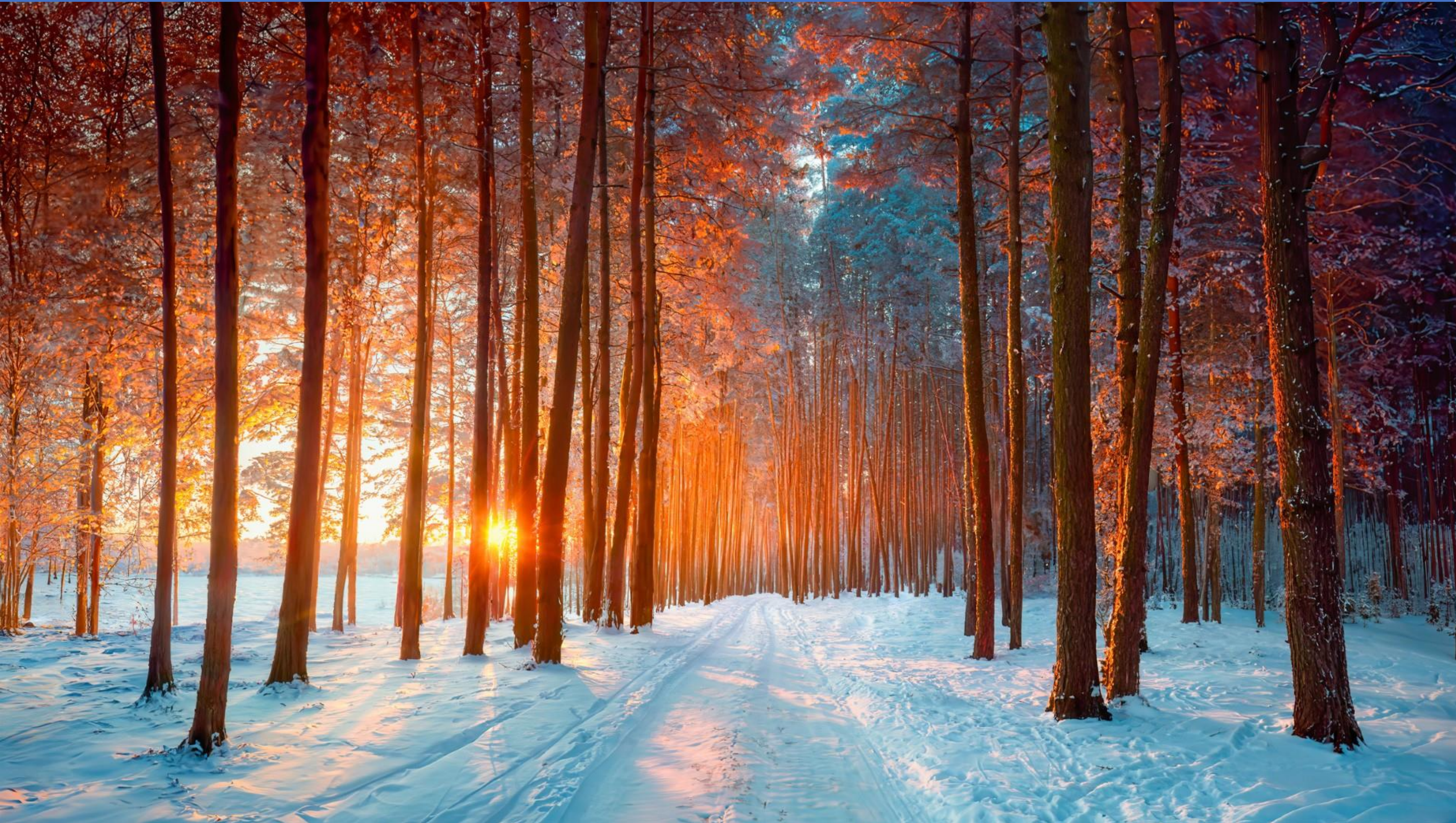
NORTHEAST SEQUOIA
PRIVATE CLIENT GROUP



2025 Outlook

Miles To Go And Promises To Keep

Christopher Pike, CFA®
chris.pike@northeastprivate.com
973-422-4107

Mark Murphy, CLU®, ChFC
Benjamin Bush, CLU®, ChFC®
Adam Schlosberg, CFP ®
Christopher Viola, AIF®

Table of Contents

Executive Summary 2
Year In Review 2
Just When You Think You've Seen It All 2
Sector and Style Recap 6
Style Tilts -- Déjà vu All Over Again 8
Recessions...Slowly At First, Then All At Once 11
2025 Outlook 18
Miles To Go And Promises To Keep 18
Fiscal Policy 21
Trade Policy 21
Deregulation 22
Immigration 23
Is Division Additive? 24
Economic Outlook 26
Nice, Nice, Not Thrilling But Nice 26
The Bill Always Comes Due 36
Returning For A Limited Time Only: Inflation 39
Growth Expectations 43
Capital Market Outlook 45
Don't Wake The Bear 45
Earnings-Yield Multiple Model: 47
Valuation-Mix Multiple Framework: 47
Disclosures: 49

Executive Summary

- The post-pandemic era continues to bring unprecedented economic and geopolitical challenges. In 2024, national elections across 60+ countries representing 50% of global GDP will shape politics, policy, and capital markets. Expect the unexpected in 2025, as geopolitical uncertainty remains high, laying the foundation for potential disruptions and surprises.
- Despite potential challenges, we remain **opportunistically cautious** in the near term for both the economy and capital markets. While expansionary fiscal policy and deregulation may provide a modest boost to GDP by late 2025 and early 2026, tariff uncertainty and immigration restrictions may result in persistent inflation and higher interest rates. The Fed may need to choose between curbing inflation or supporting the labor market and preventing a recession.
- 2024 evoked a wide range of feelings and emotions, but one thing is sure: 2024 equity market returns were solid. The S&P 500 delivered a consecutive total return of at least 25% for only the second time in history.
- The Communication sector was the best-performing sector in 2024, followed by Technology and Discretionary names. Lagging sectors included Healthcare, Energy, Real Estate, and Materials. Cyclicals outperformed Defensives, Growth outperformed Value, Large Caps outperformed Small Caps, and Domestic equities outperformed International names. In fixed-income, Baa Corporate Bonds returned roughly 3% for the year. High Yield bonds outperformed, while Long Government Bonds lagged.
- The prevailing narrative is that the FOMC has orchestrated a soft landing, but we remain skeptical. Research that we follow suggests that soft landings are idiosyncratic, making it difficult to draw meaningful comparisons or identify consistent similarities among them.
- Vice President Harris and President-Elect Trump shaped their campaigns around policies appealing to their respective bases. Campaign promises are like proposals and play a crucial role in elections, especially when linked to polarizing issues related to money or social benefits. However, delivering on promises is frequently limited by practical constraints and opposition; in the end, actions carry more weight than words. Given this context, we believe the success (or failure) of President-Elect Trump's 47th presidency will rest in 4 key policy areas: deregulation, immigration reform, fiscal policy, and trade/tariffs.
- Despite higher interest rates, the U.S. economy remained resilient entering the final stretch of the election cycle, supported by strong productivity gains, steady employment, responsive monetary policy, and a robust consumer. While these positive trends may persist into early 2025, we expect them to become less supportive of overall economic growth as we move through 2025.

- The U.S. federal debt has risen to $36 trillion, debt-to-GDP will top 121%, and debt service costs are projected to exceed defense spending and Medicare combined. While a U.S. default remains highly unlikely, its potential consequences could devastate the global economy and capital markets.
- The COVID-19 pandemic led to unprecedented monetary policy measures, which expanded the Fed's balance sheet and contributed to historically high inflation. Inflation metrics remain above the Fed's 2% target despite subsequent cooling. While the FOMC has recently started to cut rates, recent economic revisions reflect rising concerns about inflation risks moving forward, especially amidst potential fiscal pressures arising from President-Elect Trump's policies. As economic normalization continues, concerns about the Fed's credibility and external political pressures could influence future policy decisions, especially if the economy falters in 2025.
- Consensus GDP growth estimates stand at 2.0% for 2025 and 2026, assuming fiscal easing and deregulation will balance the effects of tariffs and immigration restrictions. Notably, recession risks are not currently reflected in these forecasts, and forecasters have been known to be wrong.
- Recent market gains have been driven by momentum, advances in AI, and zealous investor sentiment. Further, we believe a significant post-inauguration bounce in economic activity is somewhat unlikely, as overall consumer confidence is not showing the same trajectory as before President Trump's first term. As a result, we expect limited multiple expansion going forward; any market increases will need to rely on earnings growth in the face of heightened uncertainty. ***We estimate that the base case fair value for the S&P (price-only) at year's end 2025 will be roughly 6,300, or as much as a 7% price-only return from year-end 2024 levels***. **Our bear case** fair value for the S&P 500 is 5,300, while our **bull case** fair value for the S&P 500 is 6,600.
- Our **base-case** sector allocation recommendations would be those benefiting from a Bear Steepener[1] interest rate regime where yields on long-maturity Treasuries rise relative to short maturities. Outperforming sectors in this scenario are historically Discretionary, Materials, Technology, Industrials, Financials, and Energy, all potentially befitting from expansionary fiscal policy and deregulation. Further, sectors that have traditionally underperformed, such as Utilities and Telecommunications, may not fare as poorly in the current climate. Utilities may benefit from AI utilization, and telecommunications may continue to benefit from remote working, positive demand trends in media/entertainment, and AI utilization.
- We believe fixed income may remain challenged in 2025, with the ultimate path of inflation and interest rates unknown. However, an economic soft patch later in 2025 could help support bonds, with credit modestly outperforming duration.

[1] For more on our Interest Rate Regime construct, see our 2024 Outlook.

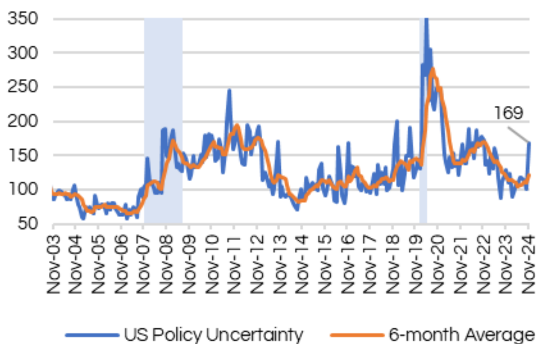
Year In Review

Just When You Think You've Seen It All

The unprecedented economic, capital market, and geopolitical events that followed the pandemic should have equipped even the most seasoned market participants with heightened resilience and adaptability. But when you think you have seen it all, 2024 reminds you to expect the unexpected.

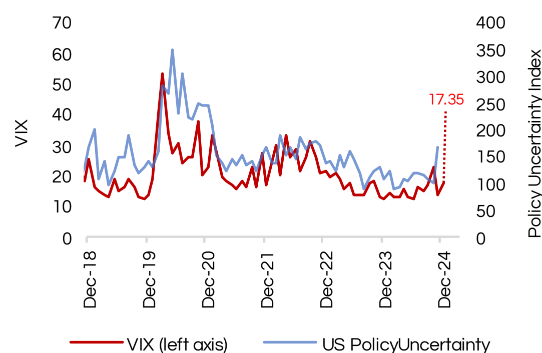
In 2024, over 50% of the world's GDP was influenced by elections, as nearly two billion people across more than 60 countries voted. Political polarization has become the norm, and leadership changes often lead to significant policy shifts, adding to global economic and geopolitical uncertainty. **While we strive to remain politically agnostic, we cannot dismiss that politics shape policy, affecting economies and capital markets.**

Exhibit 1: U.S. Policy Uncertainty



Policyuncertainty.com and NEPCG

Exhibit 2 U.S Policy vs. VIX



Policyuncertainty.com, FactSet and NEPCG

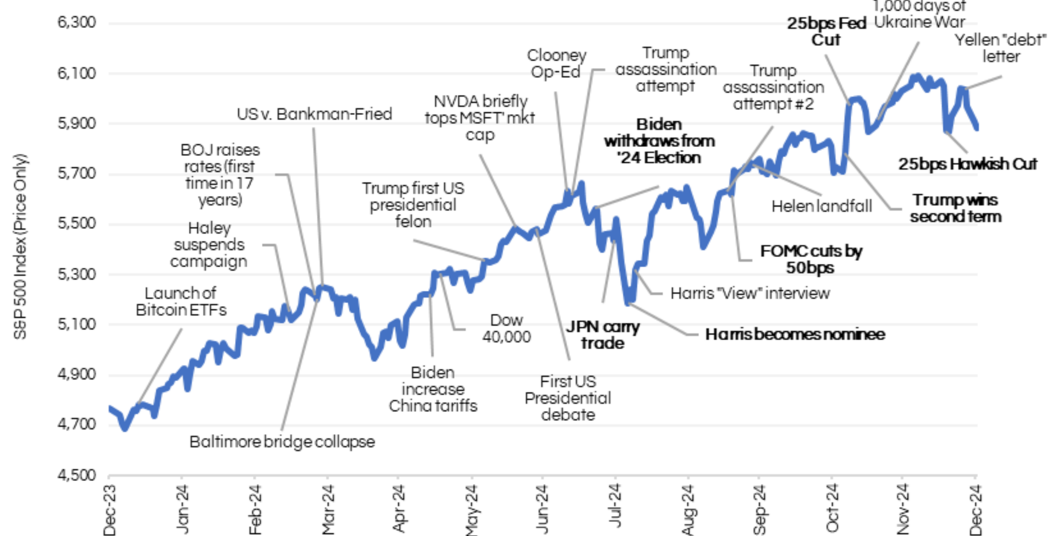
Further, when unpacking all the potential risks and opportunities that lie ahead, we remain skeptical that 2025 will be a smooth year. Further, we remind investors that they can never entirely discount black swans[2]. Recent data provided by Policyuncertainty.com highlights this notion. In Exhibit 1 we illustrate the time series of this index dating back to 2003. In Exhibit 2, we overlay the recent trends in political uncertainty to the VIX or

[2] A black swan is an unpredictable event that is beyond what is normally expected of a situation and has potentially severe consequences.

the CBOE Volatility Index. Historically, there is a negative correlation[3] between the VIX and the S&P 500, or in the simplest terms, a relationship between two variables, such as when one moves up, the other moves down.

Still, when stepping back from the tea leaves, we are left **opportunistically cautious** regarding the U.S. economy and capital markets, at least in the near term. Despite the anticipated economic drag from tariff proposals, fiscal policy and deregulation may offset much of the negative impact, resulting in a modest boost to GDP in late 2025 and 2026.

Exhibit 3: 2024 Tale of the Tape



NEPCG and FactSet data as of 12/31/2024

However, lingering tariff uncertainty and higher-than-expected interest rates may ultimately temper growth and pose headwinds to the equity capital markets. Fiscal expansion and immigration restrictions could add further inflationary pressure. We anticipate the Fed will cut rates by 50 basis points in the first half of 2025 (25bps in both March and June 2025), bringing the overnight borrowing rate to 3.75-4.00%. However, if significantly higher tariffs take hold in the second half of 2025, a supply

[3] Correlation, in the finance and investment industries, is a statistic that measures the degree to which two securities move in relation to each other. Correlations are used in advanced portfolio management, computed as the correlation coefficient, which has a value that must fall between -1.0 and +1.0.

shock may unfold. At that point, the Fed will need to determine the lesser of two evils: to pause further rate cuts to temper a return of inflation or continue to ease to avert a recession and stall in the labor market.

Depending on who you asked and when you asked them, 2024 brought feelings of excitement, anger, hope, confusion, joy, frustration, and, for some, ambivalence. **But one thing is for certain, 2024 equity market returns were solid.**

The S&P 500 returned 25.0% in 2024 (including dividends). This strong performance occurred despite an elevated level of geopolitical uncertainty. Notably, 2024 marked only the second instance where the S&P 500 posted back-to-back annual returns exceeding 25%. The last time this happened was following a period when the FOMC successfully managed what some consider the only soft landing (December 1993 through April 1995)[4].

