Cornerstone Report

Special Report | March 26, 2025 | By: Jerry E. Tuma, MS, CFP®

Topics:

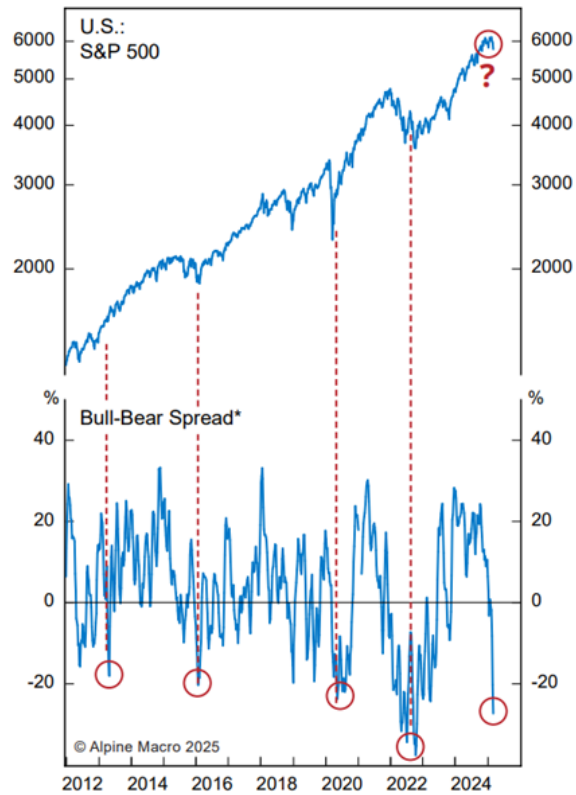
- Long-Term Top Indicators
- Is DOGE a Positive or a Negative?
- Pending Recession?
- Israel vs Iran 2025?

We're Out To Change The Way America Thinks About Investing.

Bear Market Starting?

As you can see in this chart, in the short run, the stock market is very ***oversold***. That means that it's probably gone down too far given the current market and economic conditions. This is typically because of an emotional overreaction by market participants and leverage.

Leverage oftentimes causes extreme market moves in a short period of time. This correction, was about 10% for the S&P 500 and 16% for NASDAQ in just over 2 weeks. The primary ***emotional*** driver of the correction was fear over the impact of President Trump's new tariff wars. But the bigger issue is, has the market topped for the long-term? In other words, is this the beginning of a new bear market and probable recession, versus just a garden variety correction in an ongoing bull market.



*Shown as 4-week moving average; source: AAII Investor Sentiment Survey

My view is that the market has likely topped for the long-term and will soon enter bear market territory. I will explain why in a moment.

I will be very surprised if we do not see a recession within 6 months or so.

We'll discuss the impact of DOGE as well as the tariffs in a moment, but the impact of both plus potential other shocks will almost certainly push us into higher unemployment and some sort of recession this year. DOGE is estimated, by itself to eliminate some 300,000 government jobs not counting peripheral businesses that will be affected by those layoffs. (Typical estimates are that another 2-3 jobs will be affected for every 1 person laid off. See page 6.)

These numbers should easily push us into recession territory, but most will not show up until October, as the vast majority of the DOGE layoffs are actually structured buyouts which will pay the laid-off employee a salary until September. After September they'll go on the unemployment rolls.

The chart to the right shows just how "oversold" the market has become in the short run, reaching levels only seen four times in the last decade.

The analogy I typically use about being oversold is similar to a beach ball being pushed underwater. You can push the beachball down but at some point the pressure to come back to the surface is overwhelming and the ball bounces back.

