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Monthly Market Insights

FEBRUARY 2025

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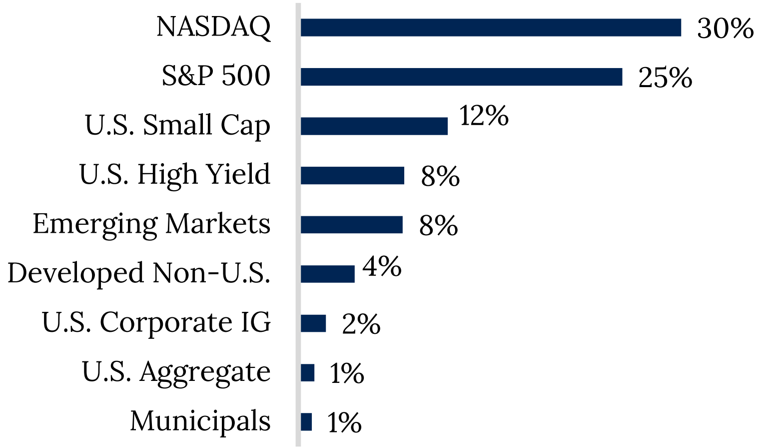
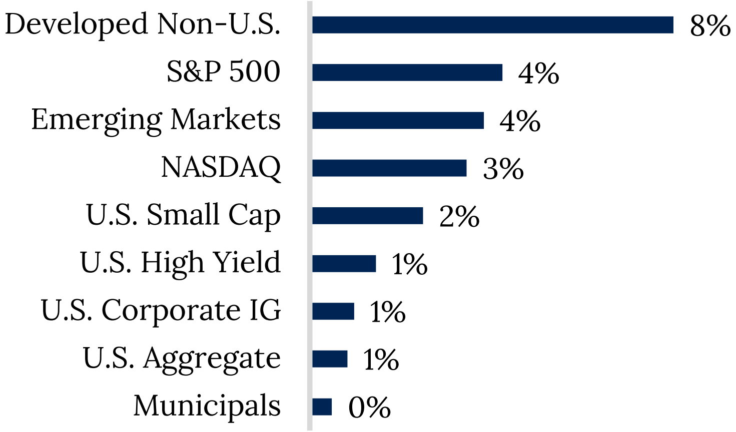
As of mid-February, global markets are experiencing a rotation in leadership, with a more balanced rally across sectors. Developed Non-US equities driven by Europe are leading the way. While the S&P 500 is +4% YTD, leadership is no longer concentrated in just the Mega Cap Tech names, reflecting healthier market breadth.

CY 2024



YEAR-TO-DATE



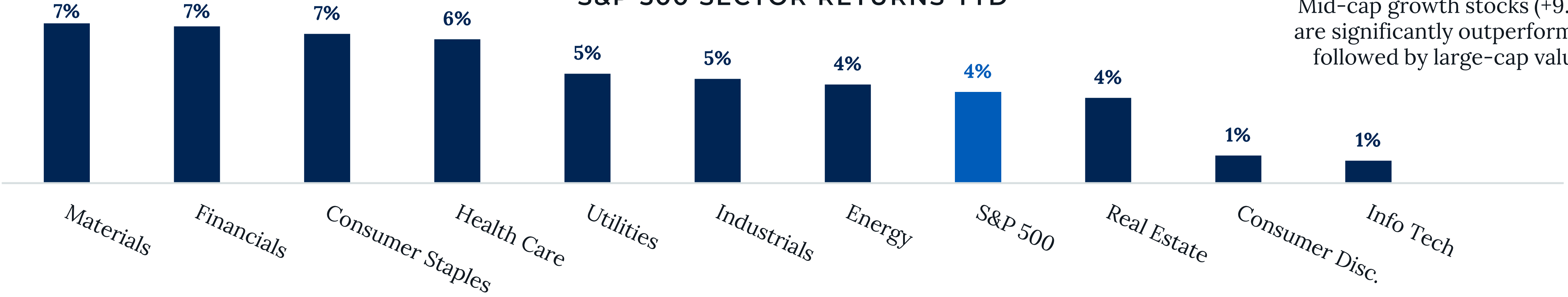
2025 YEAR-TO-DATE

Equity Style Return

	VALUE	BROAD BASED	GROWTH
LARGE	5.2%	4.4%	3.6%
MID	2.8%	4.5%	9.3%
SMALL	2.1%	2.4%	2.7%

Mid-cap growth stocks (+9.3%) are significantly outperforming, followed by large-cap value.

