At the beginning of 2022, the median forecast for the S&P 500® Index was 5,000 by December 31, 2022. Instead, the S&P 500® Index closed the year at 3,839. At the beginning of 2023, the median forecast was 4,000 by December 31, 2023. The S&P 500® Index closed at 4,770. Forecasts for both years were massively off the mark.

Where do we have the most conviction? Our belief is that the narrow market experienced over the first ten months of last year continues to broaden out in 2024 as it did in the last two months [see chart below]. As opposed to the first ten months of 2023 when only 27% of stocks outperformed the S&P 500 Index, 56% of stocks outperformed in the last two months of the year. While 2023 was highlighted by the seven largest, mostly technology related stocks leading the market, we believe 2024 will see much broader participation for two reasons: 1. Valuations are significantly better outside the largest mega-cap names in the U.S. market, 2. Technology is not the only sector expected to experience strong earnings growth as sectors such as healthcare and industrials should also grow at an above market pace.

Our final message...stay in the market and own a broad array of equities as, in our opinion, there is a wider group of companies that will reward investors in 2024 than in 2023.

Percentage of S&P 500® Index Members Outperforming the Index



Source: Capital IQ. As of 12/29/23. This example is for illustrative purposes and does not represent any actual investment.

Past performance is no guarantee of future results.

The information presented is not intended to constitute an investment recommendation for, or advice to, any specific person. By providing this information, First Trust is not undertaking to give advice in any fiduciary capacity within the meaning of ERISA, the Internal Revenue Code or any other regulatory framework. Financial professionals are responsible for evaluating investment risks independently and for exercising independent judgment in determining whether investments are appropriate for their clients.

The **S&P 500® Index** is an unmanaged index of 500 companies used to measure large-cap U.S. stock market performance. Investors cannot invest directly in an index. The **Russell 2000® Index** is a small-cap U.S. stock market index that makes up the smallest 2,000 stocks in the Russell 3000 Index.

References to specific securities should not be construed as a recommendation to buy or sell and should not be assumed profitable.