Economic and Market Review February 2025

February 28, 2025

Equity Indices	YTD Return
Dow Jones	1.88%
S&P500	-0.32%
NASDAQ	-4.83%
MSCI - Europe	10.56%
MSCI–Emerging	2.06%
Bonds (Yield)	
2yr Treasury	3.96%
10yr Treasury	4.16%
10yr Municipal	2.88%
U.S. Corporate	5.08%
Commodities	
Gold	$2,893.64/oz
Silver	$31.69/oz
Crude Oil (WTI)	$68.37/bbl
Natural Gas	$4.12/MMBtu
Currencies	
CAD/USD	$0.69
GBP/USD	$1.27
USD/JPY	¥149.61
EUR/USD	$1.05

Overview

Earnings season is close to closing out, with 78% of companies reporting earnings that beat expectations, which is around the 10-year average. However, the US stock market broadly traded down throughout the month as economic data came in below expectations amid policy uncertainty. January retail sales fell more than expected, and while manufacturing PMI (purchasing manager's index) saw growth, the services PMI fell for the first time in 2 years.

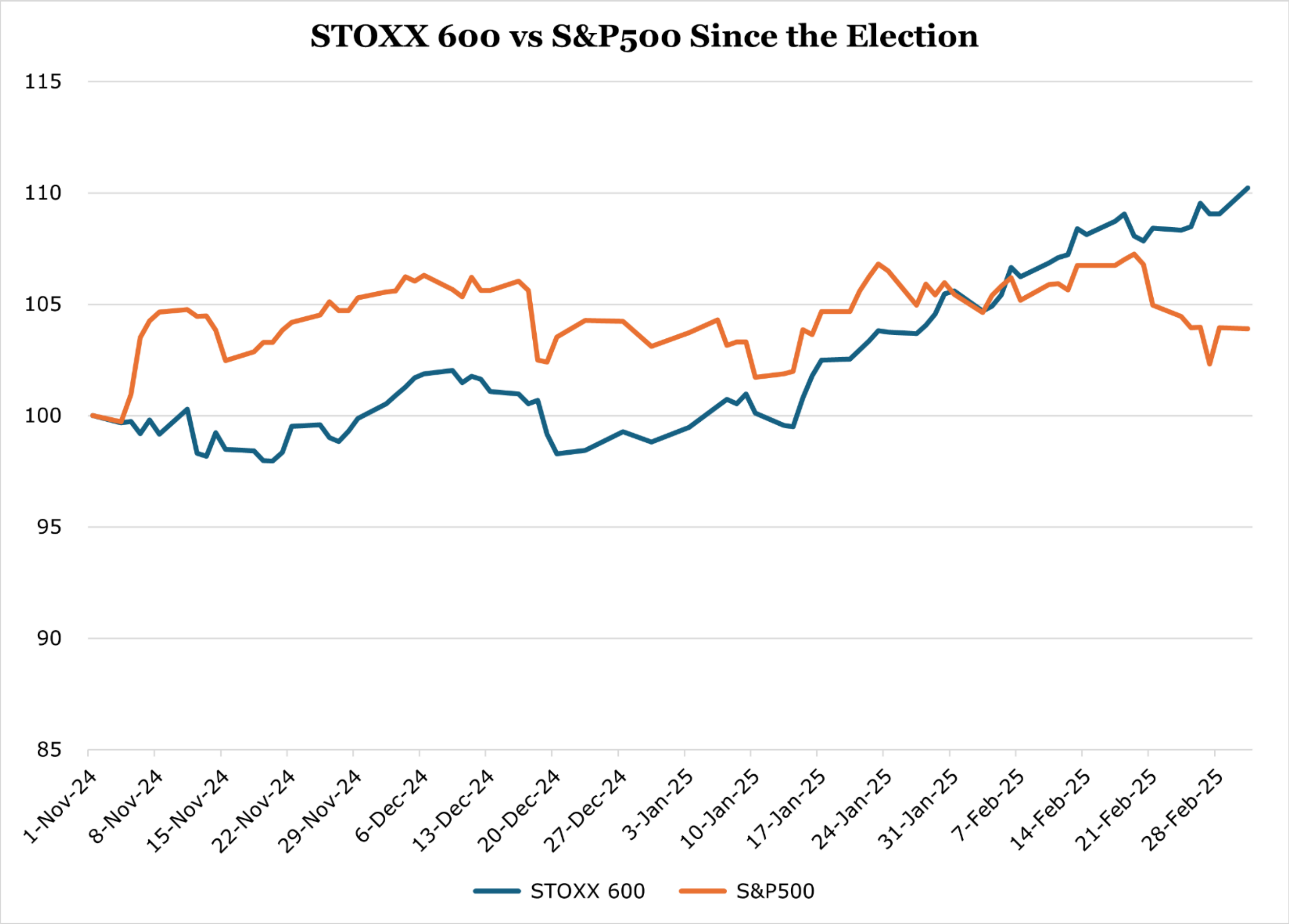
The bright spot was inflation cooled for the first time in 4 months, which indicated the Federal Reserve may be in a place to cut rates by the middle of the year. The labor market also appears to be cooling, with initial jobless claims rising – though the unemployment rate was exactly on target at 4.0%.

Housing activity in the US hit a low since record keeping began, with the Pending Home Sales Index reporting the "coldest" January in 25 years. The Pending Homes Sales index is regarded as the most accurate proxy for housing activity, as it is based on signed real-estate contracts. The economists at the National Association of Realtors state that the main reason behind this is high mortgage rates, averaging 7.04% when the data was collected, and high uncertainty in economic conditions.

Oil prices had some early month gains on data suggesting a later-year recovery for China, though OPEC+ seemed to be on track to go through with its plan to increase production during 2025, which caused oil prices to fall for the month.

European Equity Recovery

The STOXX 600 index, an index of 600 companies traded in Europe, have outpaced US equities so far, returning 10.3% YTD. With the United States reviewing its military presence on the European continent, defense stocks like the German Rheinmetall and French Airbus have led the pack.