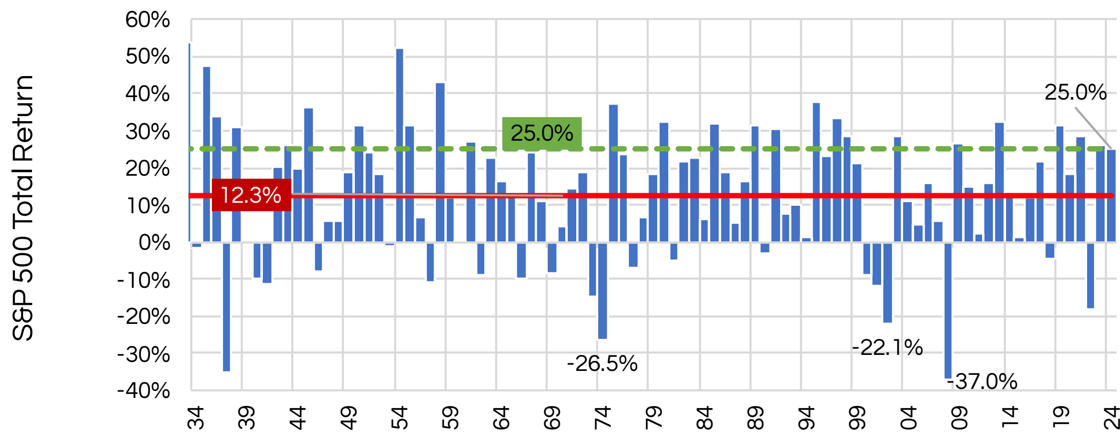
Exhibit 4 illustrates the average annual, 5-year compounded, and 10-year compounded total returns for the S&P dating back through time. We found that since 1926, the S&P has returned over 12% per year, on average. On a 5-year lookback (or 5-year compound annual holding period), the average total return has been 10.5%, and over a 10-year lookback, the average total return has been 10.6%.

Over the past 99 years, there have been 73 years (instances) of **positive** returns, averaging 21.4%. During the 26 instances of **negative** returns, the S&P fell by 13.4% on average. This implies that investors were pleased roughly 74% of the time, while 26% of the time, they were disappointed. Considering a 5-year holding period (94 instances), there have been 82 annualized periods of positive returns, averaging 12.7%. During the 12 cases of negative annualized returns, the S&P fell by 4.6% on average. This implies that investors were pleased roughly 87% of the time, while 13% of the time, they were disappointed.

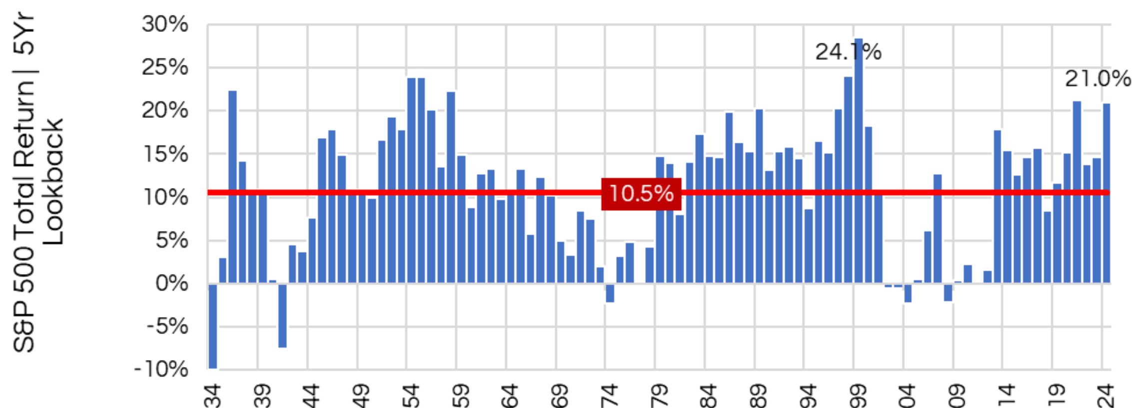
[4] See "Landing, Soft and Hard: The Federal Reserve, 1965-2022, Alan S. Blinder

Exhibit 4: Historical S&P 500 Annual Returns

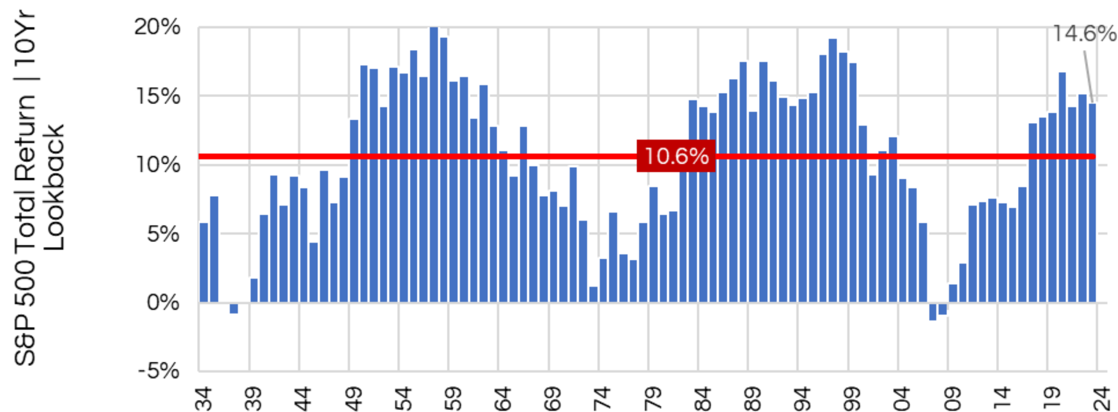
Annual Total Returns



5 Year Look Back



10 Year Look Back

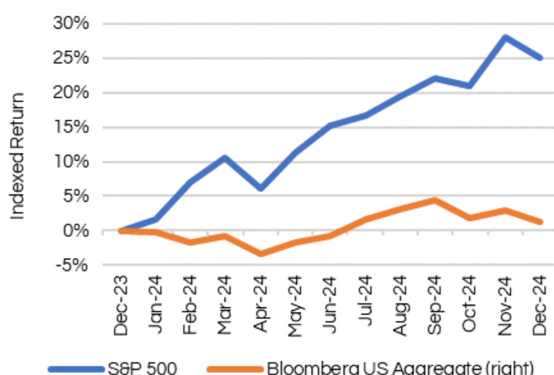


NEPCG and FactSet, data as of 12/31/2024

Finally, over a 10-year holding period, there have been 84 periods of positive returns, averaging 11.1%. During the 4 instances of negative annualized returns, the S&P fell by 0.8% on average.

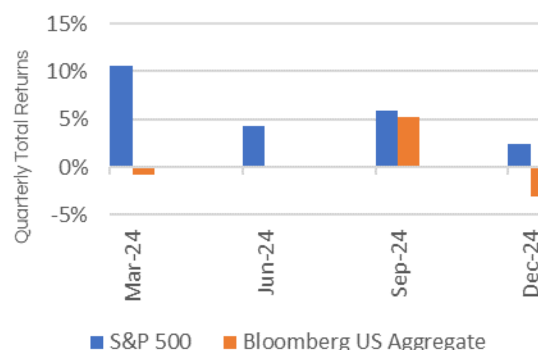
In Exhibit 5, we illustrate the monthly index total returns for the S&P 500 (our equity proxy) and the Bloomberg U.S. Aggregate Bond Index (our bond proxy). In Exhibit 6, we illustrate the quarterly returns for both equities and bonds.

Exhibit 5: 2023 Index Total Returns



FactSet and NEPCG

Exhibit 6: 2023 Quarterly Total Returns



FactSet and NEPCG

While equities enjoyed a general uptrend throughout 2024, bonds exhibited more volatility. Through the first six months of 2024, bonds delivered relatively flat returns. Conversely, Equities posted a 15.3% total return by mid-year, recovering almost 9% following a roughly 5% sell-off in April. The second half of 2024 was also solid for the equity market, gaining over 8%, while bonds again exhibited more volatility. In the fourth quarter, bonds were down 3.1%, offsetting a solid +5.2% return in the 3Q print, still ending the year down about 2%.

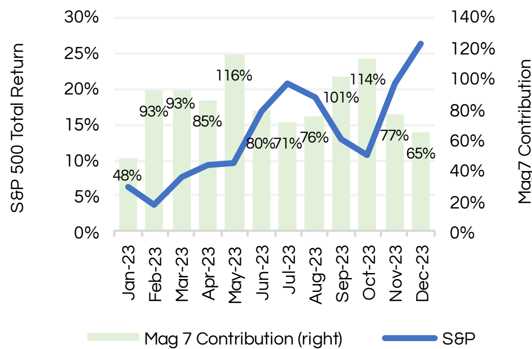
Sector and Style Recap

In general, 2024 favored Large-Cap, Growth, and Cyclical equities. However, the vector of outperformance varied throughout the year as an early rotation away from the Mag 7[5] helped support a brief relief rally for Value and Defensive names. Further, Small-cap stocks experienced a rally in mid-2024 and again in the fall, but ultimately surrendered market leadership back to Large Cap/Growth/Technology in the last few months of the year. Unlike 2023, when the Mag 7 contributed as much as 116% to

[5] AAPL, MSFT, AMZN, NVDA, GOOG(L), META, and TSLA

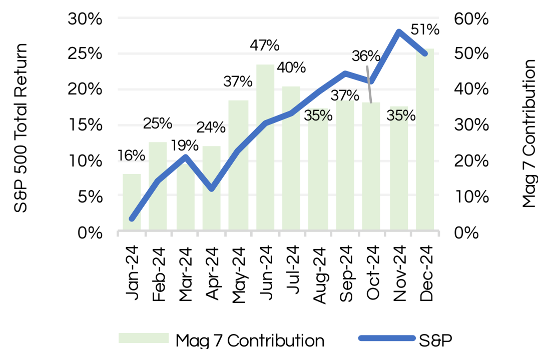
the S&P 500's return at some point, 2024 witnessed a more comparable contribution to overall returns. **At the end of 2024, the total return of the Mag 7 (roughly 43%) represented over half of the 25.0% total return for the S&P 500. In comparison, in 2023, the Mag 7 returns (75%) represented as much as 65% of the S&P's 26.3% total return.**

Exhibit 7: 2023 Mag 7 Contribution



FactSet and NEPCG

Exhibit 8: 2024 Mag 7 Contribution

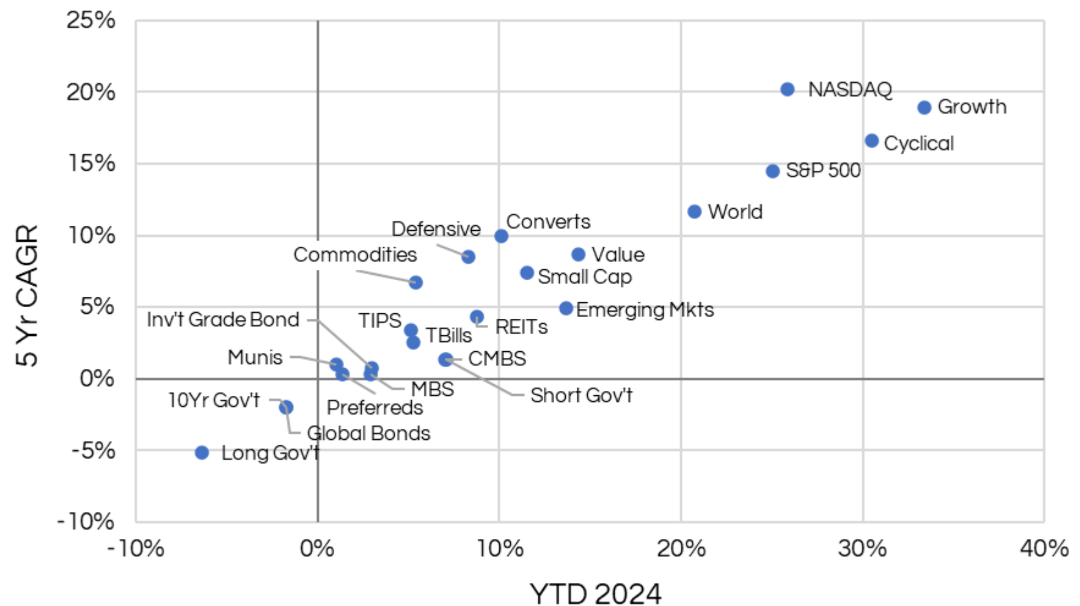


FactSet and NEPCG

Sector returns in 2024 were once again divergent. Growth and Cyclical styles within equities outperformed the S&P 500, while Value, Global Stocks, Emerging Market Equity, and Defensive names underperformed. However, even the worst-performing equity styles/sectors were higher by almost 8% in 2024.

From a **sector** perspective, the Communication sector outperformed, higher by roughly 39%, followed by Technology (+36%), Discretionary (+29%), and Financials (+28%). Underperforming, while still providing positive returns, were Utilities (+20%), Industrials (16%), Staples (+12%), Real Estate and Energy (+2%, respectively), and Healthcare (+1%); the lone negative-performing equity sector in 2024 was Materials, down almost 2% on the year.

Exhibit 9: 2024 vs 5Yr CAGR | Capital Market Total Returns



NEPCG and FactSet data as of 12/31/2024

Concerning fixed-income, High Yield (below Investment Grade) had a banner year, up by 8%, followed by Short Duration Governments (+7%), CMBS (+7%), High Yield Municipals (+6%), and T-Bills (+5%). Underperforming, relative to Investment Grade Corporates), which returned 3%, were Preferred Equities (+1%), 1-10Yr Municipals (+1%), Global Bonds (-2%), the 10Yr (-2%), and Long Government Bonds (-6%).

Style Tilts-- Déjà vu All Over Again

As we believe the political backdrop may shape capital market returns in the future, when further reviewing the 2024 style tilts, we compared them to the period leading up to and following the 2016 Election.

As we illustrate in Exhibit 10, Growth outperformed Value during 2024, with more notable outperformance following the 2024 election. In 2016, Growth underperformed Value for most of the year, but following Election Day 2016, Growth started a rally that lasted over a year. ***We would not be surprised to see Growth once again outperform Value over the near-term.***

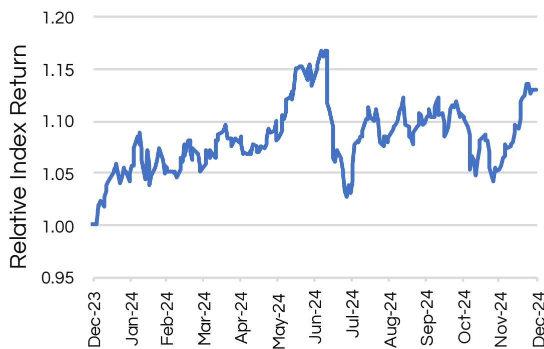
Exhibit 10: Growth v. Value 2024

FactSet and NEPCG

Exhibit 11: Growth v. Value 2016-17

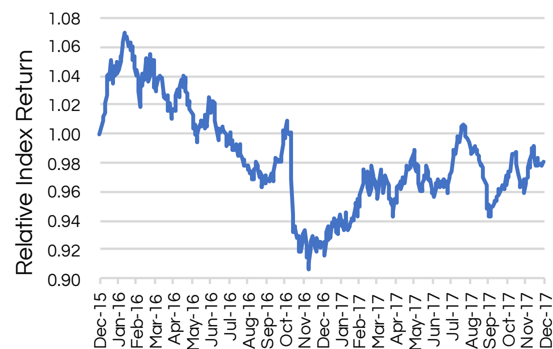
FactSet and NEPCG

Exhibit 12: Large Cap v. Small Cap 2024



FactSet and NEPCG

Exhibit 13: Large Cap v. Small Cap 2016-17



FactSet and NEPCG

In 2024, Large-Cap names outperformed Small-Cap names by about 13%. However, leadership bounced around throughout the year. Following the election, Large-Caps outperformed by almost 10%.

