osaic
Empowering Wealth

Osaic Research 2025 Themes Scorecard

Theme	Our Prediction	Results	Score
U.S. Economic Growth Outpaces International Markets	"U.S. exceptionalism" is set to continue as strong economic fundamentals at home contrast with widespread market uncertainty abroad. Investors should expect the US economic growth to outpace that of other global economies. Most forecasts predict that U.S. GDP will grow by 2-2.5% in 2025,[1] driven by a resilient labor market and robust consumer spending, expanding productivity, deregulation, infrastructure spending, greater industrial activity, and easier financial conditions. Abroad, Chinese GDP growth is projected at 4%–4.5% for 2025,[2] significantly below pre-pandemic levels, and thus far, fiscal policy stimulus has underwhelmed investors, ultimately limiting its role as a global growth driver. The eurozone economy is set to decline relative to the U.S. next year.[3] Persistent deficits, and weak consumer spending point toward weaker economic growth, suggesting that low valuations may be justified across European equities. It is prudent to remain overweight to U.S. equities.	U.S. economic growth outpaced major international economies in 2025. The U.S. economy grew near 2.0%, supported by steady consumer spending, and easing financial conditions that helped counteract the effects of a gradually cooling labor market. China's GDP came in near the mid-four% range for the year, which is considered weak relative to its long-term trend, while the EU is expecting GDP growth of 1.4% for 2025. Even though international markets delivered stronger performance than anticipated, economic growth played out as expected.	— NEUTRAL
Equities Normalize from Recent Outsized Returns but Finish the Year Positive	Despite continued earnings growth, S&P 500 profit margins have relaxed from near-record levels – exceeding 12.0%. Most earnings growth for 2025 has already been priced into equities, setting the bar higher for companies to beat lofty earnings projections. Margins may come under pressure from significant capital expenditures for Artificial Intelligence (AI) adoption and development. Corporate bond yields average 5.5%, up from 3.5% in 2022, increasing interest expenses and putting pressure on net income growth. However, non-financial corporate business net interest payments have actually declined since the Fed began hiking.[4] This is unlikely to continue as interest rates should remain higher into 2025. So economic growth is moderating, but still solidly positive, and the Trump administration's policy goals – including deregulation, lower energy costs, and tax cuts – could boost an already growing economy.[5] Investors should realize that 25%+ returns for the S&P 500 are not the norm, despite back-to-back banner years, but normal U.S. equity market returns are still likely to be one of the best allocation options next year, particularly as market leadership broadens.	Equity returns were not as strong as previous years, falling short of the 25% mark that 2024, and 2025 surpassed. However, the 17.9% that the S&P 500 returned remained well above the 20-year average return of 11.87%. Profit margins remained stronger than anticipated, and valuations continued to expand, contributing to a strong, but volatile, year for the S&P 500.	— NEUTRAL

