FINANCIAL MARKET INSIGHT
VANN EQUITY MANAGEMENT

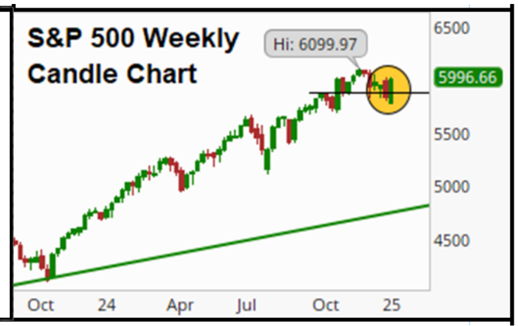
HIGHLIGHTS

- Four Key Areas of Policy and Politics That Matter Most to Markets
- **Economic Numbers**: What you need to know
- Market Multiple Table (January Update)
- Can Stocks Go Back-to-Back-to-Back?
- Hard Landing/Soft Landing Scoreboard

STOCKS

S&P 500

- Technical View: **The medium-term trend in the S&P 500 turned neutral in early 2025** after a violation of key Q4 '24 support resulted in a "lower low" on the chart.
- Dow Theory: **Bullish (since the week of July 10, 2023)**
- Key Resistance Levels: 6040, 6070, 6100
- Key Support Levels: 5950, 5836, 5725



"Stocks rebounded last week thanks to better-than-feared CPI/PPI data that eased worries the Fed was about to pause rate cuts."

SOURCE: Factset and Vann Equity Management Research Team

- ✓ **What is Outperforming**: Defensive sector, minimum volatility, and sectors linked to higher rates have relatively outperformed recently as markets have become more volatile.
- ✓ **What is Underperforming**: Tech/growth and high valuation stocks have lagged as yields have risen.

Four Key Areas of Policy and Politics That Matter Most to Markets

Donald Trump is now the 47th President of the United States and many investors are wondering how his policies will impact markets. So, our investment team wanted to identify the four key areas in Trump's policies that could impact markets, either positively or negatively. We are doing this because, now that Trump is President, the amount of news making comments, tweets, and "leaks" about potential policy decisions is likely to increase rapidly. So, to help cut through the noise, we highlight the four main areas Trump/Republican policies could impact the markets and what would make them broadly positive or negative for the economy/markets.

Finally, these are ranked in order of importance.

Area 1: Debt and Deficits

Given the relative legislative ease with which Trump can alter trade terms, we are likely to hear a lot about tariffs and trade right out of the gate, but that is not the biggest area of influence on the markets. Instead, the state of U.S. debt and deficits is, by far, the largest area of concern/interest for markets. Put simply, bond vigilantes have returned to the global bond markets in response to the post-Covid debt explosion and we are seeing that in real time in the UK.

Why Does This Matter?

The two major global economic benefits that make the U.S. "different" from other global economies are

1) The dollar is the reserve currency
2) The U.S. Treasury bond is viewed as the ultimate "risk-free" asset.

If tax cuts are passed with no spending offsets, that will jeopardize both of those advantages and the implications could be substantially negative for the economy (specifically slower growth, a weaker dollar, and higher rates). The increase in fiscal debt/deficit projections will absolutely spook global markets.

The positive however, is if, in the next few months, Trump and the Republicans can reveal concrete plans to slow spending, there is the idea that the government can simply grow its way out of the problem via tax cuts without cutting spending. However, markets, investors, and our portfolio management team want to see credible (albeit small) steps to curtail the growth of government spending. Remember, the problem with the U.S. fiscal situation is not revenue or growth, it is hands down, flat-out government SPENDING!

Area 2: Tariffs

Tariffs should be the area where we can expect the most immediate news and that has already begun with some of the executive orders on Trump's first day. Undoubtedly, there are going to be numerous and varied tariff headlines, threats, tweets, and leaks over the next four years, and we can expect these tariff-related items to cause market volatility and potentially negative headlines that will immediately hit markets while positive headlines will create relief rallies.

Why Does This Matter?