In looking at the lead-up to election day 2016, Small Caps outperformed for most of the year, leading into October. Some investors believe the several "October Surprises[6]" helped fuel a short-term bounce in more liquid stocks. However, this quickly reversed, and Large Caps fell by almost 10% through year's end and didn't fully recover until August 2017. ***We would not be surprised to see rich-valuation Large Cap names exhibit similar***

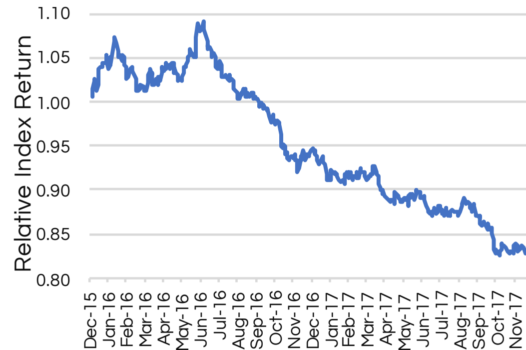
[6] An October Surprise is an unexpected political event or revelation in the month before a presidential election, especially one that seems intended to influence the outcome.

underperformance as investors try to game out the various implications of a Trump '47 policy agenda.

Exhibit 14: Defensive v. Cyclicals 2024

FactSet and NEPCG

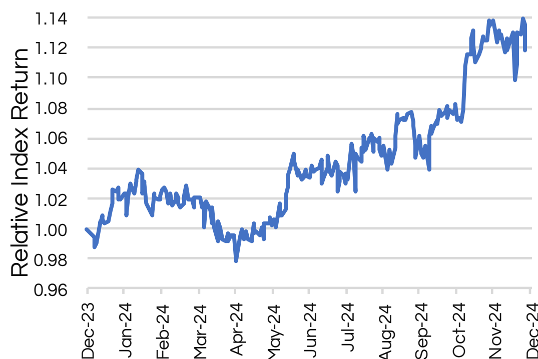
Exhibit 15: Defensive v. Cyclicals 2016-17



FactSet and NEPCG

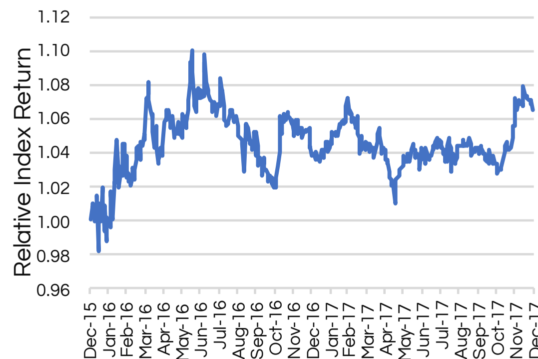
Except for a brief period during the summer, Cyclical names outperformed Defensives for most of 2024. By the end of the year, Cyclical names outperformed Defensives by almost 20%. In 2016, we noticed Defensive names also enjoyed a summer rally but, like in 2024, underperformed from Fall onward. ***We would not be surprised to see continued Cyclical outperformance once investors can fully grasp and game out the full implications of Trump '47 economic policies.***

Exhibit 16: Domestic vs. Global 2024



FactSet and NEPCG

Exhibit 17: Domestic vs. Global 2016-17



FactSet and NEPCG

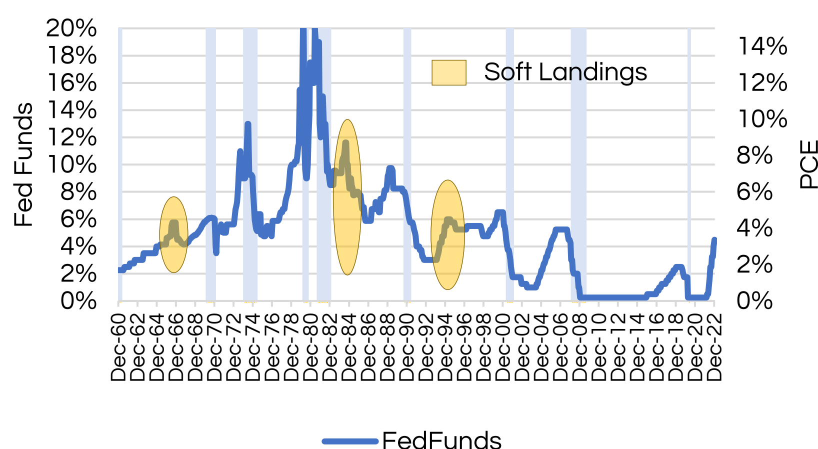
Domestic equities outperformed their global counterparts by 12% in 2024, a trend that persisted throughout the year. 2016 Domestic equities started the year strong, only to give back most of their relative gains by October. However, over the next 12 months Domestic equities modestly

outperformed. ***As detailed later in this report, barring unforeseen international policy errors, we anticipate the U.S. economy—and consequently, U.S. capital markets—to continue outperforming global markets.***

Recessions...Slowly At First, Then All At Once

For some time, pundits and analysts (including ourselves) have underestimated the resilience of the U.S. consumer, the health of U.S. corporations, the tenacity of the equity markets, and **most importantly, the ability of the FOMC to navigate a soft landing.** When drafting this report, it seems as though the FOMC may have raised interest rates just enough to temper growth temporarily, support the labor market, and avoid a recession.

Exhibit 18: Soft Landings



FactSet, Alger and NEPCG

Based on our data and research published by Fred Alger, there have been only three (3) times, dating back to 1960, that the FOMC could seemingly orchestrate a soft landing. **However, as we have noted, we remain skeptical that a soft landing is done and dusted**. Further, in our view, soft landings are very much like unicorns, a position supported by several articles and research papers[7]. And if soft landings existed, we believe

[7] A Soft Landing, June 23, 2000 by Robert Samuelson, Desperately Seeking A Soft Landing, June 20, 2023 by Louis Ashworth, A 'Soft Landing' Scenario - Possibility Or Fed Myth?, January 29, 2023 by Lance Roberts, The fairy tale of a

almost every instance was idiosyncratic, making it hard to draw similarities in cause and effect.

Despite the ongoing debate surrounding soft landings or even "softish landings," **we believe that the same factors that helped stave off recessions in 2023 and 2024 may continue to support the economy in the first half of 2025**. Key among these are **labor hoarding** and the lingering benefits of an **ultra-low interest rate environment** during and directly following the 2020 recession.

In recent years, employers have increasingly practiced labor hoarding, or the retention of employees during economic slowdowns and periods of reduced demand, even when workers are underutilized or underperforming. This approach may be born from the belief that slowdowns are temporary or the challenges of rehiring and retraining staff when demand rebounds is too costly. Additionally, consumers have benefited from historically low mortgage rates, which have reduced monthly housing costs for many. This has left more disposable income for discretionary spending, other expenses, or savings, thus alleviating financial strain and improving household cash flow and stability.

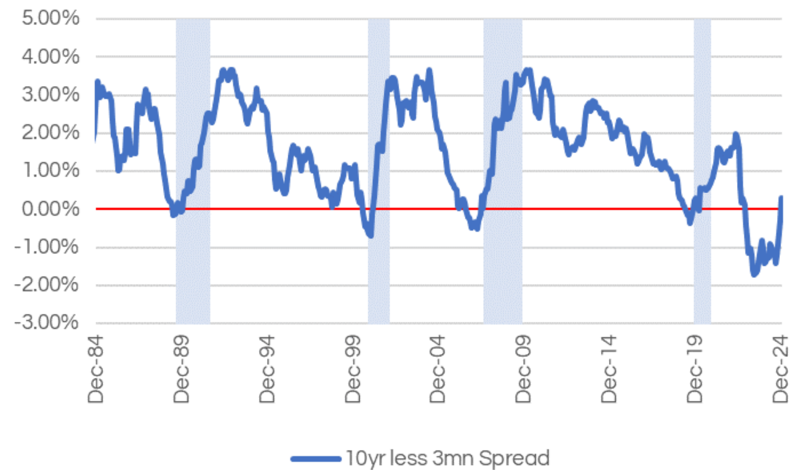
Corporations also leveraged the low-rate environment (leading into early 2022) to refinance high-cost debt, boosting earnings through share buybacks or reduced interest expenses. However, as the labor market normalizes and interest rates remain elevated, the risk of a recession grows—especially if Trump's '47 fiscal policies conflict with the Federal Reserve's focus on controlling inflation.

Further, several historical recession signals are worth monitoring. First is the spread between the 10-year Treasury Note and the 3-month Treasury Bill. Exhibit 19 illustrates that in ***every instance dating back through the 1980s, as the negative spread between the 10-year Treasury Note and the 3-month Treasury Bill turns positive, a recession shortly follows.*** Further, we

soft landing, November 23, 2023, by Arif Husain, The Boundless Foolishness Underlying 'Soft Landing' Mythology, September 23, 2023, by John Tamny, The "Soft Landing" Fallacy, December 29, 2023, by Jason Nuridjanian. Looking at the Economic Myth of the "Soft Landing", November 12, 2022, by Frank Shostak.

note that the potential only time we concede a soft landing could have occurred was in the mid-90s, when the 10yr-3mn spread consolidated but did not turn hostile. **There is a 30bps positive spread between the 10-year Treasury Note and the 3-month Treasury Bill after being as much as 150bps negative over the last year.**

Exhibit 19: 10Yr Treasury Less 3 Month TBill Spread



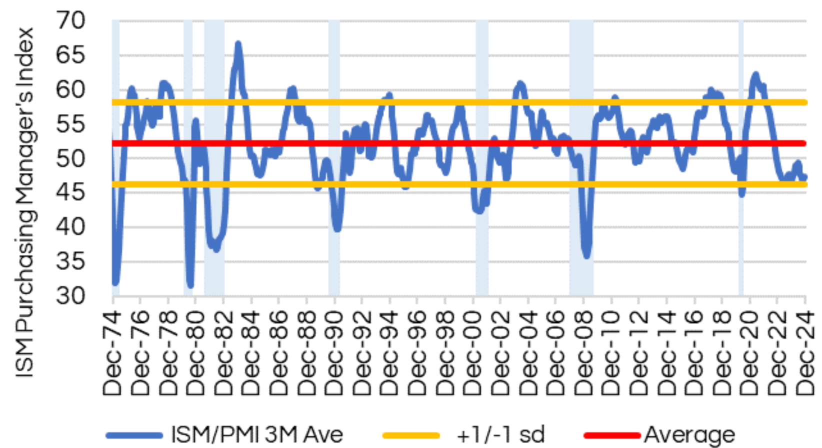
FactSet and NEPCG

We also watch the Institute for Supply Management's Purchasing Manager's Index for additional recession validation. Exhibit 20 shows that the U.S. almost always enters a recession whenever the 3-month average PMI level reaches one standard deviation below its long-term average of 52.6. Once again, the only true exception here was the early/mid-90s "Greenspan" soft landing scenario.

However, there are also offsetting data supporting the notion that a soft or no-landing[8] scenario may prevail. For example, as Exhibit 21 illustrates, a recession seems to occur shortly after the Philadelphia Federal Reserve Anxious Index breaches 40.

[8] A "no landing" scenario refers to an economic situation where the economy continues to grow without slowing down, despite efforts by central banks, such as the Federal Reserve, to cool it down through measures like interest rate hikes.

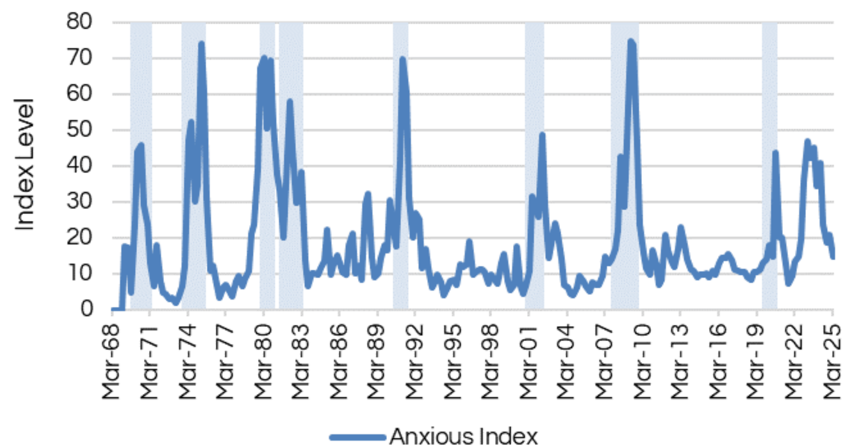
Exhibit 20: ISM Recession Indicator



FactSet and NEPCG

In fact, according to the data, this index has accurately predicted every recession identified by the National Bureau of Economic Research (NBER) since 1970. By way of background, the Anxious Index is part of The Survey of Professional Forecasters, which is the oldest quarterly survey of macroeconomic forecasts in the United States. The survey began in 1968 and was initially conducted by the American Statistical Association and the National Bureau of Economic Research.

Exhibit 21: Philly Fed Anxious Index



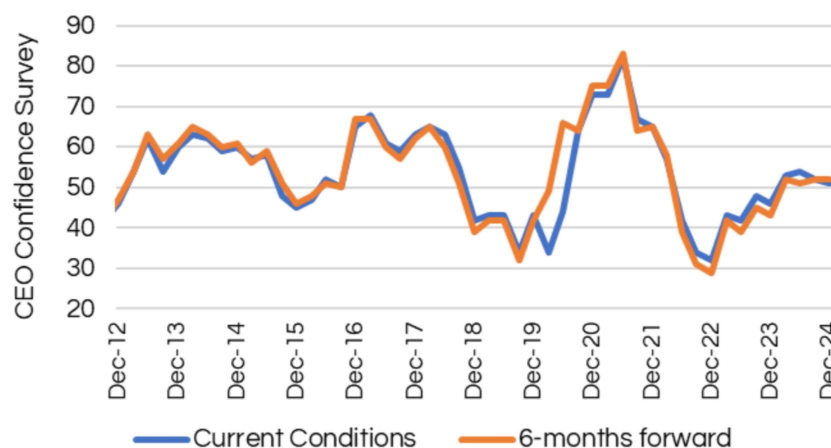
Philadelphia Federal Reserve and NEPCG

The Federal Reserve Bank of Philadelphia took over the survey in 1990. **The Anxious Index represents the estimated probability of a decline in real GDP during the quarter immediately following the administration of**

the survey. For example, in the survey taken during the fourth quarter of 2024, the anxious index level was 15.0, which means that forecasters believe there is a 15.0% chance that real GDP will decline in the first quarter of 2025. This reading is down significantly from the 41% probability for 1Q24 and 21% for 4Q24.

In addition, Exhibit 22 highlights recent trends in the Conference Board's CEO Confidence Survey, covering both current conditions and six-month expectations. According to the latest survey results, confidence has declined modestly since Q2 2024, when the index reached a two-year high of 54. However, the 133 CEOs who participated in the Q4 survey did so between September 30 and October 14; therefore, the results do not reflect any post-election sentiment. Additionally, six-month expectations have remained relatively stable over the past several quarters.

Exhibit 22: CEO Confidence



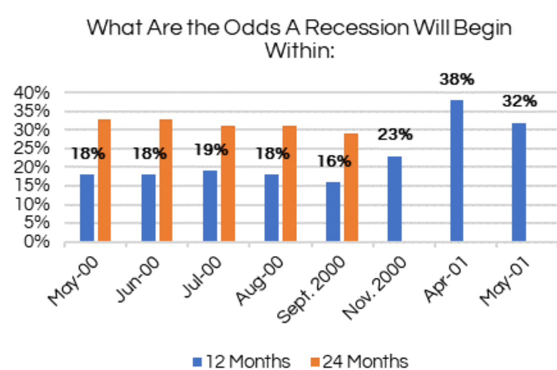
Conference Board and NEPCG

In addition, according to the most recent CEO survey, only 30% of respondents believe the U.S. will fall into a recession in the next 12-18 months, down from over 80% a year ago. Add to this, larger investment banks have also adjusted their recession expectations down for 2025. For example, J.P. Morgan and Goldman Sachs now estimate only a 15% chance of recession in the next 12 months. So, we eagerly await the following quarterly survey to gauge better CEO optimism, which may incorporate the impact of President-Elect Trump's proposed policy agenda.