Overall scoring: ✓ Right call ✗ Wrong call — Neutral

Theme	Our Prediction	Results	Score
Small Caps are Poised for Outperformance	Attractive valuations, resilient earnings, and insulation from global tariffs along with favorable cyclicality and improving operating leverage set up small caps for potentially significant outperformance. The S&P SmallCap 600, an index of profitable small-cap companies, trades at a forward price-to-earnings (P/E) ratio of ~ 13x, compared to ~ 22x forward P/E for the S&P 500,[6] signaling a significant relative value opportunity. Deregulation in sectors such as financials, energy, and manufacturing supports higher margins for small-cap companies, which are projected to achieve stronger earnings growth than large-cap companies in 2025. Small-cap firms generate over 80% of their revenue domestically, reducing their exposure to international trade disruptions and tariffs. Although interest rates may remain higher than originally anticipated next year, which will negatively impact the financial leverage of smaller companies, higher nominal growth will spur operating leverage and further accelerate marginal profitability. History suggests smaller companies' positive operating leverage generally wins versus their negative financial leverage.[7]	Small caps significantly outpaced last year's returns and reached new all-time highs not seen since 2021 but lagged the S&P 500 by 5.07% for the year. Although earnings growth did outpace large cap peers but unfortunately did not translate to stronger performance comparatively. Additionally, low valuations persisted throughout the year, in spite of concerns around heightened valuations in large caps. A meaningful rebound in performance throughout the third and fourth quarters helped to close the performance differential versus large caps but fell short.	— NEUTRAL
Interest Rates Are Likely to Remain Elevated	The Federal Reserve's (the Fed) funds rate will remain higher for longer than originally anticipated. The Fed's December Summary of Economic Projections (SEP) now forecasts just two 25-bp cuts next year.[8] Core services inflation remains elevated at 4.5%, driven by labor market strength and demographic trends. Meanwhile, the US budget deficit exceeds $1.8 trillion,[9] necessitating higher interest rates to attract investment and stabilize debt levels. A flattening yield curve and lack of term structure make long-duration assets less attractive – investors are not rewarded for taking on interest rate risk. Stable yields limit potential fixed-income price appreciation but provide investors with a higher starting yield. A flat yield curve means short- to intermediate-term bond allocations appear attractive. Areas where spreads are wide, like securitized credit, exhibit better valuations. Adding structure to fixed income exposures should enhance yields and add downside protection – critical improvements amidst higher rate volatility.	Interest rates remained elevated throughout most of the year, with the Fed holding policy steady until late in the third quarter before delivering its first cuts. Inflation stayed sticky, and the Fed continued to stress caution in easing policy. Our original estimate for two rate cuts was close to the delivered three cuts by the Fed, which opted to cut in the final month of the year amid softening labor market data.	✓ RIGHT CALL

Overall scoring: ✓ Right call ✗ Wrong call — Neutral

Theme	Our Prediction	Results	Score
Housing – The Obstacles of Tight Supply & Record-Low Affordability	Affordability remains a significant problem for the housing market. Median home prices are projected to increase by 5% in 2025, while 30-year mortgage rates remain elevated at 7%, keeping home ownership about as prohibitive as it's been since the early 1980s.[10] Supply is also constrained, as the number of housing starts remains below 1.5 million units annually, well below demand levels, exacerbating the inventory shortage. Costs may increase given policy changes to tariffs on lumber and immigration which may affect the cost of materials or availability of labor. The two largest generations, Baby Boomers and Millennials, are driving both supply and demand. Boomers are retaining homes for longer periods, while millennials account for over 35% of home-buying activity, intensifying market competition.	Affordability remained extremely strained throughout the year, with mortgage rates staying elevated and home prices continuing to rise. Housing supply failed to improve, as home building starts stayed below demand and existing homeowners remained reluctant to sell. Structural pressures like labor constraints and higher material costs kept inventories tight.	✔ **RIGHT CALL**
Energy, AI, and Crypto are Key Areas to Watch in 2025	While these are not economic or market predictions, they highlight key areas to watch for valuable insights into emerging trends and market dynamics. Rapid growth is expected in and around AI as adoption and integration expand across all manners of businesses and yet untapped industries. AI has the ability to increase productivity which can be a strong disinflationary force as well as an impetus for growth. There is a substantive demand for energy given the level of power that AI consumes. Nuclear energy made a resurgence in 2024 with both Uranium futures rising, and companies exposed to operating or developing nuclear plants seeing strong returns. Renewable energy, which was anticipated to struggle under Trump's first administration, flourished on the back of lower taxes and yields, but can green policy remain relevant given the voracious consumption expected from AI? Traditional energy faces volatility from geopolitical tensions but remains critical for global energy security. Crypto had an impressive climb in 2024 driven by the approval of spot bitcoin ETFs and hopes of a more pro-crypto incoming administration, which were ultimately realized, further boosting already exuberant market action. Look for additional ETF approvals for other crypto assets and a swath of crypto-related IPOs to impact the digital asset markets next year.	AI adoption continued its rapid expansion across industries, reinforcing expectations for meaningful productivity gains and broader economic impact. Energy demand surged alongside AI growth, while renewable energy demand continued to grow, particularly among nuclear energy. Crypto markets initially rallied in the first quarter of 2025 with increased ETF approvals and policy support, but found sharp volatility throughout the rest of the year that negatively impacted its overall performance. Each of the three areas continued to be areas of focus for investors in 2025.	✔ **RIGHT CALL**

Overall scoring: ✔ Right call ✕ Wrong call — Neutral

Economic Definitions

CPI (headline and core): Consumer prices (CPI) are a measure of prices paid by consumers for a market basket of consumer goods and services. The yearly (or monthly) growth rates represent the inflation rate.

