2024 was highly positive for stocks, albeit a tough ending as expectations for lower inflation and interest rates rapidly diminished heading into the third week of December. The S&P failed to provide a yearend rally, creating a negative December for the 2nd time in six years. While year over year progress has been achieved, the Fed 2% target rate for inflation has remained elusive, more so as the year progressed. Interest rates rose on the long end into yearend due to multiple factors, creating some opportunities to lock in the long end of the yield curve (mid to longer dated bonds). Although continued inflation and a rate drift higher have created headwinds, these have been offset to some degree by resilient consumers. Strong nonfarm payroll number for November (227,000 jobs added) reflected the bounce-back from the October hurricanes and a resolution to the Boeing machinists strike. The November read on unemployment was 4.2%. Fed expectations for unemployment in 2025: 4.4%, with a long term projection of 4.2%. 4.0 to 4.5% are considered full employment, a range that is consistent with price stability. Forecasts for the overall large cap market are averaging approximately 12% EPS growth for the upcoming year. 2026 EPS growth is forecast at 11% growth.

Sector rotation has been persistent in the latter half of '24, resulting in a more balanced and theoretically stable market for 2025 (see chart on page 2). Anticipation of fed rate decreases eased after the post-Fed (FMOC) commentary released in mid- December. The pace described in the statement is a slower easing path, with rate decreases back loaded toward the end of 2025. Further headwinds could reside in political uncertainty, as the post election rally was predicated on tax and regulatory reform, which now appear distant with a thin majority in the house. The implications of possible increased tariffs are unknown. If additional tariffs are implemented, the heightened probability of retaliatory tariffs will become problematic for equities and longer dated bonds, with any renewed inflation pressure representing the primary risk for the coming year.

Over the past few years, much of the US economy's momentum has been driven by progress on disinflation, the direct result of vast improvement in the supply side of the economic equation. If this dynamic is disrupted in any fashion, there will be risks to economic growth. The supply of goods and workers could be disrupted by geopolitical events, renewing pressure on the supply chain. The biggest unknown for the markets and the economy in 2025 is the policy path in Washington. New Tariffs, tax cuts, and deregulation are campaign promises that were made, but it is unclear if this will translate into legislative action. While impossible to forecast, the fixation on tariffs may not be as bad as one might think. Any improvement in US/ China/ Mexico/ Canada relations will change the narrative for the better. Much of the tariff bluster is an attempt to have trading partners fall into line with the new administration's policies.

While it is unlikely that the equity markets will return another stellar year, the outlook is optimistic and balanced. For continued growth a period of corporate change is being accelerated by AI and AI inspired new products, along with a shakeup in company leadership and corporate strategy. It is probable that Merger and Acquisition activity will expand in an environment of less restrictive regulation. There are long term structural changes at work, which include the transformative effects of AI, an aging population and energy transition to name a few. The outlook is not without risk. New policies with trade and immigration may prove to be inflationary. These concerns are offset somewhat by valuations for the majority of the equity markets trading within historical norms (P/E price to earnings ratios are not extraordinarily high).

Please call or email anytime with questions or concerns, to update objectives or to review strategy/ allocation. Note that the Morningstar portal has now been active for several quarters. The purpose is to deliver an easy and secure portal for account information, document transfer and reporting. Any issue experienced can easily be remedied with a call/ email to contact information below. Thank you and best wishes for the New Year!

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