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January 2025 Market Commentary

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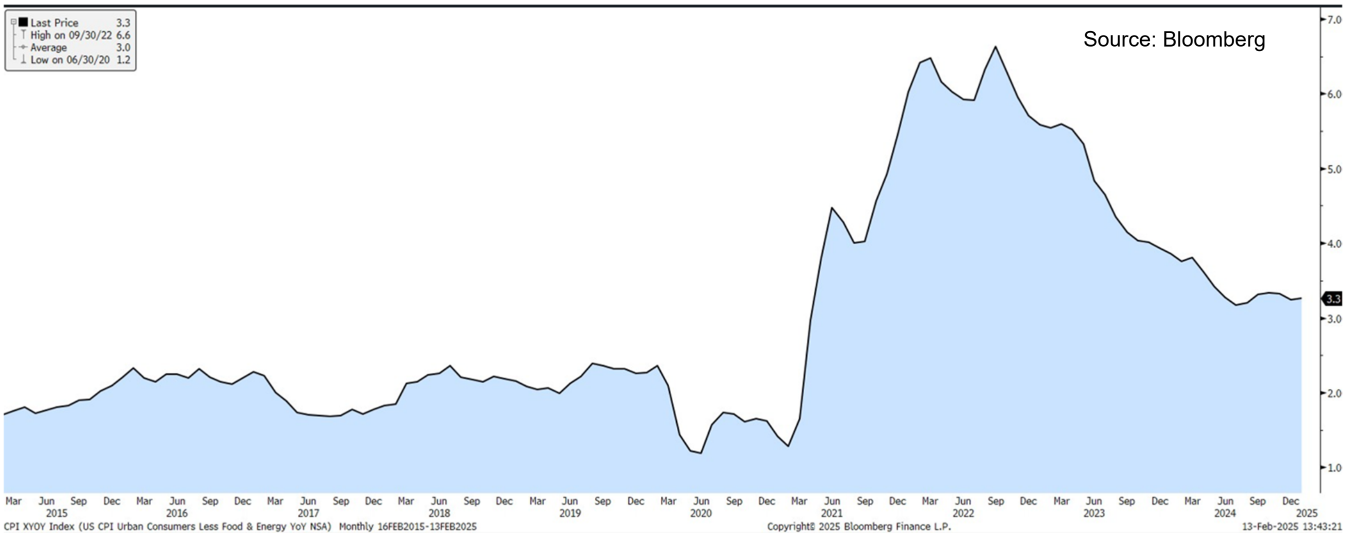
Stocks contend with some volatility but start the year in the black. Optimism around the new administration's economic policies, including the potential for deregulation and tax cuts, helped boost stocks to start the year. The S&P 500 gained 2.8%, the NASDAQ rose 1.7%, and the Dow jumped 4.8%. In a turn from last year, the Russell 1000 Value Index was up 4.6% for the month, outperforming the roughly 2% gain for the Russell 1000 Growth Index. Every sector was higher for the month except for technology, which dropped 0.7%. The emergence of China's DeepSeek AI model reportedly developed for a fraction of the price of U.S. companies' models and some lackluster earnings reports weighed on the sector.

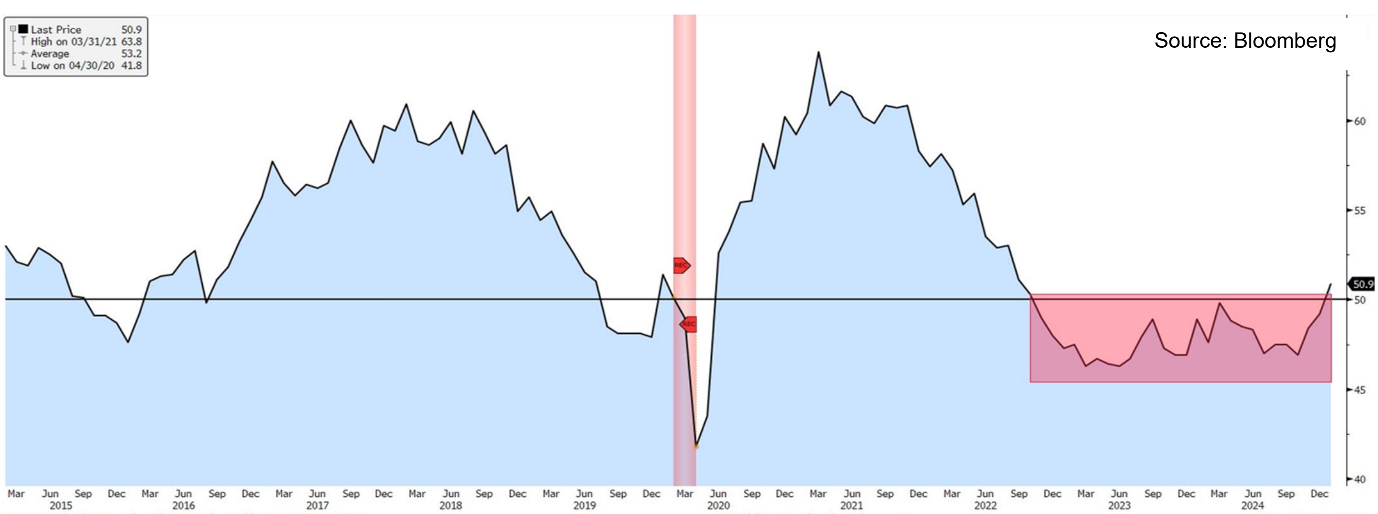
Inflation remains sticky, pushing additional rate cuts to the backburner, while tariff negotiations take center stage. The Consumer Price Index (CPI) released earlier in the week came in higher than expected with the less volatile Core CPI (excluding food and energy prices) increasing 0.4% month-over-month and +3.3% year-over-year. The seasonal exercise of companies pushing through annual price hikes to start the year (perhaps exacerbated by potential tariff moves this year) could explain some of the increase. At the same time, another contributing factor is likely related to the recent bout of natural disasters around the country, which can temporarily drive prices of things like used cars, hotel rooms, and building materials higher. Despite the potential transitory factors in the latest report, core inflation remains sticky, which will likely keep the Fed comfortably in a wait-and-see mode over the next few months given still restrictive policy, especially with immigration policies, tariff measures, and federal spending all in flux. Yet importantly, we also do not foresee a rate hike in the offing and given strong corporate earnings (fourth quarter 2024 earnings growth is on track to be the highest since 2021), a stable employment backdrop, improved business optimism under the new administration, and staggering ongoing AI-related investments, we generally remain constructive on the backdrop for equities. Over the next few weeks, tariff negotiations ahead of an April deadline for reciprocal tariffs will likely be a source of volatility.

Core CPI plateauing above Fed target



ISM Manufacturing data is encouraging for broader equity market participation. The January ISM manufacturing reading came in above expectations at 50.9. This is the first reading in expansionary territory (above 50) in 26 months—an extended stretch by historical measures that typically would be associated with a recession. In addition, the New Orders component also ticked up to a 3-year high. A sustained upswing in manufacturing parts of the economy would bode well for broader equity market participation, in our view, and we are constructive on names leveraged to a turn, including in the transportation, software, and industrial areas.

ISM Manufacturing posted first reading in expansionary territory in 26 months



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