Domestic Equities

Large Cap

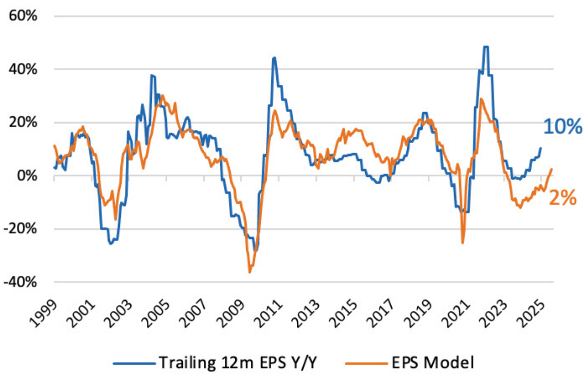
Touchstone Investments®
DISTINCTIVELY ACTIVE®

Authors: Crit Thomas, CFA, CAIA / Erik M. Aarts, CIMA / Brian Cheyne, CFA, CIMA

March 11, 2025

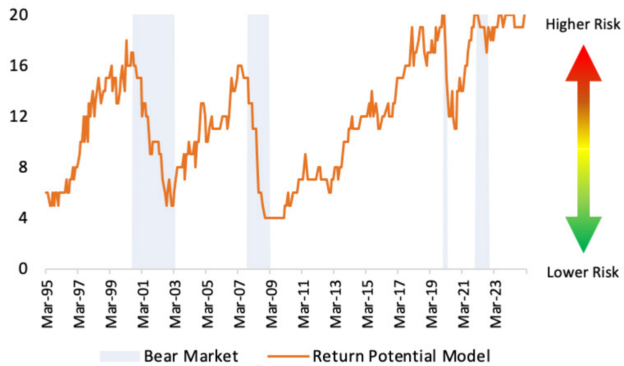
- We reduced our large cap exposure to neutral, reallocating toward investment grade fixed income and developed non-U.S. assets. Recent government statements acknowledging potential economic pain prompted us to reassess our 2025 assumptions.
- While 2025 S&P 500 earnings estimates continue to decline, we believe they could fall further. Policy shifts aimed at downsizing the government, restricting immigration, and using tariffs as a stick to reshore manufacturing may weigh on corporate earnings. Analysts currently project 10% earnings growth, but we see potential for low single digit gains.
- We believe that significant tariff actions, and likely retaliatory measures, could dampen exports, weaken demand for U.S. goods and services, and pressure corporate profits, equities, and the broader economy.
- Consumer surveys indicate potential cracks in resilience. February's consumer confidence survey posted its sharpest decline in four years, marking a third consecutive monthly drop. Consumers expect long-term inflation to be higher than pre-pandemic levels. While we prioritize hard data (actual spending), we remain attentive to sentiment trends.
- We may need to further adjust our positioning if small cracks in the economy deepen into a recession (not our base case). Conversely, signs of economic stress could lead to a quick reversal in policy implementation; the backdrop remains quite fluid.

Touchstone S&P 500 EPS Model



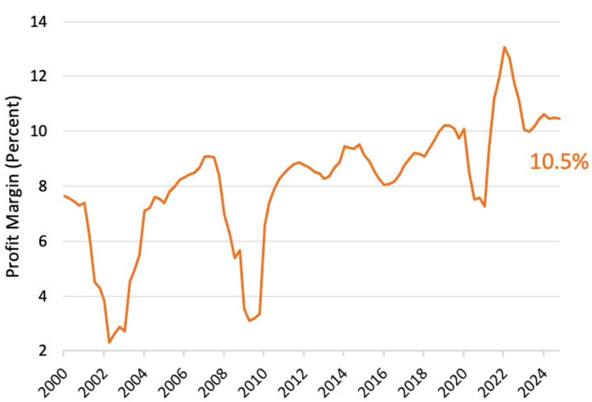
Source: Bloomberg. EPS Model looks forward 7 months, actual EPS through Feb 2025; Model composed of 10y Yield, LEI, and Mfg New Orders

Touchstone Fundamental Equity Risk Model



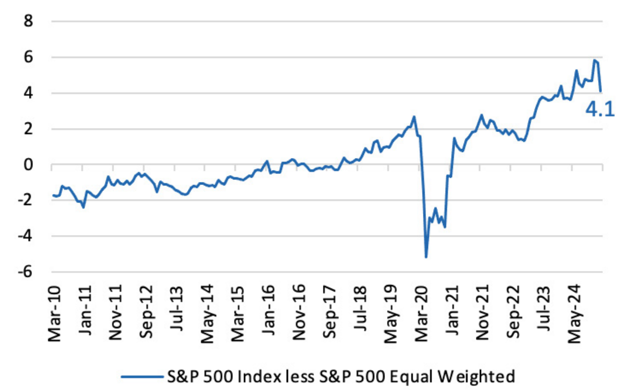
Source: Bloomberg. 30 years of monthly data through Jan 2025; Risk model based on S&P 500 Index valuation metrics (EV/EBITDA, P/S, P/CF) profit margins, Unemployment Rate and LEI.