S&P 500 SECTOR RETURNS YTD

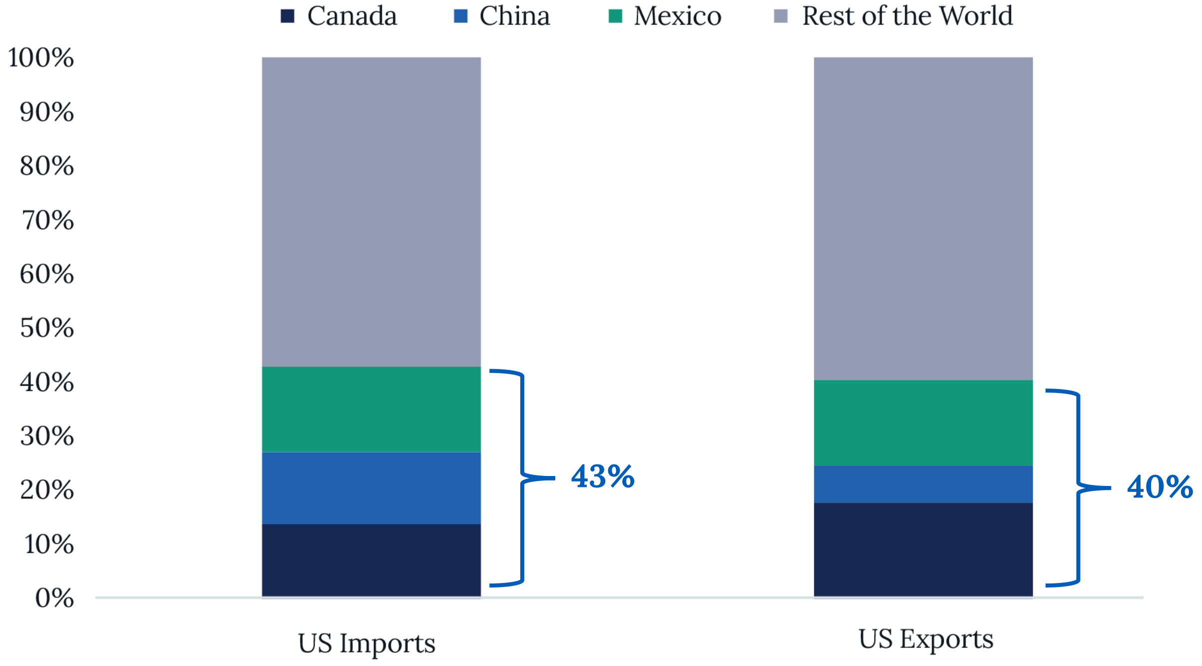


Source: FactSet, 02/13/25.
Past performance is no guarantee of future returns. As with any investment, there is the risk of loss.

TRUMP TARIFF PROPOSAL INDUCES "HEADLINE VOLATILITY," USING TARIFFS AS A POLICY TOOL

On February 1st, President Trump announced tariffs of 25% on imports from Canada and Mexico (with a carve out for only 10% tariff on Canadian energy), and an additional 10% tariff on imports from China. However, within 48 hours, the administration delayed implementation for Canada and Mexico by 30 days, triggering market swings driven by headline volatility. Subsequently, we have seen 25% tariffs declared on all aluminum and steel products and "reciprocal tariffs," intended to match the tariff rates that other countries impose on U.S. goods, although the details of how these tariffs would be implemented are quite unclear. Canada, China, and Mexico are our three largest trading partners, and collectively account for 43% of U.S. imports and 40% of exports, including key importers of aluminum and steel. If these tariffs are fully implemented, the effective tariff rate could rise to 10%—its highest level in over 75 years. While we must remain attune to rapidly developing policy matters, we must also remain calm and disciplined in our analysis amidst the volatile news cycle. **Given Trump's very public and often unpredictable approach to policy announcements, this type of "headline volatility" is likely to persist, even though such proposals may or may not actually result in immediate material changes.**

US TRADE (2023)



TAKING US TARIFF RATES BACK DECADES

Source: Bloomberg Economics, USITC, Census Bureau, Bureau of Economic Analysis, Peterson Institute for International Economics
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PROPOSED TARIFFS COULD HIT GDP AND EARNINGS AND BE NEAR-TERM INFLATIONARY, BUT TBD…

Potential Impact on GDP: Analyzing the full "just pay it" cost of the February 1st announced tariffs, if fully absorbed by U.S. consumers, would equate to just under 1% of GDP. However, this simplistic assumption is not entirely how it would play out, partially because negotiations are underway to alter the terms, and the subsequently tariffs would have some crossover effects as well. Furthermore, factors such as tariff cost-sharing (foreign companies lowering prices or reducing margins), substitution effects (shifting to alternate goods or reducing discretionary purchases), reshuffling of supple chains (already underway), retaliatory measures (already ongoing but uncertain), and tariff revenue recycling (may reduce the deficit) would likely soften the overall impact. Both Goldman Sachs and Apollo have forecasted the actual drag on GDP would be significantly lower, closer to 0.4%.

Potential Impact on Inflation: Most economists suggest that tariffs would result in more of a "one-time price adjustment" rather than a sustained inflationary trend, with the impact concentrated within the first year. Goldman Sachs estimates a 0.7% increase in core inflation under full tariff scenario.

Potential Impact on Corporate Earnings: Tariffs are also expected to weigh on corporate earnings, but for reasons noted above, estimating that exact impact is challenging, leading to a wide range of forecasts and potential outcomes. Goldman Sachs estimates that for every 5% increase in effective tariff rates, corporate earnings would decline by 1-2%. Under the proposed February 1st tariffs, this translates to a 2-3% drag on forecasted earnings. J.P. Morgan projects a slightly higher 7-8% drag on earnings, factoring in announced tariffs plus potential further European tariffs. However, they caveat that their base case is that this full level of tariffs will not materialize, as that would negatively impact stock prices, dampen corporate investment, and weigh on future economic growth—outcomes that the current administration is very much looking to avoid.

2024 Estimate, Nominal U.S. Dollars ($ billions)					
	U.S. Imports	U.S. Exports	U.S. Exports as % of GDP	Proposed Tariff	Tariff Impact
Canada	$415	$350	16%	25%	$104
Mexico	$515	$340	19%	25%	$129
China	$430	$145	1%	10%	$43
All Trading Partners	$4,161	$3,211			
					$276
	U.S. GDP				Proposed Tariffs as % of GDP
	$29,350				0.94%