While the trend now suggests a lower probability of recession in 2025, our contrarian biases remind investors that sometimes the consensus is wrong, and it is difficult to estimate when recessions start and stop.

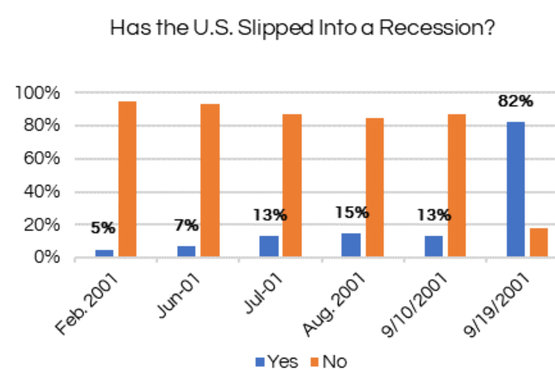
For example, even leading into the 2001 recession, forecasters.[9] were found to be incorrect. As we illustrate in Exhibit 23 and Exhibit 24, research suggests that by the end of the Summer of 2000, economic forecasts estimated the probability of a recession in the next 12 months was only 18%. And by May 2001, which was already two months into the recession, this estimate ticked up to only 32%. Further, as of September 10, 2001, only 13% of forecasters believed the U.S. had already entered a recession.

Exhibit 23: 2001 Recession Forecasts



Blue Chip Economic Indicators, FRB of St. Louis

Exhibit 24: 2001 Recession Survey



Blue Chip Economic Indicators, FRB of St. Louis

However, by September 19, 2001, this statistic increased to 82%. The irony is that the 2001 recession began in March 2001 and ended in November 2001.

We believe the story's moral is that everything is good until it is not. Furthermore, sometimes, recessions start slowly and then happen all at once.

Consequently, in our view, the big risk for 2025 is whether a mild recession will occur and how it may impact growth.

[9] Blue Chip Economic Indicators (BCEI). BCEI is a is a monthly survey and associated publication by Wolters Kluwer collecting macroeconomic forecasts related to the economy of the United States. The survey polls America's top business economists, collecting their forecasts of U.S. economic growth, inflation, interest rates, and a host of other critical indicators of future business activity.

To this end, we reiterate research conducted by Kevin Kliesen, an economist and research officer at the Federal Reserve Bank of St. Louis. In a research paper he published in 2003[10], he reviewed characteristics of recessions dating back to the post-WWII recession of November 1948. Based on that research, he concluded:

1. Expansions have gotten longer, averaging only 36 months pre-WWII to over 56 months post-WWII (56% longer).
2. Contractions have gotten shorter, from 21 months pre-WWII to a little over 13 months post-WWII (38% shorter).
3. The deeper the prior recession, the stronger the recovery.
4. The milder the prior recession, the milder the recovery.
5. The longer the recovery, the shorter the next recession.

Specifically, Kliesen's research found that the three (3) most prolonged expansion phases (as of 2003) were between March 1991-March 2001 (120 months), February 1961-December 1969 (106 months), and November 1982-July 1990 (92 months). During these extended periods of economic expansion, the economic resilience exhibited through the ensuing recession was stronger than typically observed. Moreover, the moderate recession following the three longest expansions was only 9 months, versus the average post-WWII period in Kliesen's work of 11 months and our longer-term estimate of 13 months.

We continue to suggest that if it were not for COVID-19, the U.S. would not have entered the 2020 recession and that the U.S. economy could have still been in an expansion phase. **Therefore, we reiterate our belief that even if a recession took place in 2025, it would be shallow and short.**

[10] The 2001 Recession: How Was It Different and What Developments May Have Caused It?

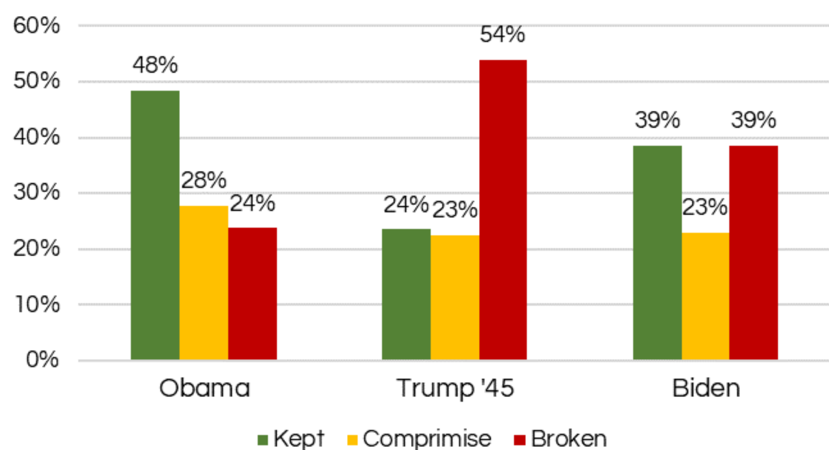
2025 Outlook

Miles To Go And Promises To Keep

Vice President Harris and President-Elect Trump made campaign promises aimed at shaping governance, influencing policy, and thus impacting the economy and capital markets. Each promise reflected an ongoing strategy and appealed to their base. Trump's commitments emphasized protectionism and his version of conservative values, exploiting the economy and immigration. Harris focused on globalist and progressive objectives, addressing inequalities in healthcare, economic opportunity, and civil rights.

Campaigning for the Presidency is essentially a marketing exercise where candidates present themselves as products, distinguish themselves from their opponents, and outline plans for governing if elected. Therefore, regardless of who makes them, we feel promises made during a presidential campaign are better described as proposals. Nevertheless, campaign promises are a central part of the election process, particularly when they focus on issues that polarize a nation or evoke strong emotions—often related to money or social benefits.

Exhibit 25: Better Broken Promises Than None At All



Politifact.com and NEPCG

We believe social benefit promises sometimes disproportionately influence voters with less economic security, exploiting fear, anxiety, or inequality.

However, keeping constituents' long-term support requires regular policy improvements rather than one-time pledges. Also, election promises face practical challenges and opposition that may limit their effectiveness or lead to legal disputes. While these promises can be compelling at first, actions ultimately carry more weight than words, and even the most well-intentioned elected officials often face challenges in delivering on them.

In Exhibit 25, we illustrate the track record of promises kept, compromised, and broken by the prior three administrations, both leading up to and during their presidencies. Based on this data supplied by Politifact.com, we found that President Obama kept almost 49% of the 526 promises he made. President Biden kept nearly 28% of the 83 promises made, while President Trump ('45) kept only 24% of the 102 promises made. ***We caution readers that i) not all promises are created equal, ii) not all promises have a direct economic impact, and most importantly, iii) not all promises are best kept.***

Therefore, in drafting our 2025 Outlook, we reviewed the major campaign promises that President-Elect Trump ran on, attempting to identify which ones we felt had direct implications for the economy and capital markets; we present this in Exhibit 26. Further, based on this information, we believe that President Trump's economic legacy will be judged by the success or failure of promises/policy in four key areas: (i) fiscal, (ii) trade, (iii) deregulation, and (iv) immigration.

Exhibit 26: Promises to Keep

Campaign Promise	Outline	Economic Impact
Ending the Ukraine War	Trump has claimed he could end the Ukraine war within 24 hours by leveraging U.S. aid, though he has not provided details. His stance on reducing U.S. involvement in foreign conflicts appeals to voters who are weary of prolonged wars but raises concerns about potential impacts on U.S. global influence.	Positives include the potential for energy market stabilization, lower energy prices, and reduced defense spending. Negatives include market volatility and weakened alliances (e.g., NATO) due to reduced US global influence and diminishing international investment and trade opportunities.
Tariffs & Trade	Trump advocates for renewing tariffs on goods from key U.S. trading partners, particularly China, to protect American jobs and industries. While admitting uncertainty about the impact on consumer prices, he argues that these tariffs will boost domestic production. This strategy fits his broader protectionist economic philosophy but faces significant opposition from economists who warn of higher consumer costs and potential trade retaliation.	Positives include a potential boost to domestic production and a reduced trade deficit. Negatives include inflationary pressure as tariff costs are passed to consumers, supply chain disruptions, and retaliatory tariffs imposed by key US trade partners.
Retribution Against Political Foes & Pardons for Jan 6 Rioters	Trump has expressed intentions to seek retribution against political opponents, particularly those involved in investigating the January 6 Capitol riot, such as Liz Cheney. He has suggested that his appointed officials could pursue actions against members of the "deep state." Additionally, he pledged to pardon individuals convicted for their roles in the January 6 riot, framing them as political prisoners, which aligns with his broader view of punishing perceived political enemies. This promise demonstrates Trump's commitment to his base.	Positives include that by consolidating political loyalty, Trump might avoid policy gridlock. Negatives include pushing through initiatives that cater to his priorities, such as infrastructure spending or protectionist trade policies. Further, concerns about the politicization of institutions or the potential for widespread unrest may increase market volatility, particularly in the equity market and real estate sectors. In addition, it emphasizes loyalty and retribution but risks undermining legal fairness and national unity.
Rollback of Climate Regulations	Trump has pledged to reverse Biden's climate initiatives by scaling back environmental protections and supporting fossil fuel production, including in the Arctic. His policy aims to lower energy costs through increased domestic oil and gas drilling but faces criticism for its potential environmental harm and long-term climate risks. This promise reflects his skepticism toward climate change policies, favoring traditional energy sources at the cost of environmental sustainability.	Positives include reduced energy prices, domestic growth in the fossil fuel industry, and the potential for lower consumer costs and reduced inflation pressures. Negatives include reduced investment in renewable energy and volatility in domestic energy production due to regional boom and bust cycles. American carbon-intensive exports may be less competitive in nations that levy a carbon-border tax.
Cabinet and Leadership Appointments	Trump's approach to cabinet and leadership appointments centers on selecting loyalists who align with his political goals, potentially reinforcing his influence within the federal government. This strategy raises concerns about politicizing key federal agencies, especially with controversial figures like Kash Patel being considered. These appointments will likely continue Trump's trend of consolidating power within his administration, which could limit checks and balances.	Positives include streamlining decision-making and reducing bureaucratic pushback, enabling the administration to implement its economic and political agenda. Negatives include perceptions of federal agencies as politicized or unpredictable. This could unsettle markets, particularly in heavily regulated industries such as finance, energy, and healthcare.
Abortion Policies	Trump emphasized a states' rights approach to abortion, asserting that overturning Roe v. Wade was sufficient and vowing to veto a federal abortion ban. However, his stance creates ambiguity regarding access to abortion pills and medical exemptions, particularly in states with restrictive laws. This position seeks to strike a balance between conservative voters and moderates but may not resolve the legal complexities surrounding abortion rights.	Negatives include reduced access to abortion services, thus increasing public healthcare costs associated with unintended pregnancies, neonatal care, and long-term social services for families in need. States with restrictive abortion laws may face challenges attracting biotech and pharmaceutical companies involved in reproductive health, potentially limiting innovation in those areas.
Education Policy Overhaul	Trump has proposed eliminating the Department of Education, enforcing merit pay for teachers, and creating a new "American Academy" to promote conservative educational content. He also pledges to defund schools teaching Critical Race Theory and other "inappropriate" subjects. This overhaul reflects his populist rhetoric and desire for more federal control over education but faces significant legal and logistical challenges.	Positives include cost savings on reduced Department of Education spending and a more competitive compensation structure for teachers. Negatives include increased risk of education inequality and demoralization of teachers in underfunded schools.
Civil Rights and DEI Rollbacks	Trump calls for the elimination of diversity, equity, and inclusion (DEI) programs in government and education, and he supports stricter gender identity laws. His stance includes repealing Title IX protections for transgender individuals and limiting gender recognition to biological definitions. This promise aims to reverse Biden-era civil rights initiatives but has provoked strong opposition from civil rights advocates, potentially leading to legal and societal tensions.	Positives include enhanced productivity and operational efficiency by prioritizing performance and qualifications. Also, eliminating DEI programs could reduce federal and educational administrative costs, particularly in training and compliance. Negatives include policies that may be perceived as discriminatory, promote groupthink, and discourage skilled workers, particularly from marginalized groups. These policies reduce the talent pool and reduce innovation and creativity.

NEPCG

Regardless of all the potential positives and negatives associated with these proposed policies, a Republican sweep of the 2024 elections significantly increases the likelihood of swift implementation, whatever the ultimate policy stance.

Notwithstanding the final policy framework, we foresee fiscal stimulus and deregulation providing a temporary economic boost. However, long-term growth may be constrained by persistent/above-trend inflation, higher interest rates, and the unexpected blowback of more controversial policy initiatives. Challenges such as tariff uncertainty (including potential retaliation), stricter immigration policies, and rising debt levels will likely create significant obstacles in the intermediate term. In the following, we break this down further.

Fiscal Policy

A Republican-controlled Congress is expected to extend expiring individual provisions of the Tax Cuts and Jobs Act (TCJA), reinstate full expensing for capital expenditures, maintain the federal estate and gift tax exemption at $13.6 million per individual, potentially lower corporate tax rates, and increase the State and Local Tax (SALT) deduction cap. Additional proposals include eliminating taxes on Social Security benefits and tips. While these measures could help offset the economic drag from tariff and trade policies, boosting growth in late 2025 and early 2026, their fiscal costs are uncertain. ***Our research estimates these initiatives could add $4 trillion to the budget deficit over the next decade, increasing it to over $9 trillion***.

Trade Policy

We anticipate U.S. tariffs on imports, particularly from China, to rise significantly in 2025-26. This could lead to a short-term surge in imports and inventory buildup ahead of full implementation, though the immediate impact on GDP is expected to be minimal. Any near-term boost to GDP is more likely to come from continued domestic productivity growth, especially in terms of AI. However, starting in Q3 2025, we believe trade

policies are expected to slow GDP growth, primarily affecting capital expenditures (business investments in assets like machinery and infrastructure) rather than consumer spending. Due to higher import costs and trade uncertainties, businesses may delay or reduce investments. Consumers may continue to spend as trade policies less directly impact households. However, inflation may shift higher if there is no direct domestic substitute good or if trade partners impose retaliatory tariffs on US-imported goods; at this point, consumers may feel this impact.

Deregulation

During Trump's first term, deregulation helped boost business confidence and supported stock market gains. Following the 2024 election, similar trends preceded the December 2024 FOMC meeting. Yet, a hawkish rate cut led to a noticeable pullback in the S&P 500 (down over 3% in two trading days) and threatened the much-anticipated Santa Clause Rally. Further, recent sentiment surveys show mixed results. The December Michigan Consumer Sentiment Index, the first clear post-election measure, increased to 74.0 from 71.8, slightly above the forecast of 73.3. However, the 3.5-point rise from October to December is far smaller than the 11-point jump seen after Trump's 2016 election win.

Offsetting this, the NFIB Small Business Optimism Index surged to 101.7 in November, up from 93.7 in October, beating expectations of 95.3. This increase in sentiment among small business owners (who typically vote Republican) is stronger than the post-election boost in 2016. ***Still, despite the increased optimism, we found that the 2016 spike in the NFIB Index did not significantly impact GDP growth. In fact, GDP grew by an average of 2.1% in the first half of 2017, down from 2.6% in the second half of 2016.***

Still, we believe Trump's deregulation policies will ease burdens on businesses by lowering operational costs and promoting expansion. Reduced compliance costs and faster approvals could encourage investment, improve productivity, and boost competitiveness, particularly in the energy and construction sectors, where streamlined project approvals can drive growth. Financial services may benefit from relaxed

oversight (e.g., Dodd-Frank and Basel III), enabling greater lending activity for consumers and businesses. Technology, AI, telecommunications, and cryptocurrency could thrive under reduced antitrust scrutiny and lighter regulations.

However, we caution that deregulation carries potential risks. These include environmental harm, increased financial instability from reduced oversight, excess risk-taking, and social backlash from concerns over worker safety, public health, or environmental impacts. Not all outcomes of deregulation may be positive.