S&P 500 Index Profit Margin



Source: Bloomberg. 25 years of quarterly data through Mar 2025

Forward P/E Multiple Difference



Source: Bloomberg. 15 years of monthly data through Feb 2025

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Growth and Value

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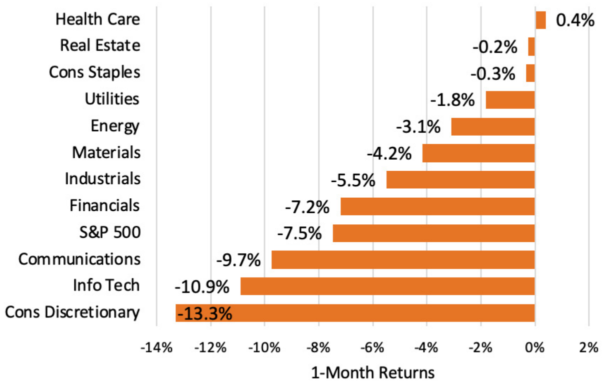
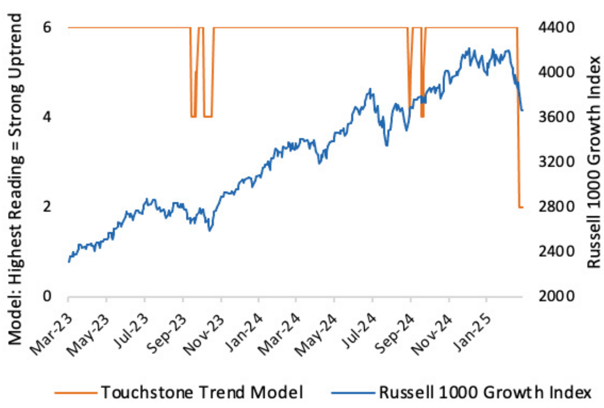
- In early March, we reduced our slight Value overweight to neutral while maintaining a moderate underweight in Growth stocks.
- Concerns over economic risks drove our Value exposure adjustment. Value stocks are more economically sensitive and reliant on imported inputs like steel and aluminum, making them vulnerable to trade disruptions.
- Value stocks, as measured by the Russell indices, outperformed Growth by about 6% through February, largely due to falling Growth valuations.
- Industrials and Health Care, two of the largest Value sectors, are projected to post stronger earnings growth in 2025 as they rebound from 2024 declines. Both should benefit from wider margins.
- Growth earnings remain strong, but sentiment has weakened, reversing some recent multiple expansion. This shift was triggered by DeepSeek, a Chinese AI model challenging U.S. technology dominance. Additionally, ongoing antitrust scrutiny and across the board tariffs on China signal a shift in Trump's approach, no longer prioritizing large companies like Apple as he did in his first term.
- The Technology sector is expected to lead 2025 earnings growth with a projected 20% increase, though Apple, Nvidia, and Meta may see slowing momentum. Meanwhile, Consumer Discretionary and Communications Services—home to Amazon, Tesla, and Meta—are expected to grow earnings less than the S&P 500.
- Market concentration remains a concern. While Trump's tariffs focus on goods, potential retaliatory tariffs on services could disproportionately impact Growth stocks.
- If the economy slows meaningfully, our Growth underweight could become a disadvantage, as investors favor growth stocks in a decelerating economy. We will have a better indication of how far the Trump administration is willing to go with Tariffs in early April.