Because Tariffs, if done incorrectly, have the potential to

1) Hurt economic growth and
2) Boost inflation. That is what is known as stagflation[1]. However, as we saw during the first Trump administration, tariffs can also be applied while not dramatically impacting the economy and providing some benefits in revenue for the federal government. The key is in the scope and the exclusions. We can likely count on draconian and scary tariff headlines that could impact a wide swath of consumer goods. However, the devil is in the details.

[1] Stagflation is an economic cycle characterized by slow growth and a high unemployment rate accompanied by inflation. Economic policymakers find this combination particularly difficult to handle, as attempting to correct one of the factors can exacerbate another.

The positive here is the most popular and frequently used items are excluded from tariffs (for example, iPhones imported from China). The negative is if Tariff headlines are carried out to their full extent, thus impacting a wide inclusion of consumer goods, boosting inflation, and hurting the economy and corporate earnings.

Area 3: Taxes

The major issue with taxes is the extension of the Tax Cuts and Jobs Act (TJCA). Virtually everyone expects that this extension will be completed, likely towards the end of the year. However, as we all know in Washington, nothing is guaranteed.

Why Does This Matter?

Because time matters here! It is not great for the markets or the economy if they have to be dragged through 11-1/2 months of tax cut drama only to have a deal made at the very last minute. That would put a wet blanket over stocks for most of the year while investors generally assume that the TCJA extension gets done but are not sure.

We think the positives and negatives are very clearly stated in why these matter; but to keep consistent with format, the positives are if Republicans can pass an extension of TCJA it needs to be early in the year, preferably in the first half. The negatives are the extension of TCJA is delayed for virtually all of 2025, creating a sense of uncertainty and an unneeded headwind on stocks.

Area 4: Immigration

This is a hot-button topic, so we are not going to get into the politics of it, but it does matter from a market and economic standpoint.

Why Does This Matter?

Regardless of anyone's opinion on the state of immigration in the country, the U.S. economy is set up to rely on consistent immigration and the availability of relatively cheap labor. The cessation of that flow would potentially boost prices for numerous goods across industries as producers and service companies have to scramble for labor and pay up (we saw this during the pandemic). On the mass deportation side of things, that also poses economic risks as the removal of established labor would potentially create increased demand that could see service wages rise and begin to fuel a rebound in inflation.

The positive here is that current immigration laws are enforced to a fuller extent, but not in a way that disrupts the economy. The negative could be draconian immigration steps are taken and either halt the flow of labor or cause major disruptions to the existing labor supply.

Bottom line: Expect increased noise and volatility surrounding the incoming administration's new policies, but these are the four main areas whereby those policies could impact the markets and the economy, and this should help you cut through that noise and stay focused on what matters most to the markets.

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Economic Data (What You Need to Know in Plain English)

Markets started the month of January very nervous about a Fed pause and needed some tame inflation data to calm those worries and that is exactly what it got via the CPI and PPI reports. Core PPI rose 3.3% vs. (E) 3.5% y/y while Core CPI increased 3.2% vs. (E) 3.3%, so both metrics were slightly better than expected and definitely better than feared. However, neither was great in an absolute sense as they remain far from the Fed's 2.0% target and the pace of declines has slowed to an absolute crawl.

However, the rest of the data was solid and the question of whether the Fed has already paused, or not, remains open (which means at least until the Fed meeting next week any "hot" data will be a negative for stocks/bonds and any weak data will be a positive).

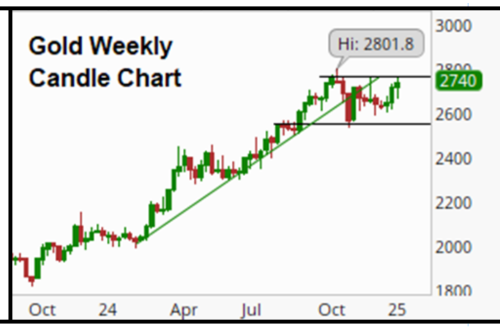
Turning to growth, the data was almost universally solid. The key report was the December retail sales report and while the headline was a slight miss vs. expectations (0.4% vs. (E) 0.5%), the more important Control Retail Sales (which is retail sales excluding gas, autos, and building materials) rose 0.7% vs. (E) 0.4% and implied that discretionary consumer spending remains solid.

