UNITED™
ASSET STRATEGIES, INC.
Planning for a Lifetime®

Quarterly Letter January 2025

Comments as of January 22, 2025

EXECUTIVE SUMMARY

Dear Clients and Friends,

Equity markets generated 2% returns in the 4th quarter, the 5th straight quarter of positive returns, and closed out the year 25% higher. While there were short periods of broad participation in 2024, as seen in Exhibit 1, the major theme for the year continued into the 4th quarter, with returns concentrated in a handful of Big-Tech names and the average stock and bond markets down 1 to 3% for the quarter. The most recent head fake in market breadth occurred in November, when stocks rallied post-election on the removal of election-related uncertainty, with cyclical sectors and small and mid-cap stocks further boosted by the increased likelihood of Trump's pro-business policies. That market strength faded in December, however, given the lateral implications of these policies on inflation and the budget deficit, as well as a more hawkish tone from the Fed on interest rates. As such, treasuries sold off in the quarter alongside a steepening yield curve.

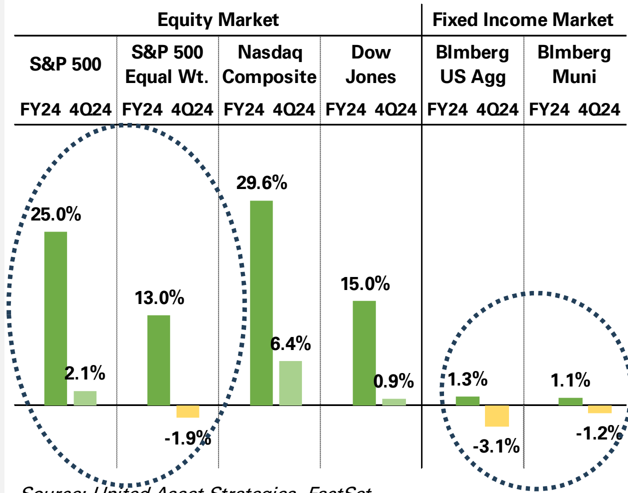
Entering 2025, we are positive on macro fundamentals, where fiscal policy and artificial intelligence should be tailwinds. Still, it would not surprise us if those fundamentals were partially priced-in, translating into more modest market returns. Indeed, 2024 marked the 2nd straight year of over 20% stock market returns which, outside of the formation of the Dot-com bubble, has historically been followed by a more muted year as highlighted in Exhibit 2. Further, there is potential for volatility as the market becomes increasingly sensitive to macro data points, given the data dependence of the Fed, and Washington headlines, as Trump's policies move through Congress. As we will detail, there is a silver lining for active managers, with opportunities to invest in these healthy fundamentals at below market valuations and moments of volatility providing increasingly attractive entry points.

While we actively harvested tax losses, two years of over 20% stock market returns, and the positive impact on client accounts, may drive larger taxable gains this year. Please reach out to discuss your realized gain-loss report.

Respectfully submitted by the Professional Staff at United Asset Strategies.

Exhibit 1: While equities were higher in 4Q, narrow breadth remains the dominant theme.

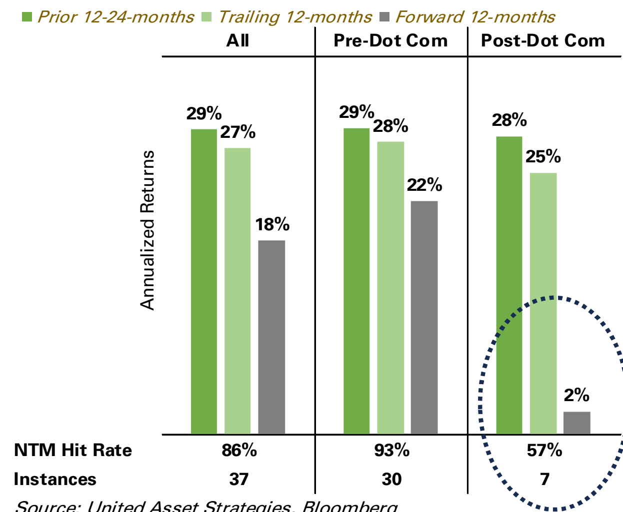
Equity and Fixed Income Index Returns for the 4th quarter and 2024



Source: United Asset Strategies, FactSet

Exhibit 2: Past periods of consecutive +20% years have been followed by muted returns.

