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Investment Institute

Market Commentary

Weekly perspective on current market sentiment **January 8, 2025**

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Last week's S&P 500 Index: -0.5%

New year thoughts

Key takeaways

- A casual observer likely looks at the state of the economy and world events and wonders how 2025 will play out.
- We expect opportunities in both equites and fixed income to broaden as the economy grows in 2025.

As the calendar turned to the new year, investors looked back and almost certainly were happy with the results as the S&P 500 Index (SPX) notched its second consecutive year of gains in excess of 20% (+23.3%). We are looking for another year of positive, if more modest, returns for stocks and see the SPX finishing this year in the 6,500 – 6,700 range. Not bad at all by historical standards.

A casual observer likely looks at the state of the domestic economy and all that is happening around the world and wonders how 2025 will play out. Is inflation going to further impact my personal spending? Will jobs be easy or hard to find? Will any of the various conflicts happening around the world, particularly in Eastern Europe and the Middle East, turn into a more widespread concern? Those are just a few of the questions that may have been asked and discussed at holiday gatherings over the last couple of months. Many of our regular readers may have those same questions.

This week we are going to attempt to tackle the big picture: the economy. Growth last year came in stronger than we anticipated, and we see the domestic economy turning in a year of modest growth in 2025. Note that relative to the rest of the world, particularly the developed world (i.e., the eurozone and Japan), we see the U.S. as the global growth leader in 2025. That will likely keep the U.S. dollar stronger than might otherwise be the case and should bode well for domestic assets (stocks and bonds) relative to international equities and fixed income. Hence our preferred overweight to the U.S.

Inflation is sure to be a hot topic this year. We believe the Consumer Price Index (CPI) will rise 3.3% in 2025. Note that this estimate is well above the current 2.5% increase the consensus on Wall Street is expecting. Sources of higher inflation as we move through 2025 include commodity prices (i.e., oil) and increased consumer and/or business activity, especially in services, which have been the main driver of inflation since 2022. In particular, we see continued inflation in the price of health care, insurance (auto and home), and housing/shelter costs. New tariffs should increase the prices of imported goods. Higher-for-longer inflation and better economic growth in 2025 are also likely to help push interest rates somewhat higher. For example, we see the yield on the 10-year Treasury note ending the year in the 4.5% to 5% range. The current 10-year yield has recently breached the lower end of that range.

Our outlook on the economy also results in opportunities for large, diversified companies with robust cash flows and strong balance sheets to grow earnings. We see earnings for the SPX rising at a double-digit rate this year, and accounting for the gains, we believe that will take the S&P 500 Index into our target range.

We expect opportunities in both equites and fixed income to broaden as the economy grows in 2025.

Risk considerations

Forecasts and targets are based on certain assumptions and on views of market and economic conditions which are subject to change.

Each asset class has its own risk and return characteristics. The level of risk associated with a particular investment or asset class generally correlates with the level of return the investment or asset class might achieve. **Stock markets**, especially foreign markets, are volatile. Stock values may fluctuate in response to general economic and market conditions, the prospects of individual companies, and industry sectors. **Foreign investing** has additional risks including those associated with currency fluctuation, political and economic instability, and different accounting standards. These risks are heightened in emerging markets. **Bonds** are subject to market, interest rate, price, credit/default, liquidity, inflation, and other risks. Prices tend to be inversely affected by changes in interest rates. Although **Treasuries** are considered free from credit risk, they are subject to other types of risks. These risks include interest rate risk, which may cause the underlying value of the bond to fluctuate.

Definitions

Consumer Price Index (CPI) produces monthly data on changes in the prices paid by urban consumers for a representative basket of goods and services.

S&P 500 Index is a market capitalization-weighted index composed of 500 widely held common stocks that is generally considered representative of the U.S. stock market.

An index is unmanaged and not available for direct investment.

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