Bottom line: In an absolute sense economic data was almost perfect for stocks in that it showed solid economic growth and better-than-expected inflation; and given the anxiety that had developed around a potential Fed pause on rate cuts, it is not surprising that stocks rallied.

COMMODITIES, CURRENCIES & BONDS

Gold

- Technical View: Gold has turned sideways since a late-2024 advance stalled and notably failed to reach new record highs, but the primary uptrend remains intact.
- Primary Trend: **Bullish (since the week of November 27, 2023)**
- Key Resistance Levels: $2754, $2787, $2802
- Key Support Levels: $2717, $2682, $2610



SOURCE: Factset and Vann Equity Management Research Team

"Commodities rallied last week led by industrial metals as cooler-than-feared inflation data eased worries about a prolonged restriction. Fed policy stance also supported gains in energy and precious metals. Easing geopolitical tensions and a late-week rebound in bond yields proved to be headwinds for oil and gold, resulting in underperformance."

Commodities rallied last week thanks to the combination of less-hawkish money flows supporting risk - on flows as well as a weaker dollar and lower yields, which all acted as tailwinds for the broader asset class.

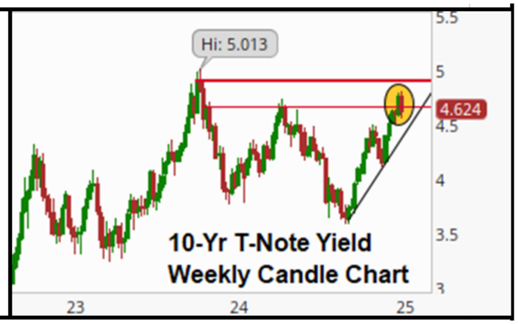
Gold lagged modestly with cooler-than-anticipated inflation data released over the last month which has been the primary driver of gold gains. The uptrend in gold remains intact and resistance at $2,750 was tested for a second time in

January, but a new break higher has yet to materialize.

Oil has been the upside standout in commodities with WTI futures charging to and through $80/barrel thanks to worries about a potential deficit in the physical markets due to new U.S. sanctions on Russia. A ceasefire deal between Israel and Hamas saw profit taking pickup as geopolitical fear bids were unwound and WTI futures ended the week well off the highs with a less-pronounced 1.04% gain.

10-Year T-Note Yield Futures

- Technical View: The 10-year yield broke out to fresh 52-week highs in early January, shifting the previously bearish outlook back to neutral with 5% resistance in focus.
- Primary Trend: **Neutral (since the week of January 6, 2025)**
- Key Resistance Levels: 4.656, 4.789, 4.868
- Key Support Levels: 4.563, 4.515, 4.420



"The 10-year yield pulled back from recent highs last week amidst the softer-than-expected CPI/PPI reports although the trend in the 10-year yield remains solidly higher."

SOURCE: Factset and Vann Equity Management Research Team

Special Reports and Editorial

Market Multiple Table (January Update)

The major change in the first Market Multiple Table of 2025 is a re-ordering of the major market influences, and this re-ordering is occurring courtesy of the Fed.

Specifically, the December "hawkish cut" that introduced the idea that the Fed may soon pause (or has already paused) rate cuts makes Fed rate cut expectations now the most important influence on stocks as we start the year. That replaces Hard Landing/Soft Landing, and for proof of this change in leadership, we just need to look at the market declines of the past three weeks, which have been mainly driven by concerns the Fed is not going to cut rates (which has helped push Treasury yields higher). Going forward, expectations for Fed rate cuts are the main influence on stocks.

Looking at the remaining three major influences on stocks right now, they are all roughly balanced. The Hard Landing/Soft Landing debate over economic data has also helped pressure stocks over the past few weeks not because investors fear a soft landing, but instead because economic data has been "Too Good" and that is combined with the aforementioned concerns about a Fed rate cut pause to push the 10-year Treasury yield to one-year highs.

Now politics has added to that upward pressure on Treasury yields. Tariff threats are dollar and yield positive, so Trump's tariff threats (and other threats about Greenland, Canada, the Panama Canal, etc.) are impacting markets.