Rolling 2 year periods with consecutive +20% returns, since 1989



Source: United Asset Strategies, Bloomberg

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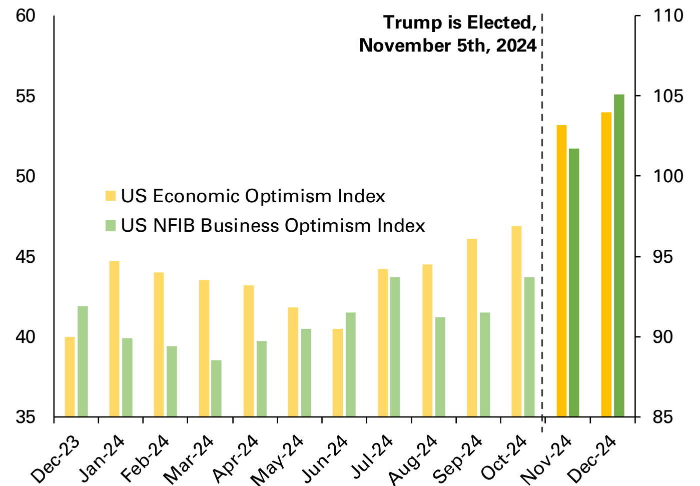
ECONOMIC & POLICY BACKDROP

Macro proves resilient, optimism now on rise. In 2024, a strong job market, low unemployment, and wage increases boosted consumer spending, which accounts for 2/3rds of US Gross Domestic Product (GDP) and led to a surprisingly strong economy. Recently, the Atlanta Fed Real GDPNow estimate of 2.7% for the 4th quarter exceeds the 2.1% consensus estimate. Further, the Conference Board's Leading Economic Index (LEI) rose sequentially in November for the 1st time in two years and has not signaled recession risk since early 2024. Also, its Coincident Economic Index has accelerated in recent months.

Positive economic momentum may continue into 2025, with the election results contributing to the renewed optimism evident in the US NFIB Small Business and US Economic Optimism indices shown in Exhibit 3. These monthly surveys indicated economic pessimism for businesses and consumers throughout most of 2024, but November results represented a clear inflection point higher. Only time will tell if this optimism translates into continued economic strength going forward.

Exhibit 3: A clear sign of the rise in animal spirits is the increase in consumer & business confidence seen since the election.

US Economic Optimism Index (Left), and US NFIB Business Optimism Index (Right)



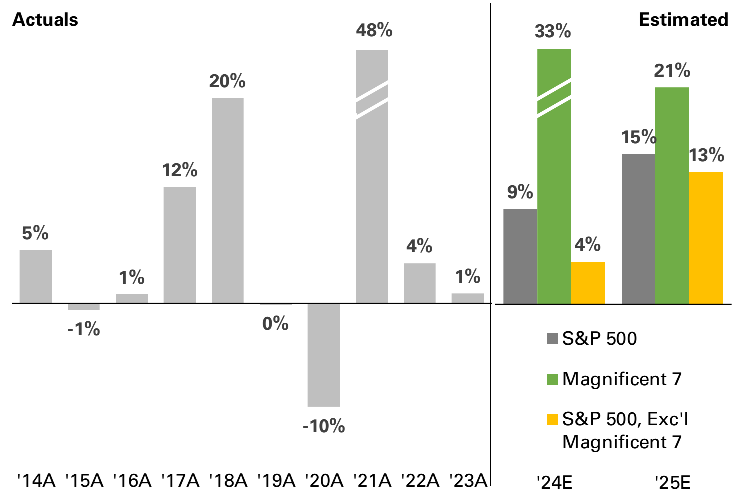
Source: United Asset Strategies, FactSet

Resilient economy supports healthy corporate profits. Business fundamentals were healthy this year, with S&P 500 3rd quarter profits beating expectations by 4% and growing 6% year-on-year, marking the 5th consecutive quarter of growth. Further, growth is expected to accelerate to 12% in the 4th quarter, the strongest quarterly rate in three years.

