Weekly Commentary with Professor Jeremy J. Siegel

Markets Resilient Amid Historic Week and Fed Meeting in Focus

Monday, 1/27/2025

Donald Trump's second term as president came with a flurry of executive orders and his policies are rippling across the global markets. Meanwhile, investors are awaiting the Federal Reserve's first meeting of the year this week. There will be no rate changes and Chairman Powell will likely reiterate his satisfaction with recent inflation trends. The CPI and PPI data suggest the Fed is achieving its goal of gradual disinflation, though the upcoming PCE deflator, out post-meeting, will provide additional context. Powell is likely to avoid any forward guidance for March, leaving his stance contingent on incoming data.

Trump's remarks at the World Economic Forum, particularly his assertion that oil prices should drop, and interest rates should follow, dominated headlines. While the media sensationalized his demand for immediate rate cuts, his full comments linked rate reductions to a significant drop in oil prices. Were such a scenario to occur, it would indeed ease headline inflation, potentially giving the Fed room to adjust rates lower. However, the Fed remains independent, and Powell, despite his missteps in 2020-2021, has since regained Wall Street's confidence. I have been one of his harshest critics for those past mistakes, but think current policy is appropriate based on the current conditions. A conflict between the administration and the Fed could arise if market conditions deteriorate and Powell keeps rates 'too high' in the President's mind, but for now, stability prevails.

Economic data continues to support a soft-landing narrative. Weekly jobless claims remain in the sweet spot of 200,000-240,000, signaling labor market strength and balance. Next week's GDP report is expected to show Q4 growth between 2.5% and 3.0%, a solid pace that balances healthy expansion with moderated inflation risks. While strong employment can weigh on productivity growth, the overall trajectory for the economy remains very positive.

Trump's pro-growth stance, particularly regarding AI, continues to bolster tech stocks. The $500 billion commitment to AI infrastructure underpins the ongoing growth narrative, and there are no signs of momentum faltering in this sector. Recent earnings data reinforce optimism, with few companies issuing downward revisions. While some concerns about valuation persist, particularly around the AI and tech sectors, these fears often stem from flawed comparisons. For instance, using the nominal 10-year Treasury yield to assess equity risk premiums overlooks the fundamental difference between nominal and real yields. Adjusting for inflation via TIPS, the forward-looking real return on equities still exceeds that of bonds by a wide margin—there is no "negative equity premium."

On the geopolitical front, Trump's initial tariff measures on Canada, Mexico, and China were less aggressive than markets feared. The decision to impose only a 10% tariff on Chinese goods, down from earlier threats of 20-60%, was well-received, as was his willingness to engage with President Xi. This measured approach to tariffs is encouraging, reducing uncertainty and supporting global trade. However, Trump's cryptocurrency policy remains ambiguous, particularly regarding a potential Bitcoin strategic reserve. Markets are awaiting clarity as this will have significant implications for the crypto space.

In conclusion, the economy and markets are navigating a delicate but encouraging equilibrium. Growth remains robust without overheating, inflation is moderating, and geopolitical risks are being managed more deliberately than feared. The Fed's cautious stance reinforces stability, while Trump's policies, though unconventional, appear growth-focused in key areas like AI and investment into the U.S.

As we go to press, the Chinese developments with DeepSeek's AI model have shaken the tech world, particularly Nvidia and other firms with large investments in technology. We have spoken about what could derail the Magnificent 7 and the tech narrative and this is an example of one of them. This could finally signal the shift from growth to value stocks. We will watch developments closely.

Please see the WisdomTree Glossary for definitions of terms and indexes.