Finally, these three factors are influencing the 10-year yield, which hit a one-year high last week. Technically, stocks are trading off the 10-year, but the movements in the 10-year are just a function of the first three influences: Fed expectations, hard landing/soft landing, and politics/tariffs threats. Reduced Fed rate cut expectations, better-than-expected data, and tariff threats have combined to lift the 10-year yield, which is now weighing on stocks.

Bottom line: Right now, Fed rate expectations and data are the main drivers of this market, and both have been marginally negative over the past several weeks. If we continue to see Fed pause fears rise, better-than-expected data, 10-year yield rise, and tariff threats start to be seriously believed, we should expect further and potentially substantial declines in stocks.

What Does this Mean for Market Valuation? Despite the Declines, There's Room to Fall

The valuation message from the January MMT is the declines in stocks are warranted because fundamentals are deteriorating; and despite the declines, this market could fall another several percentage points before we are at levels that are fundamentally justified. **Despite the pullback, this market has further to fall before we get to levels where stocks are fundamentally supported and potentially attractive.**

A Game of Multiples (Updated 1/14/2025)			
Market Influence	**Current Situation**	**Things Get Better If…**	**Things Get Worse If…**
Fed Policy Expectations	The Fed guided to just two cuts in 2025 but investors are worried the Fed may pause rate cuts and not cut at all in 2025.	The Fed reiterates its commitment to rate cuts this year in the January statement and pushes back on "pause" fears.	The Fed doesn't change the January statement and fear of a pause in rate cuts grows.
Hard Landing vs. Soft Landing	Economic data has been solid and better than expected recently, bordering on "Too Hot" and increasing Fed pause fears.	Economic data gets more Goldilocks, so meeting or slightly missing expectations and implying solid activity but not encouraging a rate cut pause.	Economic data keeps coming in better than expected and increases pause concerns or data suddenly drops and raises slowdown fears.
Tariff Threats	Trump has increased tariff threats, although for now, markets still view them as more of a negotiating tool than actual policy.	There are no major tariff increases or applications during the first quarter, reinforcing the market's expectations that tariff threats are a negotiating tool.	Trump increases existing tariffs or introduces new ones on major trade partners without major exclusions, backing up election tariff threats.
10-Year Treasury Yield	The 10-year yield has climbed above 4.75% to a near-one-year high.	The 10 year stabilizes in the mid-to-low 4.00%.	The 10-year yield surges towards and through 5.00% (which would be a warning sign on growth).
Expected 2025 S&P 500 EPS	**$270**	**$277**	**$260**
Multiple	21X	22X	17X-18X
S&P 500 Range	5,670	6,094	4,420-4,680
S&P 500 Target (Midpoint)	5,670	6,094	4,550
Change from today	**-2.84%**	**+4.42**	**-22.04%**

That does NOT mean however, that the pullback will continue (if the Fed reiterates a commitment to rate cuts, data is Goldilocks and tariff threats do NOT become reality, markets will rebound), but fundamentals have legitimately deteriorated from early December and at this point, 5,900 in the S&P 500 is "rich" given the reality of 1) Possibly no more rate cuts, 2) A possible 5% yield and 3) Tariff headlines.

Current Situation*: The Fed's "hawkish cut" in December has created fears the Fed has paused, economic growth is showing signs of re-accelerating, the 10-year yield has climbed to a near-one-year high and Trump tariff threats are ratcheting up.* The current situation reflects legitimate deterioration in the market set up since early December, as continued Fed rate cuts are legitimately in doubt, growth is borderline "hot," the 10-year yield is near 5.00% and Trump headline volatility is picking up. However, the underlying fundamentals of solid economic growth and (hopefully) still-easing monetary policy are still supporting stocks.

Things Get Better If: *The Fed clarifies it has not paused rate cuts; economic data moderates and returns to Goldilocks readings, the 10-year stabilizes in the mid-to-low 4.00% and Trump's tariff threats prove to be more bark than bite.*

This turn of events should legitimately send the S&P 500 back through 6,100 as it reinforces the near-perfect market narrative of:

1) Still-easing Fed
2) Solid economic growth (soft landing)
3) Stable Treasury yields
4) Re-focus on the pro-growth benefits of a Trump administration.