Source: Chart – Citi, Haver Analytics, Commentary Statistics – Goldman Sachs, Apollo, JPMorgan.
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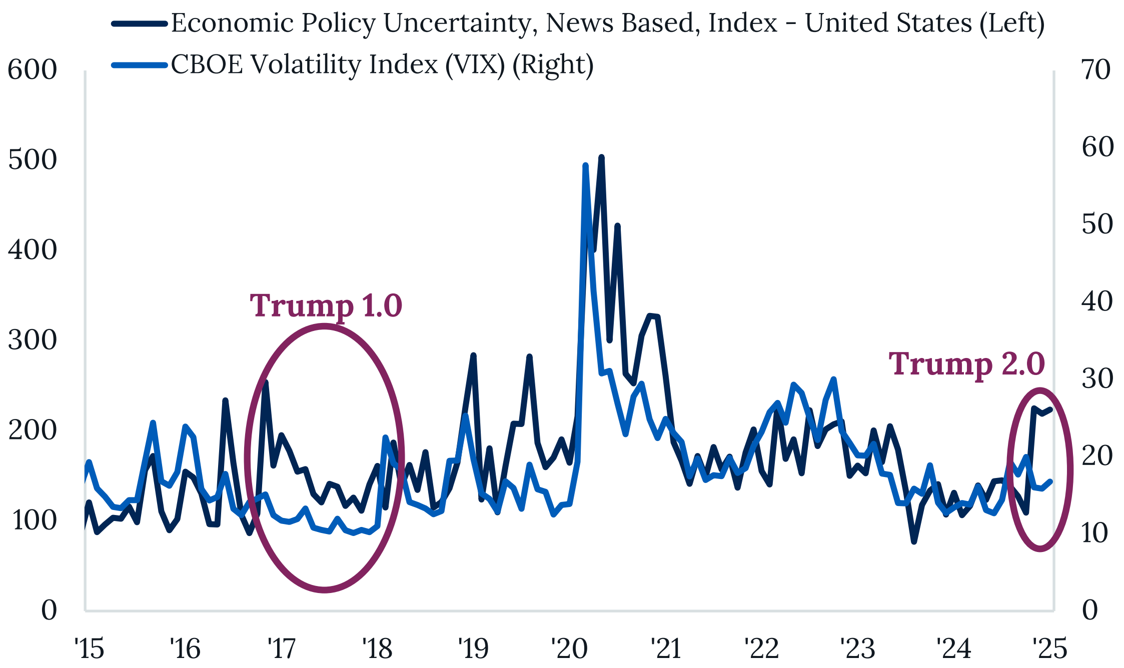
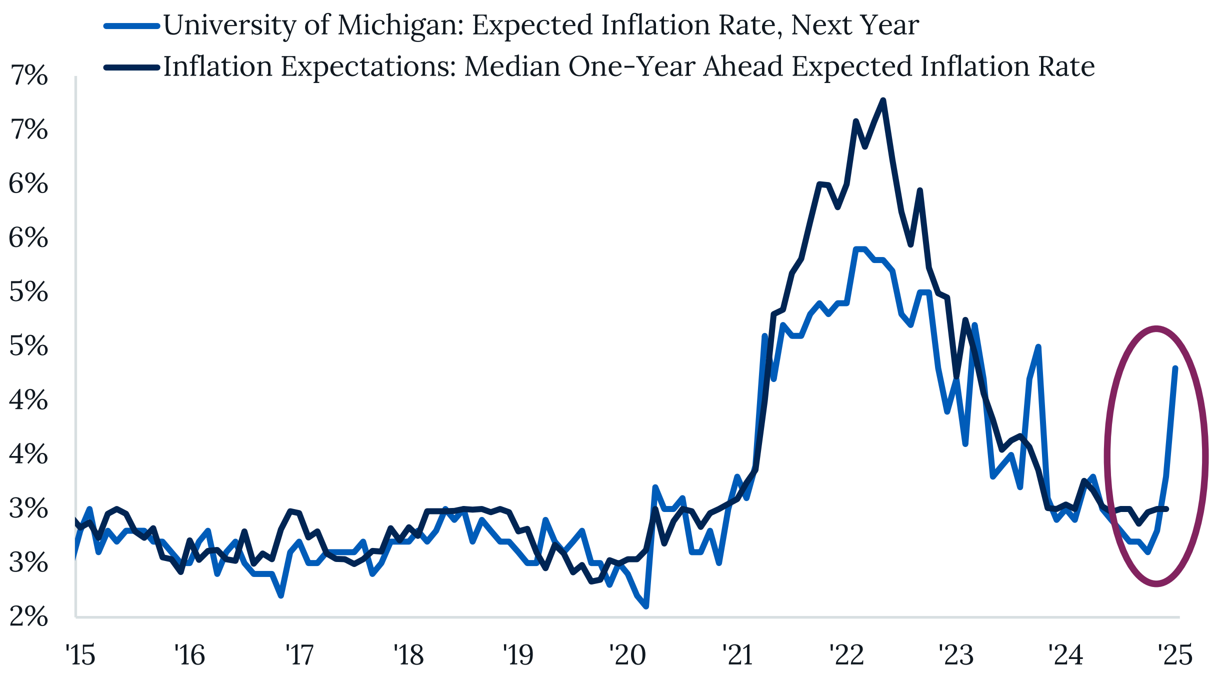
WE MIGHT WANT TO GET USED TO MORE "HEADLINE VOLATILITY"

"Headline volatility" is likely to drive up "soft data" indicators such as uncertainty indices and sentiment surveys, but paying attention to the "hard data" will be important as we may see unusually wide gaps forming between the two. While a heightened Global Policy Uncertainty Index typically drives increased U.S. stock market volatility (VIX), the relationship has disconnected recently—much the same way it did the last time Trump entered office. Markets reacted to the initial shock and awe announcements, but after seeing how quickly the Canadian and Mexican tariffs were set aside, equity investors may have concluded that it's just a negotiating tactic, and subsequent tariffs announcements have not spiked the volatility index thus far. Similarly, the University of Michigan's consumer inflation expectations have spiked, though noting that this forecast appears to be higher than most other estimates. Broader Trump 2.0 policy uncertainty around implementation and efficacy of tariffs, DOGE, and immigration is contributing to a wider range of potential economic outcomes, which may act as a headwind for markets if it causes inflation to pick up and keeps interest rates "higher for longer."

