



## Year in review

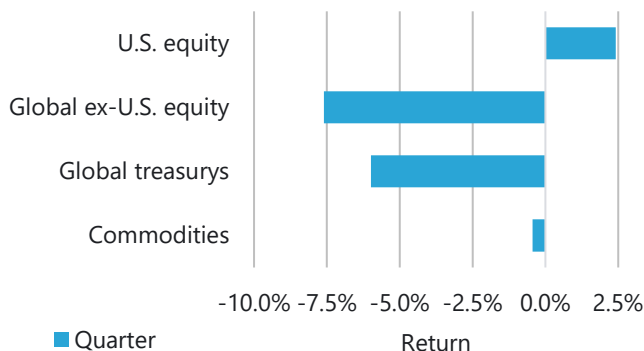


**James Smigiel**  
Chief investment officer

Global investors weathered quite a year in 2024, including global central bank pivots to easy monetary policy, voter pivots to opposition parties, rapidly rising national debt levels, and escalating geopolitical strife. Markets responded with solid returns for risk assets as monetary stimulus was added to the fiscal stimulus punch bowl. Fixed-income returns struggled, with rising longer-term yields fostered by stubborn inflation and swelling government debt. Precious metals and cryptocurrencies were notable performers on heightened demand from central banks and retail investors, respectively, while familiar themes repeated themselves—including another banner year for the Magnificent 7 in the U.S. and another disappointing (if not slightly encouraging) year for Chinese stimulus expectations. Lastly, investors were treated to a lump of coal from U.S. policy-makers in December, as the Federal Reserve (Fed) took a hawkish turn, calling into question the future path of policy rates in the world’s largest economy.

With that highly abridged look back, let us turn our attention to 2025 and the road that lies ahead. Last year at this time, we expressed our contrarian market views that inflation would remain stubborn instead of subdued and that longer-term interest rates were likely to increase rather than follow central bank policy rates lower. This year, we find ourselves in a somewhat uncomfortable position of being *in consensus* with market expectations...at least in part. After two consecutive years of strong equity returns, most market strategists are predicting more of the same in 2025. Our view is slightly more nuanced, as we do find ourselves broadly positive on risk assets (both equities and credit) yet also keenly aware of the potential challenges in the coming year.

## Tales of the tape\*



Source: Bloomberg, SEI as of 12/31/24.  
Past performance does not guarantee future results.  
Returns in USD unless otherwise noted

## Notables for the quarter

- **Emerging equity:** Down 8% on tariff concerns.
- **Bitcoin:** Up over 45% on new U.S. administration favorable to crypto.
- **Tesla:** Gained 54%, boosted by Elon Musk’s relationship with new U.S. administration.
- **U.S. 10-Year Treasury yield at 4.6%:** Stronger data and a hawkish Fed push interest rates up about 80 basis points.

## Balancing act

We believe that the relatively robust state of the global economy, particularly in the U.S., combined with continued monetary stimulus measures from central banks around the world, will be enough to keep the rally going into the New Year. However, we say “in part” given what we also see as a precarious balancing act for global markets in 2025. Investors will need to weigh pros and cons on several fronts, including:

