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2025 Market & Economic Update

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2025 MARKET & ECONOMIC OUTLOOK

The books are now closed on 2024, and what a year it was. The highlight, of course, was the Presidential election, won by Donald Trump. As we look forward to 2025, there are numerous factors to consider, from potential policy changes under the returning Trump Administration to broader economic and market dynamics. This outlook seeks to provide a clear, educational, and apolitical perspective on the year ahead.

ECONOMY

Consumer Strength

The U.S. economy remains robust, with the consumer in excellent shape. As of November 2024, unemployment stood at 4.2%, well below the full employment threshold of 5.5% (source: Bureau of Labor Statistics).

Manufacturing Sector Challenges

The manufacturing sector has struggled, remaining in recession since October 2022, except for a brief expansion in March 2024 (source: Trading Economics). This divergence highlights the uneven economic experiences across regions and industries and helps to explain why some experience “two economies” over the past few years.

Services Sector Dominance

The services sector continues to drive growth, supported by strong consumer spending and full employment.

Key Indicators for 2025

One key to look out for in 2025 is to see if the manufacturing sector can finally break out of its funk and accelerate above 50 which would signal expansion. One critical input to this may lie, in the opinion of FSInsight, oil falling below \$50/barrel which alone could seriously alleviate inflationary pressure allowing the economy to expand with lower rates.

TAXES AND DEREGULATION

Tax Policy

The extension or permanence of the 2017 tax cuts appears likely given the recent Republican sweep, which could sustain corporate earnings, disposable income and economic growth.

Deregulation

Regulatory reductions may act as a "stealth tax cut," reducing compliance costs for businesses. According to the House Committee on the Budget, regulatory costs have totaled approximately \$1.4 trillion over the past four years. A rollback could boost corporate profitability and market performance.

THE FEDERAL RESERVE

Interest Rate Outlook

The Federal Reserve's approach to rate adjustments will remain a focal point. Slower rate cuts extending into 2026 could support a "soft landing" scenario, where growth moderates without significant unemployment spikes (source: FSInsight).

Inflation Trends

Inflationary pressures remain concentrated in shelter costs, insurance, and labor markets. These categories show signs of easing, which, coupled with potential declines in oil prices, could create a favorable economic environment (source: FSInsight).

POLICY UNDER TRUMP 2.0

Deregulation

During Trump's first term, deregulation was one cornerstone of his economic policy, aimed at reducing compliance burdens on businesses. The incoming administration has pledged to further streamline regulations, which could stimulate corporate growth (source: Government Executive).

Tariff Policy

Tariff threats and actions will be closely watched. Between 2016 and 2020, \$89 billion in tariffs were collected under Trump, compared to \$144 billion under Biden from 2021 to 2024 (source: The Tax Foundation). So far, the economy has been able to absorb the additional tariffs under both Administrations. While tariffs can act as a one-time inflationary pressure, their long-term economic impact will depend on their implementation and scope (FSInsight).

ENERGY AND OIL

Oil Production and Prices

U.S. energy policy is shifting toward expansion, which could drive oil prices below \$50/barrel (source: FSInsight). Lower energy costs would likely reduce inflationary pressures, creating room for the Federal Reserve to lower rates. Some analysts project the 10-year Treasury yield could fall to a range as low as 3.25%. This “call” is an outlier but worth paying close attention to. A move like this in the Treasury market could allow for P/E expansion and alleviate a lot of anxiety in the markets.

FAVORABLE SECTOR OUTLOOK

Fixed Income

Long-duration, high-quality bonds remain attractive, given the asymmetrical risk of lower rates, which could enhance total returns.

Small Caps

The Russell 2000 index has underperformed since 2021, but a more balanced economic expansion, potential deregulation, and lower rates could lead to a resurgence. Valuation gaps between large- and small-cap stocks are at multi-decade highs, presenting opportunities (source: Bloomberg).

Cyclicals

Financials and industrials may benefit from a more expansionary economic environment.

Technology

The sector remains strong, but any pullback in AI spending could pose risks. Close monitoring of this subsector will be crucial.

CONCLUSION

The return of the Trump Administration brings potential for significant economic and market shifts. While challenges persist, such as manufacturing weakness and tariff risks, there are also opportunities, including lower energy costs, a supportive consumer base, and deregulation. By staying informed and adaptable, investors can navigate the complexities of 2025 with confidence.

(Charts and supporting data will be provided separately to complement this outlook.)

Regards,

Tim

Listen to my interview on Sirius XM's Business Briefing:
<https://youtu.be/URCkH5TQpa4?si=TzpkZdtKEvQnWDio>

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