S&P 500 Index Sector Price Returns



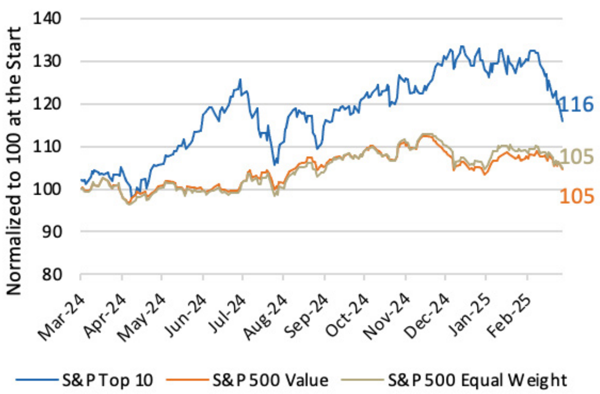
Source: Bloomberg. All data as of Mar 10 2025

Russell 1000 Growth Trend Model



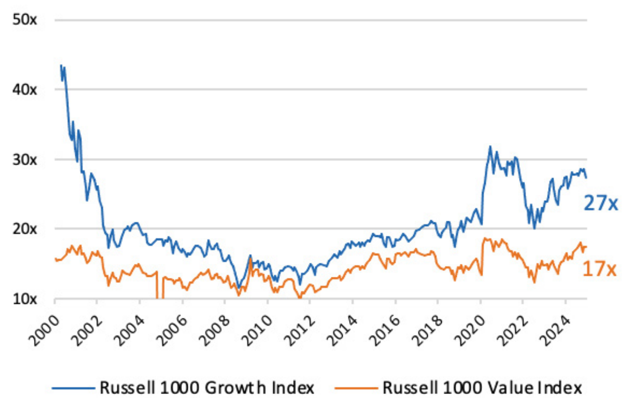
Source: Bloomberg. 2 years of daily data through March 10 2025. Model based on moving averages and price trends

1 Year Price Returns



Source: Bloomberg. 1 year of daily data through Mar 10 2025

Price/Earnings Ratios: Forward 12 Months



Source: Bloomberg. 25 years of monthly data through Feb 2025

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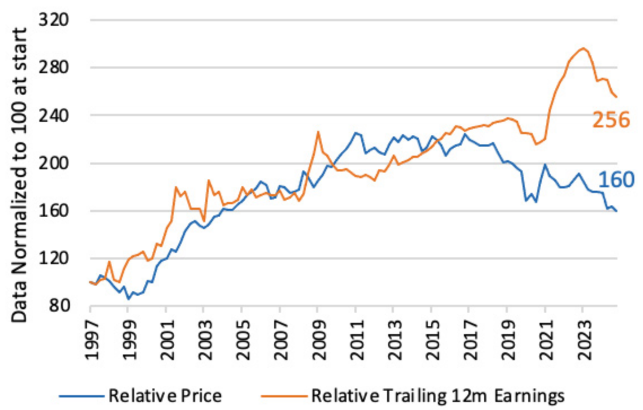
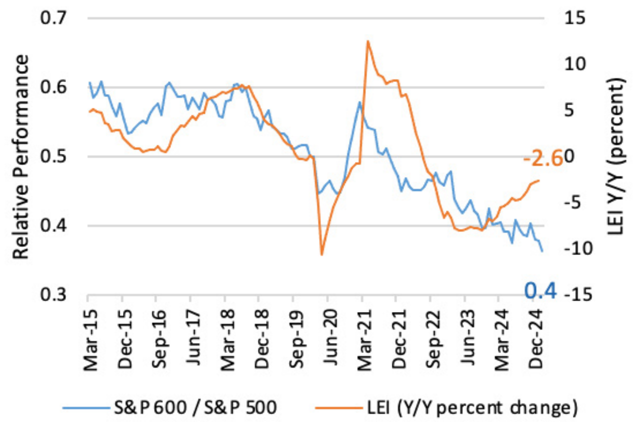
- We lowered our small cap weighting from neutral to a slight underweight while keeping a mid cap overweight. Reduced earnings growth expectations and greater cyclical exposure drove this decision.
- Nearly half of small cap sectors are expected to see earnings decline in 2025, compared to just one sector in mid caps and none in large caps. Small cap earnings growth is projected at under 7%, but downside risks remain if economic stress intensifies.
- Cyclicality remains a key challenge: nearly 50% of the S&P 600 Small Cap Index is in cyclical sectors, compared to under 30% for large caps. Historically, small caps have been more sensitive to economic downturns.
- Mid caps, while also exposed to cyclicality through Industrials and Financials, benefit from stronger balance sheets and comparable valuations, supporting better relative performance. Additionally, mid caps are less sensitive to interest rates and have greater access to capital markets.
- Mid caps have maintained higher relative quality, as measured by return-on-equity (ROE), versus small caps. Over the past two years, small cap ROE has declined more than 50%, while mid caps have held up better.
- Entering 2025, we expected an uptick in M&A activity, but uncertainty around tariffs and the economy has stalled dealmaking, a trend likely to continue. Tax reform appears months away, and any eventual cuts will likely be far smaller than those in 2017.
- Inflation remains the key swing factor. A faster-than-expected decline could give the Fed room to cut rates and lower financing costs. Long-term rates have edged down recently, slightly improving housing affordability.