Housing Starts: Housing (or building) starts track the number of new housing units (or buildings) that have been started during the reference period.

Federal Reserve (Fed): The Federal Reserve System is the central banking system of the United States of America.

GDP: Gross domestic product (GDP) measures the final market value of all goods and services produced within a country. It is the most frequently used indicator of economic activity. The GDP by expenditure approach measures total final expenditures (at purchasers' prices), including exports less imports. This concept is adjusted for inflation.

P/E Ratio: A fund's price/earnings ratio can act as a gauge of the fund's investment strategy in the current market climate, and whether it has a value or growth orientation. Companies in those industries enjoying a surge of popularity tend to have high P/E ratios, reflecting a growth orientation. More staid industries, tend to have low P/E ratios, reflecting a value orientation. Morningstar generates this figure in-house on a monthly basis, based on the most-recent portfolio holdings submitted by the fund and stock statistics gleaned from our internal equities databases. Negative P/Es are not used, and any P/E greater than 60 is capped at 60 in the calculation of the average.

Index Definitions

S&P 500: The S&P 500® is widely regarded as the best single gauge of large-cap U.S. equities and serves as the foundation for a wide range of investment products. The index includes 500 leading companies and captures approximately 80% coverage of available market capitalization.

S&P SmallCap 600: S&P DJI introduced the S&P SmallCap 600 to the market in 1994. Measuring a segment of the market that is typically known for less liquidity and potentially less financial stability than large caps, the index was constructed to be an efficient benchmark made up of small-cap companies that meet investability and financial viability criteria.

Russell 2000: The Russell 2000 Index is comprised of the smallest 2000 companies in the Russell 3000 Index, representing approximately 8% of the Russell 3000 total market capitalization. The real-time value is calculated with a base value of 135.00 as of December 31, 1986. The end-of-day value is calculated with a base value of 100.00 as of December 29, 1978.

Bloomberg US Agg Bond: The Bloomberg US Aggregate Bond Index is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate securities, MBS (agency fixed-rate pass-throughs), ABS and CMBS (agency and non-agency).

Housing Affordability Index: Housing Affordability Index measures whether or not a typical family could qualify for a mortgage loan on a typical home. A typical home is defined as the national median-priced, existing single-family home as calculated by NAR. The typical family is defined as one earning the median family income as reported by the U.S. Bureau of the Census. The prevailing mortgage interest rate is the effective rate on loans closed on existing homes from the Federal Housing Finance Board. These components are used to determine if the median income family can qualify for a mortgage on a typical home. To interpret the indices, a value of 100 means that a family with the median income has exactly enough income to qualify for a mortgage on a median-priced home. An index above 100 signifies that family earning the median income has more than enough income to qualify for a mortgage loan on a median-priced home, assuming a 20 percent down payment.

Disclosures

1 First Quarter 2025 Survey of Professional Forecasters

2 World Bank raises China's GDP forecast for 2024, 2025 | Reuters

3 Boom_Or_Bust_An_Investors_Playbook_For_2025_&_Beyond.pdf

4 2025 Economic Outlook: Firing on All Cylinders - Apollo Academy

5 From Rare Soft Landing to Common Bull Market

6 S&P 500 P/E Ratio Quarterly Trends: S&P 500 Earnings | YCharts

7 Certainties for an Uncertain World - RBA, December 16, 2024.

8 The Fed - December 18, 2024: FOMC Projections materials, accessible version

9 U.S. deficit tops $1.8 trillion in 2024

10 US house prices are forecast to rise more than 4% next year | Goldman Sachs

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