WEALTH MANAGEMENT 360
FARMERS TRUST COMPANY

MARKET UPDATE & OUTLOOK
FOR FIRST QUARTER 2025

COMPANY PROFILE

Farmers Trust Company is licensed by the Ohio Division of Financial Institutions as a bank, authorized to conduct trust business and exercise full fiduciary powers. Our efforts are focused on the administration and management of trust assets. As an independent trust company, Farmers Trust Company offers several investment management options.

We are committed to providing the highest level of service in the areas of investment management, estate settlement, living trusts, testamentary trusts, charitable trusts, charitable endowments and employee benefit plans. Tax and estate planning services are available to our clients as well.

Farmers Trust Company has the unique ability to integrate investment, trust and estate management at a local level. Our clients appreciate the fact that their financial affairs are handled personally and confidentially. They also value our ability to work closely with their attorneys, accountants and insurance professionals to achieve a comprehensive financial strategy.

MARKET RECAP

The fourth quarter of 2024 was the most challenging one of the year for the markets. While the S&P 500 Index was able to register a positive return, equity market performance was mixed across categories and geographies. Increased levels of enthusiasm surrounding the results of the November Presidential election in the U.S. faded in the month of December as the economic reality set in. With that said, last year was another good year for the markets. The S&P 500 finished the year up roughly 25%, recording the first set of back-to-back gains of over 20% since '95-'96 and only the second one going back to 1932.

The S&P 500 Index returned 2.4% in the fourth quarter, but was down as much during the month of December. Growth stocks outperformed value stocks in the quarter, with the S&P 500 Growth Index up 6.8%, beating the S&P 500 Value by almost 9%. Small capitalization stocks, as represented by the Russell 2000 Index, ended the quarter up 0.3%, giving up all of their initial post-election gains in the month of December and finishing the month down 8.3%. Consumer Discretionary was the best performing sector in the quarter, up 14.3%, finishing the year up 30.1%. Communication Services (8.9%), Financials (7.1%), and Information Technology (4.8%) were the other sectors with positive performance in the quarter. Materials (-12.4%) and Healthcare (-10.3%) were the worst performers of the quarter. In terms of the full-year performance, Communication Services (40.2%) and Information Technology (36.6%) sectors were the leaders, with Materials (0%), Healthcare (2.6%), Real Estate (5.2%) and Energy (5.7%) being the most notable laggards.

International equities faced a headwind in the quarter in the form of the resurgent U.S. Dollar. The MSCI EAFE Index of developed markets was down 8.1% in the quarter, which was just slightly worse than the MSCI Emerging Markets Index's 7.9% decline. The Eurozone STOXX 50 Index was down 8.8% and Japan's Nikkei was down 4.1% in the quarter. In terms of the full year, international markets delivered double-digit returns in local-currency terms but gave up 7% on the currency exchange side, as the U.S. Dollar represented a headwind.

Commodity performance in the quarter was mixed, with Energy holding up better than Metals and Agriculture. The GSCI Commodity Index was up 3.3% in the quarter and up 9.3% for the year. Despite all of the political and economic uncertainty, oil prices were flat on the year per the WTI Crude Oil Futures index. Gold had another strong year, up 27.5%, finishing up with the title of the best-performing major asset class over the last three years.

With the exception of Short-term Treasuries and High Yield Corporates, bond market returns in the fourth quarter were negative across the board. The Bloomberg Global Aggregate Bond Index was down 5.1% in the quarter, with Treasuries and Investment Grade Corporates down equally (3%) while High Yield Corporates finished up 0.2%. The US Aggregate Bond Index finished the year up 1.3%.