Into 2025, as highlighted in Exhibit 4, growth should accelerate above the 8% averaged over the prior decade and broaden beyond the Magnificent 7 mega-cap tech stocks to also include the other 493 stocks in the S&P 500. This growth should benefit from a cyclical upturn supported by President Trump's pro-business policies, as well as secular tailwinds from a multi-year build out of Artificial Intelligence (AI) capacity.

Exhibit 4: Earnings expected to accelerate again in 2025, to above historical avg. pace, all while earnings breadth widens.

Y/Y Earnings Growth for S&P 500, Magnificent 7 and S&P 500 Exc'l Magnificent 7



Source: United Asset Strategies, FactSet

Markets trade policy headline to policy headline... We outline four Trump policy proposals expected to be key in 2025.

1) Immigration policy that includes a deportation plan that could reduce the supply of cheaper labor, thus risking labor shortages and higher wage inflation in certain industries.

2) Trade policy that includes potential tariffs that may increase US revenue and reduce competition but also risks higher inflation and complicating global supply chains.

3) Tax policy that may extend individual tax cuts from the Tax Cuts & Jobs Act and reduce corporate taxes, boosting profits and spending but risks adding to the budget deficit.

4) Deregulation, notably in energy and financial sectors, may increase animal spirits and corporate profits but also result in longer-term risk as regulations are reduced.

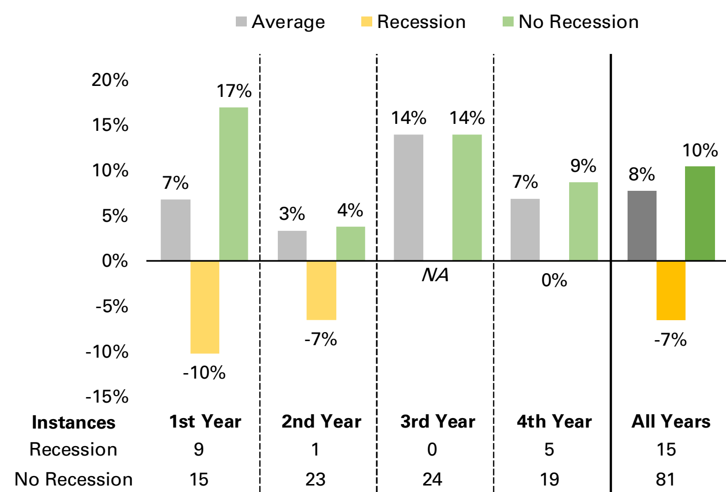
Each proposal presents opportunities and risks, driving volatility as they move through Congress. Absent a recession, however, stocks usually rise in the 1st year of a new president's term. As discussed, economic fundamentals are healthy, and as highlighted in Exhibit 5, returns in the 1st year of a presidential term historically rank strongest among non-recessionary years. We would attribute this strength to policymakers enacting large fiscal bills, such as those proposed by Trump.

… And macro data point to macro data point. Despite decreasing the Fed Funds rate (FFR) by 1 percentage point in 2024, the Federal Reserve (Fed) believes monetary policy remains restrictive, with the 4.25%-4.5% FFR target range far above the recent 2.9% annual inflation (CPI). While the market expects the Fed to continue lowering rates toward a more neutral policy stance, the pace of those rate cuts has become increasingly hard to accurately estimate, even for the Fed.

With inflation far above its 2% target for 2022 and much of 2023, the Fed primarily focused on the inflation side of its dual mandate, clearly articulating that rates would remain higher for longer as a result. Since December 2023, however, with inflation nearing the Fed's target, the Fed's outlook for the future path of rates has become increasingly data dependent. Exhibit 6 shows how the Fed's FFR expectations for 2025 were increasingly volatile last year, rising with hot inflation prints and falling with cool ones. We expect the Fed to remain data-dependent in 2025, with potential volatility in its policy outlook driving potential volatility in the broader financial markets.

Exhibit 5: Market returns have been healthy during the 1st year of an election cycle, more so if you exclude recessions.

