CYPRESS
ASSET MANAGEMENT, INC.

MARKET COMMENTARY **January, 2025**

2024 ASSET PERFORMANCE

	QTD	YTD
S&P 500	2.07%	23.31%
S&P 500 Equal Weight	-2.60%	10.60%
NASDAQ	6.17%	28.64%
Dow Jones	0.51%	12.88%
Russell 2000	0.01%	10.02%
World ex. US	-7.50%	6.09%
Oil ($71.72/bbl)	5.31%	0.20%
Long Term Treasury (4.79%)	-8.68%	-5.93%

As of December 31, 2024

The S&P 500 rose 23.3% in 2024 to post a second consecutive yearly gain exceeding 20%, only the seventh time that has occurred in the past 100 years and first time since the historic 1995-1999 market run. The Equal-Weighted S&P 500 again lagged far behind, up only 11% as equity performance continued to be driven by the Magnificent 7 (Apple, Nvidia, Microsoft, Alphabet, Amazon, Meta, and Tesla - the 7 largest stocks in the S&P 500) and a handful of other preeminent large cap companies. Collectively the “Mag 7” represent 33% of the S&P 500 Index and if you add #8 ranked Broadcom you reach 35% of the S&P 500 in 8 extraordinary technology-driven mega cap stocks.

2025 Outlook; Big Picture

- Current mid-cycle economy good for U.S stocks, can last for many years
- Fed rate hike cycle is over and rate cut cycle has begun
- Inflation has come down but still above Fed target zone
- AI spending boom, favorable pro-business policies of incoming Trump administration including deregulation & lower tax rates support strong economic growth and double-digit earnings growth

POSITIVE	NEGATIVE
• Resilient U.S. Economy in steady mid-cycle growth phase	• Questions Remain About Underlying Inflation and the Pace of Future Rate Cuts
• U.S. Markets Benefit As Best House in a Rough Global Neighborhood	• Restructuring of Global World Order
• Fed Rate Cut Cycle Began Fall 2024	• Ongoing Wars in Ukraine and Middle East & Flashpoints of Conflict in Taiwan, Korea, and Asia Pacific
• Fed Policy Working – Growth, Jobs, and Inflation Approaching Equilibrium	• Too early to declare victory on inflation; longer term rates remain stubbornly high
• Double Digit Earnings Growth: Product of AI spending boom, deregulation, lower taxes, and increased productivity	• Market Valuation: PE Level at High End of Historic Range
• AI & Technology Investment Spending Boom	• US National Debt at Record High Level ($36T), @1.25x Greater than Nominal GDP

We believe the backdrop for stocks remains favorable. The current mid-cycle economy is characterized by steady economic growth, a healthy jobs market, strong growth in corporate profits, and moderating inflation. Mid-cycle expansions can last for many years as we saw in the 1980s, 90s, and more recently in 2011 -2019. Since our last commentary in October there are three significant developments that will influence markets in 2025.

A Growth Agenda Comes to Washington

First, the incoming Trump Administration has prioritized pro-business and pro-growth policies including deregulation, lower tax rates, reductions in government spending and headcount and increased government efficiency. Its agenda also includes greater investment and incentives across industry for domestic manufacturing, production and job creation together with tariffs and other disincentives against overseas goods and production. The prospect of all this has boosted investor and business confidence. Given Republican control of the Senate and slim majority in the House, there is a window of opportunity for Trump 2.0 to actually implement significant portions of its economic agenda. This could boost growth, productivity and earnings in 2025 and beyond, a big positive for equities. An "America First" industrial and jobs agenda could also raise prices, at least temporarily, and heighten inflation concerns.