Things Get Worse If: *The Fed confirms a pause in rate cuts, ending the easing cycle, economic growth accelerates or suddenly reverses implying a growth scare, the 10-year yield surges towards and through 5.00% and Trump enacts sweeping and extensive tariffs that disrupt global trade and the economy*.

This set of events would essentially destroy the positive market narrative that fueled the entire 2024 rally and a steep drop in the S&P 500 should be expected as this is an environment of:

1) No Fed support and/or the re-introduction of rate hikes
2) Volatile economic data that implies rate hikes or a slowdown
3) Bond market weakness
4) Political volatility. While this outcome is unlikely, it cannot be wholly dismissed, and it is something we need to continue to be on guard for (which we will) because this would result in intense declines in stocks.

Can Stocks Go Back-to-Back-to-Back?

As we enter year three of this bull market, our investors are curious if this remarkable rally can continue. There is legitimate reason for optimism as there are positives such as solid economic growth, looming pro-growth policies from Trump and the Republicans, (likely) more rate cuts, and purportedly $7 trillion of cash on the sidelines waiting to be deployed.

However, there are reasons to be cautious, including stretched valuations, concentration risk (Mag 7/AI stocks), a softer labor market, the chance of a Fed misstep, a bulging deficit, Trump-inspired tariff issues, and geopolitical conflicts.

Last year, all of Wall Street's top 20 strategists' price targets came in well below where the S&P 500 finished (the closest forecast was 9% off!) This year, they have largely ratcheted up their projections. In early January our investment team collected forecasts from 25 firms. The average forecast, updated for the S&P 500's year-end close, predicts an 11.7% gain in 2025. Obviously, we can take that with a grain of salt. Interestingly enough, however, we would not take a gain like 11.7% off the table.

But lately, we have heard from multiple financial analysts that they think a double-digit gain—or even an average gain—is a distant possibility this year. Basically, they subscribe to the "due theory," meaning they simply think stocks are due for a bad year. Well, we did some digging because we wanted to dispel the notion that the stock market cannot have a good third year in a row. Here are some of the research and data we dug up that has historical significance:

- ✓ Going back to 1950, there were eight times when the S&P 500 delivered back-to-back 20% returns (not counting 2023 and 2024). The following year produced an average return of 12.3%, with positive performance in six of those eight cases. (Summarized from Ryan Detrick, Carson Group.)

Up 20% Two Years In A Row Isn't A Reason To Be Bearish

S&P 500 Returns After Back-To-Back 20% Returns (1950 - Current)

	S&P 500 Total Returns		
Years That Gained 20%	Year 1	Year 2	Year After Back-To-Back 20% Gains
1950 and 1951	30.8%	23.7%	18.2% (1952)
1954 and 1955	52.6%	32.6%	7.4% (1956)
1975 and 1976	37.0%	23.8%	-7.0% (1977)
1982 and 1983	20.4%	22.3%	6.1% (1984)
1995 and 1996	37.2%	22.7%	33.1% (1997)
1996 and 1997	22.7%	33.1%	28.3% (1998)
1997 and 1998	33.1%	28.3%	20.9% (1999)
1998 and 1999	28.3%	20.9%	-9.0% (2000)
2023 and 2024	26.1%	26.7%	?
	Average		12.3%
	Median		12.8%
	Higher		6
	Count		8
	% Higher		75.0%

Source: Carson Investment Research, NYU 11/24/2024
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- ✓ In the previous three instances where the S&P 500 went up by 25% in two straight years, the index was positive the following year two out of three times. When it rose by 53% and 33% in 1954 and 1955, respectively, it added another 7% in 1956; and when it went up 33% in 1997 and 28% in 1998, it jumped 21% more in 1999 (summarized from Ben Carlson, Ritholtz Wealth Management.)

- ✓ Since 1988, investing at a "new high" led to higher forward returns than investing on "any day" over forward 6-month, 1-year, 2-year, 3-year, and 5-year periods. In 2024, the S&P 500 set 57 all-time highs (summarized by JPMorgan Guide to the Markets.)

