



ASPECT PARTNERS
Advice to Wealth

Market Perspective

2025



2025 Market Perspective

We write our Market Perspectives after the turn of the year, which provides some benefit of hindsight and some delusion of foresight.

If we do have any insight, it is that markets are unpredictable with any short-term specificity. And over the long term, distinguishing *ex ante* between secular market trends, market cycles, and market noise is an exercise in creativity, imagination, and narration, making market outlooks sometimes fun to read but rarely prescient or actionable.

That doesn't stop us from humoring ourselves and penning our thoughts about the markets. But it is worth highlighting that we take our market predictions, along with all others, more as folly than prophecy. We therefore employ them only lightly, if at all, in our portfolio construction decisions.

In rereading our Market Perspectives from the past decade, what stands out are some consistent themes: positive performance, limited volatility and variability, and the supremacy of the US financial markets. Valuations of US equities have remained elevated, US interest rates have, by and large, remained low, facilitated by a strong dollar and an abundance of foreign capital.

2025, however, may mark the end of those secular trends. As of this writing, the US equity market has experienced significant volatility and gyrated wildly, while developed and emerging international markets have strengthened. Part of that performance disparity is the result of a weakening dollar, spurred by new and threatened US trade policies and geopolitical maneuvering. The current presidential administration, along with prevailing geopolitical forces, seem inclined to diminish US hegemony and dollar dominance. In our view, this may usher in a new global paradigm with long-range consequences for the US financial markets.

We will explore that theme in the pages that follow. As always, we appreciate your interest in our thoughts, and most importantly, the trust and confidence you place in us.

Sincerely,



Bard Malovany, CFP®
Principal
Aspect Partners



Setting the Table

Much like the decade preceding, 2024 continued the post-Great Financial Crisis paradigm: easy credit, muted volatility, a benign economic backdrop, and a resurgent appetite for risk-taking. These factors sustained relatively tranquil financial markets and rising asset prices.

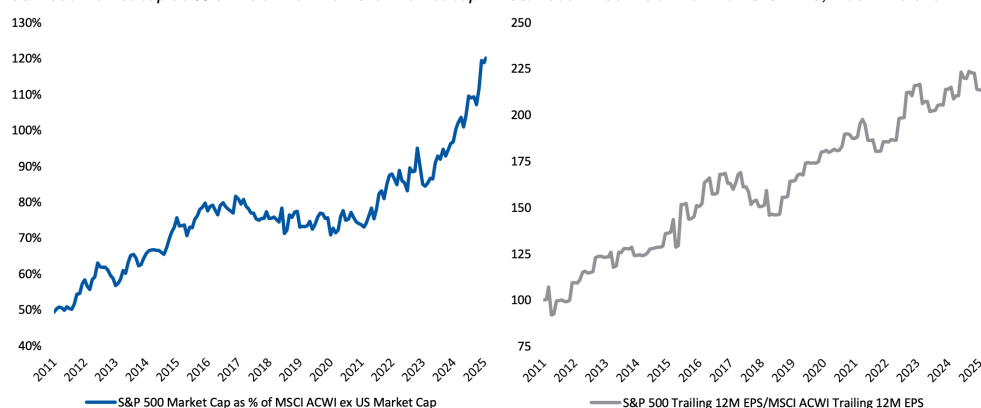
Real US GDP increased by 2.8% in 2024, with inflation cooling slightly from 3.1% to 2.9%. That trend encouraged the Federal Reserve to cut interest rates three times, totaling 100 basis points. Bond markets responded positively. The yield curve, which began the year inverted, ended the year significantly flatter, signaling optimism about the economic outlook.

This dynamic was not unique to the US. Europe and Japan saw real GDP growth of 0.8% and 0.1%, respectively, while China signaled a shift toward policy normalization with “moderately loose” monetary policy and “proactive” fiscal guidance.

Global equities gained 16.9% in 2024, led by the US and China, which returned 23.9% and 19.7%, respectively. This marked the second consecutive year of 20%+ gains for the S&P 500—something not seen since 1999. The AI-driven performance of the so-called “Magnificent 7” tech stocks was a major driver. Those seven stocks now account for roughly one-third of the total market capitalization of the S&P 500, trading at an average price-to-earnings ratio of 26.8.

The dominance of the US financial markets has been driven by a variety of factors. Earnings growth has supported the US’s growing percentage of the global stock market capitalization.

