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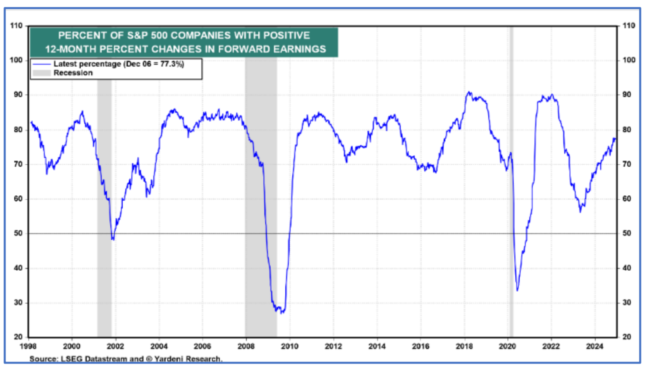
# John’s Market Outlook – December 16, 2024

In the last Outlook, I said “*My outlook remains for continued earnings growth and a broadening market through the rest of this year*”.

3Q earnings were positive. The market has broadened. Compared to last quarter, a higher percentage of companies (77%, left chart) showed positive earnings growth. Business and consumer confidence are higher.

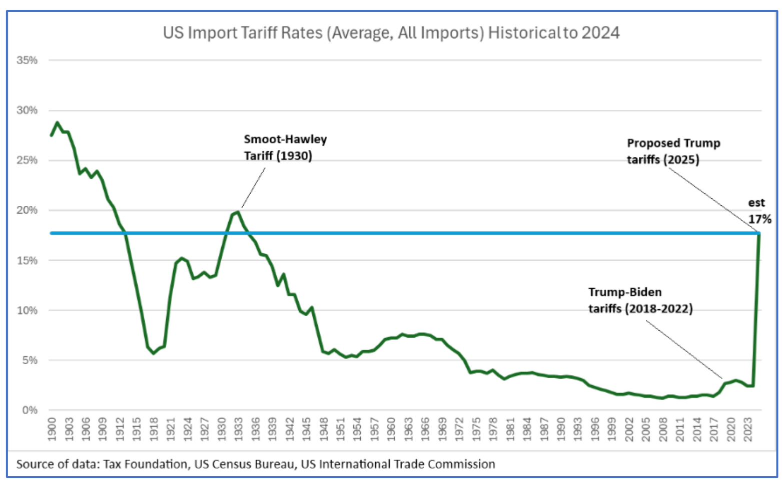



I also said “*Elections bring policy uncertainty”,* which now takes center stage.

The incoming administration’s priorities include i) large import tariffs including 60%+ on China and 10-25% on other countries, ii) deporting several million immigrants[1], iii) renewing and adding to the 2016 tax cuts, iv) large cuts to federal programs and spending, and v) broad deregulation and privatization.

These would be big changes. As illustration, the average tariff under the administration’s proposal[2] (right chart, 17%) would be by far the highest in the modern era, similar to peak tariffs in 1930.[3]

We do not know which priorities will be pursued, how effectively or aggressively, what reaction from other countries, and thus what effect on the economy. The uncertainty may peak in early-mid 2025, when we start seeing concrete actions by the administration.




[1] Most are employed in the agriculture, construction, hospitality, and other low wage/service industries.
[2] Tax Foundation estimate 10/1/2024: average tariff on all US imports.
[3] Referring to the Smoot-Hawley tariffs, imposed in 1930 at the start of the Depression.

*My opinions and judgment on the date written. Not investment recommendations or guarantees.*
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Some investors believe many of these priorities are mere campaign talk, negotiating tactics, or will not be seriously pursued. I think the administration's ambitions should not be underestimated.

The administration's long-term economic goals are to revitalize the US manufacturing sector, accelerate economic growth, and reduce the Federal deficit – all highly positive aims.

**Long-term benefits are often preceded by short-term costs.** Tariffs, trade wars, and labor force shrinkage tend to be inflationary. Tax cuts typically increase deficits, at least initially. Spending cuts often depress employment. Higher inflation may push long rates up or slow the Federal Reserve's rate cuts. Disruption and uncertainty are market risks. US stocks are more expensive than any time since the market peaks in December 2021 and April 2000.

As we approach year-end, I have modestly lowered equity exposure. I am prepared to further reduce equities and raise cash/defensive exposure, as we did in late 2021.

- The new administration wants to increase oil & gas exploration, benefiting Schlumberger (SLB) and Halliburton (HAL), and home building, helping building materials names like Owens-Corning (OC) and James Hardie (JHX). More infrastructure, manufacturing, and energy projects funded by the 2021-2022 investment bills[4] will break ground in 2025, benefiting construction-related names like Knife River (KNF), Jacobs (J), and CRH Ltd (CRH).
- Consumer sentiment has improved and retail spending is holding up. We added to consumer/retail names such as Amazon (AMZN), Molson-Coors (TAP), Delta Airlines (DAL), and Ulta Beauty (ULTA).
- China has restricted export of rare earths, specialized semiconductor materials, and high-grade graphite for EV batteries. We added MP Materials (MP), a US rare earth producer.
- Rising Great Power military tensions and more regional wars, reminiscent of the Cold War, will drive defense spending higher. We added Rheinmetal (RNMBY), a leading European defense name.
- The big online names had middling 3Qs with slowing growth despite very large investments in AI. The administration may not be entirely friendly to Google (GOOG), Meta (META), and Microsoft (MSFT), who have not been among its core business influencers.
- The rush to train more and ever-larger AI models may be nearing its peak. Investors will shift expectations to profitable uses of AI software to accelerate revenue, increase productivity, or cut headcount. Software companies have little tariff risk. We hold Salesforce (CRM) and Oracle (ORCL), added to SS&C Technologies (SSNC) and Checkpoint (CHKP), and reduced Fortinet (FTNT).
- Healthcare faces risk from changes at Health & Human Services, CDC, and FDA, and cuts in ACA and Medicaid enrollment. The sector is economically defensive. I think the pullback is overdone. Lilly (LLY) has the most effective obesity drug; it may be approved for cardiovascular disease with more insurance coverage. CSL Ltd (CSLLY) and Moderna (MRNA) have vaccines for H5/avian influenza.
- Banks may see less regulation and more mergers. Higher rates may benefit lending margins but raise credit risk and stress weaker banks. We added to Bank of America (BAC) and Fifth Third Bank (FITB).

I would be happy to go deeper into this outlook and other investment topics than was possible in this brief summary. Please email johnliu@laurelhurstasset.com or call 510 847 0070. Thank you!

[4] 2021 Infrastructure Act (roads, bridges, electricity, etc), 2022 CHIPS Act (semiconductor manufacturing), 2022 Inflation Reduction Act (renewable and nuclear energy); it can take 2-3 years for projects to be funded and start construction.