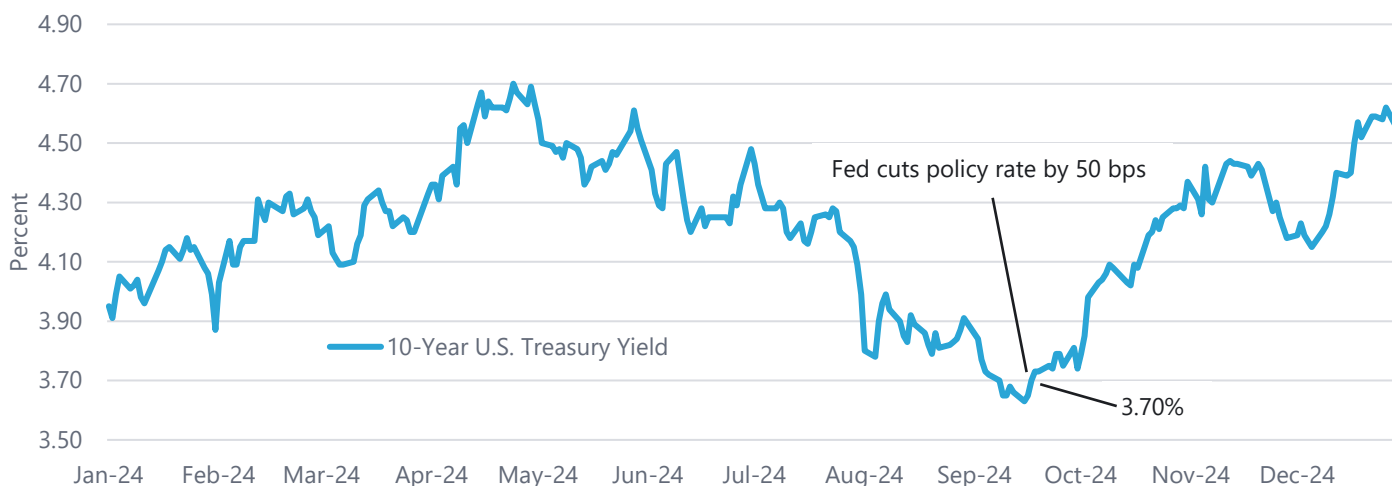
- Higher earnings from less regulation and lower corporate taxes versus higher inflation from tariffs and immigration policies.
- Easy monetary and fiscal policies boosting risk assets in underperforming economies versus stimulus measures leading to higher interest rates in outperforming countries.
- Austerity efforts leading to meaningful long-term reform versus tax cuts and inertia failing to alter the current growth rate in government debt.
- Policy changes lessening pressures on commodity prices versus escalating global conflicts and trade wars keeping prices and volatility high.
- Broadening earnings supporting higher equity valuations in the U.S. versus lofty earnings expectations setting the bar too high for elevated price/earnings multiples.

Our trepidation is due to our own weighing exercise and what we see as too many potential outcomes leading to a reacceleration in inflation and higher long-term interest rates.

### Guide for '25

The bond market seems to share our concerns, as long-term U.S. yields have *risen* roughly 90 basis points since the Fed pivoted to lower interest rates with a surprising 50-basis-point cut in mid-September of 2024. Equity markets began to pay attention into year-end as yields rebounded from a post-election rally. In short, we think inflationary pressures and higher interest rates can potentially spoil the risk-rally party. The yield on the 10-year U.S. Treasury is *our guide for 2025*. We will get concerned about equity markets once the yield reaches 5%, as tighter financial conditions may begin to weigh on growth prospects.

## Exhibit 1: Will higher yields spoil the party?



Source: Federal Reserve Economic Data, Federal Reserve Bank of St. Louis, January 1, 2024 to December 31, 2024.

Within equities, we continue to expect a broadening of participation in the rally. Earnings have surprised to the upside and have shown strength outside of big tech, while lower taxes and less regulation should be a bigger boost to mid- and small-sized companies. In addition, markets outside of the U.S. are far from priced to perfection as both earnings expectations and valuation multiples have more room to move higher. We expect additional stimulus from the European Central Bank given weakness in the core of Europe and further efforts from China to find the right mix of both fiscal and monetary stimulus measures.

Not surprisingly, we maintain our strategic recommendations for investors to stay diversified globally and focus on profitable companies with strong earnings momentum trading at reasonable prices. Given our views on the likelihood of higher interest rates and heightened volatility, we continue to lean into **value** and **active management** across our equity strategies. We favor sectors such as financials, industrials, and staples.

Within fixed-income markets, we remain cautious on interest rates and sanguine on credit. We believe the Fed is still biased toward lower rates (although we may see a pause in early 2025) despite core consumer price index and gross domestic product readings both above 3%. In addition, the reality of tariffs and immigration reforms may add additional fuel to the inflation fire early in the year. Therefore, given our outlook for higher long-term interest rates, we see headwinds for fixed-income returns. On a more positive note, while credit spreads have limited room to tighten, absolute yields remain attractive, defaults remain low, and maturities have been extended. Carry strategies in high-yield bonds and collateralized loan obligations (CLOs) should perform well.

Commodities represent a mixed bag for 2025. The energy complex could buck the inflationary trend on increased supply, while precious metals should benefit from central bank demand. We remain overweight, but cautious, in this space as an inflation hedge.