Immigration

We do not expect the large-scale deportation policy that candidate Trump proposed (15-20 million people). Instead, we anticipate gradually tightening immigration flows over the next four years. Within the first 100 days, an Executive Order will likely target immigration restrictions through parole and asylum. Parole, which allows temporary entry to the U.S. for humanitarian or significant public benefit reasons, could be restricted by narrowing eligibility criteria, imposing stricter case-by-case standards, suspending or eliminating certain programs, or introducing additional screening requirements to delay or discourage applications.

In addition, stripping Protected Status from certain groups of immigrants could lead to the deportation of up to 1 million individuals. However, this effort could face significant challenges, including (i) legal obstacles, as courts may block attempts to end protections, as they did during Trump's first term, (ii) public backlash and opposition from advocacy groups, businesses, and lawmakers, which could hinder implementation, and (iii) humanitarian and economic risks, as displacing large numbers of people could lead to crises and disrupt key industries.

Our research estimates net migration could be negative 0.5-1.0 million annually at the low end and up to 2-3 million at the high end. This is expected to create a drag on labor supply by late 2025. If labor demand

decreases more quickly than supply, wage pressures will ease, keeping wage inflation in check.

Is Division Additive?

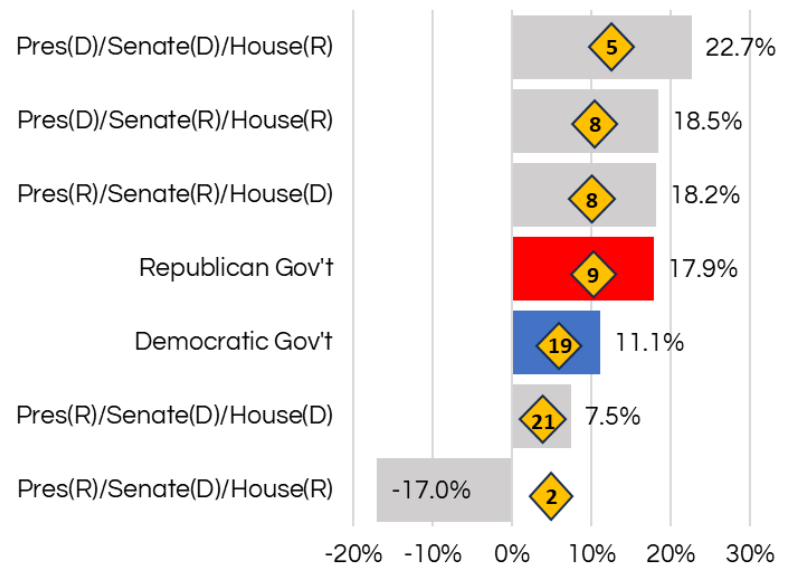
We have always suggested, all else equal, that a "divided government" is a good harbinger for market returns, as the status quo is typically maintained through legislative and fiscal checks and balances. Since all else is rarely equal, we updated our analysis in Exhibit 27 to include an additional year of returns and the frequency of each governing scenario while also breaking down returns by individual presidential term. Based on our updated analysis, the best governing outcomes for equity market returns remained a Democratic President, a Democratic Senate, and a Republican-controlled House (DDR), whereby the S&P increased by 22.7% over the next 12 months. However, this outcome occurred only 5 times: Obama (2012-2014) and Biden (2023-2024). The next best average 12-month period was DRR, up 18.5% on average, occurring 8 times (Clinton 1995-1999 and Obama 2015-2016). The worst performing average 12-month period happened only 2 times, down 17.5%, under the Bush ('45) presidency between 2001 and 2002. President Bush ('45) had to, unfortunately, navigate the 9/11 Terror Attacks and the 2001 Recession.

Republicans fully controlled[11] government only nine times, returning 17.9% on average. Two (2) instances occurred during the Trump '45 administration (2017-2018) but averaged only +8.8%. Four (4) occurrences represented the entire Bush ('41) administration, averaging 15%, although all four years were positive. The remaining three instances occurred under the Eisenhower presidency (1953-1955), averaging 25.8%, but one year had a slightly negative return (1953) of -1%.

Democrats controlled government 19 times. During these individual periods, the S&P averaged about 11% per year.

[11] We highlight the fact that although Republicans have a majority in the House Of Representatives, it is the smallest majority in 100 years.

Exhibit 27: Dems, the GOP, and S&P 500



FactSet and NEPCG

Based on our analysis, we now believe it is increasingly difficult to state that a divided government will produce the best market returns, especially when the best-performing governing outcome (DDR) only happened 5 times. Further, the timing of elections (the last two months of the year) adds additional challenges to our analysis, given the potential for animal spirits or sentiment shifts that drive year-end returns. Based on the "numbers," the two most frequent government outcomes were when Democrats were in control (19 times) or when there was a split between the Executive Branch (Republican) and Congress (Democrat), which historically happened 21 times. During this "divided" instance, the average return for the S&P was only 7.5%, below the long-term average of over 12%.

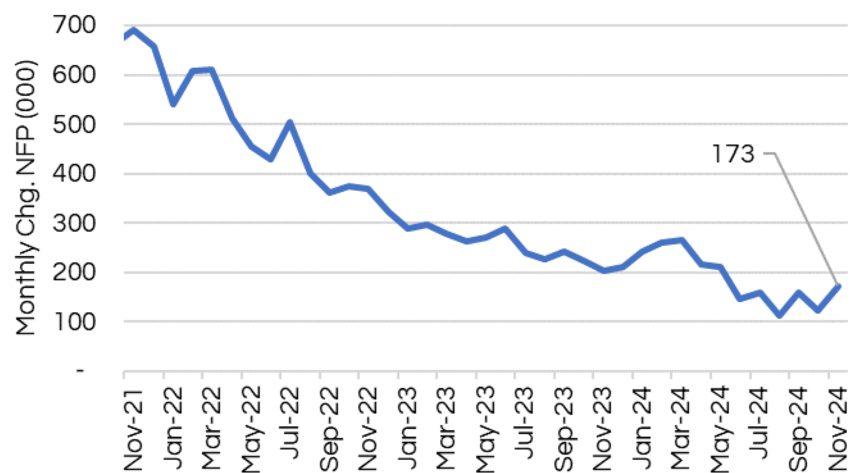
Economic Outlook

Nice, Nice, Not Thrilling But Nice

Despite higher interest rates, the U.S. economy entered the last lap of the election cycle with structural and cyclical tailwinds. Strong productivity growth, a relatively solid employment backdrop, a responsive FOMC, a robust consumer, and a constructive inflation outlook supported a resilient U.S. economy (and thus equity market). We believe several of these same trends may continue into the first several months of 2025.

Consumers will continue to benefit from solid real income growth and relatively healthy balance sheets. We expect real income growth to remain positive in the near term, supported by steady, albeit contracting, job growth and wage increases, which continue to outpace inflation.

Exhibit 28 Trailing 3-Month Job Growth

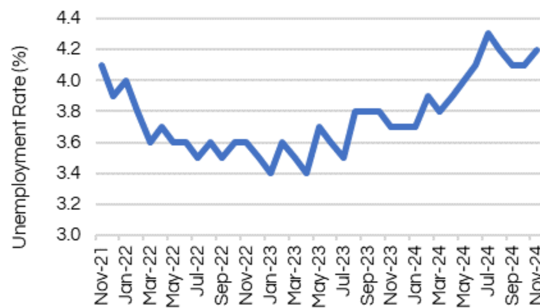


BLS and NEPCG

However, as the economy continues to normalize, we believe the labor demand surge following the pandemic will start to wear off despite varying degrees of labor hoarding. Still, as long as monthly trending BLS job numbers remain at a level concurrent with population growth (~100-150k/month), the narrative from economists and strategists will remain positive. But as we drill down into data, we see cracks forming. Exhibit 29 illustrates that although the unemployment rate remains at decade lows, the overall trend seems to be rolling over. While the recent December job

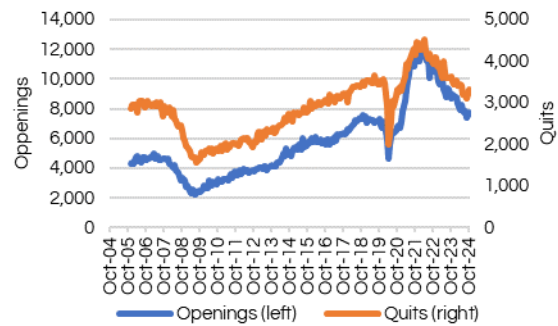
results were better than expected, employment growth was fueled by the government, healthcare, and leisure categories; the first two can be argued to have less elastic demand drivers. Further, Exhibit 30 illustrates that both Openings and Quits continue to roll over.

Exhibit 29: Unemployment Rate



FactSet and NEPCG

Exhibit 30: U.S. Job Openings & Quits

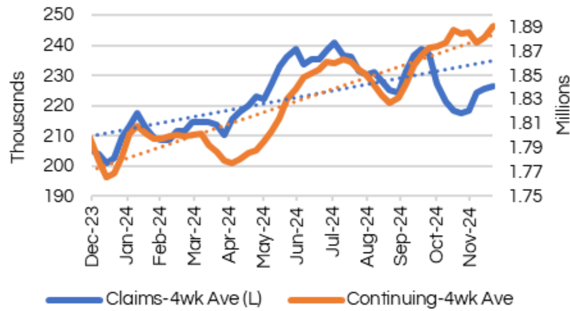


FactSet and NEPCG

As the chart indicates, the overall level of Job Openings[12] has rolled over from 12,182 in March of 2022 to 7,372 in September 2024, with a modest bounce in October to 7,744. At the same time, Quits have also moderated, from 4,471 in November of 2021 to 3,098 in September 2024 and 3,326 as of October 2024. ***Quits are particularly useful to monitor, as conventional wisdom would suggest that individuals are only quitting jobs when there is a better offer to move to.***

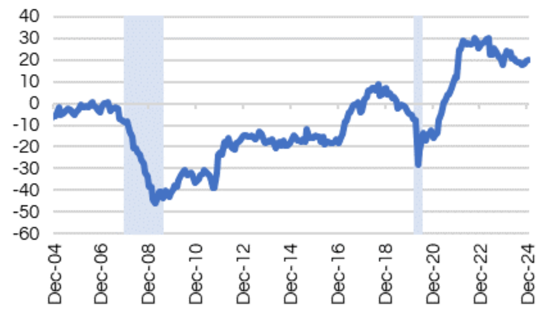
[12] The Job Openings and Labor Turnover Survey (JOLTS) tells us how many job openings there are each month, how many workers were hired, how many quit their job, how many were laid off, and how many experienced other separations (which includes worker deaths).

Exhibit 31: Claims: Initial vs. Continuing



FactSet, Conference Board, and NEPCG

Exhibit 32: Jobs Plentiful Less Hard To Find

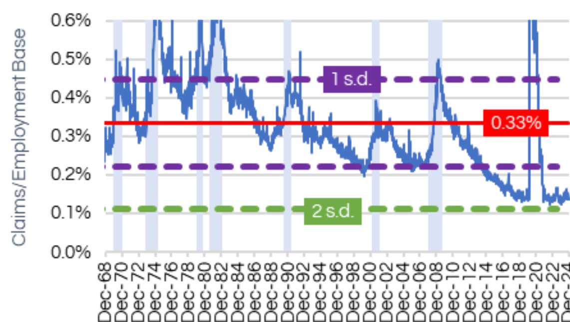


Conference Board and NEPCG

In addition, Exhibit 31 illustrates the recent uptrend for both Continuing and Initial Claims. While Initial Claims are down from peak levels in July 2024, trends have increased over the last several months.

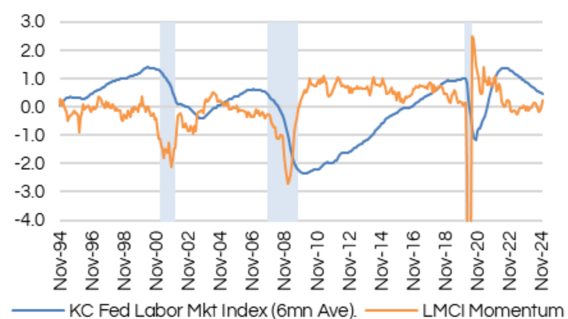
Further, despite a modest trough in Continuing Claims during the summer months, laid-off workers seem to find it harder and harder to regain employment. Exhibit 32 shows that, according to the Conference Board, the net number of jobs being "Plentiful" versus "Hard To Find" continues to soften. We note that a material reduction in this index typically accompanies a potential for recession, but the current level of this time series in isolation should not raise concern.

Exhibit 33: Claims As % Of Jobs



FactSet and NEPCG

Exhibit 34: K.C. Fed Labor Market Index



Federal Reserve Economic Data and NEPCG

Next, in Exhibit 33, we show the overall level of unemployment claims as a percentage of the employment base. We note that the Claims/Jobs ratio has been stuck at two standard deviations wide of the long-term average of 0.33% and back to levels last seen before the COVID-19 pandemic.

Historically, this ratio has been a good indicator of relative economic health, and its vector typically signals expansions and contractions. However, its predictive attributes have been misleading following the Great Financial Crisis.

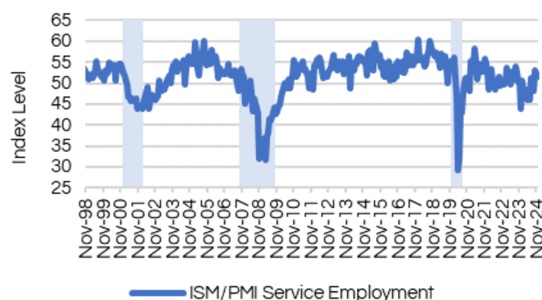
Further, Exhibit 34 above illustrates that the recent trend in the Kansas City Fed's Labor Market Conditions Indicator deserves monitoring. While the composite 6-month trend for the 24 disparate components remains a concern, the momentum of this data series suggests forward trends are neither strengthening nor deteriorating. However, we interpret this as a potential inflection point, where the labor market might transition from expansion to contraction (or vice versa).

The National Federation of Independent Business (NFIB) Compensation Plans Index for the Next Three Months has shown a notable uptick, supporting a more optimistic outlook on the labor market. However, as previously observed, the positive responses from NFIB surveys following the 2016 Trump election had only a modest or negligible impact on subsequent GDP growth. Further, we believe much of this positive trend was driven by strong "service-related" employment through the back half of 2023.

Exhibit 35: NFIB Compensation Plans

NFIB and NEPCG

Exhibit 36: ISM/PMI Service Employment Index



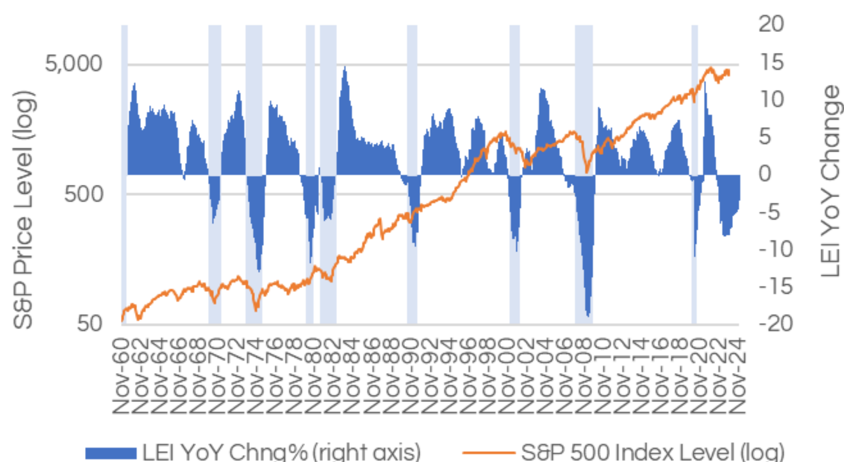
Federal Reserve Economic Data and NEPCG

As illustrated in Exhibit 36, the recent trend in the ISM Service PMI for Employment[13] Index has recovered since early 2024. As we surmised in

[13] https://www.reuters.com/markets/us/us-service-sector-slows-december-employment-plummets-ism-survey-2024-01-05/

our 2024 Outlook, we anticipated this rebound, which, together with the NIFB data, suggests employment demand may hold relatively stable in the near term. One more concerning data series we monitor is the Index of Leading Economic Indicators (LEI), published by the Conference Board.

