

The BEAT – Outlook for 2025

Today we look at five key themes for 2025:

1. How To Invest in a Fully-Valued Market
2. The Bull Market Matures on Optimism
3. In Fixed Income, Securitized Credit Might Be the Sweet Spot
4. Stimulus Fatigue: China Can't Band-Aid Its Way to Recovery
5. The Potential Impact of Generative AI on Private Markets

Thank you all for listening in 2024. Have a joyous holiday season and a happy, healthy and safe 2025!

Jim Caron: Hello, this is Jim Caron, CIO of the Portfolio Solutions Group. In this edition of Caron's Corner we are going to focus on our outlook for 2025. The investment environment to start the new year is actually quite interesting. If we look at equity and fixed income markets, they appear to be fully valued, and the Republican sweep in the U.S. could have global ramifications. China continues to struggle to find its footing, while AI (Artificial Intelligence) might provide significant investment opportunities in alternative investing. There are five key themes in 2025 that we want to go through.

The first is how to invest in a fully-valued market, which is what it seems like today. Investors rarely agree on any one point; after all, there is a buyer and a seller at every price. But as we enter 2025 most investors do agree on one thing. Market valuations seem to be full and not many think assets are cheap. The question we then ask about 2025 is how do you invest in a fully-valued market? The simple answer is to optimize asset and investment selection in portfolios, because their return attributions may be a bigger difference than has been the case over the last several years. Said differently, we must prioritize alpha creation over beta.

The second point relates to equity markets and that and we say “the bull market matures on optimism.” If we go back to September 30th of 2022 the S&P 500 hit a -25% low bear market correction from earlier in the year. But historically, -25% corrections have generated excellent buying opportunities. As it turned out, the 12-month return for the S&P 500 at the end of September 2023 was +20%, and 2024 has been equally consistent as a second year of this bull market. We are now entering what we believe is the optimism phase of the bull market where we expect investors to be even more optimistic than they have been in the past two years. The final leg of a bull market before the next bear market is the “euphoria” stage and that's the danger zone. But that comes later. So expect to enjoy 2025.

Now turning to fixed income, we think that securitized credit might be the sweet spot. Our central view heading into 2025 is that we believe monetary policy will outpace current market expectations driven by moderate growth and a bumpy yet persistent disinflationary trend. While the base case remains data dependent, the post-U.S. election environment has made it increasingly policy dependent as well. If fiscal policy does materialize amid higher tariffs, we anticipate further upward pressure on yields,

steeper yield curves and rising risk premiums, ultimately pushing terminal rates higher overall. We believe the best opportunities will be in securitized credit, particularly U.S. mortgage-backed securities.

Now let's turn to China, where we're going to talk about stimulus fatigue and say that China can't merely band-aid its way to recovery. Since September, Chinese policy makers have focused on delivering a series of stimulus packages to inject new life into their struggling economy and boost share prices. However, high debt levels, over investment, an unresolved property bubble, underwhelming domestic consumption and international trade pressures all contribute to the structural weakness in China's economy that stimulus packages alone cannot resolve. Lessons from other debt-laden economies suggest the path to stability requires cleaning up bad debt through either write-offs or restructuring, followed by bank recapitalization. This approach is undeniably painful but without such drastic measures, stimulus packages will continue to provide fleeting relief. A deeper transformation must occur in China for lasting economic health and this is what we're going to be watching in 2025.

Lastly, let's look at private markets. It's interesting here because we think that the potential impact of generative AI on private markets will be quite significant and is expected to be a key theme in 2025. While private equity is expected to participate through both investing in "AI-natives" and companies that attempt to expand revenue and profitability through AI applications. We recognize that some of the earliest opportunities are identifiable in private infrastructure. Two key infrastructure related themes driving this has been the digitization of society and economies, and the global energy transition. These two mega-themes meet, where data requirements lead to power demand and this is leading to an extensive investment opportunity in 2025 and beyond. So with those five points behind us now, I want thank everyone for following us in 2024 and wish you all a happy and healthy 2025!

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