POLICY UNCERTAINTY DOESN'T ALWAYS TRANSLATE TO MARKET VOLATILITY



MICHIGAN INFLATION EXPECTATIONS SURGING, FED SURVEY MORE BENIGN



Source: Left – CBOE, Economic Policy Uncertainty. Right - FactSet, University of Michigan, Federal Reserve Bank of New York
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SPEAKING OF "HARD DATA," JANUARY INFLATION NUMBERS SHOWED MORE SIGNS OF PRESSURE

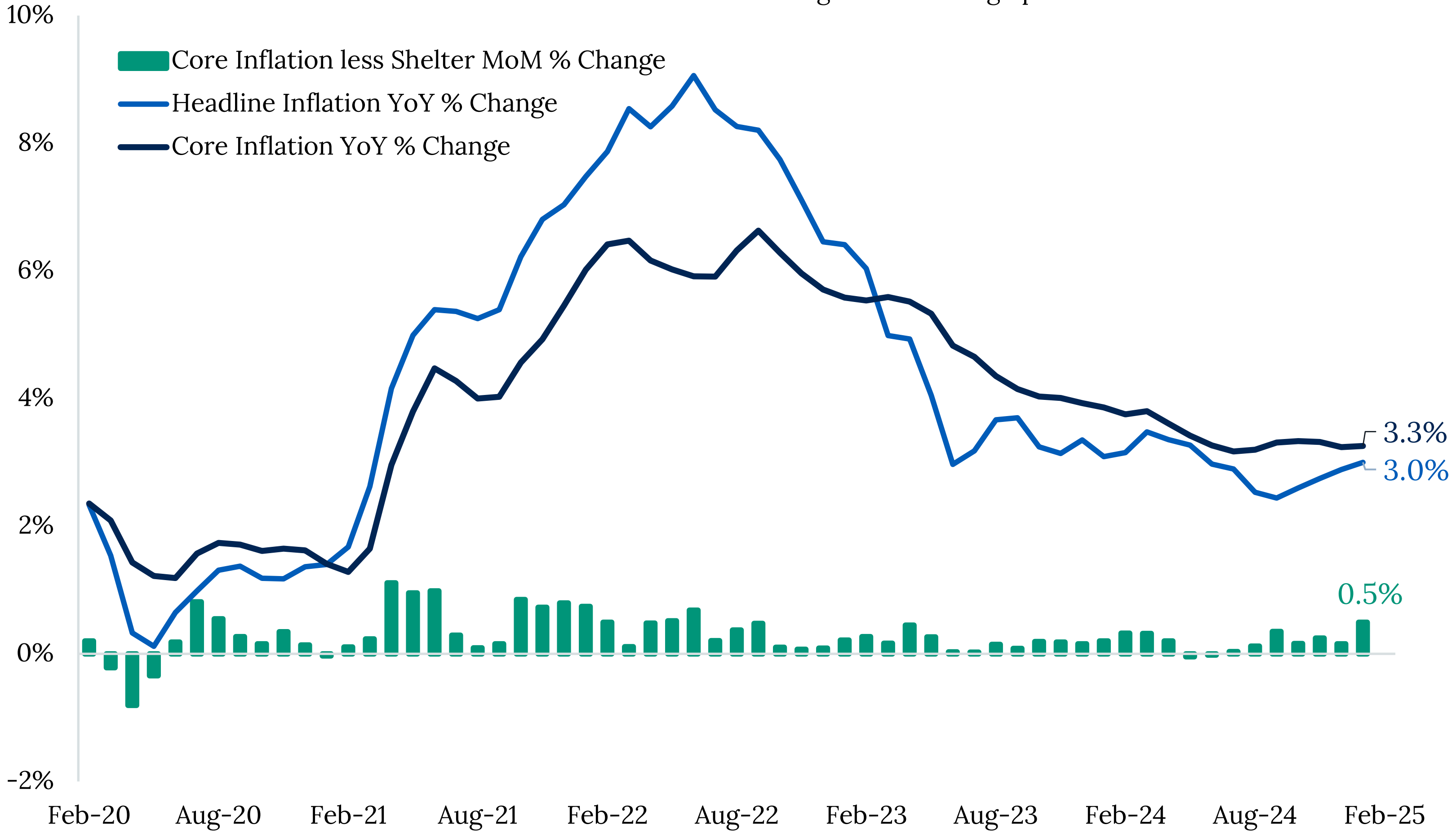
January CPI was hotter than expected, coming in above consensus forecasts:

- Headline CPI was up 0.5% m/m & 3.0% y/y.
- Core CPI was up 0.4% m/m (the largest increase in nearly two years), and 3.3% y/y.
- Shelter has been a lagged CPI component that has kept the numbers higher, but January's print reflected a relatively benign shelter number.
- Rather, we saw a notable jump in core inflation excluding shelter, reflecting broadening out of inflation, a net negative.
- We have seen some January and February pops the last two years, so seasonality is a factor we're watching.

