Richard Rose Wealth Management January 13, 2025

WEEKLY COMMENTARY **Richard Rose AIF®**

Good morning,

What's in this week's Report:

- To Pause or Not to Pause? That is the Fed Question
- Weekly Market Preview – Could Inflation Data Reintroduce Rate Hike Possibilities?
- Weekly Economic Cheat Sheet – Wednesday's CPI Report in Focus
- What Does Wall Street Expect for 2025? (SPX Forecasts)

Futures are tracking global equity markets lower this morning with rate-sensitive small caps and tech shares leading declines as bond yields continue higher on the back of Friday's "hot" jobs report and new highs in the price of oil.

There were no economic reports overnight, however, the U.S. announced new curbs on AI-chip exports (specifically NVDA chips) which is pressuring mega-cap tech stocks in pre-market trade.

Today, there are a limited number of market catalysts as there are no noteworthy U.S. economic reports on the calendar and no Fed officials are scheduled to speak.

There are two Treasury auctions at 11:30 a.m. ET today (for 3-Month and 6-Month Bills) and given the hawkish reaction to Friday's jobs data, their outcomes could impact stocks. Bottom line, if Treasury yields hold pre-market levels with the 10-Yr and 30-Yr both approaching 5%, stocks will have a very difficult time stabilizing today.

Market	Level	Change	% Change
S&P 500 Futures	5,830.75	-35.50	-0.61%
U.S. Dollar (DXY)	109.98	0.33	0.30%
Gold	2,690.76	-24.24	-0.89%
WTI	76.79	1.04	1.37%
10 Year	4.767%	-0.007	-0.15%

Stocks

Last Week (Needed Context as We Start a New Week)

Stocks steadily declined last week as strong economic data and warmer-than-anticipated inflation metrics sent Treasury yields to new 52-week highs, pressuring stock benchmarks to post-election lows. The S&P 500 fell 1.94% on the week.

Stocks gapped higher to start the week last Monday as a Goldilocks Composite PMI report paired with a *Washington Post* article suggesting Trump's tariff policies would be less aggressive than feared, saw bond yields pullback and stoked risk-on money flows. Trump was quick to push back on the WaPo article, however, and yields rose after a weak 3-Yr Treasury Note auction that saw stocks give back morning gains. The S&P 500 added 0.55%.

Stocks gapped higher Tuesday with chip-giant NVDA notably hitting an all-time intraday high early. NVDA then came under heavy selling pressure, which weighed on tech, while the ISM Services Index and JOLTS were both "hot," which weighed on stocks. Bond yields accelerated higher in the afternoon after a soft 10-Yr Treasury auction and the S&P 500 ended lower by 1.11%.

On Wednesday, CNN reported that the Trump administration was mulling emergency measures to quickly implement tariff measures. That sent yields higher again and sparked a fresh wave of risk-off money flows. Economically, weekly jobless claims fell to near-one-year lows, adding more upside pressure on yields which saw the S&P 500 test critical support at 5,900 throughout the session, but the index stabilized thanks to a strong 30-yr auction and SPX ended higher by 0.16%.

Equity markets were closed in observance of President Jimmy Carter's funeral service, which left futures to chop sideways in anticipation of the December jobs report. The BLS report was "hot" with a headline topping estimates by nearly 100,000 jobs while the unemployment rate cooled to 4.1% and a gauge of wage inflation unexpectedly declined. Furthermore, long-term consumer inflation expectations in the latest UofM Consumer Sentiment release spiked to the highest level since 2008. Stocks attempted to stabilize midday but follow-through bids failed to materialize and the S&P 500 rolled over to end the day down 1.54% at a new, post-election low.

To Pause or Not to Pause? That is the Fed Question

Hot economic data has furthered the idea that the Fed may be done with rate cuts (and has already paused) and that is the main reason we're seeing stocks extend the year-end 2024 declines, as the less-dovish expectations push yields higher. Given that, I want to look at the Fed from different angles and see if these fears of a pause are legitimate.

What does the market expect? This has changed substantially. As of Friday's close, fed fund futures have priced in just one rate cut for 2025 with that cut coming in June at the earliest. Additionally, there's a 25%-ish chance of no cuts in 2025. Bottom line, while concerns about a Fed pause have pressured stocks, market expectations have reset to a much-less-dovish place. So, while the Fed announcing a pause would still hit stocks, a lot of damage has likely already been done.

