



Market Update: February 2025

Welcome to the first edition of our monthly investment commentary, where we'll share our latest thoughts on the markets, economy, and key areas we're focusing on. Our goal is to provide insights that are informative, useful, and a solid complement to our ongoing conversations. If you have any feedback—whether it's suggestions, critiques, or ideas for improvement—please don't hesitate to share!

2025: A Page-Turner So Far

If January 2025 was the first chapter of a novel, the writer has done a great job to intrigue us to want to continue reading. Back-to-back 20%+ years of gains for the S&P 500, the Fed starting an easing cycle and a presidential election are the preface to this book.

Before diving into recent developments, here's a quick recap of our 2025 outlook, which we've discussed with many of you. After strong equity returns in 2023 and 2024, we expect more moderate gains this year, forecasting mid to high single-digit returns for the S&P 500. We also anticipate greater volatility—a 10%+ correction wouldn't surprise us, something that used to be a common annual occurrence but has been absent the past two years. However, as long as broad economic indicators remain stable, we're not inclined to take a pessimistic stance on the market's medium-term direction.

Now, let's dive into January's key themes.



New Administration & Market Volatility

It's impossible to ignore the biggest event of the month—Donald Trump's inauguration as the 46th President on January 21st. When we talk about volatility and uncertainty, this tops the list. While we could spend pages discussing every policy change, we'll focus only on those that we believe will have the greatest economic and market impact.

Trade War: Round 2

As we write this (now a few pages into the second chapter of 2025), new tariffs on Mexico, Canada, and China have been announced, set to take effect at midnight on February 3rd—well, except for Mexico and Canada, which have been given a one-month pause. By the time you're reading this, things may have already changed.

Predicting the impact of these tariffs is nearly impossible. While they do pose economic risks—potential inflation, earnings pressure, and trade disruptions—we won't be making investment decisions based on uncertainty alone. We'll continue monitoring the situation as more clarity emerges.

The Fed: Rate Cuts Coming?

In January, the Federal Reserve held off on rate cuts, maintaining current levels. As of February 4th, CME Group's Fed Fund Futures suggest a 75.5% probability of zero to two rate cuts in 2025 (31.9% expect two cuts, 31.1% expect one, and 12.5% expect none). However, history has shown that these market predictions aren't always reliable. If the past few years are any indication, we may end up seeing more rate cuts than currently expected—or even an unexpected hike.

For now, we lean toward expecting more cuts. If the market experiences the correction we anticipate, along with softer economic data and inflation, four or more cuts wouldn't surprise us.



DeepSeek: AI Disruption?

Perhaps the most significant market-moving event last month was the release of DeepSeek-R1, a chatbot from Chinese company DeepSeek. The concern isn't so much the competition with ChatGPT, but rather DeepSeek's reported efficiency improvements—it supposedly requires far fewer chips to operate.

This news rattled markets, particularly for AI-related stocks. Nvidia and other chipmakers saw some initial volatility, as investors questioned whether lower AI computing costs could impact demand. However, there's another way to look at this: cheaper and more efficient AI could encourage more companies to invest in their own AI capabilities, sustaining chip demand rather than reducing it. So far, earnings reports from major tech companies haven't signaled any slowdown in capital expenditures for 2025—in fact, some have even increased their spending plans.

Final Thoughts

We believe 2025 will be a positive year for equities, but returns won't come as easily as they did in the past two years. Volatility is here to stay. While we remain long-term bullish on technology, this could be the year where the rally broadens to other sectors and smaller-cap stocks that haven't fully participated yet. We also expect fixed income to offer competitive returns relative to equities in 2025.



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