Index: 100 = Nov 1, 2024

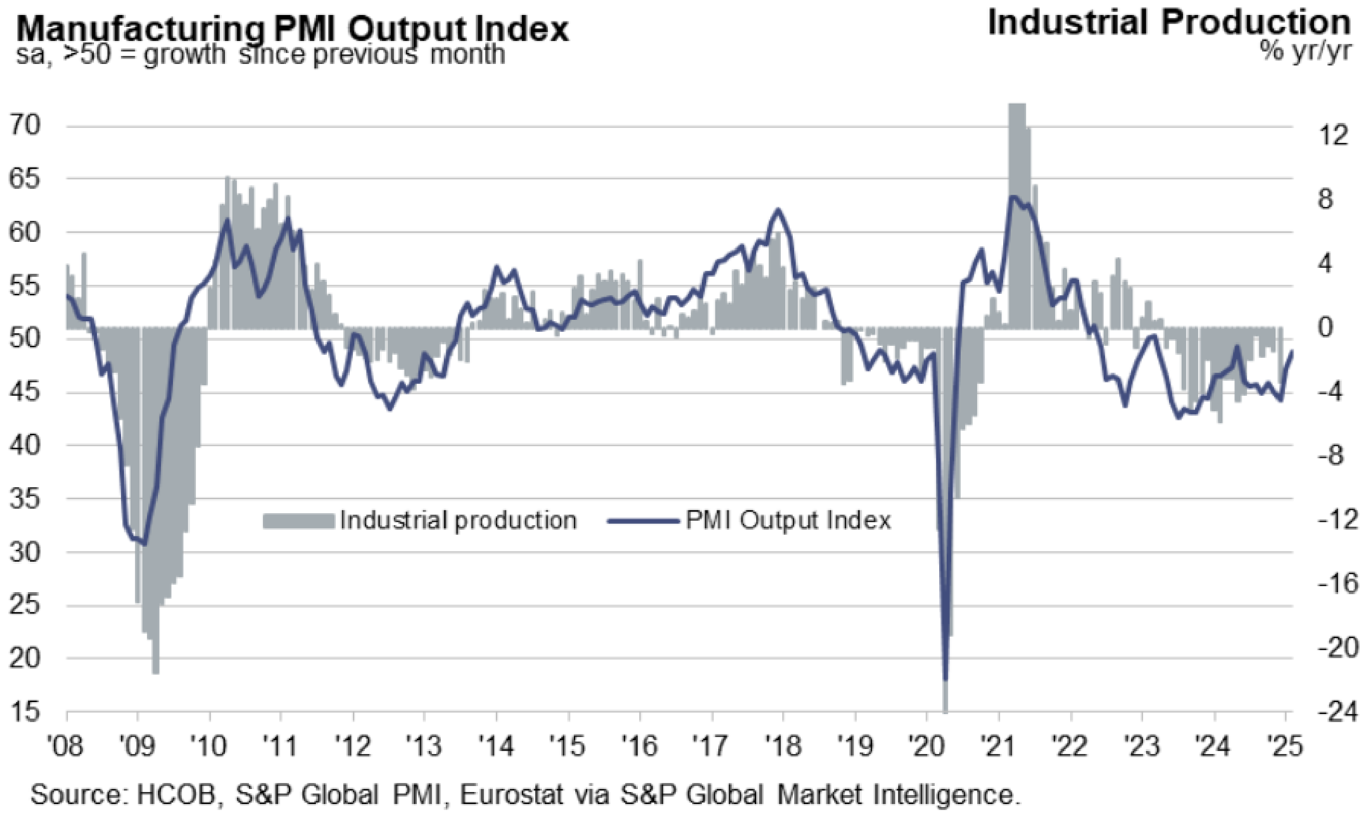
Domestic producers saw a boost late in the month after the EU Commission posting a draft for legislation that would exempt most of Europe's companies from CO2 import taxes. First entering into force in 2026, the CBAM (carbon border adjustment mechanism) was designed to prevent companies from circumventing carbon taxing by importing raw materials from areas without or less than the EU's carbon pricing. The new proposal will exempt firms from the carbon tax if they import less than 50 metric tons of inputs per year. This covers more than 200,000 companies across the EU, close to 80% of firms previously subject to CBAM.

	Steel Cost	Carbon Tax	Tariffs and Duties	CBAM	Total Cost per Ton	No CBAM
Domestic EU Production	$750/ton	$75/ton	0%	$0	$863	
Emerging Market Import	$500/ton	$0/ton	25% + 20%	$75/ton	$875	$725
Developed World Import	$700/ton	$30/ton	25%	$45/ton	$987	$920

Assumes it costs: 1.5 tons of carbon to make 1 ton of steel in developing markets, 2.0 tons in emerging markets. Assumes a 20% anti-dumping duty from emerging markets.

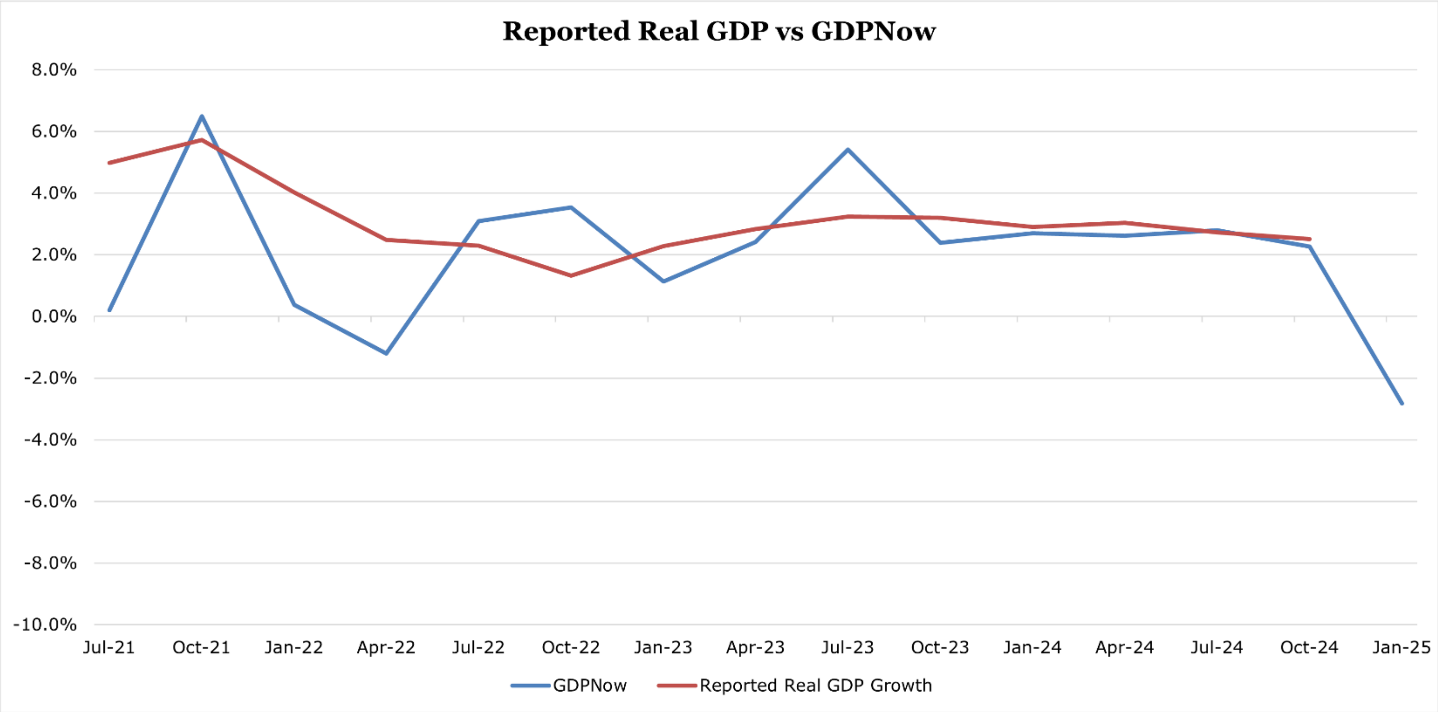
Companies with little import activity or importing from places with opaque emissions reporting must still bear bureaucratic cost of reporting on top of facing higher input costs. This is especially true for goods that the EU does not domestically produce in high quantities, such as lumber or fertilizer.

Despite the equity recovery and hope for a more tempered approach to emissions control, European PMIs (purchasing manager's index) are still depressed. Largely, the headwinds in the European economy is related to energy prices, which traded at 5 times higher than the US throughout 2023 and 2024. Offering some optimism, the February 2025 release was the highest in 2 years.