MARKET RECAP & OUTLOOK FIRST QUARTER 2025

MARKET SCORECARD as of 12/30/2024	TOTAL RETURN IN USD	
	Q4	2024 TR
DOW JONES IND AVG	0.9%	15.0%
S&P 500	2.4%	25.0%
NASDAQ	6.4%	29.6%
MSCI EAFE EQUITY (GROSS)	-8.1%	4.4%
RUSSELL 2000 INDEX	0.3%	11.5%
MSCI EMERGING MARKET EQUITY (GROSS)	-7.9%	8.0%
BLOOMBERG GLOBAL AGG BOND INDEX	-5.1%	-1.7%
BLOOMBERG INTERM. TREASURY	-1.7%	2.4%
BLOOMBERG INTERM. GOVT/CREDIT	-1.6%	3.0%
BLOOMBERG 5 YEAR MUNI INDEX	-1.0%	1.2%
BLOOMBERG HIGH YIELD CORP INDEX	0.2%	8.2%
ishares S&P GSCI COMMODITY TR INDEX	3.3%	9.3%

Note: All returns include invested cash flows expressed in U.S. dollar terms.

KEY POINTS

- The election of Donald Trump has been welcomed by investors with high expectations of "pro-growth" economic policies. The Trump agenda includes supply-side initiatives that have potential to unleash the productivity of the U.S. economy.
- A resilient U.S. labor market, stable oil prices, and an accommodative Fed are among the key tailwinds for the market to start the year. Rising longer-term interest rates, ballooning government debt and deficits, and a tapped out consumer are the key headwinds that will challenge expectations.
- While spending cuts are necessary to bring sustainability to the U.S. government's finances, our concern is that their potential negative short-term impact on the economy may be underestimated.
- We see record equity valuations and extreme market concentration as a potential barrier to outsized equity returns in 2025. Higher yields on bonds creates a good opportunity to extend our fixed income duration relative to the benchmark.

GLOBAL MACROECONOMIC REVIEW & OUTLOOK

Washington has some of that new-car smell entering 2025. Enthusiasm is running high on hopes that the new Presidential administration can successfully tackle the economic challenges that the old one has left behind. Donald Trump's return to the White House as well as the Republican majority in Congress offer opportunities for a new path forward. Trump, who ran on a platform of lower taxes, de-regulation, immigration reform, and economic protectionism, has been welcomed by investors as the one who can make the tough decisions necessary for the economy to reaccelerate its growth.

In Trump's corner to start will be a resilient economy, relatively stable oil prices, and an accommodative Fed. U.S. GDP in Q3 was up 3.1% and all signs point to 2-2.5% growth in Q4. Retail sales continued to grow into year-end, with holiday sales up 3.8%, which was similar growth compared with Q4 of '23. The employment picture has been weakening, with the unemployment rate moving up from 3.7% in January of last year to 4.1% in December. Nevertheless, job gains have been better than 200k in three of the last four months. The Manufacturing sector is also seeing a bit of a pickup, with the ISM Manufacturing PMI up to 49.2 in December; the best reading since March of last year. Economic activity has been supported by lower oil prices in the second half of last year, with WTI Crude Oil retreating from $87 to $70 in that time period. That buoyed consumer spending and provided profit margin relief for the corporate sector. Finally, the Federal Reserve (the Fed) has lowered the Fed Funds Rate by 100 basis points (1.0%) since September of last year, with the most recent cut of 0.25% coming on December 18th. Market participants expect additional rate cuts in 2025, with consensus expectations calling for 2 or 3 quarter-point cuts throughout the year. That would bring the Fed Funds rate into the 3.5-3.75% range by year end, which would be consistent with a neutral monetary policy given prevailing inflation levels.

Headwinds to the economy will be rising long-term interest rates, ballooning debt levels across the economy, especially at the Federal government level, and a tapped out consumer, especially on the lower-end of the income spectrum. Despite the Fed decreasing short-term rates, the bond market has moved long-term rates higher. Since the Fed started its most recent easing campaign, the 10-year Treasury rate has moved up roughly one full percentage point. The U.S. National Debt now stands at more than $36T and rising on the back of a 7% budget deficit. Higher rates have a direct negative effect on the U.S. government's ability to service its debts. That, in turn, could further exacerbate the increase in bond rates through a rising term premium, ultimately leaving the private sector vulnerable. Trump and his incoming administration understand that they have to deal with this problem head-on. They plan to make cuts to federal spending and introduce tariffs on imported goods to boost revenue to the Treasury. The problem is that Federal spending accounts for more than 25% of U.S. GDP and has been largely responsible for keeping the economy afloat. Most of the employment and wage gains in the last two years have come from the government sector. Any drastic cuts to spending are more than likely to negatively impact the overall level of economic activity, at least in the short run. Trump plans to offset this by front-loading tax cuts and decreasing the regulatory burden on the private sector. Finally, U.S. consumer finances look stretched with household debt at a record $18T exiting Q3. Credit card debt has climbed to a new record of $1.2T and is facing record-high interest rates as well, with charge-offs and delinquency rates approaching 2007 levels. Overall household obligations have come down in terms of disposable income, so as long as employment can hold, households can service their debts. A return of inflation or a weaker economy would upset the apple-cart and increase the risks for the markets.