U.S. Equities Have Increased Share of Global Market Cap... ...Since That is Where All the Earnings Growth Has Been
S&P 500 market cap as % of MSCI ACWI ex-U.S. market cap S&P 500 EPS / MSCI ACWI ex-U.S. EPS, Index = 1/1/2011



Source: Bloomberg, MSIM. As of January 21, 2025. The views and opinions expressed are those of the Portfolio Solutions Group at the time of writing of this presentation and are subject to change at any time due to market, economic, or other conditions, and may not necessarily come to pass. **Past performance is no guarantee of future results.**

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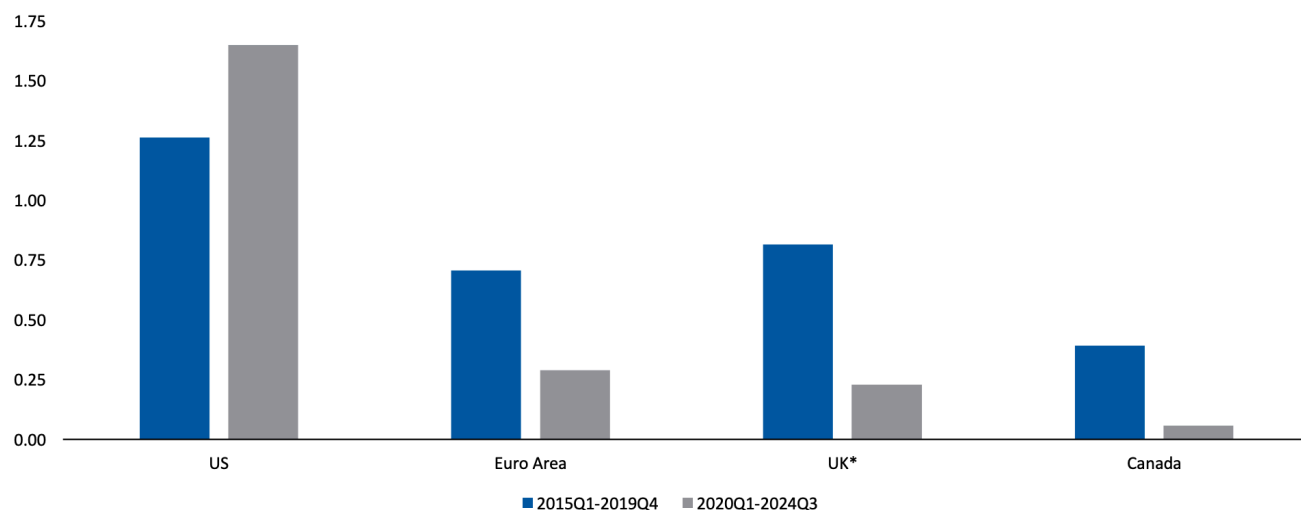
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Additionally, US labor productivity growth has expanded over the past decade and fallen elsewhere.

U.S. Labor Productivity Growth Has Widened its Outperformance Relative to ex-U.S. in the Aftermath of the Pandemic
Annualized labor productivity growth (%)



*Note: Labor productivity is defined as total-economy real value-added per hour worked. *UK 2024Q3 productivity represents a GS forecast*

Source: Goldman Sachs Investment Research, ISG, MSIM. As of September 30, 2024. The views and opinions expressed are those of the Portfolio Solutions Group at the time of writing/of this presentation and are subject to change at any time due to market, economic, or other conditions, and may not necessarily come to pass. Forecasts/estimates are based on current market conditions, subject to change, and may not necessarily come to pass. **Past performance is no guarantee of future results.**

While part of the expansion of US equity capitalization as a percentage of the overall global equity markets has been driven by these and other underlying fundamentals, another part has been simply an expansion of stock valuations relative to those fundamentals, meaning that part of the growth in stock prices has been driven not by business performance but by investor psychology, or said differently, by increased demand for US stocks.





The Secular Shift: End of an Era?

“The difficulty lies not so much in developing new ideas as in escaping from old ones.”

– JOHN MAYNARD KEYNES

For more than a decade, the supremacy of US financial markets has been sustained by:

1. A strong dollar,
2. Substantial capital inflows, often consistent with the structural US trade deficit,
3. A global appetite for risk and US asset exposure.

But 2025 may represent an inflection point. That trifecta shows signs of fatigue:

- The US dollar has depreciated over the past 18 months.
- Foreign sovereigns are divesting US Treasuries at an accelerating rate.
- Leadership instability and erosion in the rule of law have reduced the US's reputation as a safe haven.