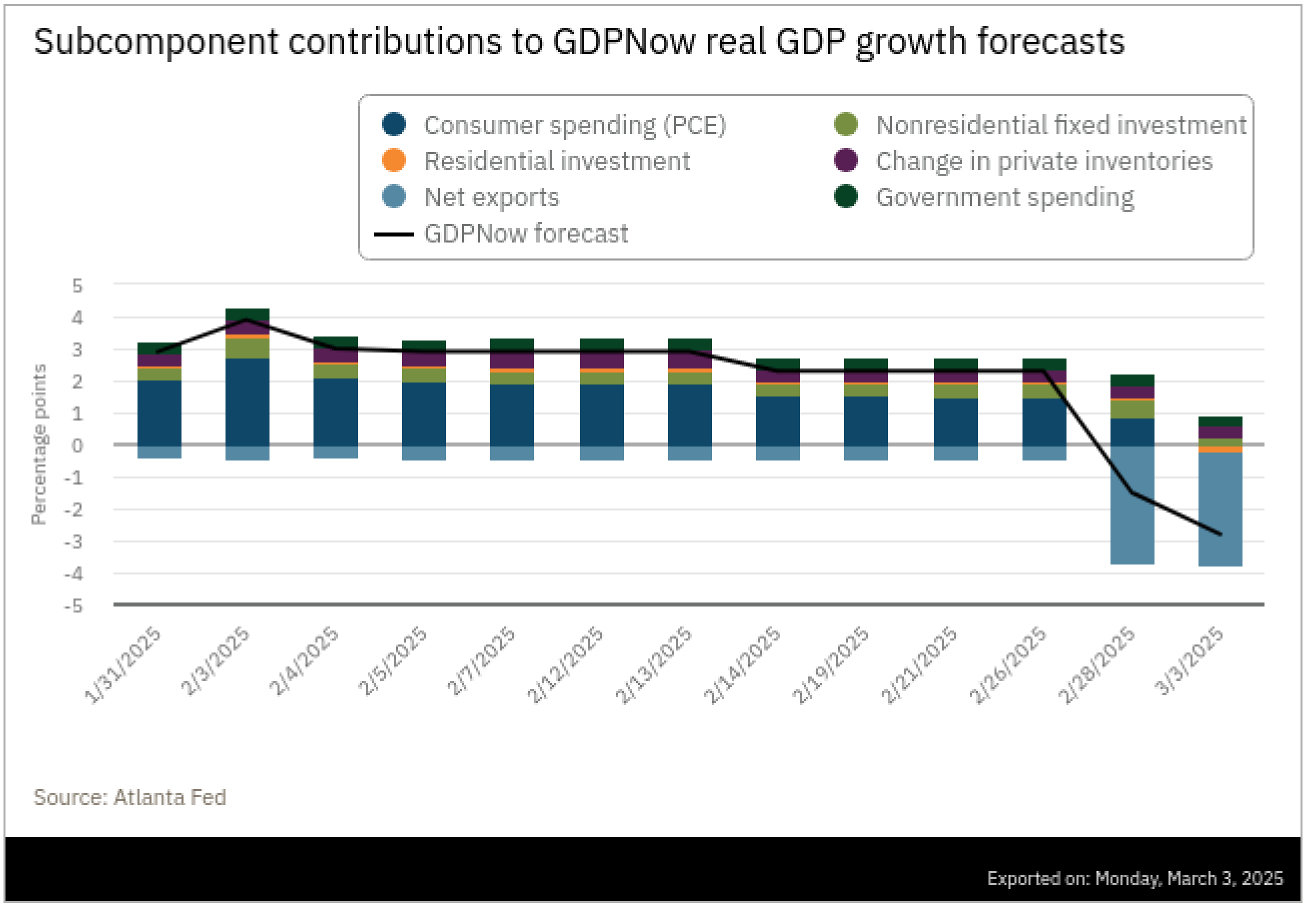
GDPNow Collapses – Is it Accurate?

The Atlanta Fed releases a 'nowcast' for estimating GDP activity at any given point, before the quarterly data releases. The 'nowcast' utilizes the same components, though more frequently, or proxy measures, and extrapolates it forward. Under normal circumstances, GDPNow ends up being close to the final GDP figure.



However, the latest GDPNow figures have collapsed to their lowest level since it began in 2012, implying a more than 2.8% annualized contraction in the US economy for the quarter ending March 2025. Numerous media outlets have picked up on the story and have stoked fears of an impending recession.

This happens because GDP is calculated as Consumption + Business Investment + Government Spending + (Exports - Imports). As the data becomes available, it is priced into the model.

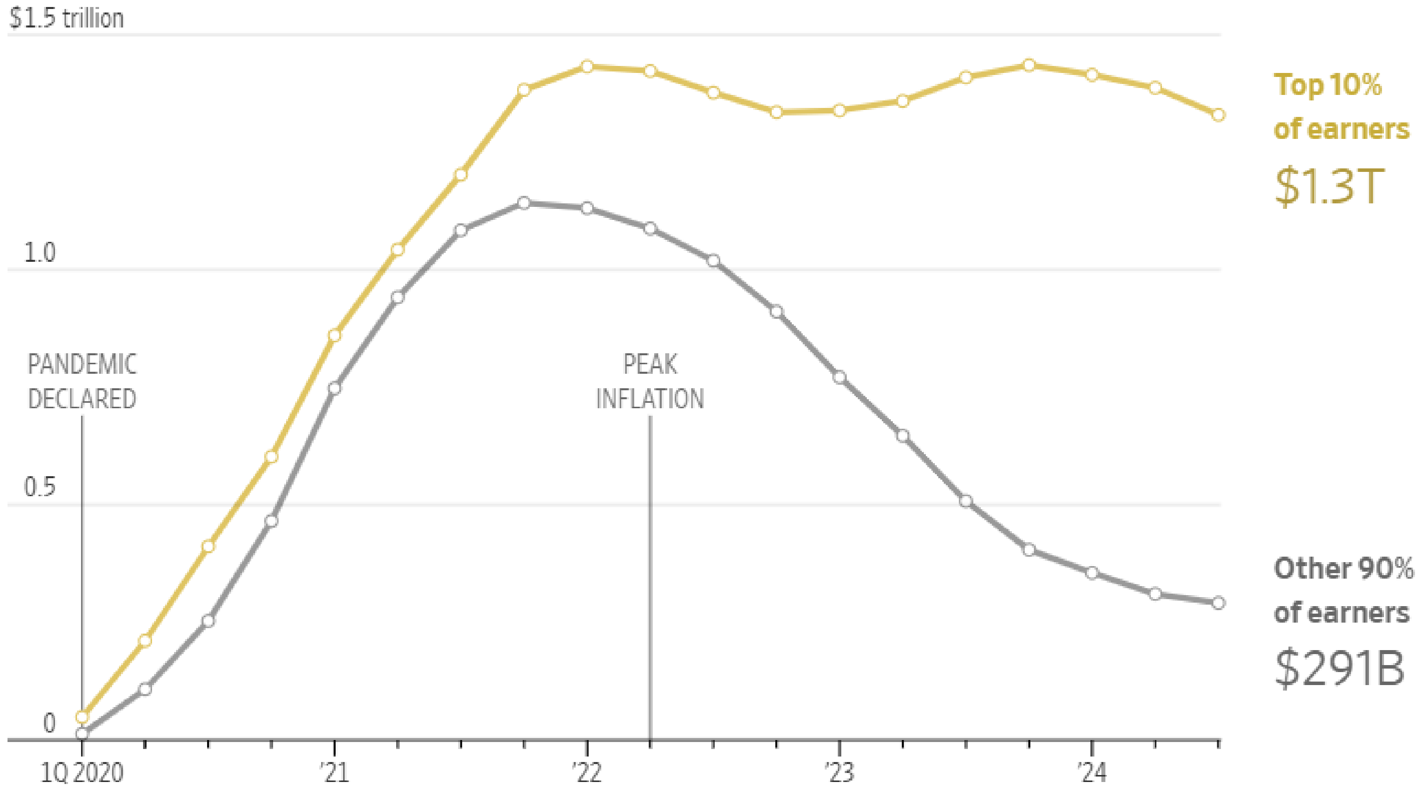


Following threats of tariffs, imports surged, which were subtracted from exports, causing a steep decline in net exports. Imports do not vaporize and are included in the investment or consumption component of GDP over time. Due to the extrapolative nature of the model, GDPNow assumes imports will keep rising all quarter, which is unlikely. As inventory and investment data reports enter the model, we expect the effect to be balanced out. While economic activity may slow due to tariffs and a projected reduction in government spending, we do not expect a meaningful contraction in GDP.

Most Consumers Begin to Save, Highest Cohort Driving Spending

We have discussed in previous months that savings rates are at cyclical lows, but a report from Moody's puts it into a more important context.