Exhibit 37: Leading Economic Indicators



Federal Reserve Economic Data and NEPCG

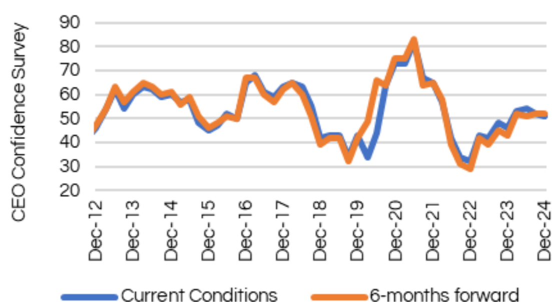
The LEI is an economic time series intended to predict economic activity by analyzing several economic trends.[14]. As we illustrate, the year-over-year change in LEI has been negative for 29 consecutive months (as of November 2024). Historically, there has not been a period whereby the LEI has been negative without the U.S. experiencing a recession. Furthermore, when we overlay the logarithmic price-only movement of the S&P 500, we observe relatively few instances, if any, where a year-over-year decline in the Leading Economic Index (LEI) did not coincide with a significant sell-off in the S&P 500. While some researchers suggest pandemic-related biases and the weighing of "goods" over "services" distort the predictive ability of the LEI, we remain skeptical, especially as post-pandemic normalization continues and geopolitical uncertainty increases.

As mentioned earlier, the Conference Board conducts a survey gauging

[14] The ten components of The Conference Board Leading Economic Index® for the U.S. include: Average weekly hours in manufacturing; Average weekly initial claims for unemployment insurance; Manufacturers' new orders for consumer goods and materials; ISM® Index of New Orders; Manufacturers' new orders for nondefense capital goods excluding aircraft orders; Building permits for new private housing units; S&P 500® Index of Stock Prices; Leading Credit Index™; Interest rate spread (10-year Treasury bonds less federal funds rate); Average consumer expectations for business conditions.

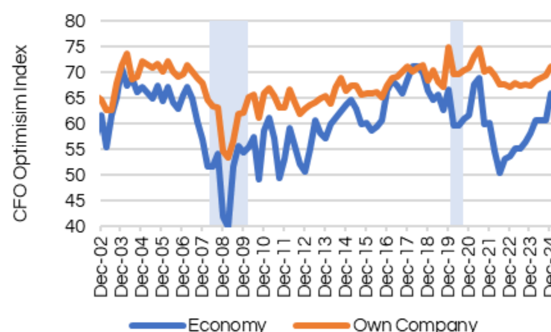
CEO optimism, which is published on a quarterly basis. The CEO Survey is intended to measure the health of the U.S. economy based on CEOs' perceptions of current and expected business/industry conditions across four key areas: capital spending, employment, recruiting, and wages. In Exhibit 38, we reintroduce this time series and then contrast it with a similar survey of CFOs conducted by the Richmond Federal Reserve and the Fuqua Business School (Duke).

Exhibit 38: CEO Confidence



Conference Board and NEPCG

Exhibit 39: CFO Survey



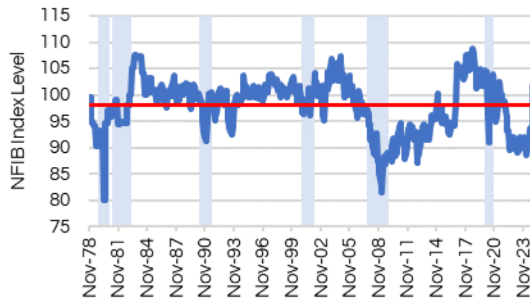
Richmond Federal Reserve and NEPCG

We believe these two time series are sending mixed messages. On the one hand, CEOs see the current and forward outlook moderating. ***However, CFOs expect a brighter economic future and continued, albeit modest improvement, for their own companies' revenue, pricing, margins, and employment prospects.*** In addition, while higher rates and post-pandemic dynamics have negatively impacted prospects for small businesses, sentiment significantly changed following the 2024 election.

As we suggested earlier, expectations for looser regulation and more pro-business policies have helped boost the outlook in the NFIB Small Business Optimism Index. The most current reading (101.7) is above the long-term average of 98.0. As a result, it should be no surprise that banks have become modestly more open to lending activity. In Exhibit 41, we demonstrate that banks are not only expanding lending capacity but also easing underwriting standards. ***While this may be sustainable in a robust economy with low interest rates, we remain concerned about its implications in even a modest economic contraction. In such a scenario, the current elevated interest rate environment could trigger a debt spiral characterized by***

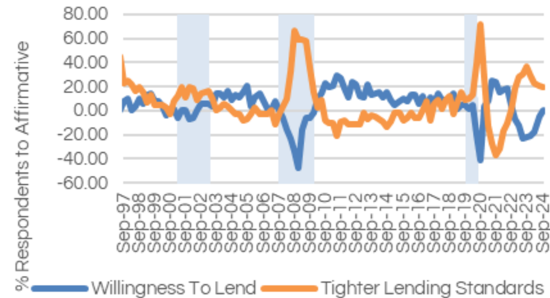
even higher interest rates, increasing defaults, and widening bond spreads, ultimately causing equities to falter.

Exhibit 40: NFIB Small Business Optimism



FactSet and NEPCG

Exhibit 41: Banks' Willingness To Lend



FactSet and NEPCG

Manufacturing trends remain weak after topping out in mid-2021. In Exhibit 42, we illustrate data from the Institute for Supply Management's PMI[15] Survey, which provides a monthly gauge regarding the overall health of the manufacturing sector in the U.S.

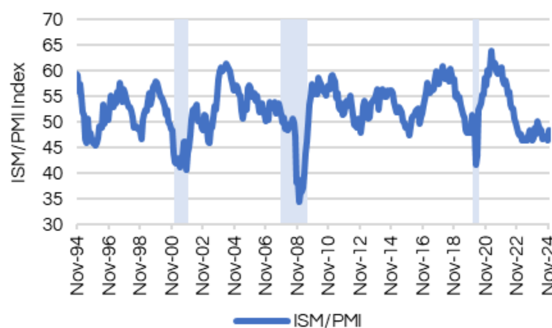
Following a rapid recovery after the 2020 pandemic and resulting recession, November's reading (48.4) remained below 50 for the eighth consecutive month. However, if we ignore the modest expansion reading (50.3) of March 2024, this index has been below 50 (contraction) since October 2022.

Exhibit 43 suggests that global manufacturing and services also remain challenged. Here, we provide data from J.P. Morgan[16]. As with the ISM/PMI Manufacturing Survey, a reading below 50 indicates contraction. ***We would not be surprised to see global PMIs for manufacturing and services remain challenged in the near term, as tariff policy (including the knock-on impact of a stronger dollar) may prove headwinds for international trade and commerce.***

[15]The ISM manufacturing index, also known as the purchasing managers' index (PMI), is a monthly indicator of U.S. economic activity based on a survey of purchasing managers at more than 300 manufacturing firms. It is considered to be a key indicator of the state of the U.S. economy.

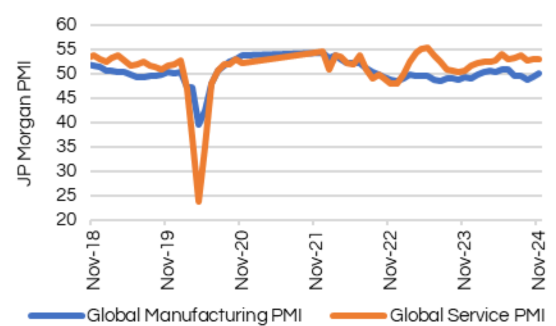
[16] The JP Morgan Global composite Purchasing Managers' Index (PMI) is an indicator of economic health for manufacturing and service sectors. The purpose of the PMI is to provide information about current business conditions to company decision makers, analysts and purchasing managers.

Exhibit 42: ISM/PMI Manufacturing Index



FactSet and NEPCG

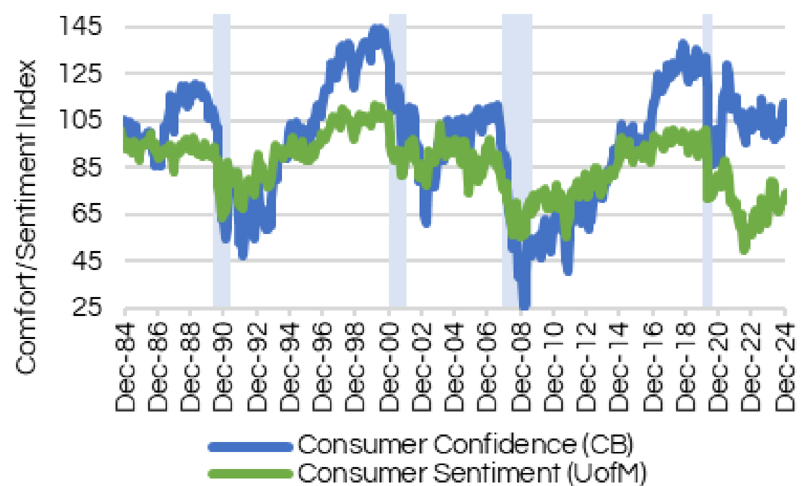
Exhibit 43: JP Morgan Global PMI



FactSet and NEPCG

In theory, broader macroeconomic trends should impact the consumer. However, as mentioned earlier, a solid labor market and low interest rates during and immediately following the pandemic have helped support consumer confidence.

Exhibit 44: The Consumer



Federal Reserve Economic Data and NEPCG

Exhibit 44 compares trends in the University of Michigan Consumer Sentiment (UofM) Survey and the Conference Board Consumer Confidence Survey. The Consumer Confidence Survey focuses on employment and labor market conditions, reflecting broader economic expectations, while the Consumer Sentiment Survey emphasizes

household finances, capturing personal economic outlooks. Despite this distinction, both surveys have trended in a similar vector recently. Looking ahead to 2025, we will continue monitoring these trends. Notably, in the period surrounding the 2016 presidential election, Consumer Confidence showed a more substantial increase compared to Consumer Sentiment.

Exhibit 45 illustrates recent trends in the Monthly U.S. Domestic Savings Rate[17]. After reaching an all-time high of 32.0% in April 2020, the U.S. Savings Rate plummeted to below trend. As of November 2024, the U.S. Savings Rate was 4.6%, 50bps higher than year-ago levels, 4.1%.

Historically, the U.S. Savings Rate increases commensurate with recessionary economic pressures, acting as a buffer against asset value devaluation, job losses, and a lower overall perception of consumer confidence. In addition, we believe that inflation pressures during the 2022-2023 period may have resulted in consumers delaying the purchase of certain goods (hence more savings) in anticipation of lower prices in the future.

Exhibit 46 highlights more recent trends in the U.S. savings rate, showing that it has plateaued and declined since January 2024. This trend can be interpreted in different ways. ***From an optimistic perspective, lower savings may indicate increased consumer spending, which is generally positive for economic growth. However, if this spending is driven by expectations of higher future inflation (or tariffs), it could signal a less favorable scenario***. And if a modest economic contraction would occur at a decreasing level of savings, a more calamitous consequence could ensue.

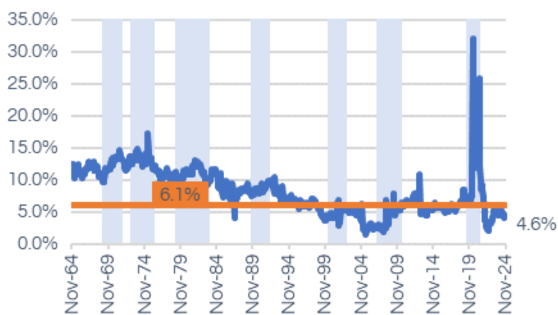
Notwithstanding an increasing savings rate and sticky inflation at already elevated price levels, retail sales continue to grow, and the consumer remains—for now—the driving force behind U.S. economic resilience.

Exhibit 47 presents year-over-year (YoY) sales growth data from the Census Bureau, offering a detailed report on total U.S. retail sales. This data covers a wide range of retail categories, including large and small

[17] The U.S. personal saving rate is personal saving as a percentage of disposable personal income. In other words, it's the percentage of people's incomes left after they pay taxes and spend money.

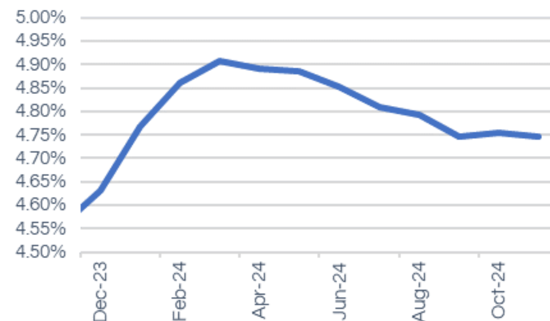
retailers, online sales, non-store retailers, and specific subsectors like food services, motor vehicles, and electronics. It provides a comprehensive view of retail trends, making it valuable for analyzing the broader economy and supporting informed decision-making. The latest November reading came in at 3.8% year-over-year, exceeding expectations and surpassing its two-year average.

Exhibit 45: Long-Term U.S. Savings Rate



FactSet and NEPCG

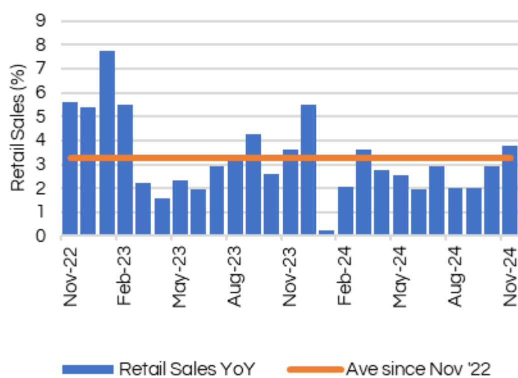
Exhibit 46: Recent Trends U.S. Savings Rate



FactSet and NEPCG

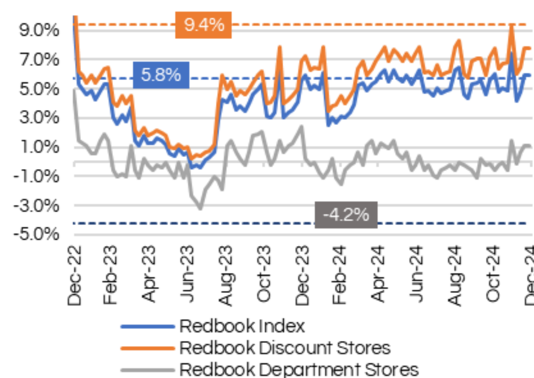
Further, Exhibit 48 presents retail sales data compiled by Redbook. This data tracks sales-weighted, YoY same-store sales growth across a large sample of U.S. general merchandise retailers, including approximately 9,000 discount and department stores.

Exhibit 47: Retail Sales YoY



FactSet and NEPCG

Exhibit 48: Redbook Retail Sales YoY



FactSet and NEPCG

A closer look at Exhibit 48 reveals several noteworthy observations. First and most importantly, the latest December Index reading (blue series) of 5.9% was in-line with the average dating back to 2017. In addition, Discount Stores appear to be performing better than larger Department

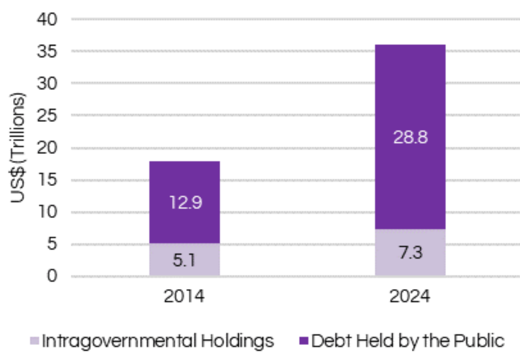
Store chains in aggregate. Specifically, the latest data shows nearly 8% year-over-year (YoY) growth for Discount stores, compared to approximately 1% YoY growth for Department stores.