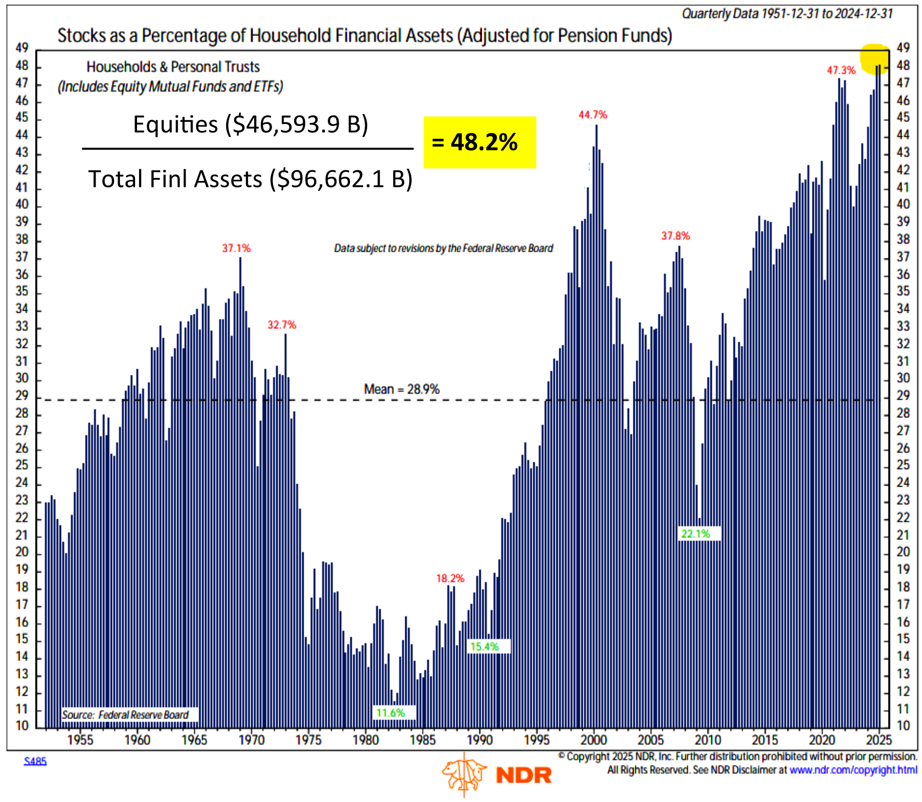
So if I'm guessing, that's where I think we are in the short run, very oversold and likely expecting a bounce, maybe a very big one before anything else is likely on the negative side of the market. We will have to watch and see.

Let's take a look at the longer term outlook for the market and bigger picture items.

Long-Term Top Indicators

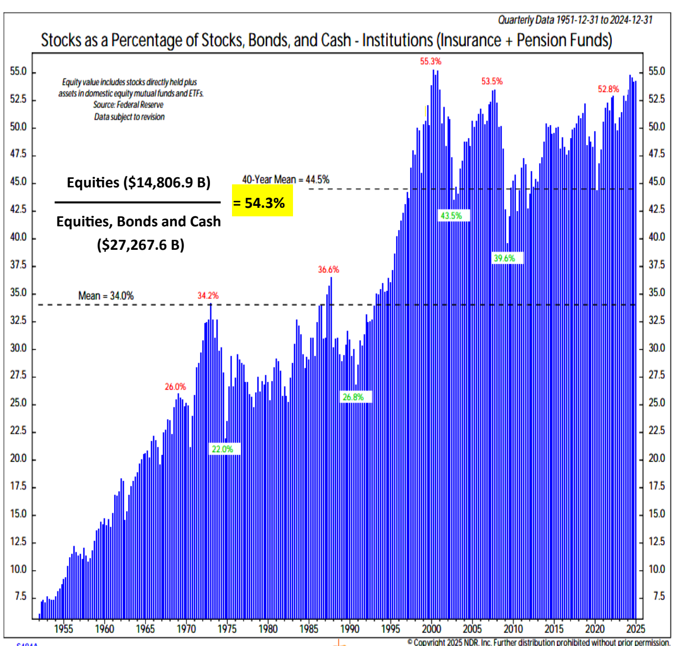
The following series of charts give us excellent perspective as to where we are on a longer term basis with the stock market. One of my long standing complaints about Wall Street and typical investors is that they tend to focus on super short time frames and frequently cannot see the "forest" —long-term outlook—versus the trees.

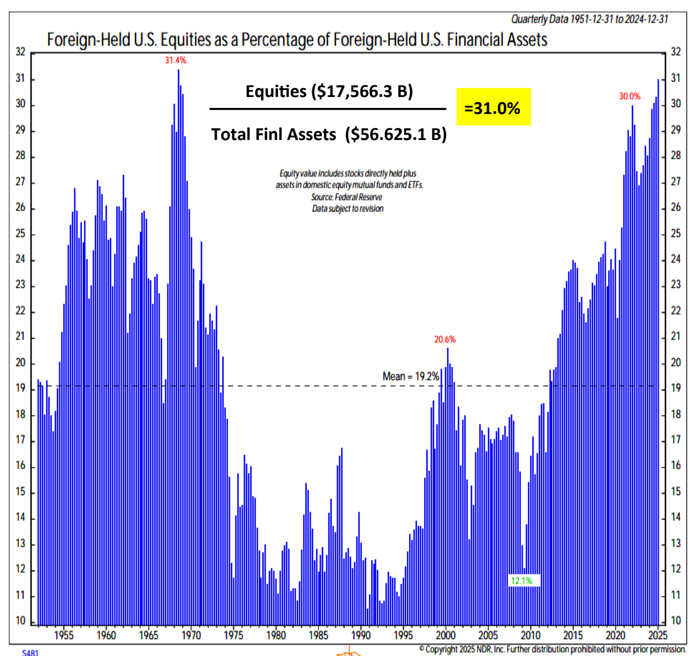
To the right you see a chart going back to 1950, showing stocks as a percentage of household financial assets and you can see that we've hit an new all time high for the ***past 75 years!*** This certainly speaks of "irrational exuberance" to me.