What does the economic data say? The data has been too hot for two additional hikes but it's important to remember that strong growth with falling inflation does still allow for another Fed rate cut. Here's what's important to remember: Strong data isn't a problem. Strong data that the Fed thinks could boost inflation is a problem. Right now, it's not clear the strong data is the type that would boost inflation (note the wage component of Friday's jobs report was the only soft part of it) and that's why it's not getting major pushback from the Fed. The bottom line, we need to focus on inflation, not just growth. Solid economic data won't stop the Fed from easing unless that activity is so strong that the Fed thinks it'll spike inflation. Right now, it's not clear growth is strong enough to boost inflation, even though the numbers are stronger than estimates.

What does the Fed say? Fed speak was mixed last week and reflects a central bank that seems somewhat divided between continued rate cuts and a pause. The most important Fed speaker last week, Vice-Chair Waller, eased market fears by stating that he believed inflation was still trending towards the 2.0% target and even if it's slowed, it's still occurring. As such, he noted, additional rate cuts remain warranted. The FOMC minutes from December echoed those sentiments, with "many" on the FOMC expressing the belief that inflation is still trending towards 2.0% (which keeps rate cuts on the table).

However, other regional officials were a bit hawkish. Fed Governor Bowman was explicit, saying she believed the December cut should be the last one for a while. Kansas City Fed official Schmid also said he believed Fed policy was close to neutral, which inherently means he'd be hesitant to cut further. Bottom line, Fed leadership matters and so far, Powell, Waller, and Williams think inflation is still trending lower. As long as that's the case, they'll still be open to another rate cut.

Where does that leave us? Despite rising fears of a pause, neither the data nor Fed speak implies that the Fed is there yet. And with Fed Funds still far above annual inflation, Fed officials have room to continue to cut. Bottom line, while the chances of a pause have risen, I don't think the data warrants it at this point, and this market could be in for a bit of a relief rally if Fed leadership echoes that sentiment.

What makes it worse? Any Fed-driven selloff will get substantially worse if we see the idea of rate hikes come back on the table. That is a worst-case scenario for stocks from a Fed standpoint and would be a bearish game-changer. If inflation reports are hot (including Wednesday's CPI) we need to watch for rate hikes to re-enter the conversation because if they do, that's a substantial negative.

Economic Data (What You Need to Know in Plain English)

Last Week

After weeks of nearly perfectly Goldilocks data that fueled the Q4 rally, metrics turned decidedly "Too Hot" last week as virtually every notable economic report was stronger than expected, and that boosted fears the Fed has already paused rate cuts (which would remove a significant reason behind the 2024 rally).

The headline report last week was Friday's jobs report and while it didn't meet all the criteria to be "Too Hot" it was close enough for a market that's worried about a Fed pause. The headline job ads were a big beat at 256k vs. (E) 164k, the biggest reading in several months. The unemployment rate dropped to 4.1% (lower end of the "Just Right" range). The lone bright spot for Goldilocks was wages, which rose 3.9% vs. (E) 4.0%, but frankly, that's not important enough to offset headline job adds.

The immediate market reaction was as we all expected: The 10-year yield spiked 10 bps and hit a one-year high and the Dollar Index jumped to just below 110, hitting a two-plus year high. Those moves pressured stocks and the S&P 500 dropped sharply.

While the jobs report was the most followed "Too Hot" report last week, it was not the only one. The ISM Services PMI (one of the "big three" monthly reports) echoed recent data in beating estimates and adding to fears the Fed could pause rate cuts (or has already and just hasn't communicated it yet). The Services PMI rose to 54.1 from 53.5 while New Orders, the leading indicator in the report, also increased to 54.2 from 53.7. That's not a "hot" reading but it's a healthy one from an activity standpoint. Prices, meanwhile, jumped to 64.4 from 57.2, and if we take the increase in the price index along with the healthy headline readings, there's enough in this report to strengthen the argument in the FOMC for a pause. And like virtually all the recent "hot" data, this reading boosted yields and pressured stocks.

Important Economic Data This Week

Have they paused, or haven't they? That's the main question for markets and this week could bring a lot of additional clarity on whether a pause becomes more likely because we get important inflation and economic growth updates. If both are hot (as they've been recently) then fears of a pause will rise and that will increase headwinds on stocks.

The most important report this week, by far, is Wednesday's CPI. Put simply, if it's hotter than expected it's going to spike pause fears and Treasury yields and likely hit stocks. Headline CPI printed 2.7% y/y and core CPI was 3.3% y/y in December. If we see increases in both it will dramatically increase support for a pause in rate cuts and that will be an incremental market negative.

CPI isn't the only important inflation report this week as we get PPI tomorrow. Normally, PPI is overshadowed by CPI (and PPI usually follows CPI) but it's flipped this month so don't be surprised if PPI moves markets temporarily if it's especially hot (or cold, which would be positive).