Annual Price Return for the S&P 500, by election year and macro scenario (since 1929)

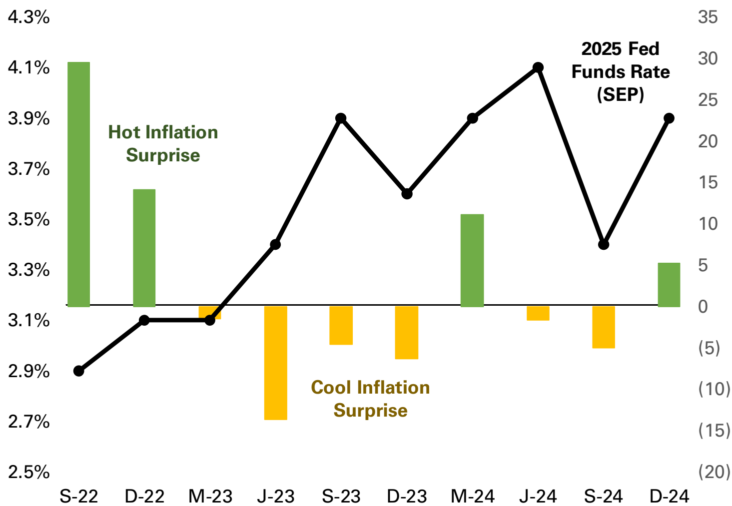


Instances	1st Year	2nd Year	3rd Year	4th Year	All Years
Recession	9	1	0	5	15
No Recession	15	23	24	19	81

Source: United Asset Strategies, Bloomberg

Exhibit 6: Macro uncertainty and data dependent Fed have driven rate volatility, and that is likely to continue in 2025

2025 Fed Funds Rate Guidance (Left) vs. Citi Inflation Surprise Index (Right)



Source: United Asset Strategies, Bloomberg

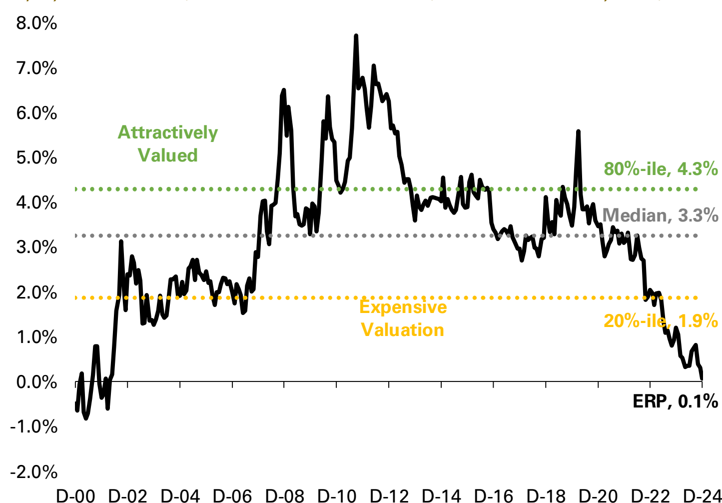
INVESTMENT ENVIRONMENT

Lofty expectations a tall hurdle for the market to clear. An optimistic 2025 earnings outlook can be a double-edged sword, in that it highlights strong fundamentals for Corporate America but also sets a high hurdle for stocks to clear to generate attractive returns. For historical context, note that the 15% earnings growth expected for 2025 would have only been met in 1/3rd of rolling 1-year periods over the past 25 years. While achievable, this is certainly no "layup."

And while the lofty valuation multiples on those earnings suggest investor confidence in meeting lofty expectations, they also imply potential market volatility if earnings disappoint. The risk investors assign to the earnings outlook can be seen in the equity risk premium, defined as the spread between the forward earnings yield and the 10-year Treasury yield or risk-free rate. As seen in Exhibit 7, the earnings yield offered above the risk-free rate is just 0.1%, below the historical median, and at a level not seen since the 2000 Dot-com bubble.

Exhibit 7: Relative to interest rates, stock valuations are rich, nearing levels not seen since the 2000's dot-com bubble.

Equity Risk Premium (Next Twelve Month EPS Yield, less 10 Year Treasury Yield)



Source: United Asset Strategies, FactSet

Trump-Powell Puts may offer downside protection. So far, we have discussed three potential market risks for 2025: political uncertainty, a data-dependent Fed, and lofty expectations. Despite this, we remain cautiously optimistic, expecting potential market pullbacks to be buyable long-term owing to the solid economic and earnings fundamentals previously discussed, as well as potential downside protection from the "Trump and Powell Puts," which we will discuss next.