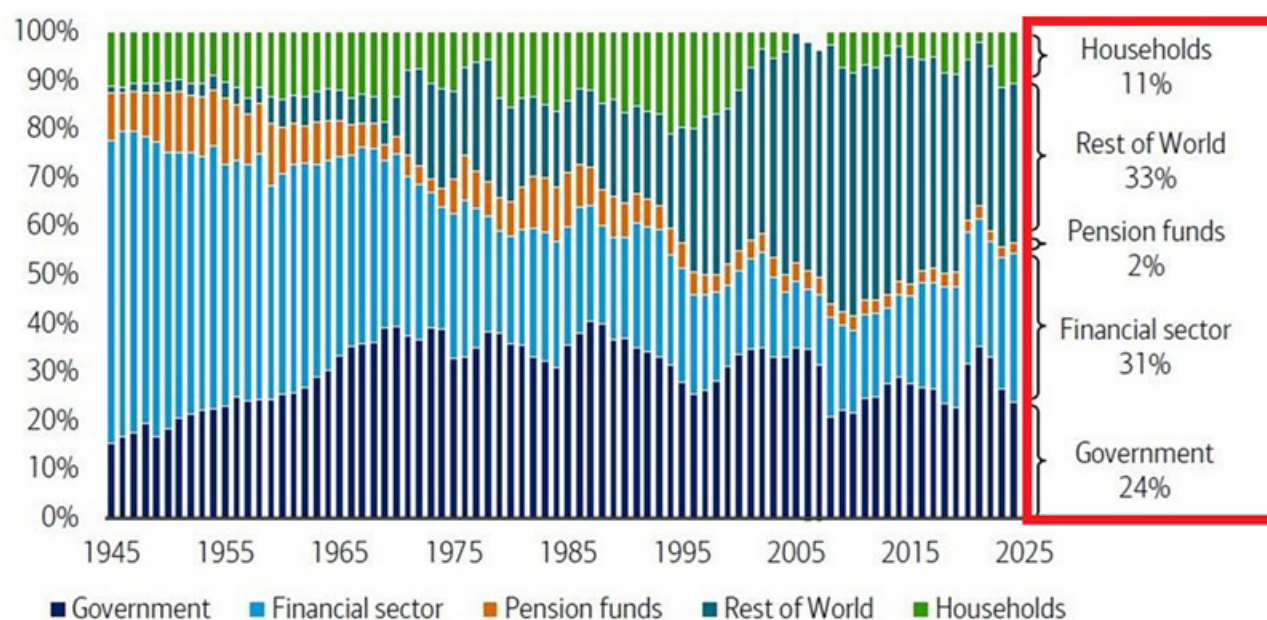
The implication? A reduced supply of capital to the US. That shift means an increasing cost of capital for US businesses, reduced investment, and downward pressure on productivity and growth.

As fewer dollars flow into US markets (meaning reduced supply), the cost of those dollars increases, meaning the US Treasury and US corporations will need to offer higher interest rates to attract investment. As interest rates increase, companies invest less and their profit margins shrink. As investment in capital goods, plant, and equipment wanes, growth slows, both because there is less demand for those capital goods, and because companies, investing less, grow less.





Chart 2: Foreigners own 33% of US Treasury market
US Treasury ownership since 1945