However, the trends diverge when comparing their relative performance to the pre-pandemic average from 2017. Discount stores are now underperforming their pre-pandemic average growth rate of 9.4%, whereas Department retailers are operating above their historical average growth rate of 4.2%. This disparity suggests that the pandemic significantly and disproportionately impacted Department store sales. The likely explanation is that Discount stores benefited from multi-channel distribution capabilities, which allowed them to adapt more effectively to pandemic-induced disruptions than Department stores, which may have been more reliant on in-person shopping, in many cases, in a small setting.

The Bill Always Comes Due

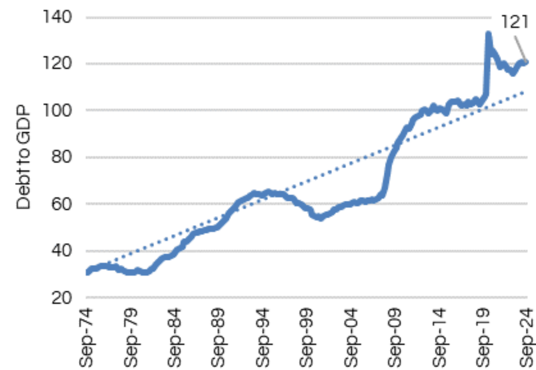
The federal debt has risen to approximately $36 trillion, or over 8% annually, over the last decade under both Republican and Democratic administrations. The post-pandemic surge in inflation has further increased government debt outstanding and borrowing costs, with debt service now projected to surpass national security spending next year. Currently, U.S. debt-to-GDP is at 121%.

Exhibit 49: Composition of U.S. Debt



Treasury.gov and NEPCG

Exhibit 50: U.S. Debt to GDP



FRED and NEPCG

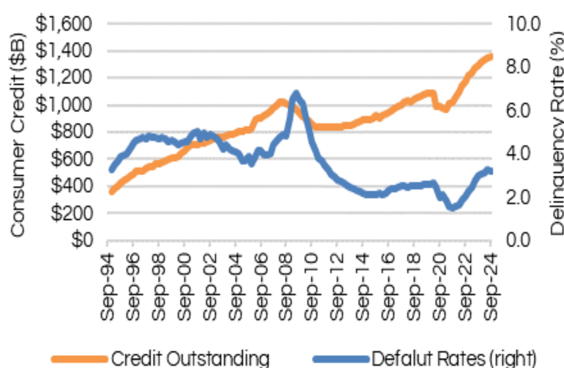
In recent weeks, the topic of ballooning U.S. Debt has been plastered across the financial news. Most recently, Treasury Secretary Yellen, in a letter to Congress, indicated that the U.S. Treasury might need to take "extraordinary measures," or special accounting maneuvers to prevent the nation from hitting the debt ceiling, as early as January 14, 2025. The U.S. last faced a debt ceiling crisis in early 2023 when it reached its $31.4 trillion limit. After months of tough negotiations between the Republican-led House and Democrat-controlled Senate and White House, Congress passed the Fiscal Responsibility Act in June 2023. This bipartisan agreement suspended the debt limit until January 1, 2025.

Some news organizations have recently floated the possibility of a U.S. default, which we believe has a low probability of occurring. The domestic and global ramifications would be unknown, given that a U.S. default has never happened. ***While we do not anticipate this scenario, we raise the issue due to the potential deficit increases associated with President-Elect Trump's fiscal policy proposals.*** Most recently, Trump suggested either eliminating the debt ceiling entirely or extending it through 2029, coinciding with the end of his presidency. This proposal has encountered strong opposition from several House Republicans. Moreover, given the slim majority in the House of Representatives, any resolution on the debt ceiling will require unanimous support within the Republican caucus. ***If a default were to occur, the potential consequences could be significant***, including salary delays for

over 2 million federal employees, 1.4 million active-duty military personnel, and delayed benefits for nearly 73 million Social Security recipients. The global capital markets would also likely experience substantial disruptions, leading to rising interest rates and declining bond prices. Further, such an event would spill over to the domestic economy. Over the following several exhibits, we present the data trends we monitor.

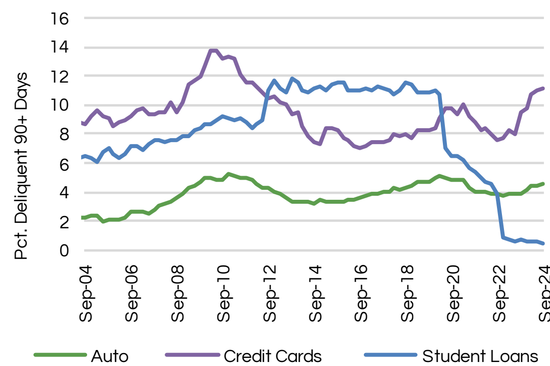
Exhibit 51 illustrates the overall rise in outstanding revolving debt with data provided by the Federal Reserve Bank of New York. Between 12/31/2020 and 9/30/2024, outstanding debt increased by 39%, or over 7.2%, on a compounded annual basis. During the same period, default rates increased over 100%, from 1.6% to 3.2%.

Exhibit 51: Revolving Debt



N.Y. Federal Reserve and NEPCG

Exhibit 52: Default Rates 90+ Days



FactSet and NEPCG

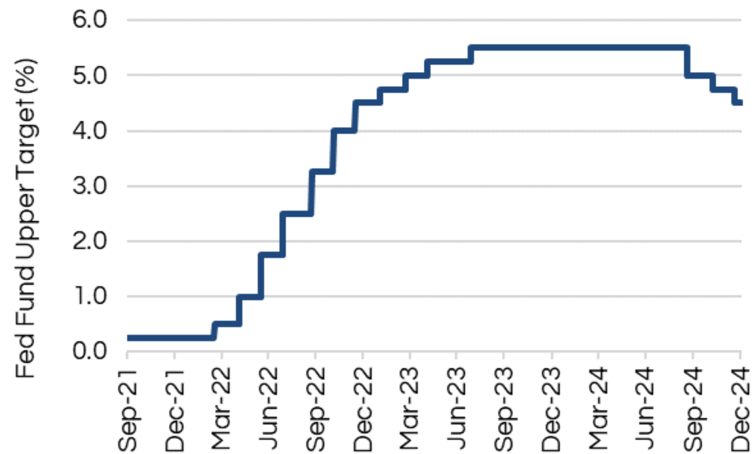
Further, Exhibit 52 illustrates the percentage of delinquencies 90+ days associated with autos, credit cards, and student loans. Credit Cards and Auto Loans have increased by 18% and 17%, respectively. Student Loan defaults 90+ days past due have dropped by almost 30%, presumably driven by loan forbearance and various other forgiveness programs instituted over the last year.

Combined with our interest rate expectations, which we further unpack in the next section, we remain concerned that increasing debt burdens (balances and debt service) will ultimately impede growth. And with lower growth rates, paying down principal becomes harder and harder, leading to a vicious debt cycle.

Returning For A Limited Time Only: Inflation

The COVID-19 pandemic required severe policy decisions, which validated an aggressive FOMC easing cycle.

Exhibit 53: 2021-2024 Interest Rate Cycle



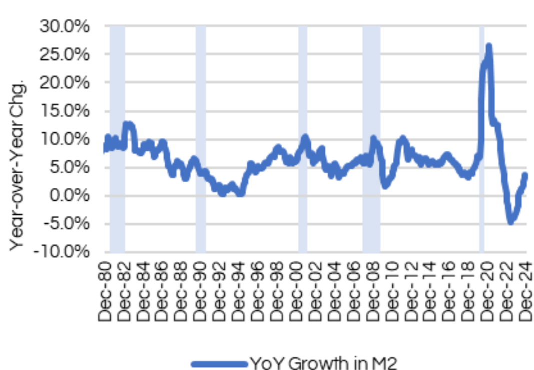
FactSet and NEPCG

Following the pandemic, policymakers and central bankers worldwide took unprecedented steps to resuscitate a faltering global economy. In the U.S., the Federal Reserve continued with Quantitative Easing.[18] (QE), an atypical monetary policy intended to support market liquidity and lower borrowing costs. This overall monetary policy response resulted in an 80% increase in the Fed's balance sheet to almost $9 trillion, while money supply, or M2, [19] grew by nearly 27%. As a result, consumers and businesses found themselves awash with liquidity, and thus, the seeds of inflation were sown. We believe the period between late 2021 and early 2022 could be characterized as a "perfect inflation storm," whereby cost-push and demand-pull forces simultaneously worked within the U.S. economy.

[1818] Quantitative easing (QE) is a form of monetary policy in which a central bank, like the U.S. Federal Reserve, purchases securities from the open market to reduce interest rates and increase the money supply.
[19] M2 is a measure of the money supply that includes cash, checking deposits, and other types of deposits that are readily convertible to cash such as CDs. M1 is an estimate of cash and checking account deposits only. The weekly M2 and M1 numbers are closely monitored as indicators of the overall money supply.

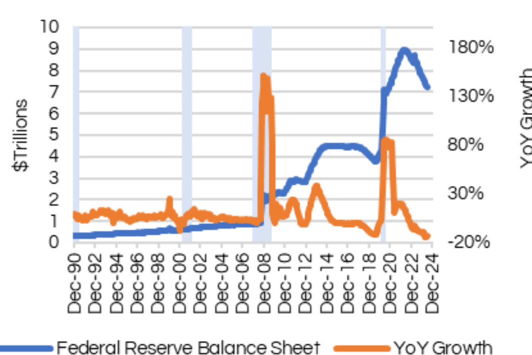
To contain inflation, the FOMC embarked (albeit late, in our opinion) on the most aggressive rate-tightening campaign since the Volcker years.[20], increasing the Fed Funds target rate 11 times from an upper range of 25bps to 5.5% over 18 months. The FOMC last raised the Federal Funds target rate on July 26, 2023. In addition, the Federal Reserve also began a process to reverse QE, formally known as Quantitative Tightening[21] (QT). Over the last year, the Fed's balance sheet has decreased by 10% to $6.89 trillion.

Exhibit 54: M2 Growth



FactSet and NEPCG

Exhibit 55: Federal Reserve Balance Sheet



FactSet and NEPCG

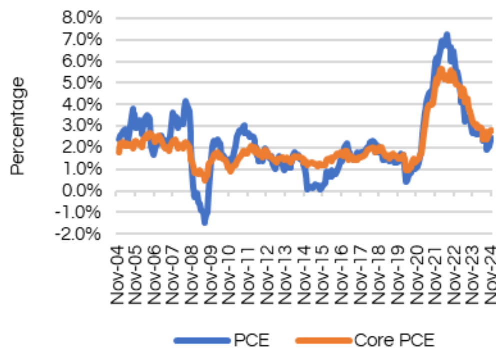
As a result, the economy began to cool, and inflation pressures subsided. However, starting in September 2024, the FOMC began to cut the Fed Funds rate in an attempt to normalize interest rates.

On one hand, some market participants believe that short-term rates are still too restrictive. Others argue the Fed has been too dovish in not calibrating current and potential future fiscal policy outcomes. In recent months, market participants have begun questioning whether inflation is truly under control and if the FOMC should continue cutting rates. Exhibit 56 shows year-over-year growth in Personal Consumption Expenditures (PCE), along with the "core" PCE (the Federal Reserve's preferred measure

[20] Paul Volcker (September 5, 1927 – December 8, 2019) was an American economist who served as the 12th chairman of the Federal Reserve from 1979 to 1987. During his tenure as chairman, Volcker was widely credited with having ended the high levels of inflation seen in the United States throughout the 1970s and early 1980s.
[21] Quantitative Tightening (QT) is a monetary policy tool where a central bank reduces the money supply by selling government bonds or allowing them to mature without reinvestment. This process aims to increase interest rates, slow down inflation, and cool economic activity.

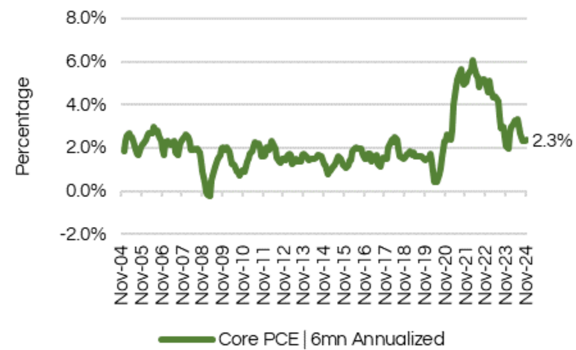
of inflation), which excludes volatile food and energy prices. The data indicates that nominal PCE and core PCE peaked in June 2022 and February 2022, respectively. As of November 2024, these measures stood at 2.4% and 2.8%, respectively, above the FOMC's target of 2.0%. However, the FOMC also considers the trailing 6-month annualized core PCE trend, which recently came in at 2.3%, closer to their target.

Exhibit 56: PCE Growth



FactSet and NEPCG

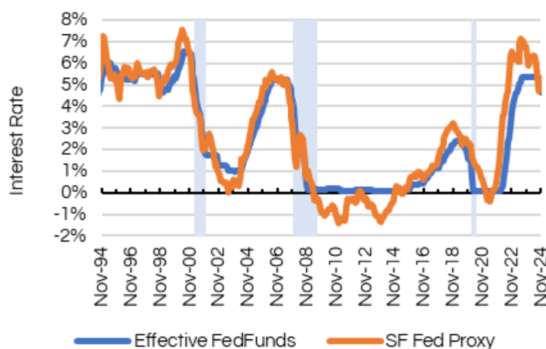
Exhibit 57: Trailing 6-Month PCE



FactSet and NEPCG

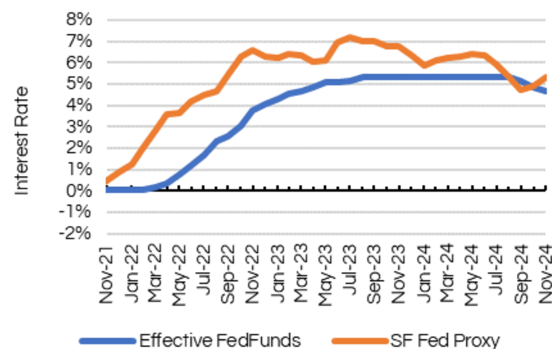
Exhibit 58 compares the San Francisco Fed Proxy Rate and the Effective Federal Funds Rate since 1992. The Proxy Rate represents an estimate of the effective Federal Funds rate adjusted to include the influence of atypical monetary policy, such as Quantitative Easing or Tightening.

Exhibit 58: SF Fed Proxy Rate



FactSet and NEPCG

Exhibit 59: SF Fed Proxy Rates



FactSet and NEPCG

As shown in Exhibit 59, the San Francisco Proxy Rate suggests the effective Federal Funds rate could be as high as 5.3%, about 70 basis points higher than the nominal rate. This indicates a more restrictive

monetary stance, strengthening the argument for continuing rate cuts. However, with mixed economic data and uncertainty surrounding President-Elect Trump's proposed policies and potential inflation risks, we believe the FOMC may pause at its January 25, 2025 meeting—a cautious approach amid unpredictable economic and policy developments.

A year ago, the market (as implied by the CME FedWatch Tool) was pricing an effective terminal rate.[22] For Fed Funds of roughly 415bps by July 2024, roughly 135bps below the then-upper limit (5.5%). Fast-forward: It wasn't until September 2024 that the FOMC cut rates. At the September 18, 2024 FOMC meeting, the board cut the Fed Funds Target rate by 50bps to an upper limit of 5.0%. In addition, contained in their Summary of Economic Projections[23], the FOMC forecasted another 50bps of cuts in 2024 and an additional 100bps in 2025 and 2026. This boosted the equity markets, driving valuations by almost 2.6% by month's end***. However, the Federal Reserve Board updated its SEP at the December 2024 FOMC meeting. In doing so, the FOMC slashed rate cut expectations for 2025 and 2026 in half. The FOMC now expects the Fed Funds rate at the end of 2025 to be 3.9%, from 3.4% in September 2024 to 3.4% in 2006, from 2.9%.*** In addition, the FOMC's projection for core PCE inflation was revised upward in 2025 and 2026 to 2.5% and 2.2%, from 2.2% and 2.0%, respectively. As a result, the market is now attaching only an 11% probability that the FOMC cuts at their January 2025 meeting, with only a 50/50 chance of a cut by May.