INVESTMENT OUTLOOK

Our investment outlook was cautious through most of last year. We recognize some of the incremental positives that the change in Administration can bring in terms of accelerating economic growth. For example, we see smaller companies with sales mainly in the U.S. benefitting from the supply-side initiatives that are likely to come from the Trump White House. We also think that the government finances will be under the microscope in the coming years, which should bring some sanity to the recent spending patterns. Extending the duration of our bond holdings would make sense with that in mind. However, we also do not think that all of the problems that have accumulated in recent years can disappear with a magic wand. The choices that are in front of the executive branch of government are difficult and will require sacrifice in the short term. Historically, the U.S. government has not been willing to make those tough choices. There are reasons to doubt that the slim majority that the Republicans have in Congress can withstand similar pressures this time around.

The equity market is not pausing, however. The excitement and enthusiasm among investors are at such high levels that the S&P 500 Index is trading at a 37x cyclically-adjusted price-to-earnings ratio (CAPE). Only once in history was this measure higher and that was in 1999. The median valuation for the market on this basis is 17x. While investors may disregard valuation in the short term, it is the key metric that has the highest correlation with longer-run future returns. The other thing that is worrisome to us is the high level of market concentration among a handful of stocks. If one analyzes the data, the evidence is clear that 1) Retail investors have their highest ever allocations to U.S. Equities in history, 2) they all mostly own the same stocks, and 3) foreign investors all joined the U.S. party last year. While there is certainly a good argument to be made for the U.S. given its relatively strong productivity and earnings growth, global investors' infatuation with U.S. (mostly Technology) companies has reached a crescendo in statistical terms.

In light of that, we expect a broadening of relative performance away from the U.S. Large-cap Growth and the Technology sector and in favor of the U.S. Small-cap and Defensive sectors. Cyclical Value is also a part of the market that does well in the aftermath of election cycles. On the Fixed Income side, with the U.S. 10yr Treasury yield at 4.60% entering '25, we see relative value in bonds and are more willing to extend our duration relative to our benchmarks than we had been earlier last year. We continue to like commodities as a nice hedge against a potential return of higher inflationary expectations on the back of easier monetary policy and resilient economic growth.

INVESTMENT TEAM

farmerstrustco.com

David A. Dastoli, President – CFA, CFP®
dastolid@farmerstrustco.com | 330.740.1231

Thomas S. Rumbaugh, VP
rumbaught@farmerstrustco.com | 330.765.0583

Igor Golalic, VP – CFA
golalici@farmerstrustco.com | 724.867.2019

John D. Stewart, SVP & Chief Investment Officer – CFA
stewartj@farmerstrustco.com | 330.740.1208

Dale Standley, VP
standleyd@farmerstrustco.com | 330.740.1207

Joe Waterman, AVP
watermanj@farmerstrustco.com | 330.609.8328

Meet the team!

YOUNGSTOWN: 42 McClurg Rd., Youngstown, OH 44512 | 330.743.7000
HOWLAND: 1625 Niles-Cortland Rd. NE, Warren, OH 44484 | 330.609.5057
HUDSON: 75 S. Main St., Hudson, OH 44236 | 330.282.4158
CANTON: 4518 Fulton Dr. NW, Suite 100, Canton, OH 44718 | 330.526.7305
WOOSTER: 305 West Liberty St., Wooster, OH 44691 | 330.439.4495
ASPINWALL: 319 Freeport Rd., Aspinwall, PA 152155 | 844.781.3623