- ✓ The S&P 500 has recorded modest gains of 5.5%, on average, during the 12 months following the initial cut of a Fed rate-cutting cycle. The gains were typically double that in the absence of a recession (summarized by LPL Research.)

Bottom line: It is natural to think that after two years of 20%-plus returns, the market is due for a breather. However, history pushes back on that natural assumption. So, while another 20%-25% gain for the S&P is NOT probable, our team would NOT rule out another decent gain in 2025.

Hard Landing/Soft Landing Scoreboard

Economic data has taken a bit of a backseat to uncertainty around rate cuts and potential political impacts on the markets. But while those issues are driving markets right now, whether we keep this soft landing, or it deteriorates into a hard landing is still the most important medium- and long-term question for markets. Positively, there are virtually no signs in the important economic data that imply the economy is deteriorating.

If anything, it is the opposite as underlying economic data has improved over the past month to the point where solid data is adding to investor fears the Fed may pause. At this point, the data is not that good, yet we have seen a solid uptick in activity over the past few months that has kept slowdown chances low.

Now, to be clear, just because a hard landing has not happened does not mean it will not happen. If the Fed does pause rate cuts that means we will get higher-for-longer rates and that likely will weigh on economic activity, so we must continue to pay attention to data, because if we get a growth scare with stocks at these valuations it is a long way down to support.

For now, the key economic reports are not showing any sort of economic slowdown as almost all the indicators in the Hard Landing/Soft Landing Scoreboard saw improvement over the past month (only one is signaling weakness).

Hard Landing vs. Soft Landing Scoreboard				
	Current	One Month Ago	Three Months Ago	Hard Landing/ Soft Landing
ISM Manufacturing PMI	49.3	48.4	47.2	Hard Landing
ISM Services PMI	54.1	52.1	54.9	Soft Landing
Job Adds (Non-Farm Payrolls)	256K	212K	255K	Soft Landing
Retail Sales	632.25B	628.73B	620.10B	Soft Landing
NDCGXA	74.31B	73.78B	73.67B	Soft Landing
Jobless Claims	217K	220K	242K	Soft Landing

- ✓ **Of the Big Three-monthly economic reports, one remains soft while the other two are showing solid activity.** The ISM Services PMI remained comfortably above 50 at the latest reading, implying there is no loss of momentum in the service portion of the economy (which is the largest part of the economy). Meanwhile, the manufacturing PMI rose to the upper end of the year-plus, 45-50 range, implying a slight contraction (although that is not enough to threaten the economy). Manufacturing has been soft for well over a year, but the continued strength in the services PMI is an economic positive and reinforces that the economy remains in solid shape. *What signals hard landing going forward? ISM Manufacturing and Services PMIs stay below 50 for two more months.*

- ✓ **Consumer spending has seen acceleration.** Consumer spending spent much of 2024 stuck in neutral, but the last few months of 2024 saw an uptick in retail sales, implying the consumer remains resilient. With consumer spending solid, a broad economic slowdown remains unlikely. *What signals a hard landing? Retail sales roll over and begin to drop sharply, falling to multi-month lows within the next three months.*

- ✓ **Business spending may be accelerating.** New orders for non-defense capital goods excluding aircraft (NDCGXA) are the best metric we have for national business spending and investment, and while it plateaued for much of 2024, we did see an acceleration in business spending and investment in November. That makes sense as election clarity will likely unlock spending and investment that was waiting until we had political clarity. *What signals a hard landing? NDCGXA falling to multi-month lows in the next three months.*

- ✓ **Employment indicators remain broadly resilient (and have improved over the past month).** Labor market data has been noisy over the past few months starting with a very soft number in August, continuing through the hurricane-influenced jobs report collapse in October, followed by two strong months of large rebounds (including the December number, released earlier this month). However, for all the noise around the monthly data, weekly jobless claims have remained very low (near 200k) while the unemployment rate has been stable at just above 4.0%. The point is, that there is noise in the labor market data, but nothing is signaling material deterioration. *What signals a hard landing? Monthly job adds drop below 100k and/or claims above 300k.*