

Winter 2025

JAMESSON *associates*

Recent Economic Events

I had toyed with leaving this section blank due to the dearth of timely economic statistics, resulting from the government shutdown. I ultimately concluded that there were enough private releases to fill the void. With that caveat, I believe we can divine that the American economy had a very solid third quarter based on a free-spending affluent consumer and a frenetic pace of AI infrastructure outlays. Normally when GDP is advancing above trend, employment is robust as well. In 2025, that has not been the case. We continue to fly blind regarding official jobs figures, but indirect evidence suggests a slowdown, if not an outright decline. Inflation is not yet dead, as indicated by the focus on affordability which produced Democratic election victories.

The Federal Reserve Bank of Atlanta regularly publishes an estimate of GDP based on an algorithm that digests each economic statistic that is released. The included items are weighted by their statistical correlation with total output. Previous estimates have been quite close to the official figures. For the third quarter (which ended just before the government shutdown), 3.6% real growth was projected. The estimate had been as low as 2.2% in early July and as high as 4.2% in November. The key drivers of growth in the projection are personal consumption, business investment, and net exports. The last of these items reflects a sharp drop in our trade deficit during the summer.

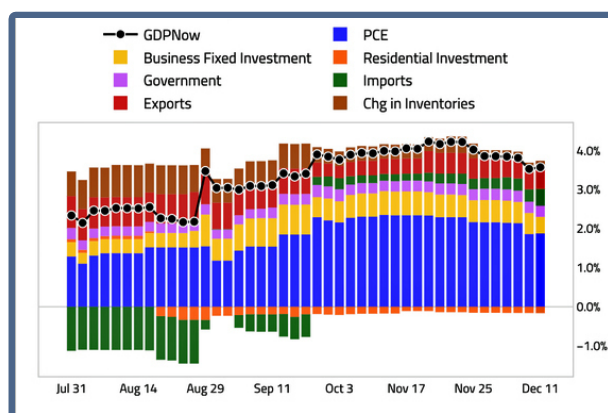
The bifurcation of the economy based on income inequality has been much commented upon. It is real. Those fortunate enough to be in the upper end of the income ladder have continued to spend at a healthy clip this year. Delta Airlines reported record sales driven by premium seat demand even as main cabin revenue fell in the third quarter. Close to 30% of the lower third of Americans by income are living paycheck to paycheck and over 20% of the middle-class falls into this category as well. These folks account for the abysmal level of consumer confidence.

Separate from the consumer, AI spending continues to be measured in billions, if not trillions, of dollars. Data centers are gobbling up land today and promise to use oceans of water and electricity in the near future. This construction spending has boosted current GDP even as it has starved non-AI business and residential investment projects.

Structures supporting machines are booming; structures housing people are not.

Employment has not kept pace with economic growth. While the official job figure for September was a gain of 119,000, the apparent strength was belied by downward revisions to both July and August. Estimates from ADP suggest that private

jobs hardly grew at all in October and November. Furthermore, the unemployment rate has continued to inch upward, hitting a post-recovery high of 4.4%. Weekly new claims for




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Recent Economic Events-continued

unemployment insurance have been stuck in the low 200,000 range, but net hiring outside of healthcare is almost nil. This suggests that those with jobs are hanging in while those who have been laid off are struggling to find new employment. The no fire, no hire job market seems to be in equilibrium, but it is a fragile equilibrium at best.

Inflation reports are delayed, but what we have suggests more a plateau than a decline. Core PCE inflation for September registered 2.8%, well above the Fed's target rate. Core goods prices are increasing again (tariffs) and core services prices are

showing little sign of slowing. While there are some instances of falling prices (gasoline and eggs), there are others of accelerating increases (electricity and beef). With Congress letting subsidies for the ACA expire, exchange health insurance premiums are poised to rise an unaffordable 100% plus.