This inflation print now sets a higher bar for the next rate cut, further cementing the expectation that the Fed remains in more of a "wait and see" holding pattern for now. **Expectations of further Fed rate cuts have been pushed out to September, from the previous 50/50 odds for June.**

CORE INFLATION *EXCLUDING* SHELTER ROSE +0.5% MONTH-OVER-MONTH

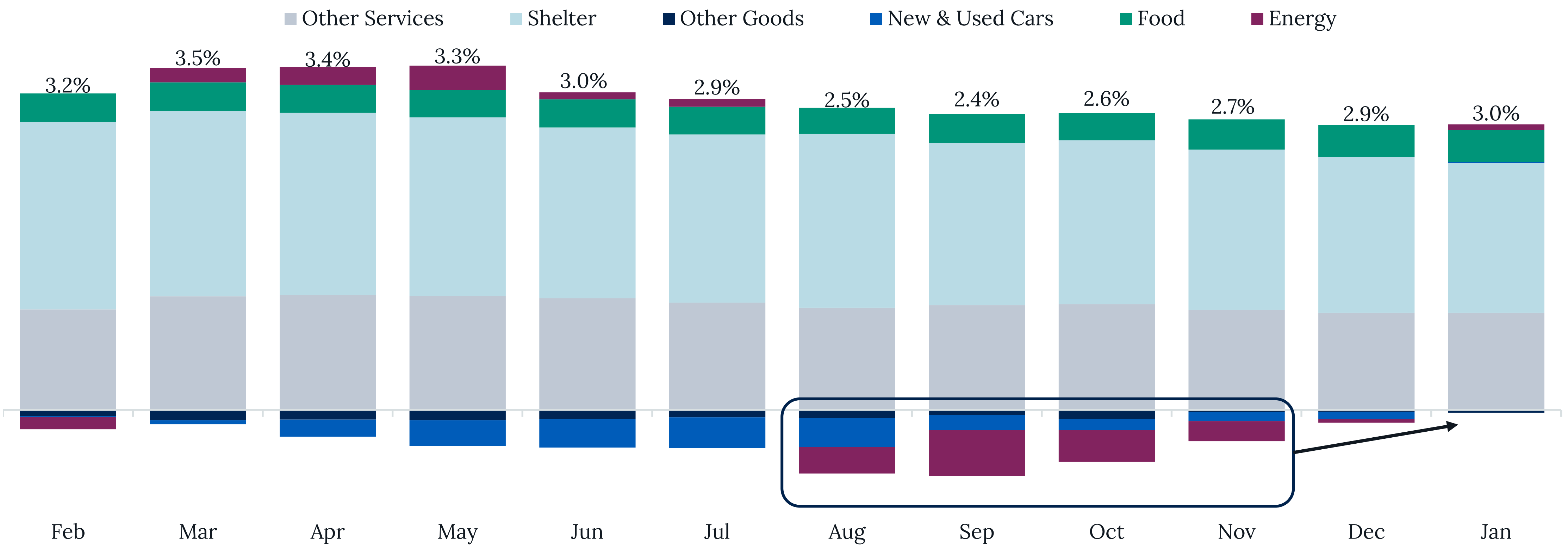
While the headline CPI reflects a continued disinflation trend in shelter—an encouraging sign—the issue is that inflation in other categories is ticking up.



SHELTER COOLED, BUT SERVICES INFLATION REMAINS STICKY AND GOODS DEFLATION IS FADING

While the lagging shelter component remains the largest absolute driver of inflation, it did continue to tick down slightly in January, a positive trend that is expected to persist. The more pressing factors are: 1) services inflation continues to prove sticky, and 2) deflation in goods, particularly new and used cars, is fading, reducing its ability to offset rising shelter and services costs. Additionally, energy has shifted from being a deflationary force in the back half of last year to now an inflationary one. While the Trump administration has a stated goal of increasing U.S. energy production to help curb inflation, we would note that many energy companies may not be incented to over-produce. Instead of driving prices down, they may prefer to maintain moderately higher prices to preserve higher profitability, especially after past periods of overproduction eroded margins.

HEADLINE CPI YOY



Source: Bloomberg.
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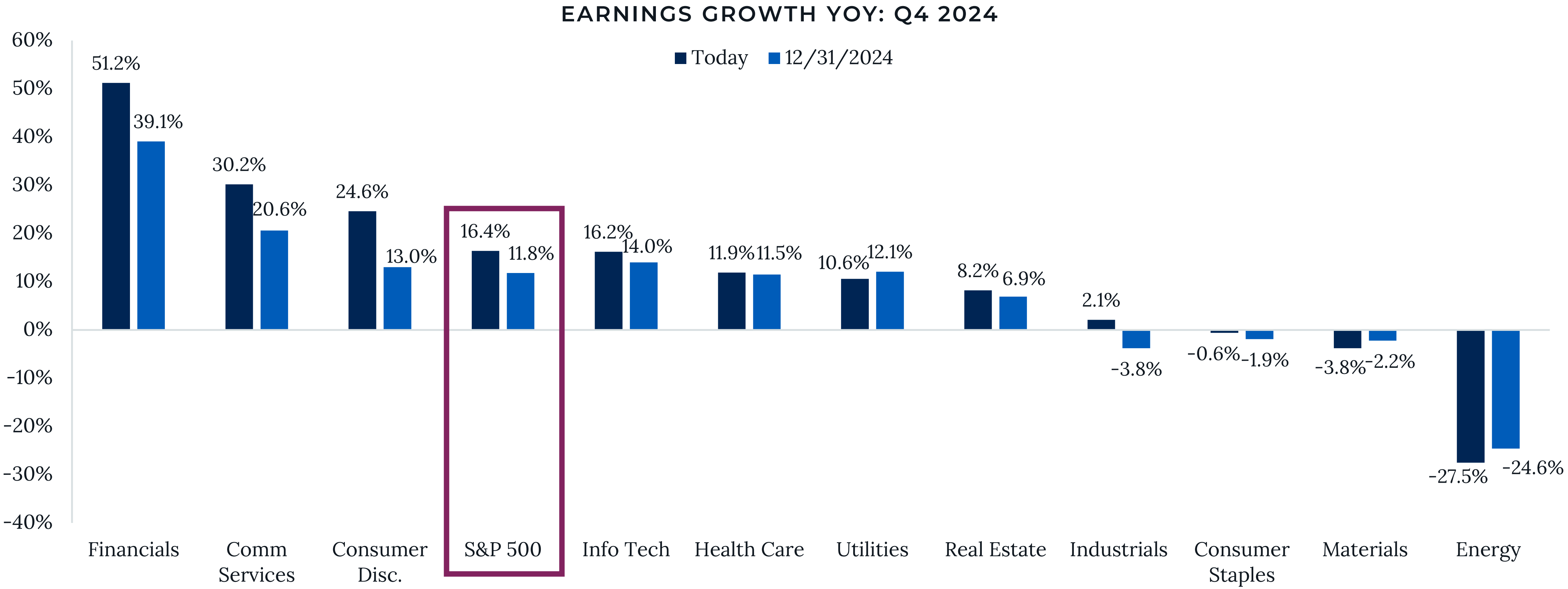
CURRENT EARNINGS ARE COMING IN STRONG, NOT IMPACTED BY POLICY OR INFLATION UNCERTAINTY

