Q1 2025 Asset Management

Index	QTD Return	2024 Return
S&P 500 Index	2.41%	25.02%
Nasdaq Composite Index	6.17%	28.64%
US Aggregate Bond Index	-3.06%	1.25%
Russell 2000 Small Cap Index	0.33%	11.54%
Bloomberg Commodity Index	-1.57%	0.11%

Q4 2024 Review

Stocks closed out 2024 with a strong fourth quarter, setting record highs due to:

- Healthy economic growth
- Stronger than expected earnings
- The Federal Reserve cutting interest rates
- Ongoing momentum from the artificial intelligence trade

...but the rally ended in December due to:

- The Fed reducing its forecasts for further rate cuts
- Slower progress on inflation
- An uncertain policy outlook

Bonds had a tougher quarter, with yields climbing steadily throughout October and after the election:

- The Bloomberg US Aggregate Bond Index fell 3.06%.
- Yields on the 10-year Treasury note rose 0.76% between October and December

Growth stocks regained ground after trailing value stocks in Q3:

- Morningstar US Growth Index returned 6.32%
- Morningstar US Value Index fell 2.23%

The Fed cut interest rates twice in the quarter, at its November and December meetings:

- Target federal-funds rate range ended 2024 at 4.25%-4.50%

The yield curve steepened slightly in Q4 after un-inverting in Q3:

- Short-term interest rates fell while longer-term rates rose

Oil prices fell as global demand weakened

Gold prices slipped as the US dollar strengthened

Bitcoin prices soared after the election, reaching $100,000 in early December.

Market Outlook

The December Global Fund Manager Survey (FMS) run by BofA indicates a highly bullish sentiment in the market, with record-low cash allocations and record-high allocations to U.S. stocks, signaling a surge in global risk appetite. This optimism is primarily driven by growth expectations tied to a potential Trump 2.0 economic agenda and a continuation of the Federal Reserve's rate-cutting stance. In particular, the cash allocation has reached levels comparable to those seen at market tops, such as in early 2002 and 2011, signaling a potential risk of an overshoot in risk assets.

One key factor to watch is the relationship between starting valuations and subsequent returns. High starting P/E ratios for the S&P 500 correlate with lower future returns. Currently, the P/E ratio for the S&P 500 is in the top decile of historical observations, suggesting that future returns could be modest. In fact, when the S&P 500 was purchased at P/E ratios similar to today's level of 22, returns over the following decade ranged between +2% and -2%.

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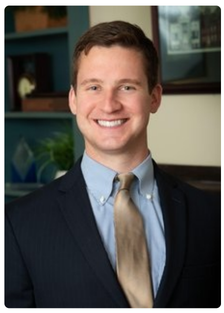

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Schedule a meeting

S&P 500 Price Index

Characteristic	3/24/2000	10/9/2007	2/19/2020	1/3/2022	12/31/2024
Index Level	1,527	1,565	3,386	4,797	5,882
P/E Ratio (fwd.)	25.2x	15.1x	19.2x	21.4x	21.5x
Dividend Yield	1.4%	1.9%	1.9%	1.3%	1.3%
10-yr. Treasury	6.2%	4.7%	1.6%	1.6%	4.6%

Source: Compustat, FactSet, Federal Reserve, Refinitiv Datastream, Standard & Poor's, J.P. Morgan Asset Management.
Dividend yield is calculated as consensus estimates of dividends for the next 12 months, divided by most recent price, as provided by Compustat. Forward price-to-earnings ratio is a bottom-up calculation based on IBES estimates and FactSet estimates since January 2022. Returns are cumulative and based on S&P 500 Index price movement only, and do not include the reinvestment of dividends. Past performance is not indicative of future returns.
Guide to the Markets – U.S. Data are as of December 31, 2024.

J.P.Morgan ASSET MANAGEMENT

There are counterarguments that mitigate some concerns about market valuations. The P/E ratio of the S&P 500 is undeniably high, but it is being driven by the Magnificent Seven tech companies whose economic moat and growth prospects could justify such multiples. There is also an absence of the extreme rhetoric typically seen during speculative bubbles, and despite concerns over high prices, the average stock is not at levels of overheating.

Several growth factors are contributing to the positive outlook. Limited recession risk and tailwinds such as strong real household income growth, less drag from fiscal and monetary tightening, and a recovery in manufacturing all support the optimism. In the U.S., Trump 2.0 expected policy changes, including new tariffs on China and a more relaxed regulatory stance, may provide additional support. However, these policies could also introduce risks, particularly regarding global trade and inflation.

On the inflation front, the risk remains that inflation could resurge, complicating the bullish outlook. A return of inflation would likely lead to higher Fed funds rates and bond yields, negatively impacting stock prices. December's market reaction to a hawkish Fed signals that any return to rate hikes could lower share prices and increase the dollar's strength, undermining the competitiveness of U.S. exports. Inflation could become a critical factor to monitor over the coming months, with a core CPI reading of 3.3% already raising concerns.

In Europe, political developments will also have a profound impact. Germany's elections in February will determine whether a more market-friendly coalition takes control, potentially loosening fiscal constraints and increasing investment. Conversely, a weak coalition could result in greater political instability, which would have negative implications for the European economy. In France, further political gridlock is expected to hinder progress, while growth expectations continue to decline across Europe.

China's economic situation also remains uncertain. Despite stimulus efforts, the country's growth prospects remain constrained, and the yield differential between U.S. and Chinese bonds suggests a lack of confidence in China's economy.

Japan, too, faces challenges, with inflationary pressures and a weakening yen impacting its economic outlook. The Bank of Japan's recent interest rate hikes could add further strain, as the yen approaches historically weak levels. Any significant moves in the currency markets could exacerbate the situation, making it a critical area to monitor.

The outlook for U.S. stocks remains highly positive, with expectations for continued gains despite high valuations. However, this optimism is tempered by geopolitical concerns, the potential return of inflation, and uncertainties around the new administration's agenda.

Positioning

- We are currently neutral looking to rebalance equities to alternatives and short-duration fixed income after two years of solid gains.
- Closer to a top than a bottom (do not be surprised by a pullback in 2025)
- Rest of S&P 500 minus Mag-7 earnings are expected to rebound while Mag-7 slight contraction should favor a broadening of performance.
- Avoid long duration as you are not compensated yet for duration risk, favor shorter duration credit.

Written by: Antonio Belmonte, CFA, Chief Investment Officer

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