S&P 400 Index / S&P 500 Index



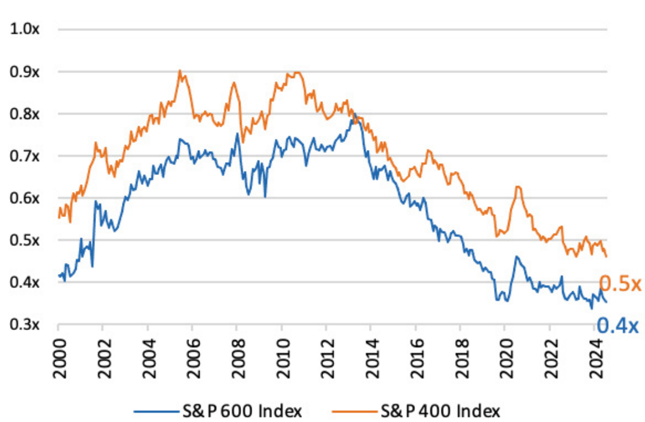
Source: Bloomberg. 28 years of quarterly data through Dec 2024

Small Cap Cyclicality



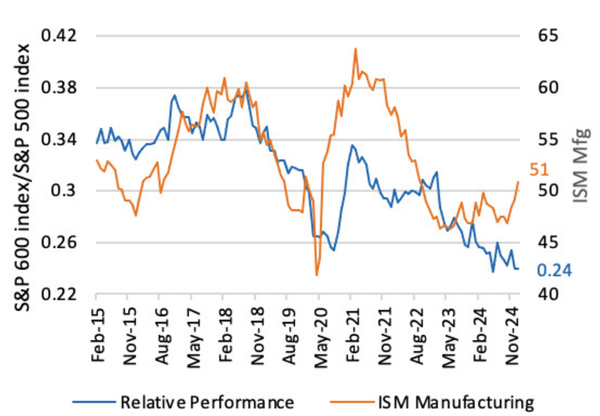
Source: Bloomberg. 10 years of monthly data through Feb 2025, LEI through Jan 2025

Price/Sales Relative to S&P 500 Index



Source: Bloomberg. 25 years of monthly data through Feb 2025

Small Cap Cyclicality



Source: Bloomberg. 10 years of monthly data through Feb 2025

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Market Characteristics

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The Indexes mentioned are unmanaged statistical composites of stock market or bond market performance. Investing in an index is not possible.

Total Returns

							EPS Growth Estimate	
	February 2025	YTD	2024	2023	2022	2021	2024	2025
S&P 500 Index	-1.3%	1.4%	25.0%	26.3%	-18.1%	28.7%	11%	10%
S&P 500 Index Equal Weighted	-0.6%	2.9%	13.0%	13.8%	-11.5%	29.6%	6%	7%
S&P 500 Value Index	0.4%	3.3%	12.3%	22.2%	-5.3%	24.9%	8%	8%
Russell 1000 Value Index	0.4%	5.1%	14.4%	11.4%	-7.6%	25.2%	0%	8%
S&P 500 Growth Index	-2.9%	-0.3%	36.1%	30.0%	-29.4%	32.0%	7%	14%
Russell 1000 Growth Index	-3.6%	-1.7%	33.4%	42.7%	-29.1%	27.6%	25%	16%
S&P 400 Index	-4.3%	-0.7%	13.9%	16.4%	-13.1%	24.8%	2%	8%
S&P 600 Index	-5.7%	-3.0%	8.7%	15.9%	-16.1%	26.8%	-7%	7%
Russell 2000 Index	-5.3%	-2.9%	11.5%	16.9%	-20.4%	14.8%	-18%	30%