Source: BofA Global Investment Strategy, Flow of Funds, Haver

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BofA GLOBAL RESEARCH



Domestic Headwinds: Demographics and Human Capital

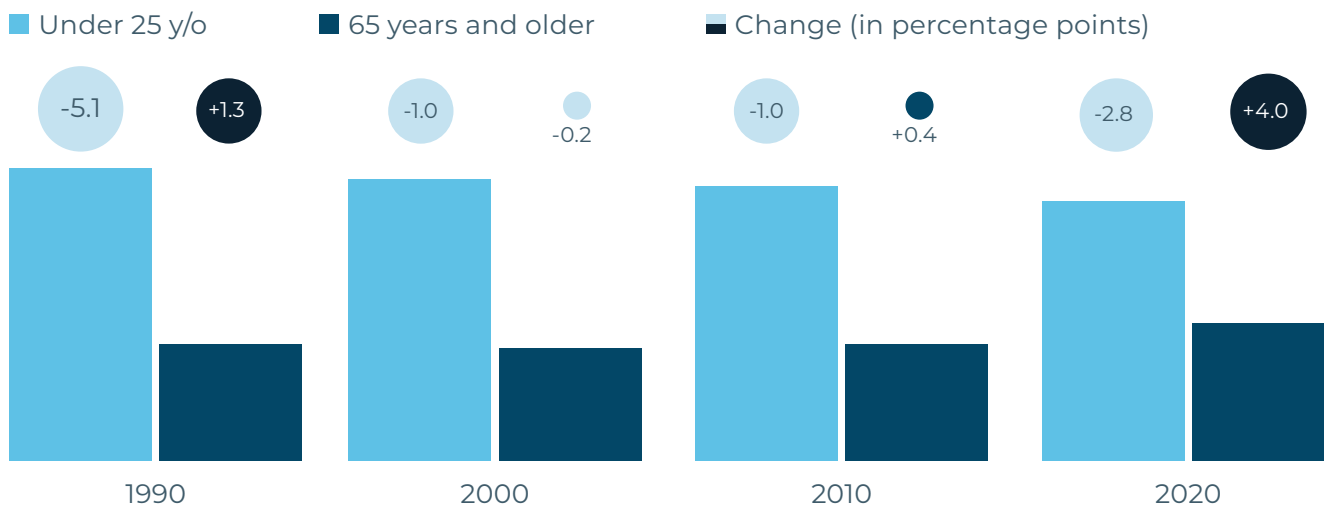
Compounding the external pressures are significant domestic challenges that will likely constrain US economic growth in the years ahead.

Shifting demographics, including an aging population and declining birth rates, are reducing the growth rate of the labor force. Simultaneously, policies aimed at restricting immigration will further exacerbate this trend, limiting the supply of available workers. This scarcity of labor will likely lead to higher labor costs, potentially squeezing corporate profit margins and contributing to inflationary pressures.

Furthermore, an increasingly adversarial atmosphere surrounding higher education and a potential decline in international students could negatively impact the long-term productivity and innovation capacity of the US workforce. A reduction in the quality and quantity of human capital could further stymie economic growth potential.

Demographic Change Accelerates in the U.S.

Share of selected age groups in total U.S. population (1990–2020)



Source: U.S. Census Bureau

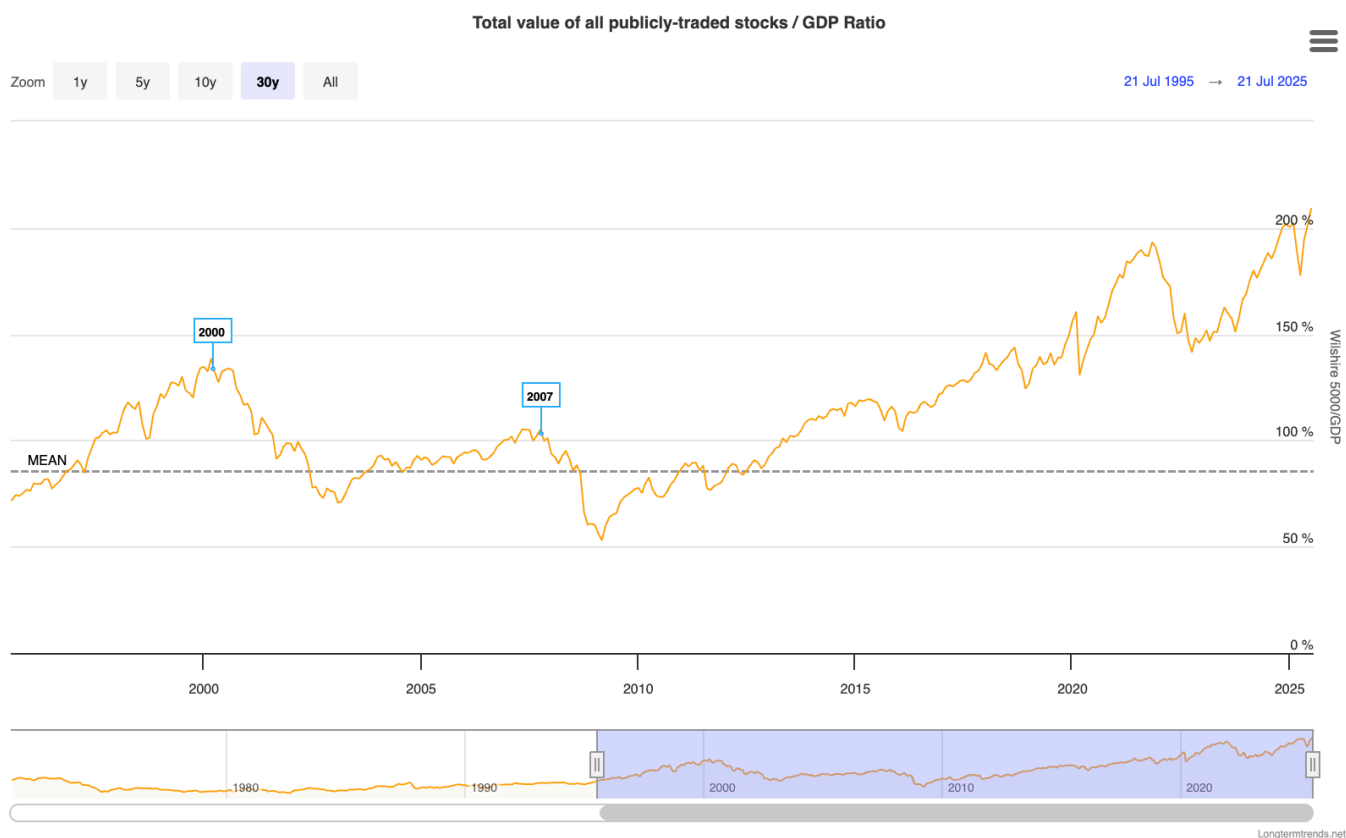
Shifts in technology will offset some of that effect, making technology – and people – more efficient. Reduced public expenditure in the development of US intellectual capital, however, will likely curtail that countervailing pressure.