Cumulative excess savings, by income

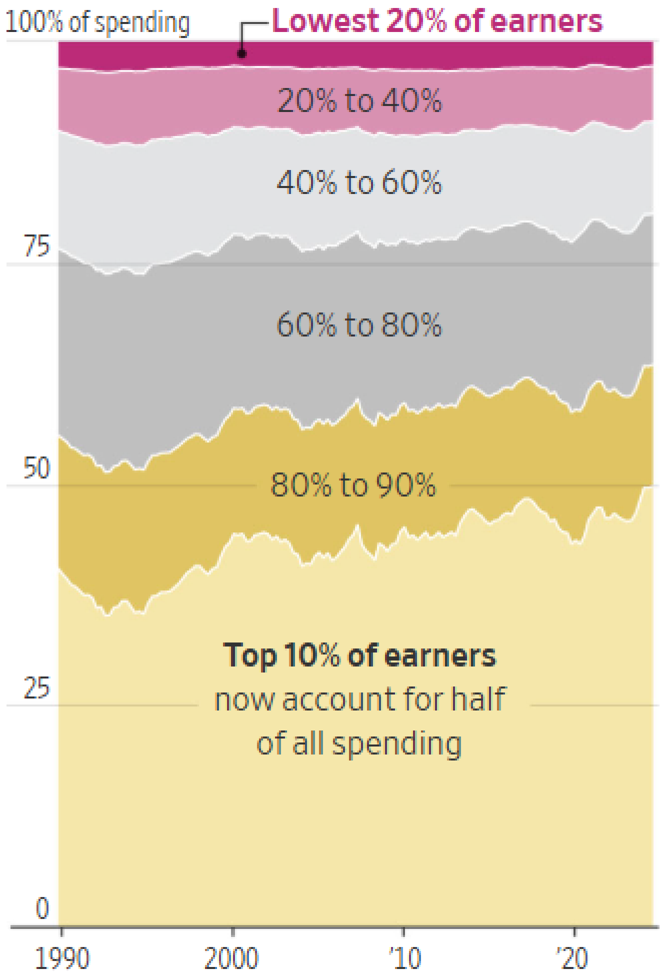


Note: Chart shows savings above the typical prepandemic saving rate.
Source: Moody's Analytics

While inflation may increase the cost of essentials for everyone, the top cohort of spenders are able to cut back in other areas to maintain savings.

The bottom 90% of earners have continued to draw down savings to maintain spending patterns. While the top 10% making up a significant portion of spending is now new, it has crossed 50% for the first time ever. In the 1990s, the top 10% represented 36% of spending.

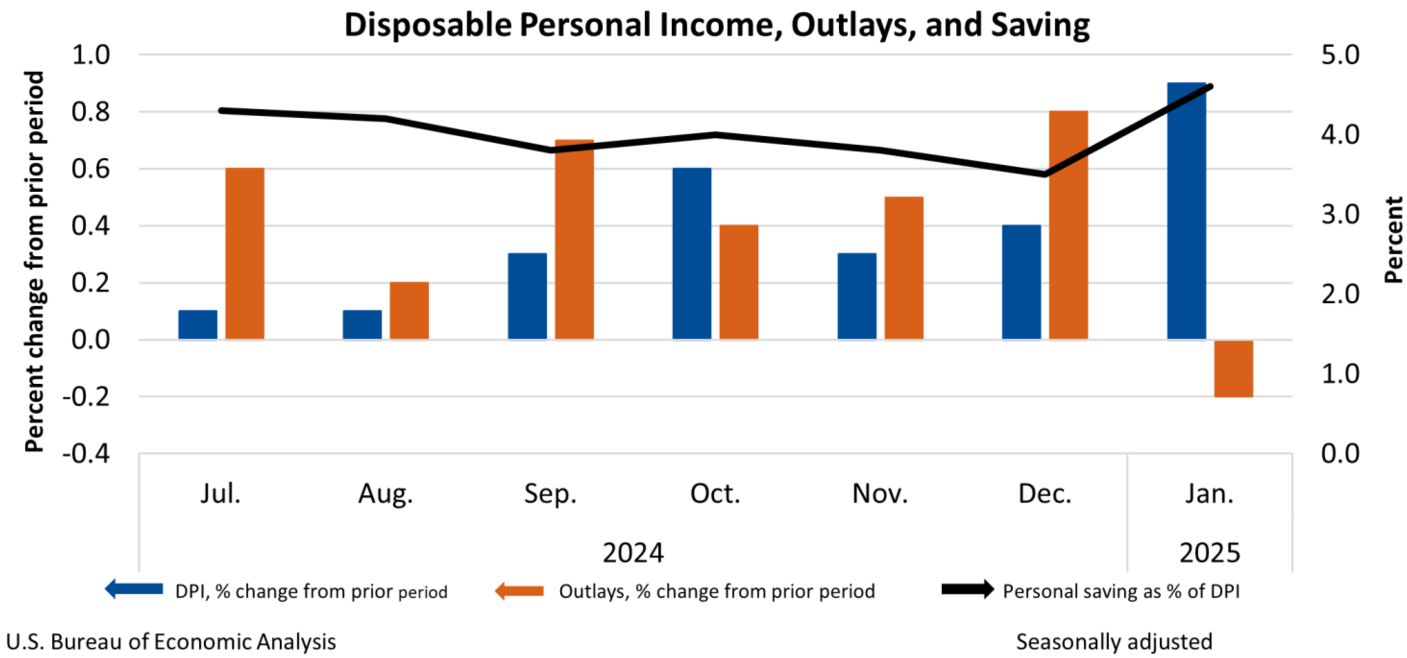
Share of spending, by income group



Source: Moody's Analytics

To put this into a markets context, the top 10% of consumers also own 87% of US equities, despite record high participation in equity markets across a wide range of income levels.

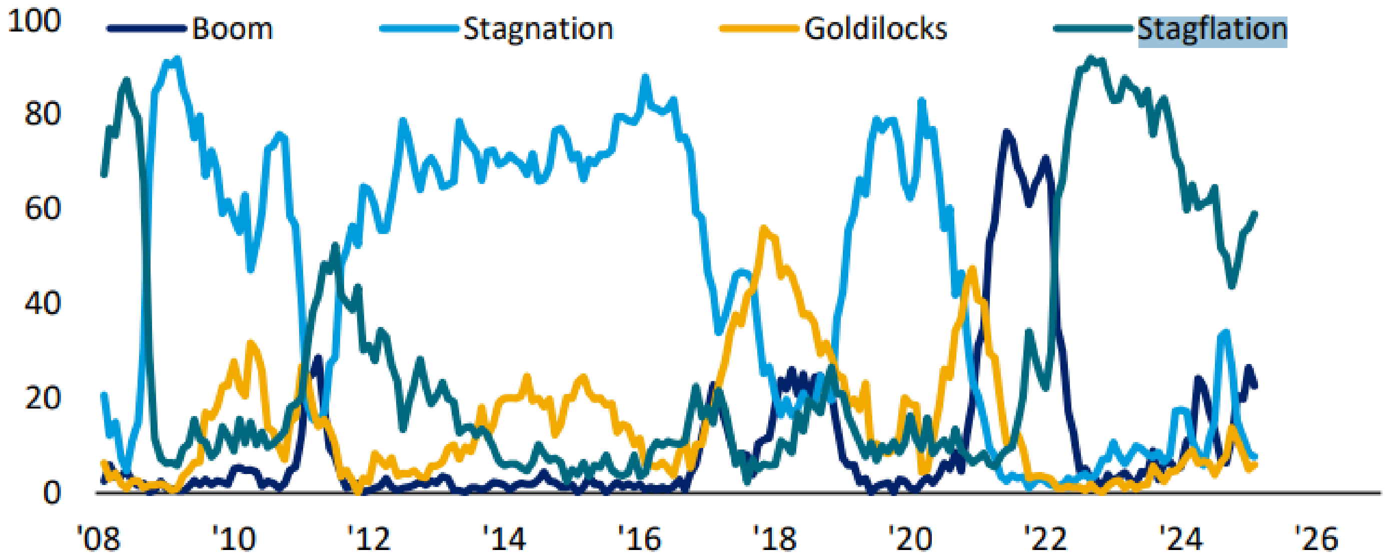
While 46% of US consumers felt optimistic about the economy when surveyed in January, there was an evident generational divide. Gen Z respondents reported an outsized drawdown of savings, with Gen X and Gen Z both reporting an intent to spend less on discretionary categories. The DPI print backs this up, with the first contraction in personal consumption since March 2023 and the highest savings rate since June 2024.