Away from CPI and PPI, we also get several notable readings on growth this week, the most important of which is Thursday's Retail Sales report. As long as employment is solid and retail sales are stable and/or trending upward, the chances of an economic slowdown are low. And given rising yields and worries about Fed rate cut pauses, Goldilocks data points to solid activity but noting "Too Hot" is needed to help support stocks.

In addition to retail sales, we also get the first look at January economic activity via Empire Manufacturing (Wednesday) and Philly Fed (Thursday). Both indices have been very volatile recently and Goldilocks readings are the preference for stocks. That means numbers around zero (slightly negative or slightly positive) that don't imply a sudden collapse in activity anecdotally strengthens the case for a pause.

Turning towards the Fed, there's a lot of communication from it this week. On the speaker front, there are a lot of officials out there this week but the key is to focus on leadership as NY Fed President Williams is speaking on Tuesday. If he echoes Waller's comments that he thinks inflation is still trending towards 2.0%, it'll be a positive and push back against pause fears. If he doesn't, and hints at a pause, prep for more volatility in stocks and bonds.

Special Reports and Editorial

What Does Wall Street Expect for 2025? (SPX Forecasts)

Wall Street loves forecasts, and with the start of the new year, I thought it'd be useful to compile the major Wall Street firms' forecasts for the S&P 500 to gauge how bullish (or bearish) the consensus estimate is for 2025.

For context, we've just finished the best two-year run in the S&P 500 since 1997-1998 as the S&P 500 had a total return of greater than 25% for two years in a row. So, did that make Wall Street strategists more bullish (with an expectation the good times will continue to roll) or did it make them hesitate the market can add a strong year of returns?

First, if we see another strong year of returns in the S&P 500 it'll be an infrequent occurrence. Three consecutive years of 10%-plus returns for the S&P 500 is rare. Going back to 1928 (price only), there were only five stretches where it happened:

· 2019-2021, 2012-2014, 1995-1999, 1949-1952, 1942-1945.

And if we're talking about three straight years of 20%-plus returns for the S&P 500 there was only one stretch that fit the bill: 1995-1998. The point is that three straight years of strong returns is pretty hard to come by, but as you can probably guess, that hasn't dissuaded Wall Street strategists from predicting strong additional returns in 2025.

Wall Street is leaning towards the S&P 500 completing a double-digit performance three-peat. Using the index's close on December 31 close of 5,881, 22 of 25 firms we observed (or 88%) are predicting 10%-plus returns in 2025. If that ends up being correct, it'd just be the sixth time it's occurred since 1928.

Investment Firm	2025 S&P 500 Forecast (High to Low)
Oppenheimer	7,100
Wells Fargo	7,007
Capital Economics	7,000
Deutsche Bank	7,000
Federated Hermes	7,000
Yardeni Research	7,000
DataTrek Research	6,840
Societe Generale	6,750
BMO Capital Markets	6,700
HSBC	6,700
Bank of America	6,666
Barclays	6,600
Evercore ISI	6,600
Fundstrat	6,600
Ned Davis Research	6,600
RBC	6,600
UBS	6,600
CFRA	6,585
Citigroup	6,500
Goldman Sachs	6,500
JPMorgan	6,500
Morgan Stanley	6,500
LPL Financial	6,325
Stifel	5,500
BCA Research	4,450

Getting more granular, the average forecast is an 11.7% return. On the high end, Oppenheimer's 7,100 forecast produces a 20.7% projected return (which would make it only the second time we've seen three straight 20%-plus consecutive returns. On the low end, BCA Research's 4,450 forecast delivers a -24% projected return.

What's with the wide variance from top to bottom? Oppenheimer's John Stoltzfus points to strong fundamentals that suggest the current resilience of the economy and the stock market can continue into 2025, with the continued development and adoption of AI technologies being a big driver of next year's projected gains.

On the other end, BCA Research's Peter Berezin expects a bear market with global economic growth slowing sharply in 2025, largely driven by a Trump-induced global trade war and global recession.

Now, how accurate have these forecasts been recently? Well, not so accurate.

Major firms' forecasts have underestimated the S&P 500's performance in four of the past five years. (This year's forecasts may have been the worst, as all year-end S&P 500 targets are well below 10% or more where the index sits now.) However, that has not been the norm. Strategists have overestimated stock performance in 13 of the last 20 years.

Bottom line: forecasts are always popular this time of year and clients ask about them so I wanted to compile the ones from the major firms so you have them to discuss and reference, if needed.

For what it's worth, I hope the consensus is right and that we see another strong year of gains, but I must admit seeing analysts increasing bullish bets after underestimating the markets over the past year is typical analyst behavior. So, again, while I hope they're right, I think it's still wise to view the start of 2025 as one that's likely to be more volatile and stressful than what we saw in 2024.

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