Valuation Matters

Valuation disparities between the US and the rest of the world have reached historic extremes. US stocks are more expensive than their global peers by nearly every measure. The Shiller PE ratio, Buffett Yardstick, and earnings yield all suggest below-average prospective returns for US large company stocks.

Relative to the size of the economy, the US stock market is exceptionally expensive.



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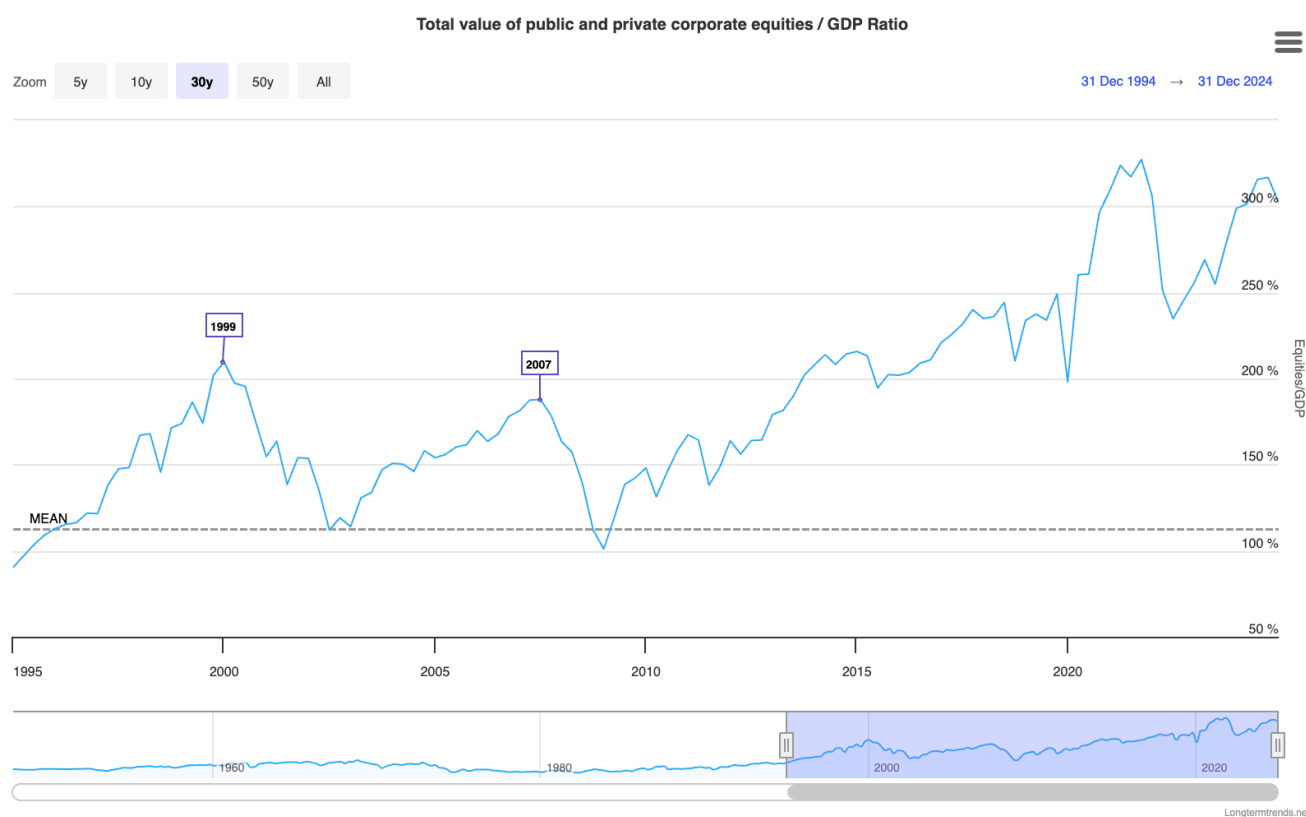
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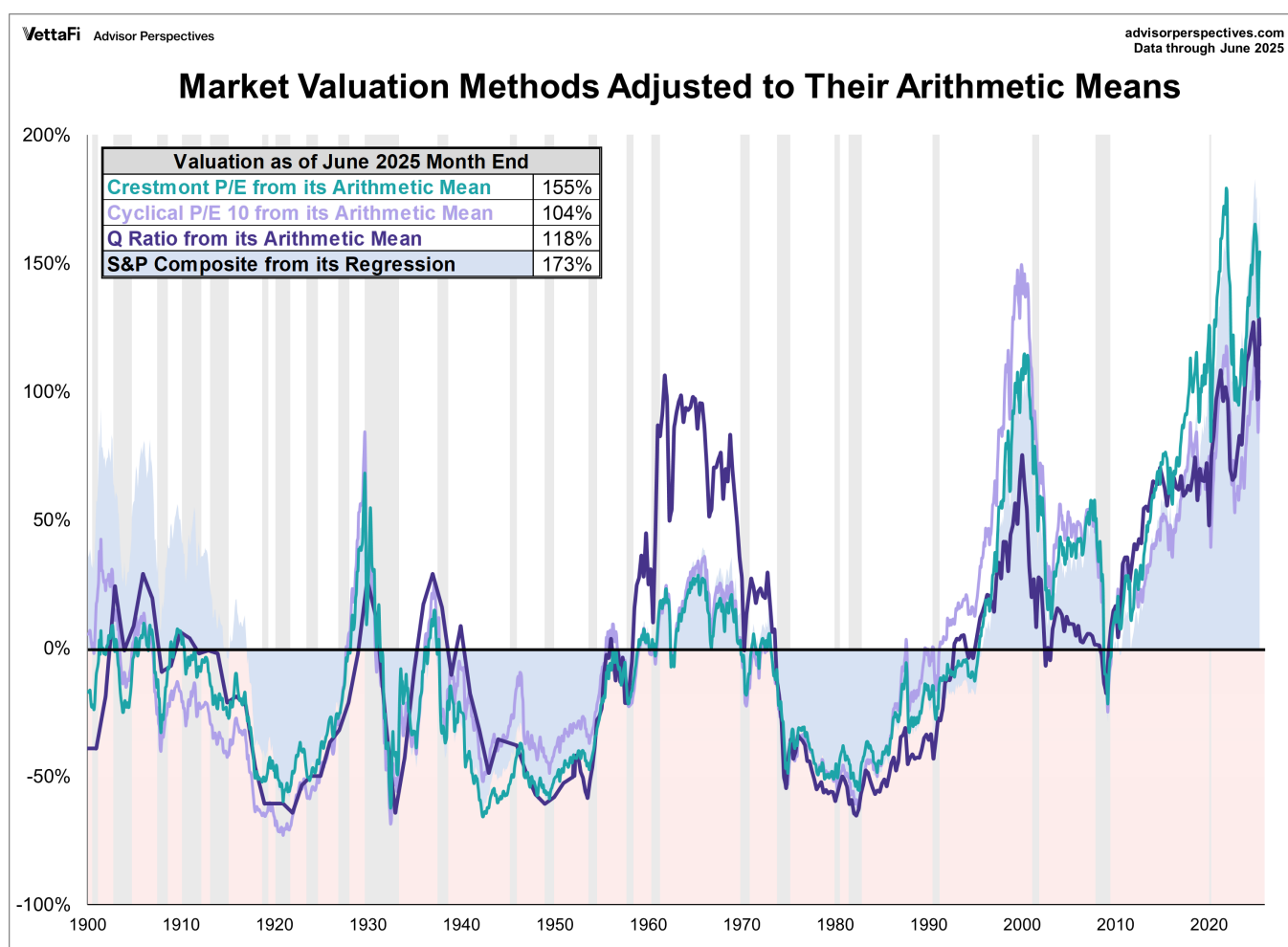


One might reasonably make the argument that there are fewer publicly traded companies today than 10 years ago, given the expansion of “private equity.” But the same underlying dynamic holds true when you include public and privately held companies.