Disposable Personal Income, Outlays, and Saving
Percent change from prior period
Percent
1.0
0.8
0.6
0.4
0.2
0.0
-0.2
-0.4
5.0
4.0
3.0
2.0
1.0
0.0
Jul.
Aug.
Sep.
Oct.
Nov.
Dec.
Jan.
2024
2025
DPI, % change from prior period
Outlays, % change from prior period
Personal saving as % of DPI
U.S. Bureau of Economic Analysis
Seasonally adjusted

Fund Managers and Analysts Becoming Pessimistic

BofA's fund manager survey has indicated a return to fears of stagflation, which dominated sentiment during the bear market in 2022.

Chart 23: How FMS investors would describe the global economy over the next 12 months
FMS expectations for the global economy over the next 12 months?

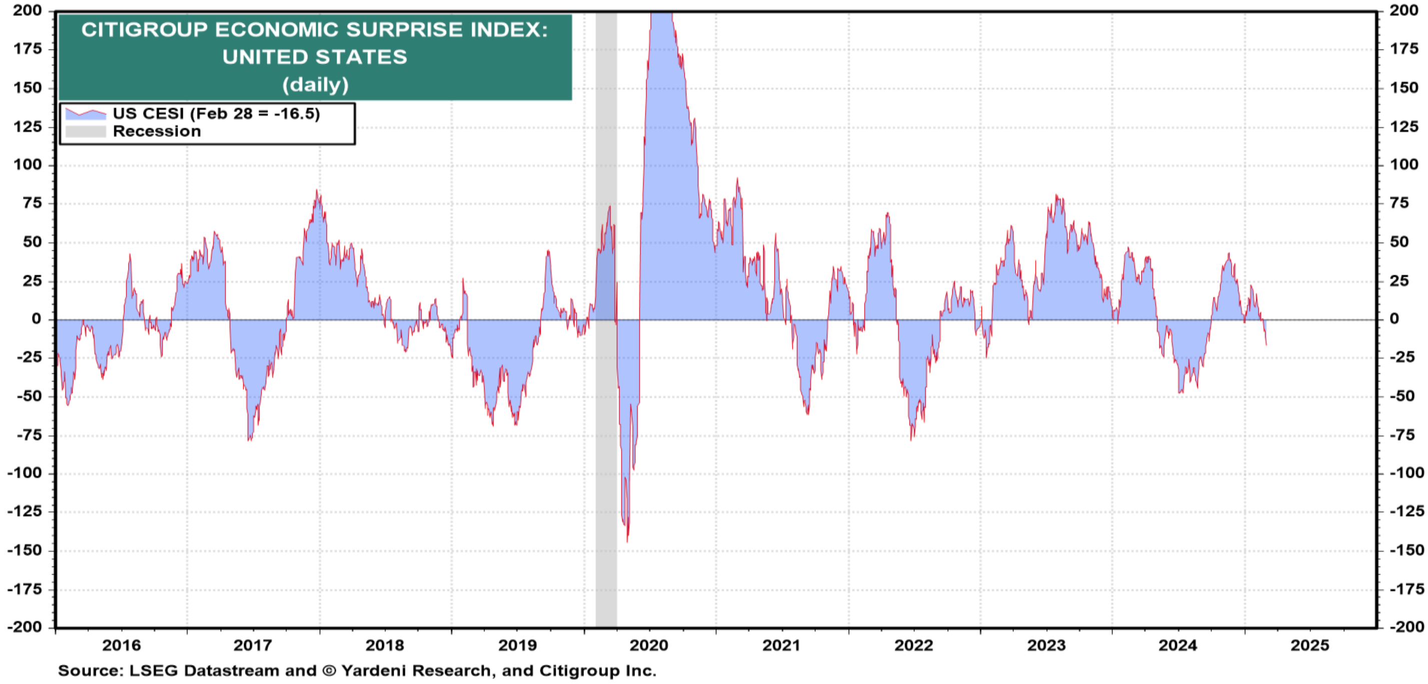


Source: BofA Global Fund Manager Survey.

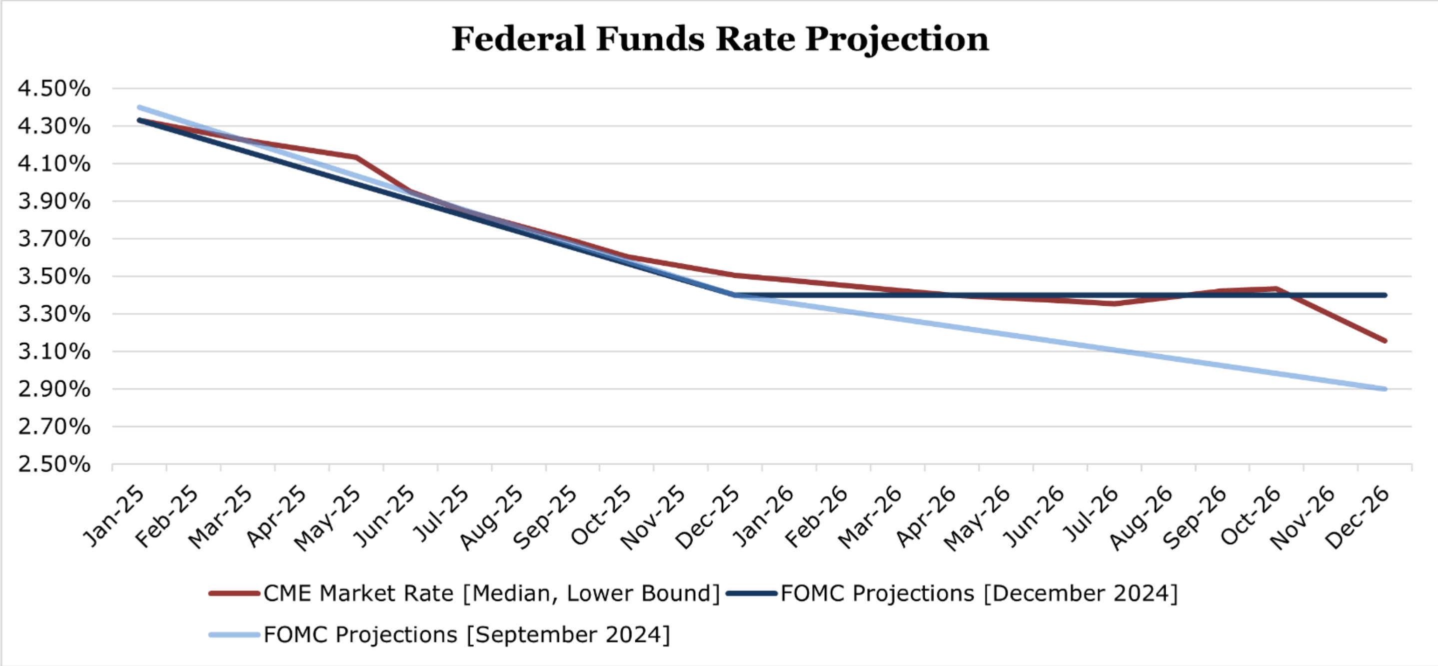
BofA GLOBAL RESEARCH

Despite economic surprise being largely negative during 2024, markets stayed resilient thanks to expectations of Fed cuts and the election pricing in a Trump win.

However, Citigroup's economic surprise index turned negative again in 2025 with renewed fears of inflation reaccelerating and tariffs putting pressure on US economic results. A print above 0 indicates that economic indicators point toward expansion above expectations, below 0 and it indicates conditions worsening faster than expected.