The next chart shows in similar fashion a percentage of stocks held in institutions versus other financial assets and it is very close to the all time high that was hit in 2000 during the dot com mania.

The third chart shows foreign held U.S. equities also at an all-time high. One of the things that we know based on past experience is that when foreign investors jump on the bandwagon pertaining to U.S. stocks, this typically peaks just about the top of the bull market. This looks likely to be happening again.





Longer term indicators will never give ***precise timing*** on the top or on the bottom of any cycle. You have to look at the “30,000 foot altitude level” to see the bigger picture. As I stated before, typically most of Wall Street and many advisors derive their compensation from short-term performance targets i.e. quarter to quarter results.

And while companies attempt to “guide” analysts with an outlook for the next 6 months or longer, the most dominant view typically revolves around quarter to quarter expectations.

At the end of December, the consensus of Wall Street analysts was that earnings would grow at an 14% annualized rate for the calendar year of 2025. Those estimates have steadily been falling, down to 10%, which means that if earnings are going to be coming in at a much lower level then stocks are “not worth as much.”

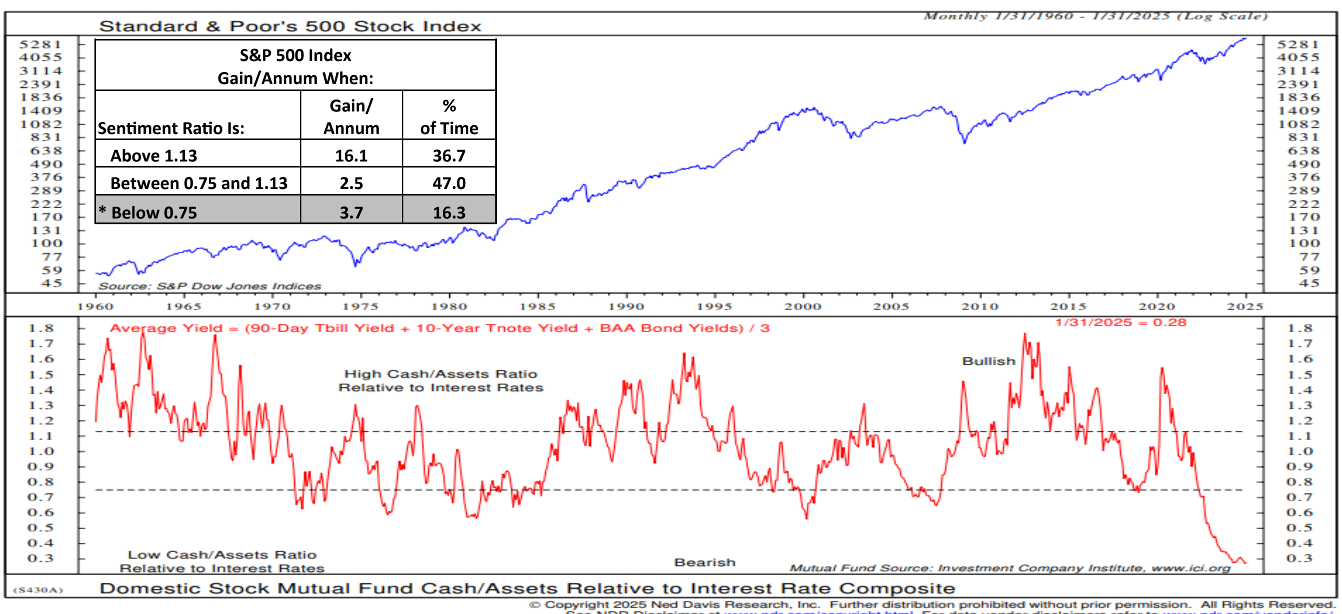
So, Wall Street earnings expectations falling takes a big tailwind away from the market for the immediate future. But the bigger question remains, but what about a potential recession?

In recessions, you don’t just have lower levels of earnings, that is earnings rising at a slower pace, but still rising. Recessions typically create ***losses*** for many companies and industries. So for market expectations to go from a high rate of growth to a slower rate of growth is one thing, but the potential for outright losses is an entirely different matter and typically causes an ***extreme*** drop in the market.

So, if we assume that this is not a super bear on the way (like 2008) then a typical bear might be in the 30-35% range. In other words, it is not likely a once in a generation type of crash, but it’s still likely to be meaningful.

Remember that from investment math a 30% decline in your stock account requires a 43% gain to make it back and this doesn’t count the emotional turmoil involved.

So, while you can never rule out the potential for a 2008 type scenario, right now I don’t see anything that would justify that level of a crash unless geopolitics (Israel vs Iran) gets out of control. We’ll talk about the risks there later in the newsletter. Here’s a few more charts.