For now, earnings continue to perform remarkably well. Nearly two thirds of the S&P 500 companies have reported Q4 earnings. **EPS growth is on track to grow by 16.4% year-over-year, the highest growth rate since Q4 2021. This is significantly higher than the 11.8% growth expected by analysts at the beginning of the year.** If this pattern of better-than-expected earnings were to continue, then it's possible that the downside of any tariffs could be at least partially offset by what would be upside surprises in reported earnings.



Source: FactSet
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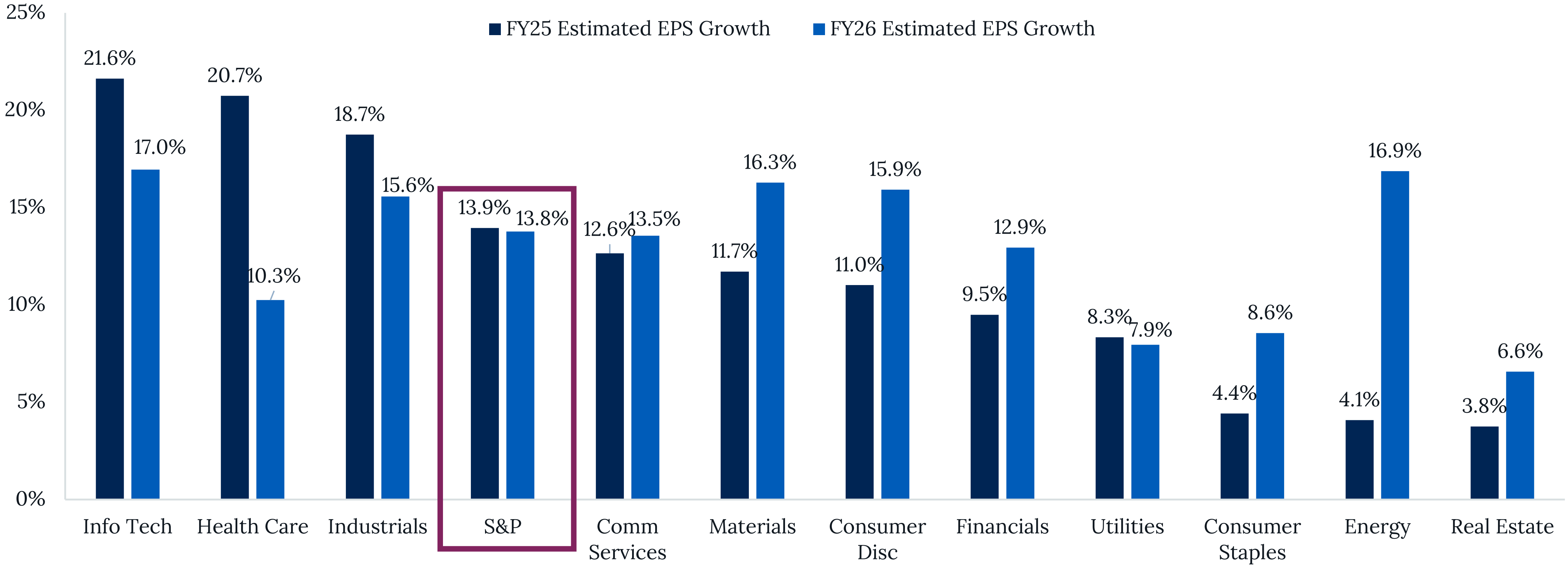
LOOKING FORWARD, EARNINGS ARE FORECASTED TO BROADEN OUT IN 2025 & 2026

Looking forward, analysts are predicting double digit year-over-year earnings growth for both 2025 and 2026, with all eleven sectors forecasted to report positive earnings growth. While Information Technology, Communication Services, and Consumer Discretionary (sectors where the Magnificent 7 are located) show healthy growth, Healthcare, Industrials, and Materials reflect notable improvements. Analysts believe earnings growth for companies outside the Magnificent 7 will improve significantly in 2025. **While the Magnificent 7 companies are expected to report earnings growth of 21% in 2025 (so still growing faster), these higher expectations across the other 493 stocks highlights a material broadening out of earnings expectations.**