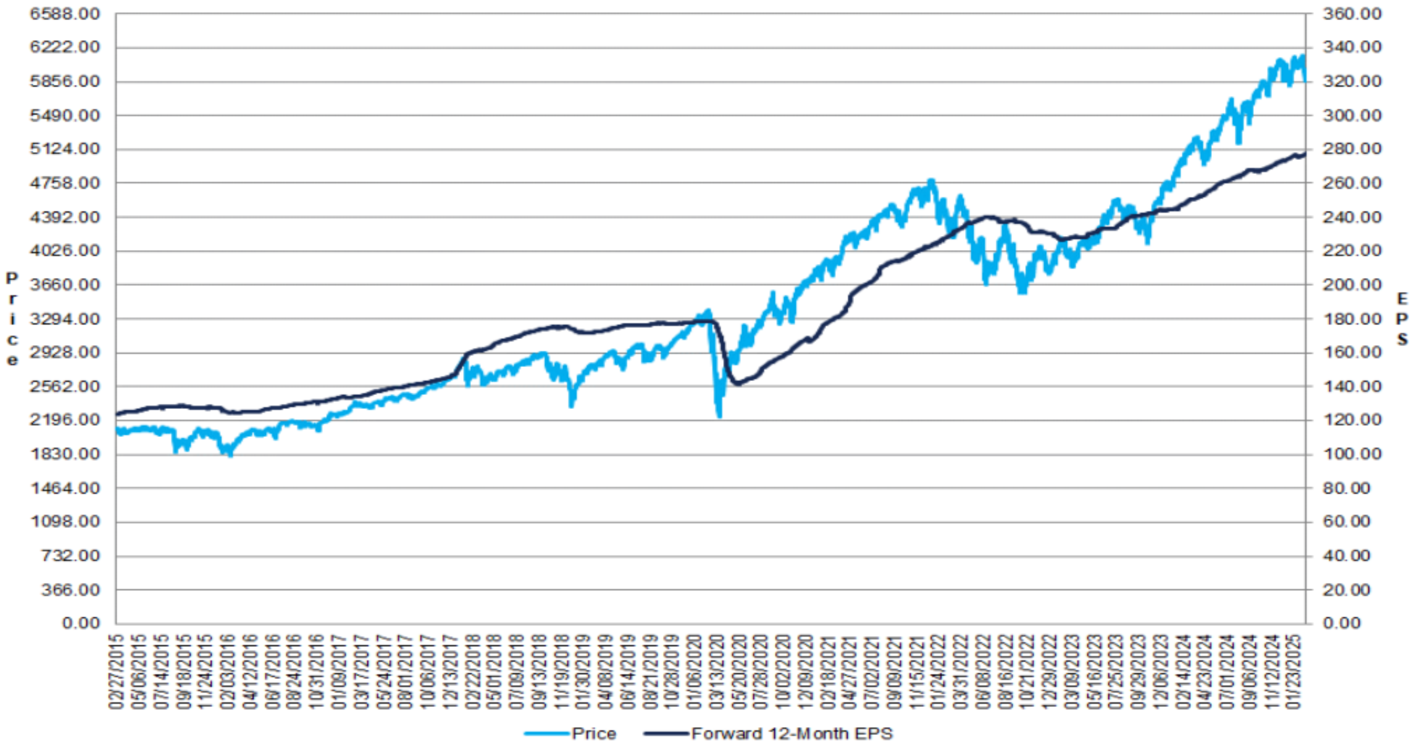
Market expectations of further Fed cuts remain uncertain, with most pricing in cuts resuming in June thanks to weaker than expected consumer spending. As of the latest FOMC projections in December, it expects to end 2025 at a median rate of 3.4%, below the market median of 3.5%.



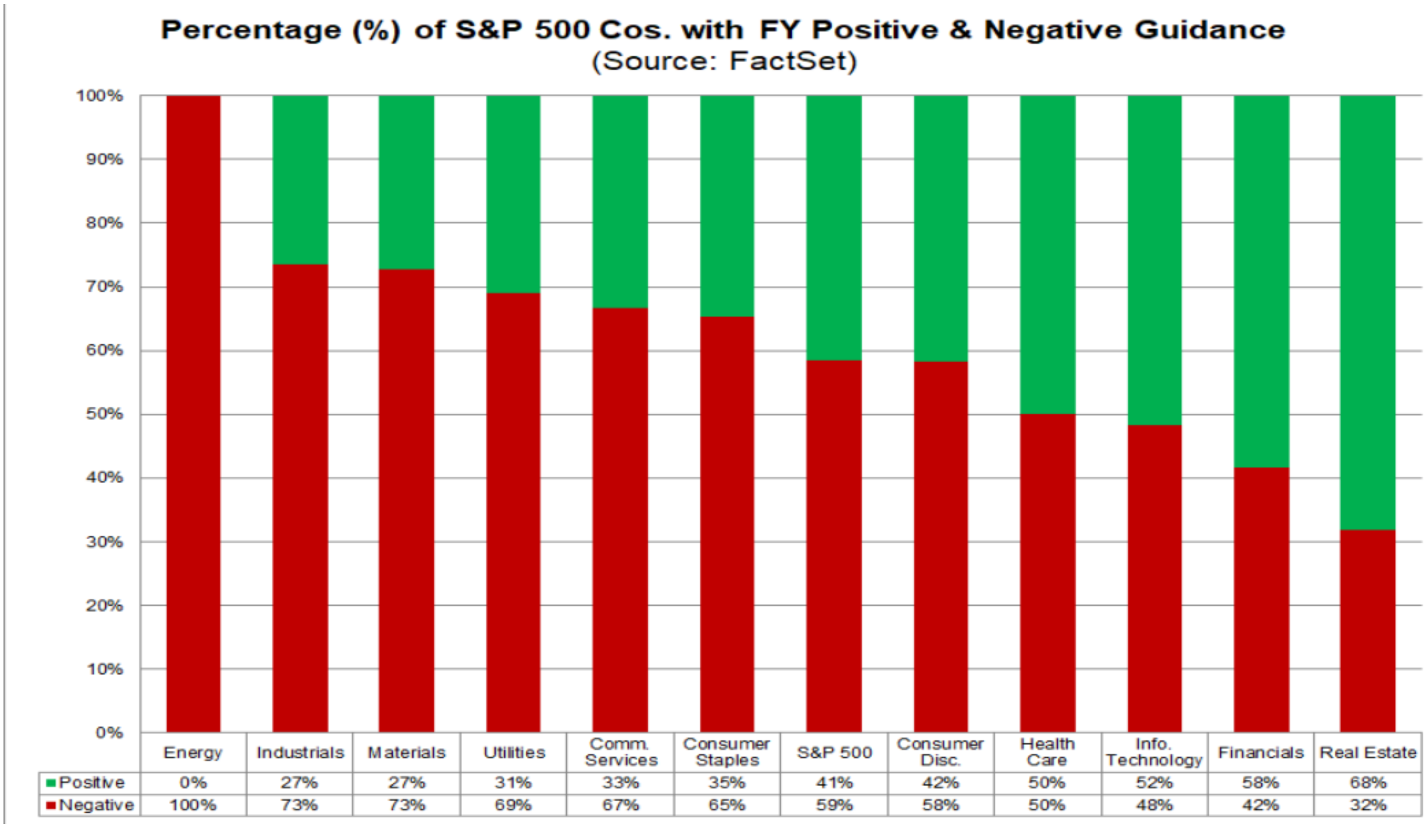
FOMC, CME

Equity markets corrected modestly during February. As shown below stock prices have grown far faster than earnings meaning valuations are stretched. According to FactSet, analysts have become more pessimistic recently with downward earnings revisions above the 20-year average – especially in the materials and consumer discretionary sectors.