Currencies could exhibit some notable moves in 2025 as monetary policy divergences and protectionist saber-rattling will likely increase volatility. While the U.S. dollar (USD) appears overvalued, it should remain in a strong position in the short term on interest rate differentials alone. The Japanese yen managed to finish 2024 substantially weaker on slower-than-expected policy responses to inflationary pressures but looks undervalued. The euro has weakened in response to a lagging economy and could test parity with the USD in early 2025.

We wish all our *Forward* readers a prosperous and happy New Year.

## Summary views

|                          |  |
|--------------------------|--|
| <b>Macro/Cross-asset</b> | <ul style="list-style-type: none"> <li>• Inflation risks are biased to the upside on monetary stimulus and protectionist policies.</li> <li>• Monetary policy is likely to diverge in the New Year, with Europe and China continuing to add stimulus while the Fed pauses early in 2025.</li> <li>• Government debt levels will continue to put upward pressure on interest rates.</li> <li>• The USD should continue to outperform in the short term.</li> <li>• Commodities remain an attractive inflation hedge.</li> </ul> |
| <b>Equity</b>            | <ul style="list-style-type: none"> <li>• Diversity in equity markets remains a focus, particularly in capitalizations and countries.</li> <li>• Strategic holdings in value, quality, and momentum; emphasis on value.</li> <li>• Active management should benefit from reflation, particularly in U.S. large-cap stocks.</li> <li>• We remain cautious, but optimistic in China and emerging equity.</li> </ul>   |
| <b>Fixed income</b>      | <ul style="list-style-type: none"> <li>• Higher 10-year yields in the U.S.</li> <li>• Positioned for a continued steepening in the U.S. yield curve.</li> <li>• Remain defensively positioned in credit. Favor securitized versus corporate debt.</li> <li>• Absolute yields in high yield and CLOs remain attractive.</li> </ul>  |

## Indexes

\*Tales of the tape: U.S. equity: S&P 500 Index; Global ex-U.S. equity: MSCI ACWI ex-U.S. Index; Global Treasuries: Bloomberg Global Treasury Index; Commodities: Bloomberg Commodity Index.

## Indexes definitions

The **Bloomberg Commodity Index** comprises futures contracts and tracks the performance of a fully collateralized investment in the index. This combines the returns of the index with the returns on cash collateral invested in 13-week (three-month) U.S. Treasury bills.

The **Bloomberg Global Treasury Index** tracks fixed-rate, local currency government debt of investment grade countries, including both developed and emerging markets.

The **MSCI ACWI ex USA Index** tracks the performance of both developed-market and emerging market countries, excluding the United States.

The **S&P 500 Index** is a market-weighted index that tracks the performance of the 500 largest publicly traded U.S. companies and is considered representative of the broad U.S. stock market.

## Glossary

The **10-year U.S. Treasury Yield** is the interest rate the US government pays on 10-year Treasury notes, which are a type of debt obligation issued by the US Treasury Department. The 10-year Treasury yield is a key indicator of the economy and financial markets. It's used as a benchmark for setting interest rates on other financial products, like mortgages and corporate bonds.

A **basis point** equals .01%.

A **carry trade** involves borrowing at a low interest rate and then investing in an asset with a higher interest rate.

**Collateralized loan obligations (CLOs)** are securities that have been created by pooling smaller high-yielding fixed income assets such as bank loans. These pools are then packaged into various tranches (a slice or portion of a structured security) according to credit quality, maturity, etc.

**Corporate debt** is money that a company owes to another party and can be in the form of a loan or bond.

**Momentum** is a trend-following investment strategy that is based on acquiring assets with recent improvement in their price, earnings, or other relevant fundamentals.

**Monetary stimulus** are actions taken by central banks with the goal of boosting economic activity by increasing the amount of money in the economy,

**Quality** comprises a long-term buy-and-hold strategy that is based on acquiring shares of companies with strong and stable profitability with high barriers of entry (factors that can prevent or impede newcomers into a market or industry sector, thereby limiting competition).

**Risk assets**, such as equities, commodities, high-yield bonds, real estate, and currencies, carry a degree of risk and generally are subject to significant price volatility.

**Securitized debt** is a type of debt security that's created by pooling individual loans into a single package that can be sold to investors.

**Value** is an investment strategy that is based on acquiring assets at a discount to their fair valuations. Mean reversion is a theory that prices and returns eventually move back towards their historical average.

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