Aggregate economic indicators are solid, but they are masking the underlying tensions of weak job growth and sticky inflation. The fortunate minority is benefiting, but the majority has remained focused on affordability which was the key to this year's election results. 

Commentary

I have always believed in the pendulum theory of American politics. Election winners overestimate the mandate that the voters provide, causing them to push extreme measures. Extreme measures seldom work, so an inevitable backlash occurs.

Barack Obama found this out in 2010 after Obamacare was passed. Donald Trump was greeted with election reversals in 2018 after his tax cuts were enacted. Joe Biden saw his chances at re-election evaporate as his border policy imploded.

We are not yet at the halfway point of Mr. Trump's second term, but voters have shifted strongly away from Republicans in the recent election cycle. Instead of focusing on the most important reason for his victory in 2024 (cost of living), the President has promoted actions which cause making ends meet to be even harder. Estimates vary, but tariff costs have added at least 0.5% to as much as 1.0%

to the annual inflation figures. The immigration crackdown may not have an immediate impact on prices, but reducing the supply of low-cost workers in restaurants, hotels, and nursing homes will have consequences over time. Finally, the Big Beautiful

Bill which cut health subsidies to pay for tax cuts is now playing out in substantially higher premiums for healthcare.

The President realizes that denying economic reality sank President Biden and has reluctantly begun a focus on the affordability issue. How

else to explain the White House visit by Mayor-elect Mamdani? Anyone unaware of the history and policy differences could be forgiven for assuming the two were quite aligned in beliefs. Mr. Trump is very sensitive to political vibes, so the meeting suggests a realization of the pendulum's initial movement. The problem the President faces in limiting the swing is that any actions he can take to reduce price pressures would require him to

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Commentary-continued

backpedal on some of his signature policies or get Congressional Republicans to reverse course. His history suggests neither is in the cards.

Polarization has solidified the base of each party, making it almost impossible for moderates from either side to win a primary. Gerrymandering has

reinforced this trend. But the slice of voters that is up for grabs has become even more volatile in recent years with Congress and the White House switching allegiance in most 21st century election cycles. Perhaps I should revise my belief in a pendulum swing to the back and forth of a tennis match. 🎾

Market View

Like mythical Odysseus, 2025 has been full of twists and turns. Even so, it has produced year-to-date gains in stocks, bonds, and commodities. The almost everything rally has bypassed bitcoin and oil, but any reasonably diversified portfolio has done quite well this year.

Is this happy state of affairs likely to continue, or is it time to pick up our marbles and go home? I believe that there are three key reasons for the synchronized rallies. Two are tactical while one is secular. The tactical supports for the markets include a rate cutting cycle from the Federal Reserve and the accommodative fiscal stance of the Federal government. It is never wise to bet against monetary expansion and government profligacy. The secular factor is the infrastructure buildout to support Artificial Intelligence.

Let's investigate each factor in turn. The Federal Reserve has lowered short-term interest rates by 1.75% since the peak in September 2024. This caused most rates out to five years or so to fall in concert. Longer-term interest rates initially resisted,

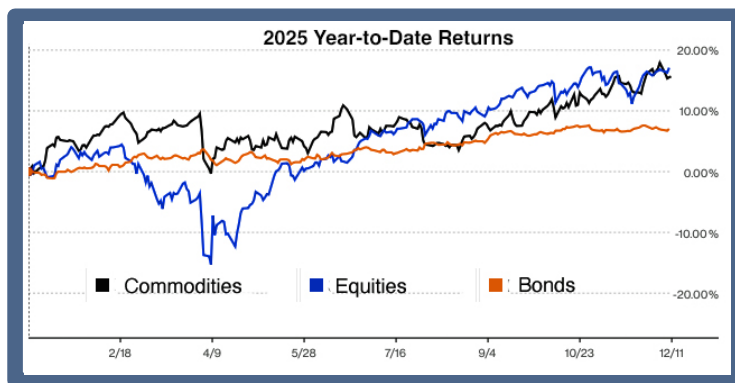
but starting in December 2024, they joined the parade. It strains credulity to believe that the rate that the Federal Reserve controls will not continue to fall in 2026 given the intense political pressure coming from 1600 Pennsylvania Avenue. The President will have appointed a majority of the

Federal Reserve Board of Governors by May, and his appointees will be doves, not hawks. Somewhat under the radar, the Fed resumed Quantitative Easing "to maintain an ample supply of reserves on an ongoing basis."