A put is an option contract that allows the buyer of the contract to sell the underlying security at a predetermined price, acting as insurance that limits downside below that price point.

While not an actual option contract, the "Powell Put" references the idea the Fed provides downside protection to the economy, and in-turn the market, through rate cuts or quantitative easing. Similarly, it has been said Trump views the market as a barometer for his administration's performance, with the "Trump Put" referencing the idea he provides downside market protection via business-friendly policies. So, while Trump and Powell may be a source of volatility in 2025, they may also be a source of downside protection through accommodative fiscal or monetary policy should that volatility result in significant economic or market weakness.

INVESTMENT MANAGMENT

Attractive opportunity set despite expensive market. The equity market trades at a lofty 22x price-to-earnings multiple, far above the 17x historically, given the premium assigned to Big-Tech stocks that account for 1/3rd of the index. Indeed, the average stock trades at a reasonable 18x multiple; attractive should the promising 2025 earnings outlook prove accurate. So, while the market appears pricey, there remains a large, attractive opportunity set to consider under the surface.

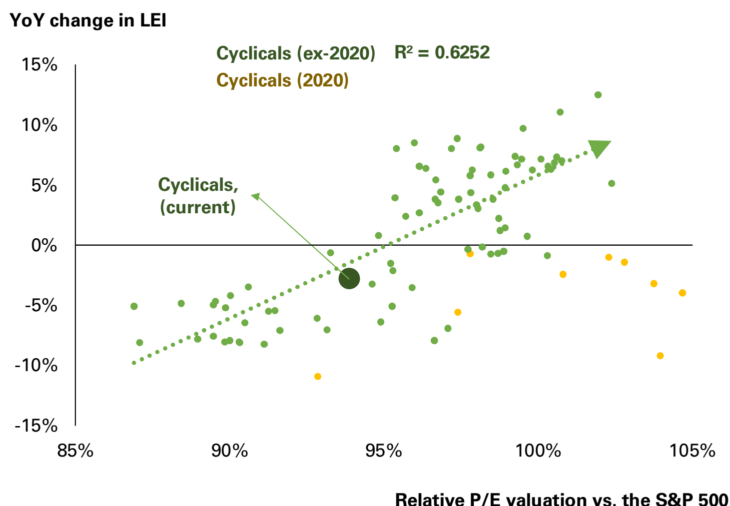
Let's Get Cyclical. One such opportunity is in Cyclicals, like Financials and Consumer Discretionary, where earnings have proven sensitive to the economy. In a prior letter, we noted the strong relationship between Cyclical earnings and the Conference Board's Leading Economic Index (LEI), which leads the economy by about seven months. After troughing at -8% year-on-year in 2023, below the Board's -4% recession signal, the LEI is now down just -3% and on an upward trajectory; a positive for Cyclicals should macro improvement continue.

Further, Exhibit 8 highlights a strong relationship between LEI and relative valuations for cyclical stocks vs. the market, with multiple expansion another potential tailwind should macro activity improve. Given the promising earnings outlook, in part due to Trump's pro-growth policies, we increased cyclical exposure, partially reducing our prior underweight position.

Artificial Intelligence (AI) Arms Race. Hyperscalers, large-scale cloud companies such as Amazon, Google, Microsoft and Meta to name a few, continue to invest heavily in a race to build out AI capacity and capabilities, with early capital expenditure guidance suggesting that pace of spend should continue in 2025. While our investments in the semiconductor industry have been one of the more obvious beneficiaries of this secular theme, our clients have also benefited from the growing power usage of AI through our targeted investments in the energy and utilities sectors.

Exhibit 8: Cyclical sector valuations sensitive to LEI; a positive for these stocks should the economy strengthen further.