Source: FactSet

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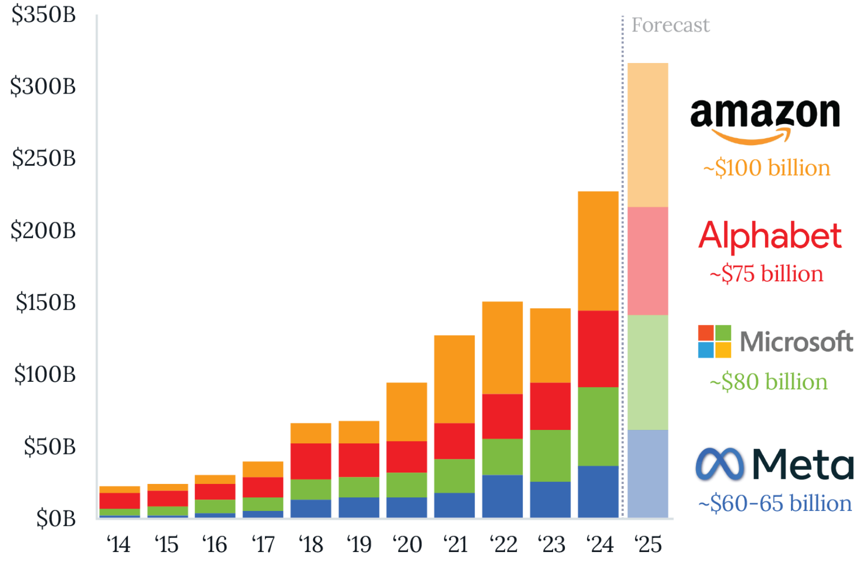
NO SLOWDOWN IN AI CAPEX SPENDING, WHICH WILL BE A KEY VARIABLE FOR FUTURE EARNINGS

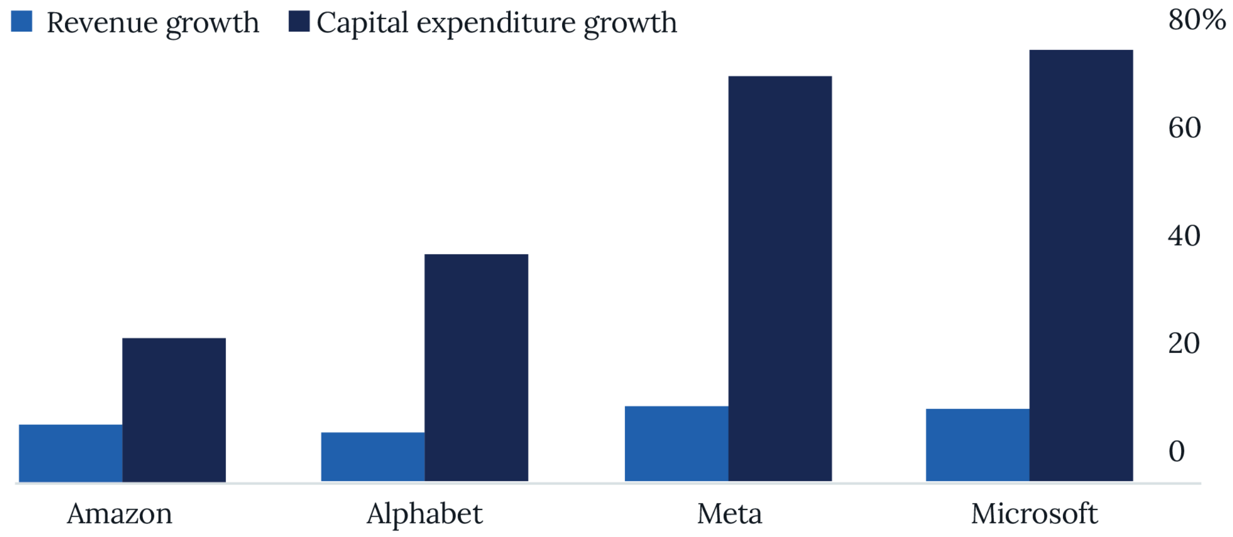
Investors continue to question when AI spending will translate into profits, especially after China's low-cost DeepSeek AI model briefly sent Nvidia's stock tumbling in January. However, the excitement over AI is still very much happening. Nvidia and other stocks affected by the DeepSeek news have largely rebounded, and companies like Meta are outlining clear paths to AI profitability. In their Q4 earnings updates in recent weeks, Alphabet committed $75 billion to capital expenditures, while Amazon announced plans to increase spending to $100 billion in 2025. Microsoft confirmed the company is on track to invest $80 billion in AI data centers, and Meta CEO Mark Zuckerberg revealed plans for up to $65 billion in CapEx, including a city-sized data center. **Altogether, these four tech giants will spend over $315 billion on capex—a 46% increase from the roughly $223 billion reported in 2024.**

The chart on the right highlights that CapEx is expected for far outpace revenue growth in 2025. These firms are aggressively investing in future technological capabilities across AI-driven services, cloud dominance, and data infrastructure expansion, hoping to maintain their leadership positions in the global AI arms race. **While uncertainty remains over when these investments will pay off long-term and the near-term effect could be lower margins and earnings, tech leaders remain confident. Amazon CEO Andy Jassy emphasized the long-term potential, stating, "*AI represents, for sure, the biggest opportunity since cloud and probably the biggest technology shift and opportunity in business since the internet.*"**