It hardly matters what valuation metric you consider.



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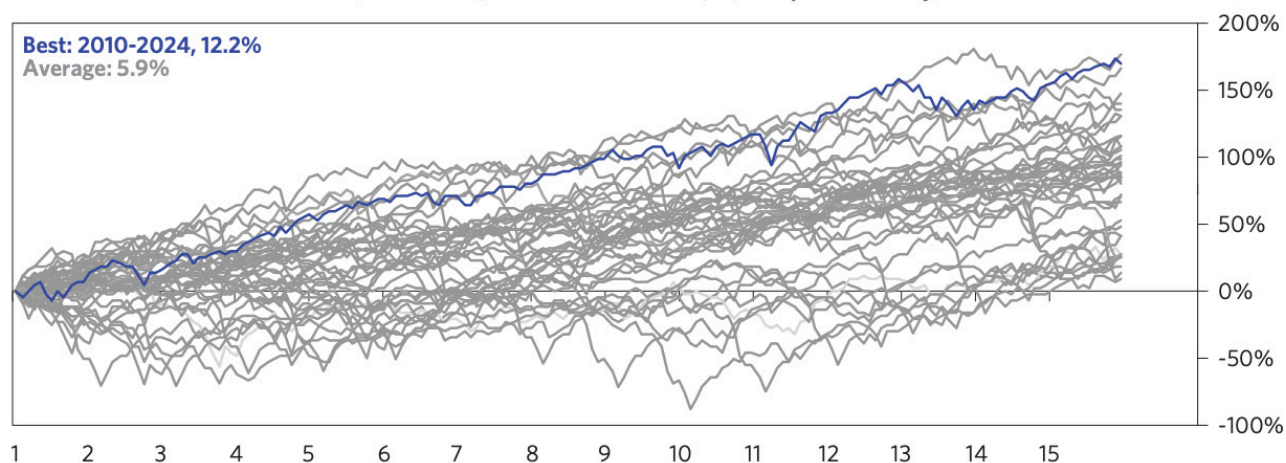
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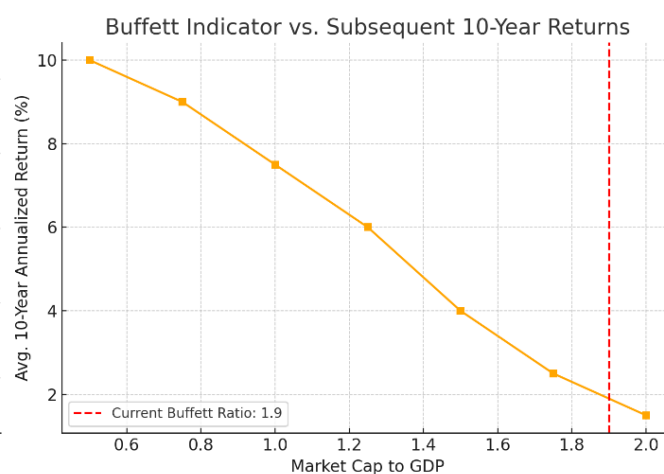
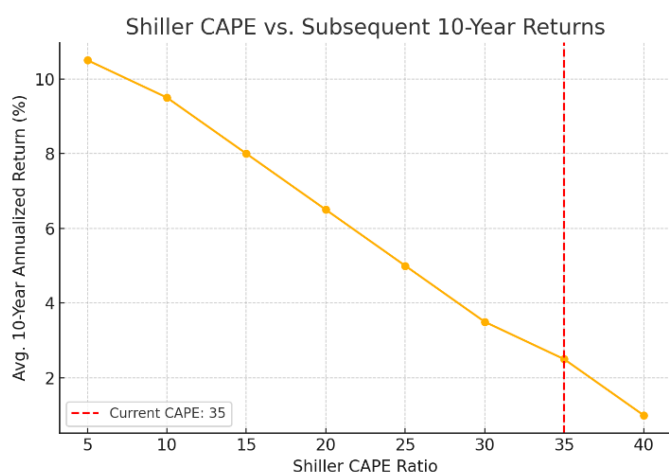
That confluence of factors has led to exceptional US stock market performance; so great, in fact, that US stocks have posted their strongest 15-year stretch dating back to 1970.