Valuations

	P/E (TTM)	Percent Rank	P/E (FTM)	Percent Rank	P/CF	Percent Rank	P/S	Percent Rank
S&P 500 Index	25.4x	85%	19.6x	81%	20.4x	98%	3.2x	98%
S&P 500 Index Equal Weighted	19.9x	68%	15.5x	56%	13.6x	91%	1.6x	71%
S&P 500 Value Index	21.0x	92%	16.6x	97%	16.5x	92%	2.1x	100%
Russell 1000 Value Index	19.7x	83%	15.6x	80%	15.2x	93%	1.9x	95%
S&P 500 Growth Index	32.0x	89%	23.6x	86%	26.6x	99%	5.8x	94%
Russell 1000 Growth Index	34.4x	82%	24.6x	78%	27.0x	93%	5.8x	99%
S&P 400 Index	18.7x	25%	13.7x	19%	11.2x	47%	1.4x	88%
S&P 600 Index	18.6x	23%	12.7x	12%	9.7x	21%	1.1x	77%
Russell 2000 Index	39.8x	76%	17.8x	37%	4.3x	0%	1.4x	94%

Fundamentals

	Dividend Yield	Percent Rank	Profit Margin	Percent Rank	ROE	Percent Rank	Net Debt / EBITDA	Percent Rank
S&P 500 Index	1.3%	9%	10.9%	95%	18.3%	96%	1.4	15%
S&P 500 Index Equal Weighted	1.9%	59%	6.1%	50%	11.7%	57%	2.6	53%
S&P 500 Value Index	1.9%	15%	8.5%	92%	14.1%	91%	1.8	24%
Russell 1000 Value Index	2.0%	13%	8.1%	81%	12.4%	58%	1.9	13%
S&P 500 Growth Index	0.6%	16%	17.3%	94%	29.1%	86%	0.6	15%
Russell 1000 Growth Index	0.6%	7%	15.7%	100%	35.3%	96%	0.6	6%
S&P 400 Index	1.5%	53%	6.1%	89%	10.9%	60%	2.0	7%
S&P 600 Index	1.7%	88%	3.0%	42%	4.9%	25%	3.5	79%
Russell 2000 Index	1.4%	48%	0.9%	26%	1.2%	25%	4.6	83%

For Index Definitions see: TouchstoneInvestments.com/insights/investment-terms-and-index-definitions

Source: Bloomberg. Percent ranks are based on 30 years of monthly data as of the end of February; EPS growth estimates based on consensus bottom-up analyst estimates

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The Touchstone Asset Allocation Committee (TAAC) consisting of Crit Thomas, CFA, CAIA – Global Market Strategist, Erik M. Aarts, CIMA – Vice President and Senior Fixed Income Strategist, and Brian Cheyne, CFA, CIMA – Senior Investment Strategy Specialist, develops in-depth asset allocation guidance using established and evolving methodologies, inputs and analysis and communicates its methods, findings and guidance to stakeholders. TAAC uses different approaches in its development of Strategic Allocation and Tactical Allocation that are designed to add value for financial professionals and their clients. TAAC meets regularly to assess market conditions and conducts deep dive analyses on specific asset classes which are delivered via the Asset Allocation Summary document. Please contact your Touchstone representative or call 800.638.8194 for more information.

A Word About Risk

Investing in fixed-income securities which can experience reduced liquidity during certain market events, lose their value as interest rates rise and are subject to credit risk which is the risk of deterioration in the financial condition of an issuer and/or general economic conditions that can cause the issuer to not make timely payments of principal and interest also causing the securities to decline in value and an investor can lose principal. When interest rates rise, the price of debt securities generally falls. Longer term securities are generally more volatile. Investment grade debt securities which may be downgraded by a Nationally Recognized Statistical Rating Organization (NRSRO) to below investment grade status. U.S. government agency securities which are neither issued nor guaranteed by the U.S. Treasury and are not guaranteed against price movements due to changing interest rates. Mortgage-backed securities and asset-backed securities are subject to the risks of prepayment, defaults, changing interest rates and at times, the financial condition of the issuer. Foreign securities carry the associated risks of economic and political instability, market liquidity, currency volatility and accounting standards that differ from those of U.S. markets and may offer less protection to investors. Emerging markets securities which are more likely to experience turmoil or rapid changes in market or economic conditions than developed countries.

Performance data quoted represents past performance, which is no guarantee of future results. The investment return and principal value of an investment in the Fund will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be higher or lower than performance data given. ***For performance information current to the most recent month-end, visit TouchstoneInvestments.com/mutual-funds.***

Please consider the investment objectives, risks, charges and expenses of a fund carefully before investing. The prospectus and the summary prospectus contain this and other information about a fund. To obtain a prospectus or a summary prospectus, contact your financial professional or download and/or request one at TouchstoneInvestments.com/resources or call Touchstone at 800.638.8194. Please read the prospectus and/or summary prospectus carefully before investing.

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