Even with record tariff revenue,

significant cuts to social safety net programs, and GDP growing above trend, the Federal deficit refuses to shrink. \$2 trillion of extra demand being poured into the economy has to go somewhere, and that somewhere appears to be corporate profits and increased equity prices. Fiscal belt tightening in an election year: no way.

Buzz Lightyear's famous words, "to infinity and beyond" apply to both the Federal deficit and to AI spending. The latter not only boosts the economy today, but the promised jump in productivity



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Market View-continued


beguiles us with a rosy future. AI changes the market's focus from the next quarter to the next decade.

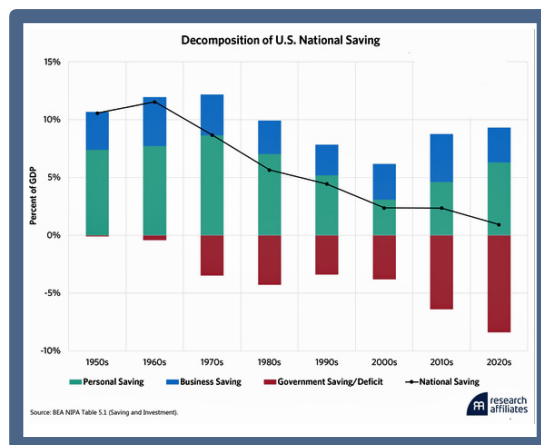
Projecting recent trends to simply continue is admittedly a lazy approach, but the three supporting factors seem well-grounded. But I think the implications for 2026 are different from 2025. Monetary and fiscal stimulus risk keeping inflation higher than we would like. It also keeps an outright recession at bay. I see the AI buildout continuing but broadening to companies that can leverage the technology to improve productivity for themselves and/or their customers.

The combination is constructive for stocks and very constructive for commodities. The equities that can benefit the most from my expectations

include financials, industrials, utilities, and healthcare. I'd be inclined to take some profits on the biggest winners of 2025. Gold and silver have shone especially brightly this year, but the entire commodity world is now on the upswing. A diversified commodity portfolio offers both absolute potential and a hedge in case the stock market takes a tumble next year.

With a lower risk of recession on the horizon, I see a higher inflation than the consensus. That means stay away from longer-term bonds. Look to shorter maturities (three years or so) or corporate credits (either high quality or junk bonds).

Crypto-currencies are a leveraged bet on liquidity. They may work out, but they will be volatile. Make sure you can stomach the rollercoaster movement if you decide to ride. 



Editor's Notes

Recently, ICE extended their immigration crackdown to Charlotte, NC. This triggered memories of what I wrote in 2004 while visiting that city.

On the Fourth of July, I was surrounded by a restaurant full of Colombian immigrants laughing, eating, and singing entirely in Spanish. I was never more proud to be an American. Independence Day 2004 found me and my family in Charlotte at Mi Tierrita (My Little Country), a Colombian restaurant celebrating their "Grand Opening." We entered and were transported to another world. The owner and his wife made us feel welcome but had to call on their daughter to translate the menu for us. We ordered; the food was served; everything was good. While we ate, a steady stream of well-wishers entered. Traditional Colombian songs were played live on guitars, and everyone was singing. As we finished and paid the bill, I saw, in the owners' faces, pride in what they had already accomplished and faith in the promise of America. I, too, was proud that our little country could still kindle the dreams of a new wave of immigrants.



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