**US Equity Performance over Every 15-Year Period Since 1970
(Cumulative, Returns Above Cash, In, Sampled Annually)**





Historical precedent, however, indicates that periods of high valuation tend to be followed by a decade of lower returns.



The elevated valuations, coupled with the headwinds discussed above – a weakening dollar, reduced capital inflows, rising cost of capital, and slower economic growth – suggest that prospective returns for US equities are likely to be significantly below their historical averages. The concentration of market capitalization in a few high-growth technology companies also presents a potential risk, as any shift in investor sentiment or regulatory scrutiny could have an outsized impact on overall market performance.

In contrast, developed and emerging international markets, which have lagged the US in recent years and often trade at more attractive valuations, may offer relatively more compelling long-term investment opportunities in this evolving global landscape.





Conclusion: Navigating a New Era

The secular trends that have defined the US financial markets since the Great Financial Crisis appear to be at an inflection point. The waning dominance of the US dollar, diminishing capital inflows, a potentially reduced appetite for risk, and significant domestic challenges related to demographics and human capital all point towards a more challenging environment for US asset returns in the coming years.

While the precise timing and magnitude of these shifts are uncertain, we feel it prudent to acknowledge the evolving dynamics. A more globally diversified investment approach, with a focus on value and long-term fundamentals, we think may be warranted in this new era of global finance.

In short, the conditions seem ripe for a shift in financial market dynamics. That does not necessarily mean a sudden shift in market performance; it suggests an inflection in longer-term trends.

But, as underscored earlier, the markets don't necessarily follow our predictions. We may be entirely correct in our views. We may be only partially correct. And we may be entirely incorrect, regardless of how strong our case might seem. And even if we are correct in our macro views, the markets will not necessarily respond 'rationally', or in the timeframe we expect.

Portfolio Implications

As a result, we continue to structure portfolios across three primary frameworks: Indexed, Traditional, and Strategic Allocations.

Our **Indexed Portfolios** are structured around the hypothesis that markets are informationally efficient, and that our predictions, like anyone's, regardless of how sound the reasoning, are likely faulty. Therefore, the most efficient investment allocation is the current investment allocation, meaning we are best served by trying to simply mirror the financial markets. We do so by recreating annually the 'global market portfolio,' which is a true index of the financial markets representing how the average dollar is invested across the investable universe.

Our **Traditional Portfolios** utilize the underlying allocations of our Indexed Portfolios, but slightly overweight US equities, not to reflect our expectations of performance, but to reflect what the average US investor expects to see in a portfolio. In addition, we employ active security selection in segments of the market where we feel it is most likely to add value: generally, some domestic bonds, emerging market bonds, high yield bonds, and emerging market equities.

The third category is where our market views most directly influence allocations.





In our **Strategic Portfolios**, we:

- **Reduce US large-cap exposure.** We do so modestly, by slightly reducing the allocation to large company, domestic stocks relative to the Global Market Portfolio. In addition, we slightly overweight 'quality' and 'value' factors: stocks that are inexpensive relative to certain accounting metrics, like cash flow or dividend growth.
- **Increasing allocation to international equities** relative to the Global Market Portfolio. Here we also have a greater focus on active security selection, primarily in the market for small company stocks in developed economies and in stocks in emerging markets.
- **Increasing diversification through liquid alternative investments**, including real assets and managed futures. Exposure to assets with low to negative correlations to the equity and fixed income markets provides the opportunity for those assets to appreciate when the core of the portfolio may be struggling.
- Given the current structure of the fixed income markets, **we may hold higher cash reserves** in certain portfolios to buffer against volatility and preserve optionality.

We are not abandoning US markets; we are simply tempering our expectations. Our goal is not to time markets, but to craft durable portfolios that can thrive across investment regimes.

In Closing

The following winds of the last 15 years—cheap capital, abundant labor, and relentless optimism—may be abating. While a full portfolio resetting would be imprudent, we are trying to better understand the prevailing forces and lightly adjust course. And, of course, we continue to monitor the weather.

We welcome your input, your questions and your continued partnership.





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