$315 BILLION IN 2025 CAPEX FROM FOUR TECH GIANTS



CAPEX OUTPACING REVENUE GROWTH REFLECTS LONG-TERM BETS



Source: Chartr, Bloomberg. Revenue figures are consensus estimates among analysts polled by Bloomberg. Microsoft data is for its fiscal year which ends in June 2025.
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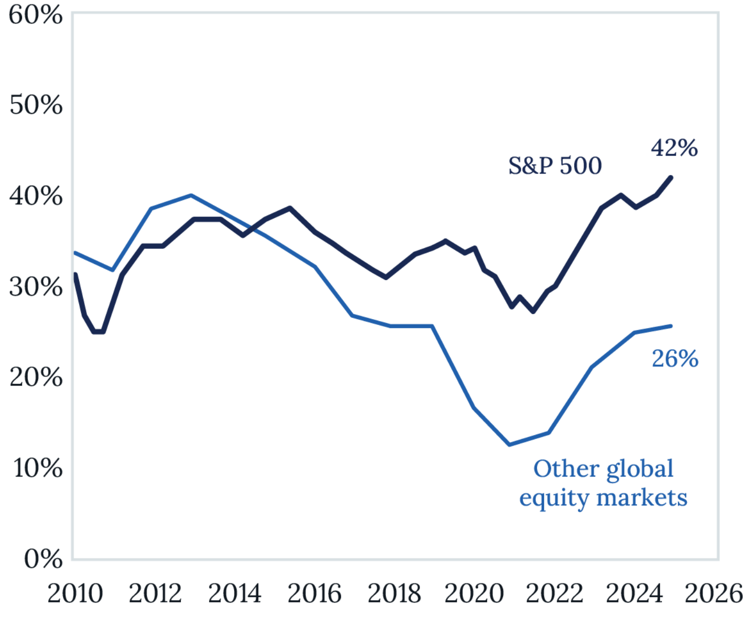
HIGHER EFFECTIVE US CAPEX AND R&D SPEND SUPPORTS "US ROLLS ON, ROW MORE CHALLENGED" THEME

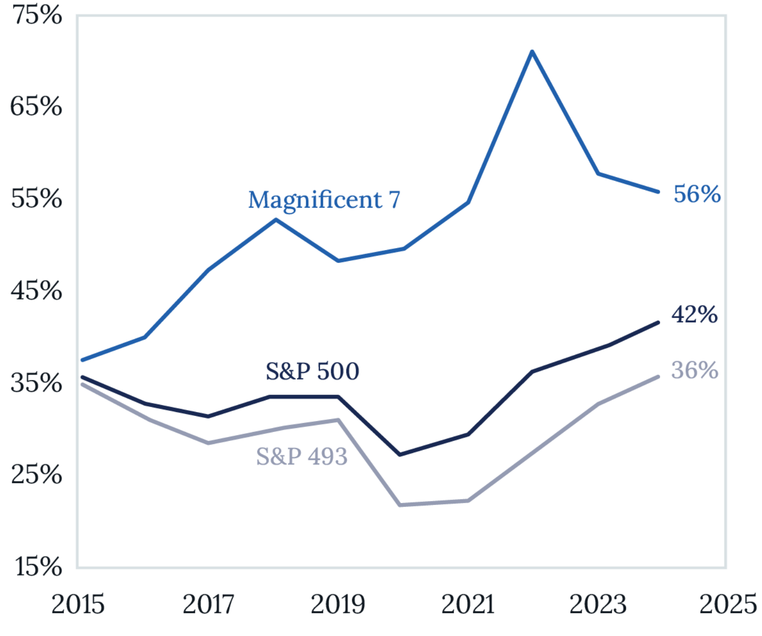
One of the key factors of our "U.S. Rolls On, Rest of World (ROW) More Challenged" theme is the U.S.'s leadership in innovation, which has consistently delivered higher returns on investment. **We have seen U.S. companies outpace other global markets in terms of reinvesting free cash flow into growth capex and research and development, with the Magnificent 7 playing an outsized role over the last decade.** However, reinvesting capital back into growth is only as effective as the return on investment it generates. Here again, **we see the U.S. has generated higher returns on investment over the last decade compared to the rest of the world. This dynamic is particularly relevant in the current debate over massive capex investments going towards AI and compute, where achieving a high return on growth investment will be critical to maintaining leadership.** Beyond tech, we are seeing Federal Reserve business survey data suggesting that capex is picking up across multiple sectors, signaling a broadening of economic growth. We believe the U.S. is well-positioned to maintain its dominant market position, with strong business fundamentals continuing to be the driving force for long-term business and economic performance.

GROWTH INVESTMENT RATIO

([Growth Capex + R&D] / CFO)

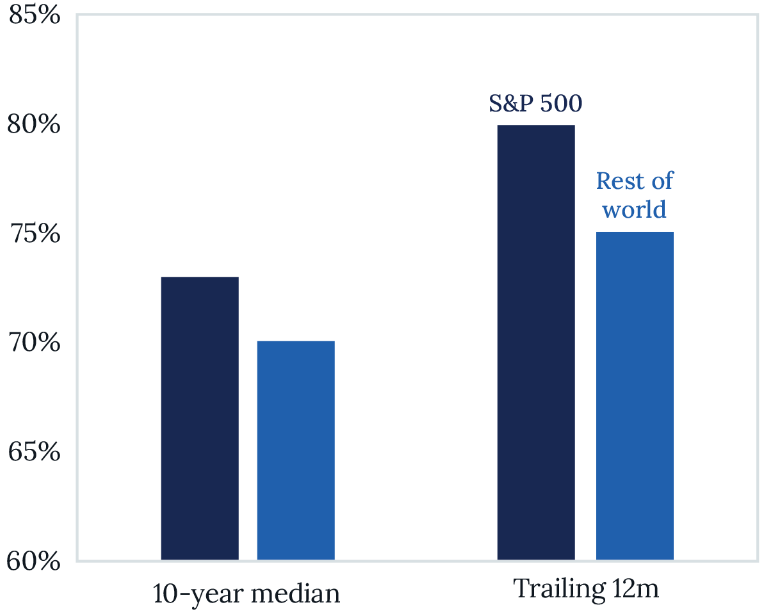


GROWTH INVESTMENT RATIO



RETURN ON GROWTH INVESTMENT

(Earnings / Trailing 3-Year Growth Capex + R&D)



Source: Goldman Sachs, Compustat, FactSet

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