S&P 500 Change in Forward 12-Month EPS vs. Change in Price: 10 Yrs.
(Source: FactSet)



Financials was the only sector that saw upward revisions in estimated earnings for 2025 from analysts. The financials sector had 58% of companies with positive guidance for 2025. Financials also lead the pack for the 4th quarter of 2024 results, with 85% of companies reported earnings above analyst estimates.



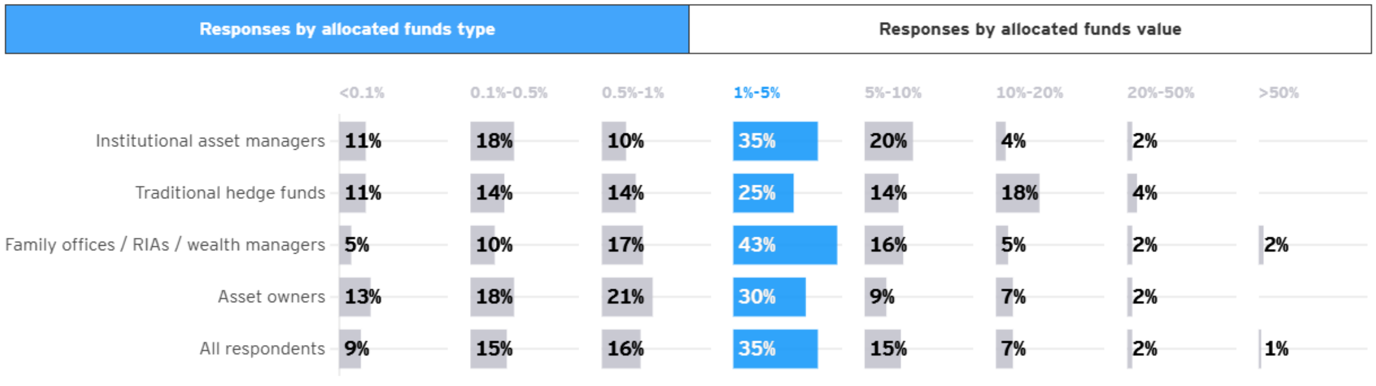
	Energy	Industrials	Materials	Utilities	Comm. Services	Consumer Staples	S&P 500	Consumer Disc.	Health Care	Info. Technology	Financials	Real Estate
Positive	0%	27%	27%	31%	33%	35%	41%	42%	50%	52%	58%	68%
Negative	100%	73%	73%	69%	67%	65%	59%	58%	50%	48%	42%	32%

FactSet

Crypto "Strategic Reserve" Draws More Interest in Alternatives

With equity markets beginning to slip, 4th quarter filings from investment managers showed a large interest in alternative assets including Gold and Crypto.

Q: What percentage of your funds have you allocated to cryptocurrencies, digital assets, or related crypto funds/products?[1]



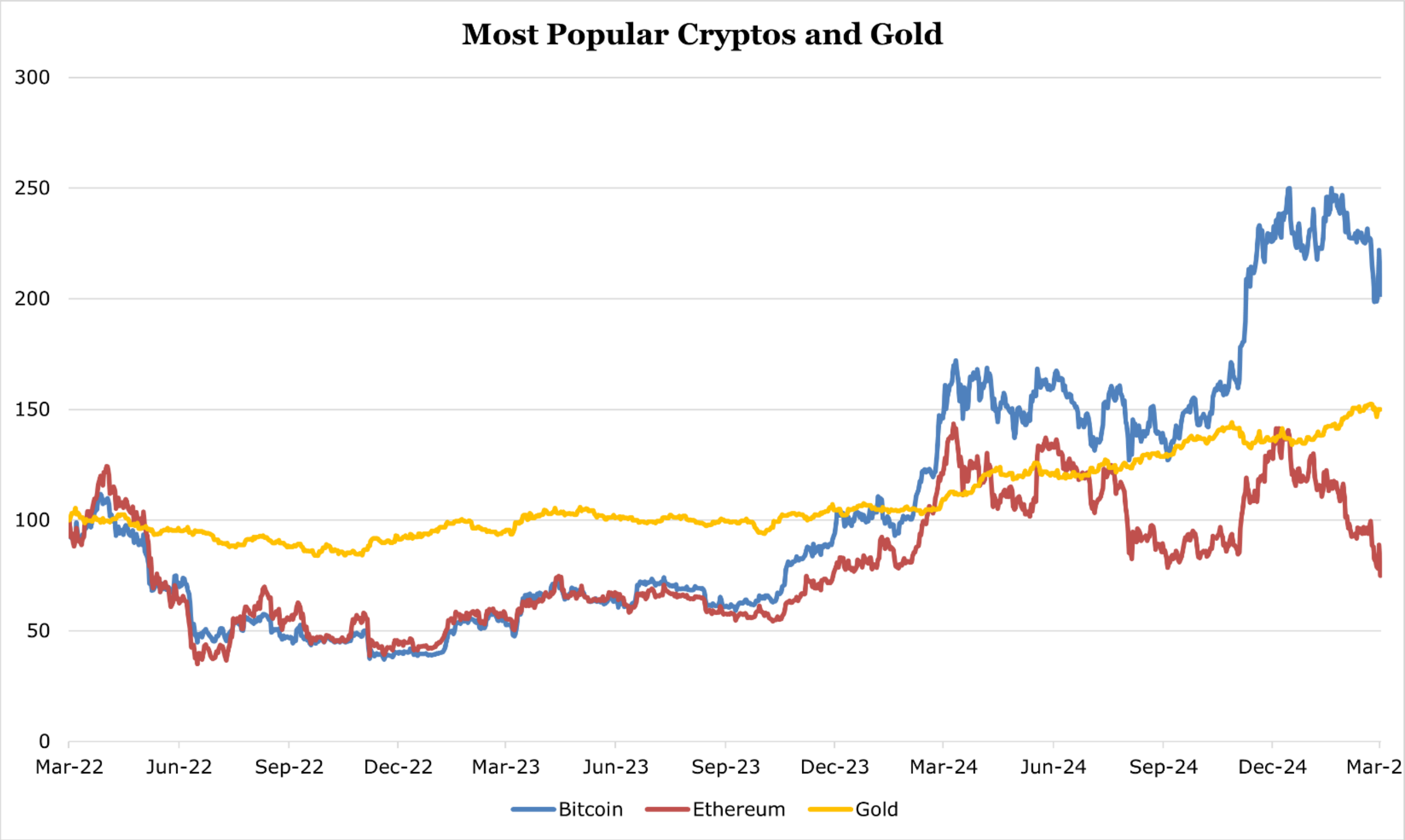
	<0.1%	0.1%-0.5%	0.5%-1%	1%-5%	5%-10%	10%-20%	20%-50%	>50%
Institutional asset managers	11%	18%	10%	35%	20%	4%	2%	
Traditional hedge funds	11%	14%	14%	25%	14%	18%	4%	
Family offices / RIAs / wealth managers	5%	10%	17%	43%	16%	5%	2%	2%
Asset owners	13%	18%	21%	30%	9%	7%	2%	
All respondents	9%	15%	16%	35%	15%	7%	2%	1%

Chart description

EY

The largest institutional holders of crypto remain hedge funds, though many others are beginning to gain exposure thanks to the rapid listing of crypto ETFs as we have discussed before. According to a survey conducted by EY, 76% indicating they have taken a <5% position in cryptocurrencies for their low-correlation nature with other assets. Additionally, 69% indicated they expect their firm to increase exposure over the next 3 years.

On the last day of February, the White House announced it would be hosting a "Crypto Summit" and creating a working group to study the idea of a crypto reserve, rallying crypto prices which had been slumping on limited rate-cut expectations.