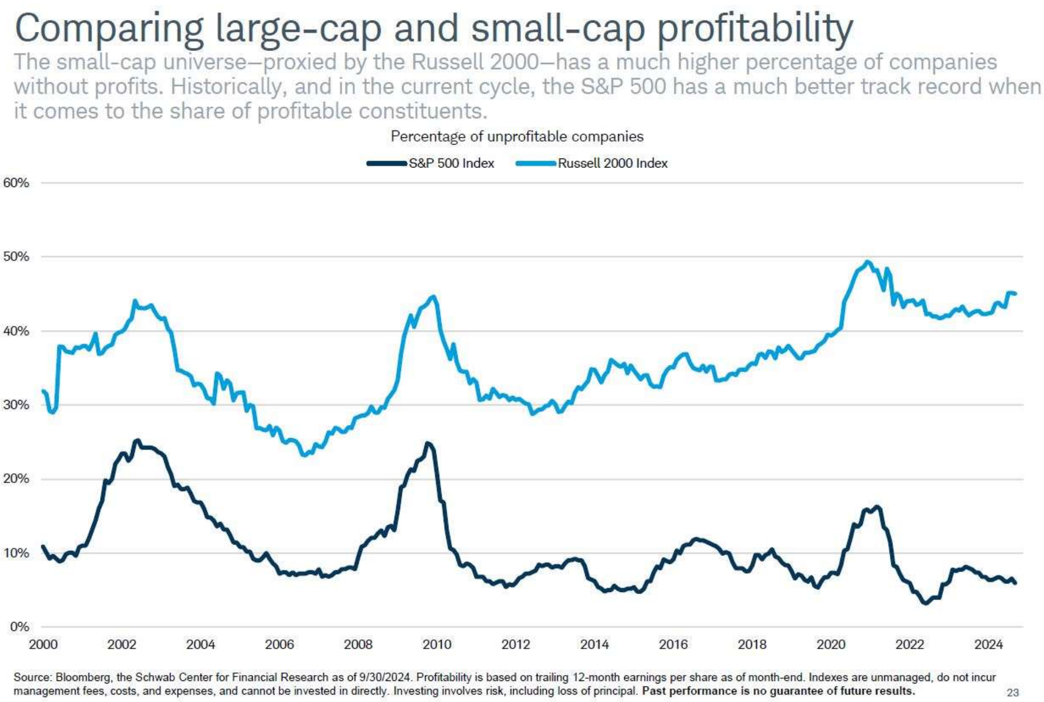
Equity valuations are expensive by historical measures and interest rates are likely to remain high in 2025, so market performance is dependent on earnings growth. We believe that we will see double digit earnings growth driven by a historic AI and tech spending boom. The long-foretold age of the machines has begun. A pro-business and pro-growth policy agenda can add to the momentum. However, if economic growth and earnings disappoint, it will not be a good year for stocks.

Interest Rates to Remain Higher for Longer

U.S. long term interest rates increased substantially in the 4th quarter as the 10-year Treasury yield rose roughly 100 basis points to end the year around 4.75%. Interest rates could remain stubbornly high in 2025 since the American economy remains strong, particularly relative to the rest of the world, and could get stronger as discussed above. If rates were to break convincingly above 5% this would be a headwind for markets and almost certainly lead to a downdraft in stocks. We do not expect this to happen, but we do expect long term rates will remain range bound around 4.5% on the 10- year Treasury and there will be limited scope for the Fed to cut rates more than once or twice in 2025. Another factor in higher rates is the sheer size of the national debt and budget deficits, which puts upward pressure on interest rates in order to meet the ever-increasing supply of government debt coming to market.

One consequence of higher rates, which could also simply be viewed as a return toward the longer-term norm from 1960 –2007 prior to the Financial Crisis, is that they pose a meaningful headwind to smaller cap stocks and a broadening out of the equity market. Without the backdrop of declining US rates, institutional investors are reluctant to place riskier bets on small caps (or "rest of world" foreign stocks). Until rates decline, they will stick to U.S. large caps since they have a powerful long run, tech-driven, secular growth story supporting them.

The S&P 500 is a best of breed asset and its largest companies are unrivaled in terms of profitability, cash flow generation, market dominance, and balance sheet strength. In contrast over 40 % of the small cap Russell 2000 is not profitable and faces balance sheet and income pressure from higher rates and interest expense. A renaissance in small caps may have to await a true step function up in US economic activity and productivity, requiring some combination of AI enhanced growth and productivity, deregulation and lower taxes to benefit small business. It may also require progress on our budget deficit. As a percentage of our economy (nominal GDP) government spending remains elevated relative to history and together with US national debt over $36 trillion is crowding out investment and funding so that only the self-funding mega cap super companies can truly thrive. Until these issues are addressed it remains a very challenging market for small to mid-cap companies and Main Street.