[22] The terminal rate is the rate that's equal to the neutral rate so that the economy is in stable equilibrium.

[23] The Federal Reserve's Summary of Economic Projections (SEP) is a report that gives an idea of how the Fed sees the economy evolving in the coming years relating to economic growth, unemployment, inflation and interest rates. It helps the public and markets understand what the Fed is thinking and planning when it comes to managing the economy.

Exhibit 60: Implied Rate Cut Probabilities

		CME Market Expected Fed Fund Rate @ Meeting Date											
	Meeting	2.25%	2.50%	2.75%	3.00%	3.25%	3.50%	3.75%	4.00%	4.25%	4.50%	Wgt.	Prob
Probailbity	1/29/25	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	11.2%	88.8%	4.47%	11.2%
	3/19/25	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	4.9%	45.3%	49.7%	4.36%	50.2%
	5/7/25	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.4%	8.2%	45.7%	45.7%	4.34%	54.3%
	6/18/25	0.0%	0.0%	0.0%	0.0%	0.0%	0.2%	4.5%	27.9%	45.7%	21.7%	4.21%	78.3%
	7/30/25	0.0%	0.0%	0.0%	0.0%	0.0%	0.9%	8.3%	30.8%	41.7%	18.2%	4.17%	81.7%
	9/17/25	0.0%	0.0%	0.0%	0.0%	0.2%	2.6%	13.4%	33.3%	36.4%	14.0%	4.11%	85.9%
	10/29/25	0.0%	0.0%	0.0%	0.0%	0.4%	3.2%	14.5%	33.5%	35.2%	13.3%	4.10%	86.8%
	12/10/25	0.1%	1.2%	6.6%	20.3%	34.0%	28.5%	9.2%	0.0%	0.0%	0.0%	3.27%	99.9%

FactSet and NEPCG

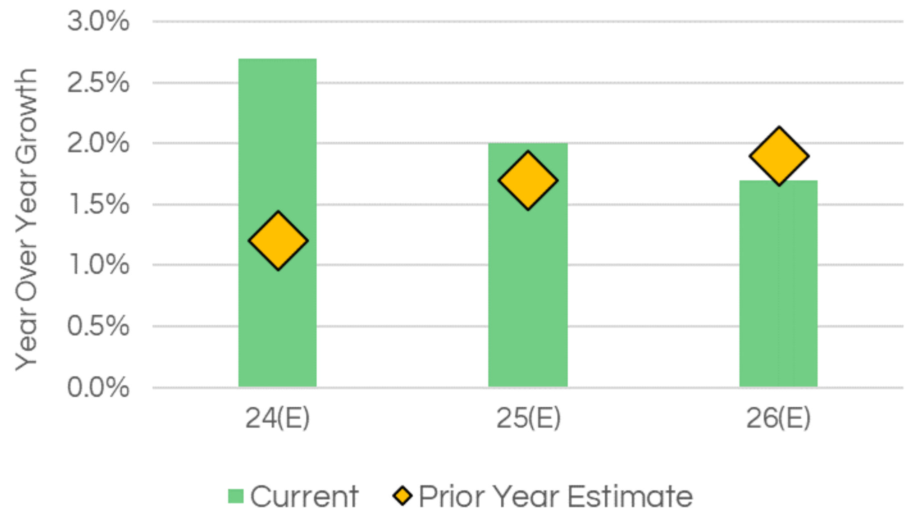
We fear the extent to which the FOMC remains data-dependent may have adverse policy decision outcomes just as the U.S. economy is finally normalizing. Our overriding thesis is that the economy will soften into 2025, and employment may need support later in the year. At this point, we would not be surprised to see the FOMC once again adjust their views. We are concerned about the Fed's credibility with all these actual and potential revisions. ***We remain further concerned that while Federal Reserve President Powell has vowed to stay until the end of his term (May 2026), manic pressure from the incoming White House may make the job untenable, especially if growth disappoints and a scapegoat is needed***.

Growth Expectations

There is considerable uncertainty surrounding President-Elect Trump's policy agenda prioritization and its potential impact on the economy and capital markets. Economic conditions have been bolstered by rising consumer net worth and a strong labor market. We anticipate real income growth to remain positive in the near term, supported by steady job creation and moderating wage inflation. Although the Federal Reserve has lowered its expectations for rates in 2025, we believe softer than anticipated growth may require more than two cuts. Putting this all together, the consensus GDP growth estimates stand at 2.0% for 2025 and 2.0% for 2026. Our baseline assumption is that the effects of tariffs and immigration restrictions will approximately offset the benefits of fiscal

easing and deregulation. We note, however, that the consensus is not projecting a recession scenario into their forecasts.

Exhibit 61: Consensus GDP Growth Expectations

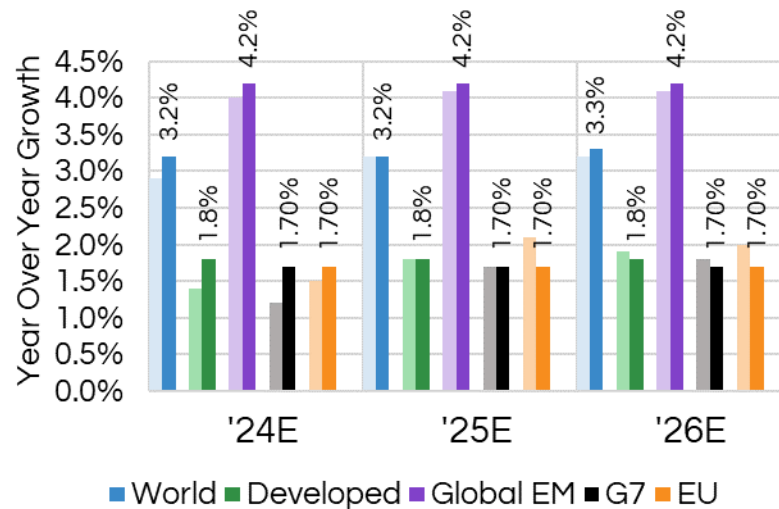


FactSet and FactSet consensus estimates as indicated by (E)

Globally, we notice similar re-ratings for GDP growth prospects compared to the U.S,

Each economic region's lighter shade/hue represents the International Monetary Fund’s prior estimate of real GDP growth, whereas the darker shade/hue represents the IMF’s current expectations. Similar to the US, except for Global Emerging Markets, we expected relatively flat growth in 2025 and slower growth in 2026. This implies, however, that the U.S. will once again fare better than the rest of the World, in part due to potential protectionist and populist policies.

Exhibit 62: IMF GDP Growth Expectations



IMF estimates, as indicated by (E)

In addition, the strong U.S. dollar, combined with tariffs, will make it more difficult for foreign economies to grow due to potentially higher import costs, capital outflows, depreciating domestic currency, and potentially higher inflation. As a result, we expect the U.S. capital market to fare better than most other developed and emerging markets.

Capital Market Outlook

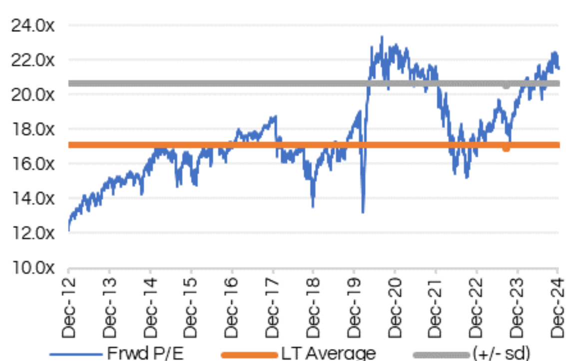
Don't Wake The Bear

Markets discount forward expectations. As we look toward 2025, we believe a significant portion of forward returns may have already been realized in 2023 and 2024, providing investors with a cumulative total return of over 51%. Over the past 12 months, forward price-to-earnings (P/E) multiples have expanded by nearly two full turns—from 19.7x to 21.6x—and over the last three years of, almost five turns from 16.7x. The S&P 500 is now trading at a forward multiple of 21.6x, notably above the historical average of 17.1x since 1997. At its current valuation, the forward multiple exceeds the one standard deviation threshold of 20.7x.

Recent market gains have been driven by momentum, advances in artificial intelligence (AI), and zealous investor sentiment. Further, we believe a significant post-inauguration bounce in economic activity is somewhat

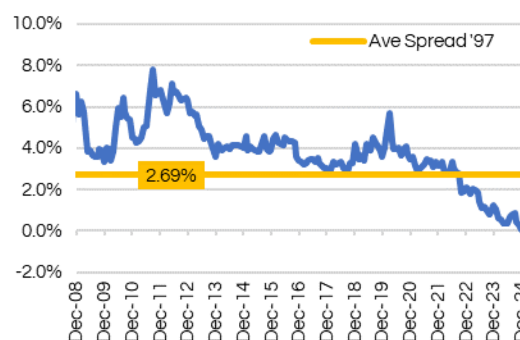
unlikely, as overall consumer confidence is not showing the same trajectory as preceding President Trump's first term. In addition, private sector investment leading up to the 2024 election was solid. Finally, sentiment has tempered somewhat over the last several weeks, and a high degree of geopolitical/economic uncertainty remains alongside elevated price pressures.

Exhibit 61: S&P 500 P/E Multiple Since '97



FactSet and NEPCG

Exhibit 62: Earnings Yield Spread



FactSet and NEPCG

While we do anticipate a temporary boost to the economy driven by fiscal stimulus and deregulation, we expect this to fade as 2025 progresses. Longer-term growth may be further constrained by persistent/above-trend inflation, higher interest rates, and the unexpected blowback of more controversial policy initiatives. We expect continued moderation in the labor market (lower demand) with only a modest offset from immigration policy (lower supply). We believe the top quintile of companies driving the S&P 500 EPS (Mag 7) will continue to provide outsized but decelerating earnings growth compared to the remaining 493 S&P names. While a soft landing seems to be the accepted narrative for now, we would not be surprised that further economic deterioration may prompt the FOMC to reaccelerate easing in the back half of 2025, despite persistent core inflation.

As a result, we expect limited multiple expansion going forward; any market increases will need to rely on earnings growth and the degree to which companies raise expectations in the face of heightened uncertainty.

Considering the totality of our analysis contained within this report, along with several qualitative assumptions, ***we estimate that the base-case fair value for the S&P (price-only) at year's end 2025 to be roughly 6,300, or as much as a 7% price-only return from year-end 2024 levels.*** However, once again, we expect considerable volatility on the way to our year-end forecast, driven by several caveats, the most controversial of which is whether the U.S. enters even a mild recession.

Our base-case forecast relies on key assumptions detailed herein and is derived from a dual approach; our earnings yield multiple model, and our valuation mix multiple frameworks. We then average the two multiple results and apply our forward earnings expectation.

Earnings-Yield Multiple Model: We estimate forward 12-month S&P 500 earnings to reach approximately $293 per share **by the end of 2025**. Our expected S&P 500 earnings yield is 4.75%, derived from a 10-year Treasury yield assumption of 4.0% and an earnings yield spread of 75bps (compared to 10 basis points as of December 31, 2024, and a long-term average of 270bps). **This implies a forward price-to-earnings (P/E) multiple of 21.1x**.

Valuation-Mix Multiple Framework: We weight 65% of the historical S&P 500 multiple of 17.1x and 35% at the market-cap adjusted multiple for the "Magnificent 7" stocks, which is approximately 31x, **equating to 21.9x**.

Averaging these two multiples, we arrive at a forecasted valuation multiple of 21.5x. Applying this to our S&P earnings expectation, we arrive at a 6,300 target one year out.

Our **bear case** assumes that forward 12-month S&P 500 earnings reach no more than $273 per share by the end of 2025. Our expected S&P 500 earnings yield is 5.95%, derived from a 10-year Treasury yield assumption of 3.25% and an earnings yield spread of 2.70% (long-term average). **This results in an implied forward earnings yield multiple of 16.8x**. We average in the same valuation mix multiple as in our base case (31x) and arrive at

an average forecasted valuation multiple of 19.4x, implying a bear case S&P target of roughly 5,300.

Our **bull case** assumes that forward 12-month S&P 500 earnings remain at $293 at the end of 2025. The expected S&P 500 earnings yield falls to 4.25%, derived from a 10-year Treasury yield assumption of 3.75% and an earnings yield spread of 50 basis points. **This results in an implied earnings yield forward multiple of 23.5x**. For the valuation mix, we assume the exact 31x approximation as above and arrive at an **average forecasted valuation multiple** of 22.7x, implying a bull case S&P target of roughly 6,600.

Thank you for reading our 2025 Outlook. We'd love to hear your thoughts.

Disclosures:

The information in this publication and references to specific securities, asset classes, and financial markets are provided for illustrative purposes and do not constitute an offer to sell or solicitation of an offer to purchase any securities, nor does they constitute an endorsement with respect to any investment area or vehicle. This material serves to provide general information to clients and is not meant to be legal or tax advice for any particular investor, which can only be provided by qualified tax and legal counsel. Certain information contained herein is based on outside sources believed to be reliable, but its accuracy is not guaranteed. Investment products (other than deposit products) referenced in this material are not insured by the FDIC (or any other state or federal agency), are not deposits of or guaranteed by Northeast Private Client Group, and are subject to investment risk, including the loss of principal amount invested. Portfolios are subject to investment risks, including possible loss of the principal amount invested. In addition, foreign investments may be less liquid, more volatile and less subject to governmental supervision than in the United States. The values of foreign securities can be affected by changes in currency rates, application of foreign tax laws, changes in governmental administration and economic and monetary policy. Investors should consider the investment objectives, risks, charges, and expenses of ETFs carefully before investing. This and other information are contained in the fund's prospectus, which may be obtained from your investment professional. Please read it before you invest. Investments in ETFs are subject to risk, including possible loss of the principal amount invested. This information is being provided to current Northeast Private Client Group clients and should not be further distributed without Northeast Private Client Group's approval. S&P 500 Index is a market index generally considered representative of the stock market as a whole. The index focuses on the large-cap segment of the U.S. equities market. Dow Jones Industrial Average is a widely used indicator of the overall condition of the stock market, a price-weighted average of 30 actively traded blue-chip stocks, primarily industrials, but also includes financial, leisure, and other service-oriented firms. Russell 2000 Index measures the performance of the smallest 2,000 companies in the Russell 3000 Index of the 3,000 largest U.S. companies in terms of market capitalization. NASDAQ Composite Index is a market value-weighted index that measures all NASDAQ domestic and non-U.S. based common stocks listed on the NASDAQ stock market. Each company's security affects the index in proportion to its market value. This commentary contains forward-looking statements and projections. Actual results may differ from current expectations based on several factors, including but not limited to changing market conditions, leverage, and underlying asset performance. Northeast Private Client Group makes no representation or warranty, express or implied that this information should be relied upon as a promise or representation regarding past or future performance. This material contains the current opinions of the author but not necessarily those of Guardian or its subsidiaries and such opinions are subject to change without notice. Past performance is not a guarantee of future results. Indices are unmanaged, and one cannot invest directly in an index. Data and rates used were indicative of market conditions as of the date shown. Opinions, estimates, forecasts, and statements of financial market trends are based on current market conditions and are subject to change without notice. Securities products and advisory services offered through Park Avenue Securities LLC (PAS), member FINRA, SIPC. OSJ: 200 Broadhollow Road Suite 405, Melville, NY 11747, 631-589-5400. PAS is a wholly owned subsidiary of The Guardian Life Insurance Company of America® (Guardian), New York, NY. Northeast Private Client Group is not an affiliate or subsidiary of PAS or Guardian. 7525807.1. Exp. 1/2027.

This material is intended for general use. By providing this content, Park Avenue Securities, LLC and your financial representee are not undertaking to provide investment advice, make a recommendation for a specific individual or situation, or otherwise act in a fiduciary capacity.