Index, March 1 2022 = 100

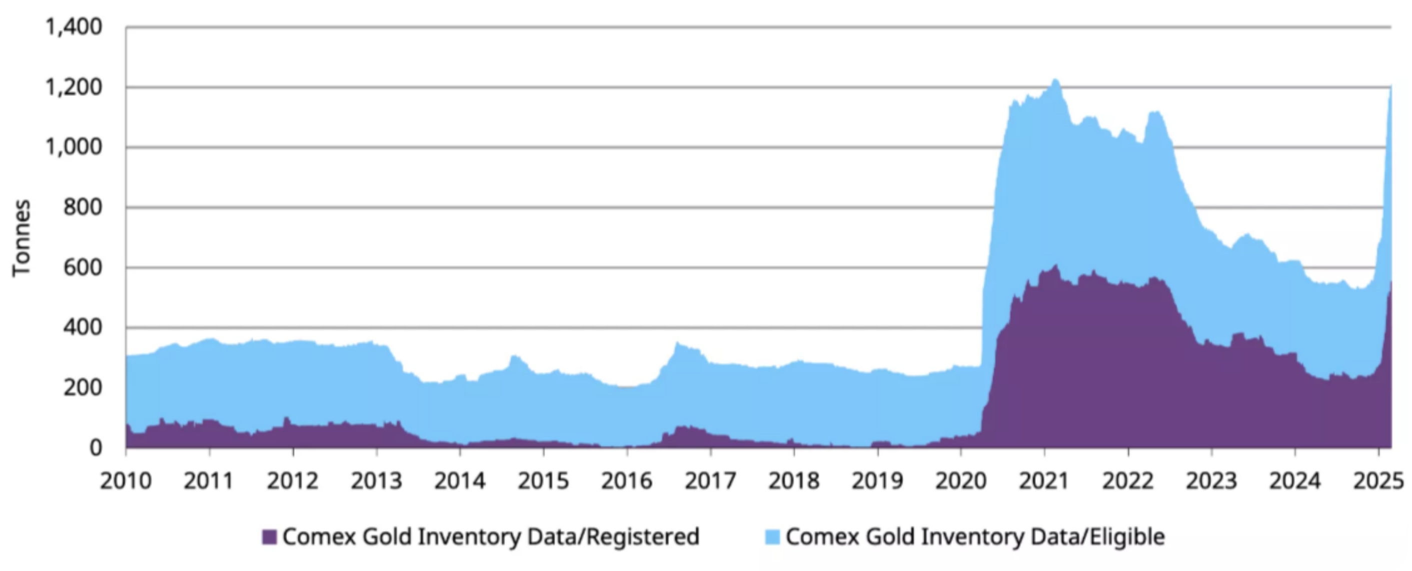
Supporters of the plan say it would allow the US an additional asset to store value independent of currency, like gold reserves. It would also allow the United States to dominate the still fledgling market, and exercise control over it. Detractors state that exposure to the crypto market adds cybersecurity risks to the government, as well as adding exposure to an asset that is historically very volatile and technically complicated.

Gold Spreads Reach 5 Year Highs

Gold has historically appreciated during times of economic uncertainty, as investors seek safe-haven assets. While the movement of gold between London's LMBA and New York City's COMEX is not unprecedented, the scale of the current shift is significantly larger than usual.

Chart 1: COMEX gold inventories reach COVID highs

Reported COMEX inventories for registered and eligible gold*

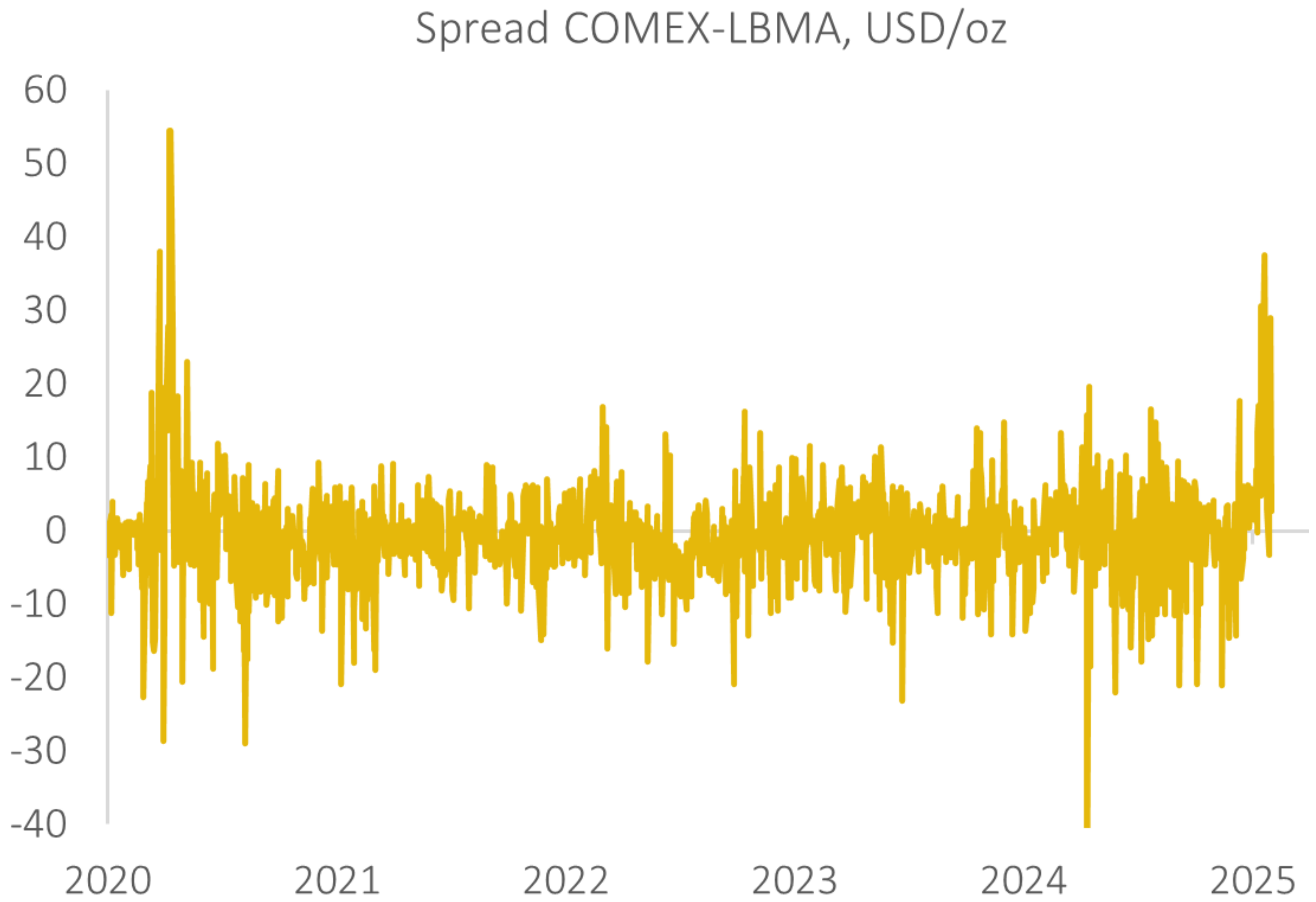


World Gold Council

Typically, investors seeking to go long on gold purchase futures contracts on US exchanges, with banks and financial institutions writing the contracts and taking temporary short positions. To hedge against the risk of these short positions, banks either hold physical gold -- often stored in London where storage costs are lower – or leasing gold from other banks. Under normal conditions, most futures contracts are settled with cash or rolled over at expiry.

However, concerns over tariffs and inflation have drastically altered the typical market dynamics. There has been a substantial reported increase in demand for physical settlement of gold futures contracts within the US. With banks and institutions scrambling to secure delivery within COMEX-approved vaults, the cost to lease gold for one-month has increased to 5.0% from its normal 0.08% level, indicating that there is not enough unpledged bullion (bullion that is not currently against an existing futures contract) to settle contracts, creating the circumstances for a squeeze.

This imbalance has further widened the price spread between gold traded in the US and spot gold in London, reaching its highest level since COVID-19 put pressure on global supply chains.



Source: COMEX, LBMA, LSEG, Redward Associates

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