YoY change in LEI, vs. Relative P/E for Cyclicals, since 2017 (ex-2020)



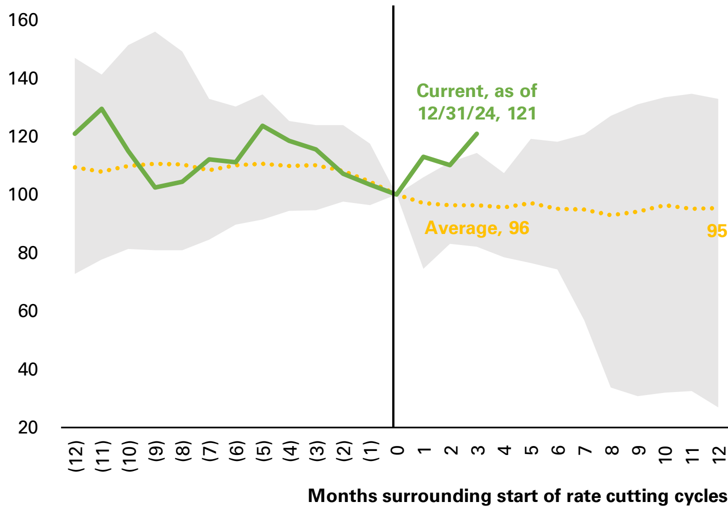
Source: United Asset Strategies, Bloomberg

Surprising opportunity to lock-in attractive yields. US economic strength kept credit spreads tight in 2024. With rich valuations not compensating investors sufficiently, we did not see an opportunity to add incremental credit exposure.

Still, fixed income's response to the onset of a new Fed rate cutting cycle provided a surprising opportunity to lock in higher rates. While the Fed cut the Fed Funds rate (FFR) by 50 basis points (bp) in September, followed by another two 25bp cuts to total 100bp of cuts before year-end, the 10-year Treasury yield surprisingly rose 80bp to 4.6% over that timeframe.

Exhibit 9: 10 Year yield substantially higher since the Fed's initial rate cut, bucking the historical tendency to move lower

10 Yr Treasury yield in months surrounding initial rate cut (base 100), since 1974



Source: United Asset Strategies, FactSet

Exhibit 9 highlights how unusual this is, as yields typically decline along the onset of a rate cutting cycle. Further, going back 50 years, rates have never risen this much in the three months following the start of a rate-cutting cycle. This may partially be due to Trump's concurrent election victory, given the inflation and federal deficit implications of his proposals.

With fixed income yields increasing into the onset of a new Fed rate cutting cycle and the yield curve steepening, we opportunistically purchased long-duration bonds during the 4th quarter. In doing so, we locked in attractive yields for longer, while also adding upside price potential should market rates decline at a pace more consistent with past rate cutting cycles. In the quarter, we rotated into US Treasuries, TIPS, and high-quality municipal bonds in client accounts, funding purchases through the sales of short-term and floating rate securities.

FINANCIAL PLANNING

Taxes are the cost of doing business, profitably. We have done our best to limit taxable gains in client accounts through low portfolio turnover and proactive tax loss harvesting. However, equity returns have been exceptionally strong, with stocks rising over 60% since the market bottom in 2022 and producing two straight years with over 20% returns, a level of momentum not seen on a calendar year basis since the formation of the Dot-com bubble in the late 1990s.

As such, despite our efforts to limit taxable gains, strong portfolio performance and growing client account values may result in a higher tax bill this year. By late February, we expect clients to receive their 1099 tax forms. Ahead of that, with tax season fast approaching, we recommend clients contact their relationship managers to discuss their realized gain-loss report.

In other tax-related news, the IRS announced inflation and cost-of-living adjustments for tax year 2025 with marginal tax bracket income ranges increased to account for inflation.

Other notable changes include:

- The 401(k) and 403(b) contribution limit rises to $23,000. The catch-up contribution limit for those age 50 and over increases to $7,500. Under a change made in SECURE 2.0, employees aged 60, 61, 62 and 63 are eligible for a higher catch-up contribution limit of up to $11,250.
- The limit for traditional and Roth IRAs contributions and catch-up remain $7,000 and $1,000, respectively. Although, the income ranges for determining eligibility to make deductible contributions all increased for 2025.
- The standard deduction for single filers increases to $15,000, and for married couples filing jointly, it rises to $30,000. For taxpayers 65 and older, additional deduction increases to $2,000.

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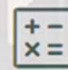

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