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US stocks likely to continue grinding higher into 2025

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The S&P 500 started the final month of 2024 by hitting a fresh record high, leaving the index up 26.8% so far this year. With the latest Conference Board consumer survey showing confidence that stock prices will increase at a 37-year high, investors may fear that markets are getting frothy.

The market's performance so far this year is backed by solid fundamental drivers. CIO believes US stocks will likely continue grinding higher into next year. In our view, the exuberance synonymous with frothy financial markets is far from widespread.

There is a lack of exuberance about the real economy. While most investors are optimistic about the macro outlook, consumer and business sentiment indicators are well below their peaks in prior cycles. Inflation has been challenging for many consumers, while high input and financing costs are a headwind for small businesses. In fact, the overarching market narrative this year has swung between soft landing, stagflation fears, and hard landing concerns. The policy risks associated with the incoming Trump administration are also keeping investors at least slightly on edge. While this isn't a necessary condition for market frothiness, investor euphoria is hard to achieve and sustain when public sentiment about the economy is not similarly optimistic.

M&A and IPO activities have remained relatively muted. Mergers and acquisitions (M&A) have increased this year. But the total value of all deals as a percentage of total market capitalization remains below the historical average. Deals are a sign of management confidence in the economy and their own company, and lukewarm M&A activity shows that sentiment is far from overheating. While corporate activity is likely to increase in 2025, we think that it may just improve to levels in line with the historical average.

Investors have not exhibited excessive optimism over the outlook for the tech sector, in our view. While the growth story of artificial intelligence (AI) has helped drive the stock rally this year, the recent performance doesn't signal exuberance. The Magnificent 7 have lagged the rest of the market since early July, and the Philadelphia Semiconductor Index has underperformed the S&P 500 by over 20% in the past six months. More telling is that baskets of non-profitable tech stocks, which are at the whim of speculation over future earnings, are still 60% below their peak, after increasing 400% in the first year of the pandemic. True market euphoria will return only when investors begin to create narratives to justify extreme valuations for the most speculative companies.

So while we expect bouts of volatility and corrections in the year ahead, we continue to believe that the S&P 500's next leg up to our December 2025 target of 6,600 will be fueled by solid economic growth, the Fed's easing, and AI advancement. Within the US equity market, we favor technology, utilities, and financials.

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Original report: [US equities show few bubble signs amid record highs, 3 December 2024.](#)

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