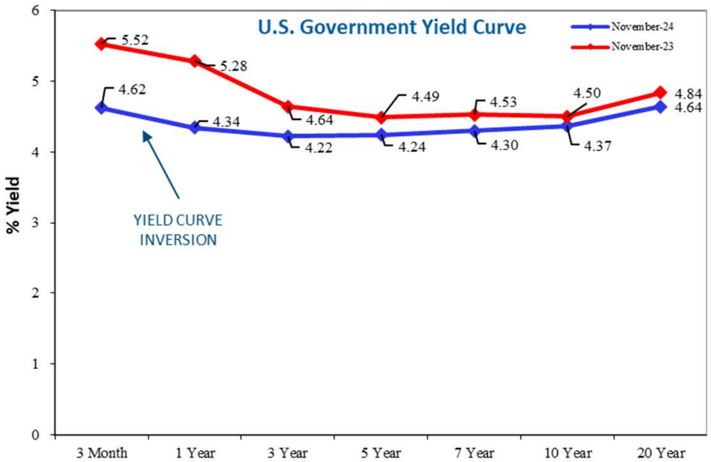
Peace Dividend

Third and finally, there are indications that the ongoing wars in Ukraine and the Middle East may be moving toward negotiation and settlement. While the peace process could take many months, a cessation of the bloody and costly wars would be positive for the global economy and mark a "return to normalcy" after 5 plus tumultuous years. Russia invaded Ukraine in February 2022 before the Covid Pandemic had ended and it has become the biggest conflict in Europe since WWII. A peace dividend would give a needed boost to the global economy and reduce inflationary pressures that have been intense since the onset of the global Covid pandemic. It also would help offset ongoing risks from an expanding US - China geopolitical conflict.

Global Economic Outlook & S&P Earnings - December 2024

Global Economic Outlook & S&P Earnings - December 2024 (S&P 500 @ 6,040)	2019	2020	2021	2022	2023	2024e	2025f
Global Real GDP Growth (y/y rate)	3.1%	-3.2%	5.9%	3.6%	3.2%	***3.1%***	***3.2%***
U.S.	2.3	-2.8	5.9	1.9	2.5	***2.7***	***2.5***
Euro Area	1.2	-6.1	5.2	3.4	0.5	***0.6***	***1.0***
Japan	0.7	-4.3	2.2	1.1	1.8	***0.3***	***1.2***
Developing Asia	5.2	-1.1	6.8	4.2	5	***4.8***	***4.7***
China	6.1	2.2	7.9	3	5.1	***4.7***	***4.5***
Latin America	0.8	-6.2	6.8	4	2.2	***1.7***	***2.0***
Emerging Market & Developing Economies	3.7	-1.5	6.7	4.2	4.2	***4.1***	***4.2***
S&P 500 Aggregate EPS	165	140	208	218	225	***245***	***275***
Earnings (y/y rate)	1.9%	-15.2%	48.6%	4.8%	3.4%	9.2%	12.2%
PE Ratio (December 2024 price @ 6,040)	19.6	26.8	22.9	17.6	21.2	*24.7*	*22.0*

Sources: IMF, ISI Group, BAML



Source: ISI, BAML, Federal Reserve

Federal Funds Target Level

2024

Date	Increase	Decrease	Level (%)
12/19	0	25	4.25-4.50
11/8	0	25	4.50-4.75
9/19	0	50	4.75-5.00

2023

Date	Increase	Decrease	Level (%)
7/27	25	0	5.25-5.50
5/4	25	0	5.00-5.25
3/23	25	0	4.75-5.00
2/1	25	0	4.50-4.75

2022

Date	Increase	Decrease	Level (%)
12/15	50	0	4.25-4.50
11/3	75	0	3.75-4.00
9/22	75	0	3.00-3.25
7/28	75	0	2.25-2.50
6/16	75	0	1.50-1.75
5/5	50	0	0.75-1.00
3/17	25	0	0.25-0.50

2020

Date	Increase	Decrease	Level (%)
3/16	0	100	0-0.25
3/3	0	50	1.00-1.25