Weekly Commentary with Professor Jeremy J. Siegel

A Cautious Take on the New Year's Market

Monday, 1/6/2025

The new year begins with economic resilience, but investors should brace for a challenging path in 2025. Key economic indicators are still "goldilocks" and signal continued growth at a sustainable pace. The Atlanta Fed's GDPNow tracker aligns closely with major forecasts, projecting about a robust 2.5% GDP growth rate for Q4 2024. Simultaneously, jobless claims remain low, reflecting a healthy labor market. Inflation-sensitive commodities are stable, aside from minor energy fluctuations driven primarily by weather. This backdrop portrays an economy maintaining balance despite heightened interest rates.

Yet, uncertainty exists regarding the Trump administration's forthcoming economic policies. The market expects immediate action on tariffs, though implementation will take months. In taxation, proposed corporate tax cuts lack the transformative scale of the 2017 tax overhaul when the corporate tax rates went from 35% to 21% and we had a dramatic expansion of the estate tax exemptions and lowering of capital gains taxes. Trump has discussed a further reduction to the 15% corporate tax for products made in the United States. This is a much smaller scale and impact. There has also been no discussion of changing the capital gains rate, even though Republicans would favor that. Regulatory skepticism for big tech persists, raising questions about the growth potential in this key sector.

Valuation levels also warrant scrutiny. The S&P 500's forward P/E ratio near 23.5x earnings is not cheap, especially as bond yields rise. If we had another 20% gain in stocks in 2025, this would harken back to the gains in 1997, 1998, and the 1999 tech bubble that caused a painful bear market starting in 2000. History reminds us that markets can sustain high valuations temporarily, but risks grow as they deviate further from earnings fundamentals. Analysts currently expect around 17-18% earnings growth in 2025. In 2023 and 2024, two very strong years for the market, we had under 10% earnings growth each year. I wonder what can drive us to these lofty expectations for earnings and that leaves us vulnerable to disappointment.

Bonds remain under pressure, driven by a strong economy, fiscal concerns, and the specter of rising deficits. Long-term Treasury yields, currently around 4.6%, may climb further, potentially reaching the high end of a 4.5-5.5% range. This forecast reflects historical norms where long bonds trade with a premium of 100-150 basis points over Fed Funds in non-recessionary conditions. Such yield dynamics heighten competition for equities, especially those relying on high growth expectations. Dividend-paying stocks, however, retain appeal as their yields remain competitive relative to inflation adjusted bonds while offering dividend growth potential that TIPs do not.

AI and technology remain focal points for market narratives. Signs of rotation into less expensive areas or defensive sectors are still notably absent, leaving the overperformance of growth, at least for the meantime, intact. I could see a market correction in the broad market and a bear market in the Nasdaq if our long-waited market rotation occurs, but the catalyst for this rotation has yet to arrive.

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

Past performance is not indicative of future results. You cannot invest in an index.
Professor Jeremy Siegel is Senior Economist to WisdomTree. This material contains the current research and opinions of Professor Siegel, which are subject to change, and should not be considered or interpreted as a recommendation to participate in any particular trading strategy, or deemed to be an offer or sale of any investment product and it should not be relied on as such. The user of this information assumes the entire risk of any use made of the information provided herein. Unless expressly stated otherwise the opinions, interpretations or findings expressed herein do not necessarily represent the views of WisdomTree or any of its affiliates.