

# Three important insights from 2024

From the Field  
January 2025



## Key Insights

- We saw three fundamental investment trends in 2024 that we believe could continue to influence capital market performance in 2025.
- These include a shift in risks from recession to inflation, extreme U.S. equity outperformance, and signs the Federal Reserve's rate-cut cycle will be modest.



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**T**here were lessons to be learned from economic and market developments in 2024, including three important insights that we think investors should keep in mind as we move into 2025.

### Risks have shifted from recession to inflation

As we entered 2024, concerns lingered about the potential economic impact of rate hikes made in 2022 and 2023 by the U.S. Federal Reserve and other key central banks. However, as the year progressed, global growth expectations for both 2024 and 2025 moved higher, with forecasted growth for the U.S. experiencing the sharpest uptick.

But inflation concerns reignited in the latter part of 2024 (Figure 1). This was partially

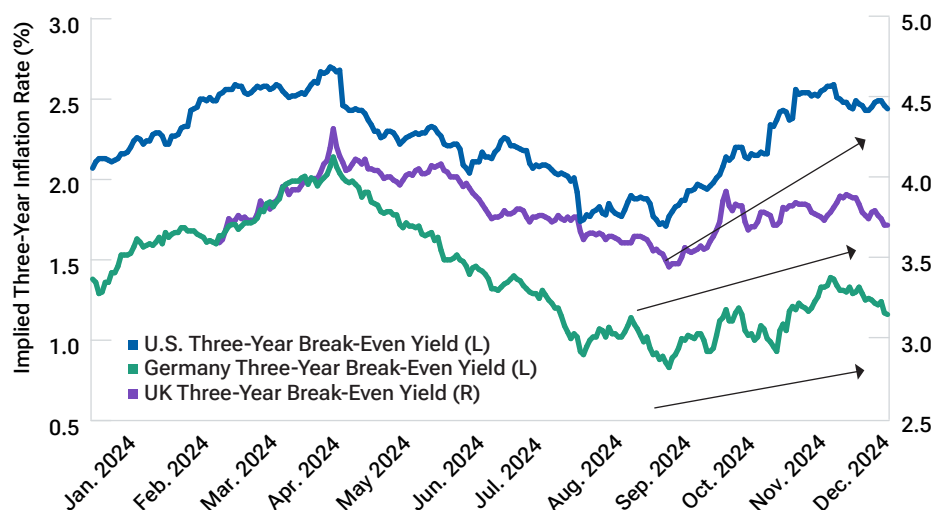
due to concerns about the potential impact of U.S. President-elect Donald Trump's campaign promises of higher tariffs and tighter immigration controls.

There also was evidence in late 2024 that inflation rates had stopped falling, with the three-month moving average for the U.S. consumer price index showing a clear upward trend since last July. Notably, services inflation remained somewhat sticky while goods inflation began to show hints of rebounding.

The implication for investors is that they should consider whether their portfolios are properly hedged against inflation risks. They may want to consider adding exposure to asset classes such as natural resources equities that historically have responded well to higher inflation.

## Inflation risks have increased

(Fig.1) Market-implied inflation expectations



January 1, 2024, to December 17, 2024.

L=Left axis. R=Right axis. Break-even yield = The yield difference between an inflation protected bond and an equivalent nominal bond with the same maturity. Break-even yields provide a forecast of expected inflation. **There is no guarantee that any forecast will come to pass.**

Sources: Bloomberg Finance L.P., U.S. Bureau of Labor Statistics/Haver Analytics.

## “U.S. exceptionalism” has become more extreme

One long-running trend that strengthened dramatically in 2024 was “U.S. exceptionalism”—the idea that the U.S. enjoys unique structural advantages over other global markets. Not only did the U.S. economy experience one of the sharpest upticks in expected growth, but U.S. earnings expectations grew at an even faster rate.

U.S. outperformance in 2024 was driven by several fundamental factors, including U.S. dollar appreciation, a surge in capital spending in artificial intelligence infrastructure, and the incoming Trump administration’s promises to relax regulatory burdens and seek lower corporate tax rates.

But the trend now appears somewhat extreme, in our view. From December 31, 2010, to December 17, 2024, the average one-year outperformance of the Russell 3000 Index relative to the MSCI All Country World

Index ex U.S. was +6.18%. But, over the year ended December 17, 2024, that difference ballooned to +13.89%.

The bottom line is that stock markets have priced in a great deal of “U.S. exceptionalism.” A partial reversal could be on the horizon if elevated U.S. earnings expectations are not met in 2025.

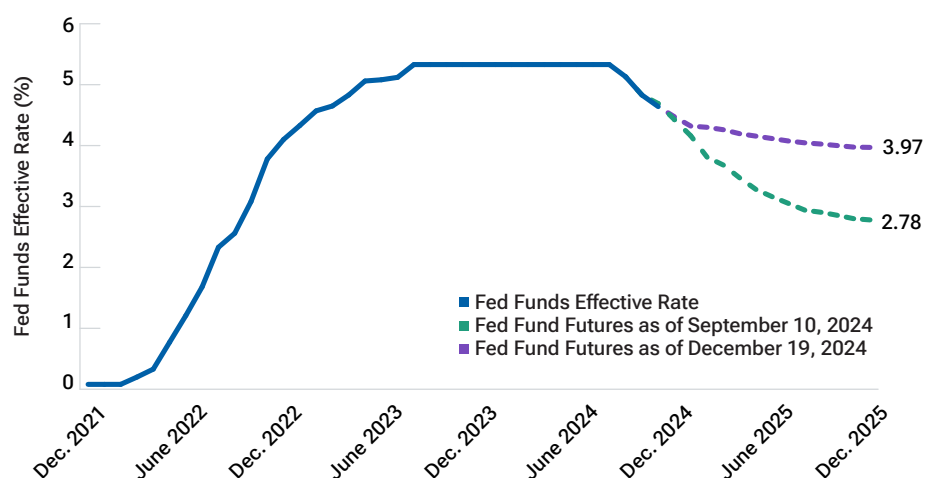
## The Fed’s rate-cutting cycle will be modest

At the end of 2023, the Fed “pivoted,” as Chairman Jerome Powell indicated that rate cuts were likely to begin some time in 2024. This led many investors to increase their allocations to longer-duration U.S. Treasury bonds.

However, the U.S. economy proved much more resilient than expected in 2024. Progress on curbing inflation also appears to have stalled. So expectations for Fed rate cuts have turned considerably more modest (Figure 2). As of December 19, 2024, futures markets

## A modest Fed cutting cycle is expected

(Fig. 2) Federal funds effective rate and futures market pricing



December 31, 2021, to December 19, 2024.

There can be no assurance that the projected results will be achieved or sustained. They are not indicators of future results.

Source: Bloomberg Finance L.P.

were pricing in an end point of 3.97% for the key federal funds rate—just 1.4 percentage points below the most recent rate peak.

This shift had numerous implications for asset class performance. Cash once again proved to be king in 2024, as very short duration bonds not only were sheltered from rising rates, but maintained healthy yield levels through the year. If inflation

remains stubborn, that might again be the case in 2025.

### Conclusion

T. Rowe Price's Asset Allocation Committee will closely monitor these and other key issues as we move forward in 2025 and will update investors accordingly as they play out.

For definitions of financial terms, please see: <http://www.troweprice.com/glossary>

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