The chart above shows the percentage of cash that mutual funds are holding in their portfolios. This represents “dry powder” that is available to go into stocks.

Seeing mutual funds cash to stock ratio at such an extreme low level gives more credence to the fact that we likely are at or near a long-term top. - Ned Davis March 2025

Bear Market Starting?

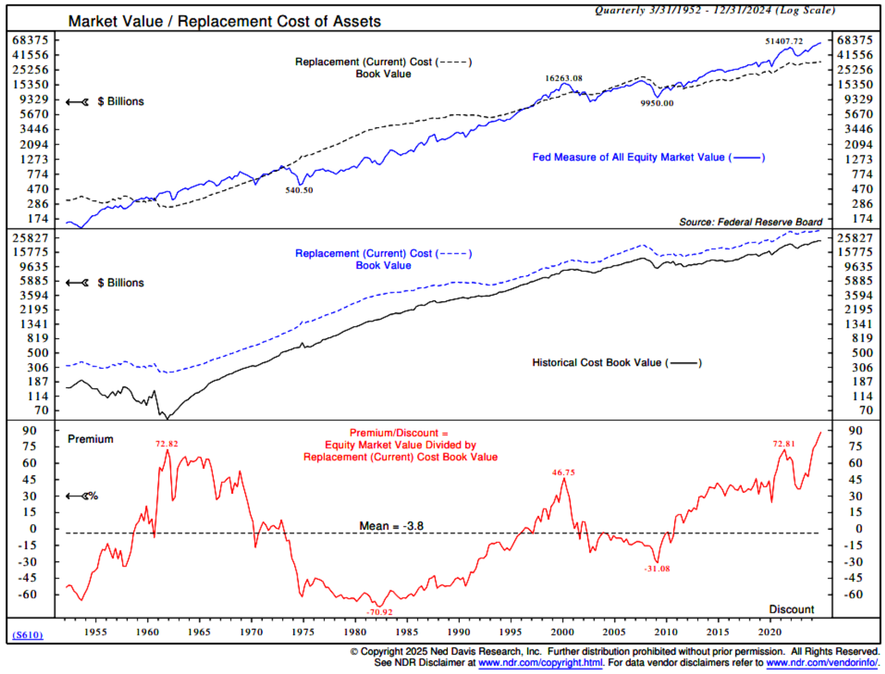
The next chart shows market value versus replacement cost of the assets which is also at a ***75-year high!***

The legendary Sir John Templeton labeled the top of the bull market as the point of maximum optimism.

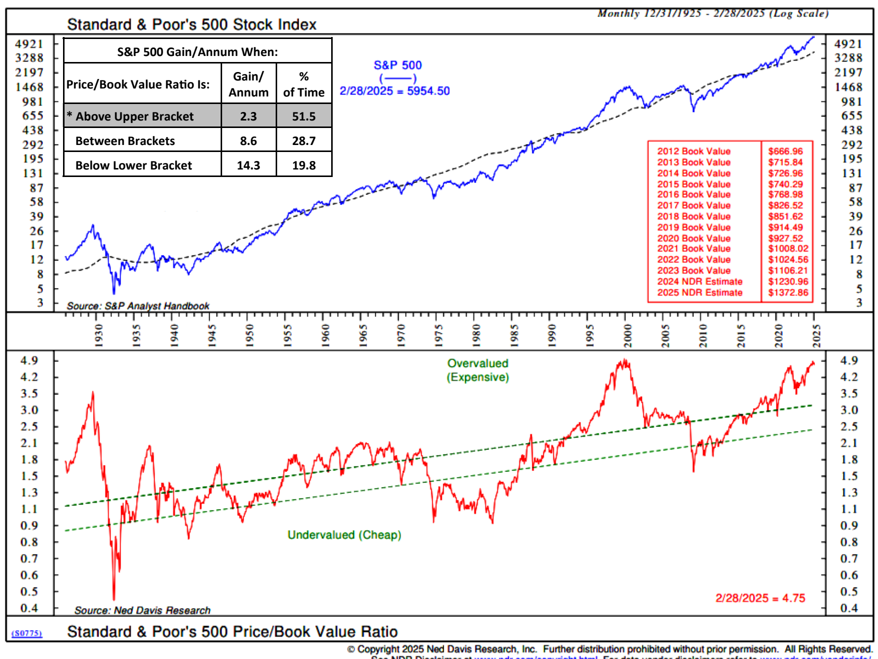
In this he stated that, in every cycle you reach a point of "maximum optimism" where economically and marketwise things look like they're going to be positive, off the charts forever.

This point of maximum optimism occurs in every cycle.

I believe we're at that point now. - Jerry Tuma March 2025



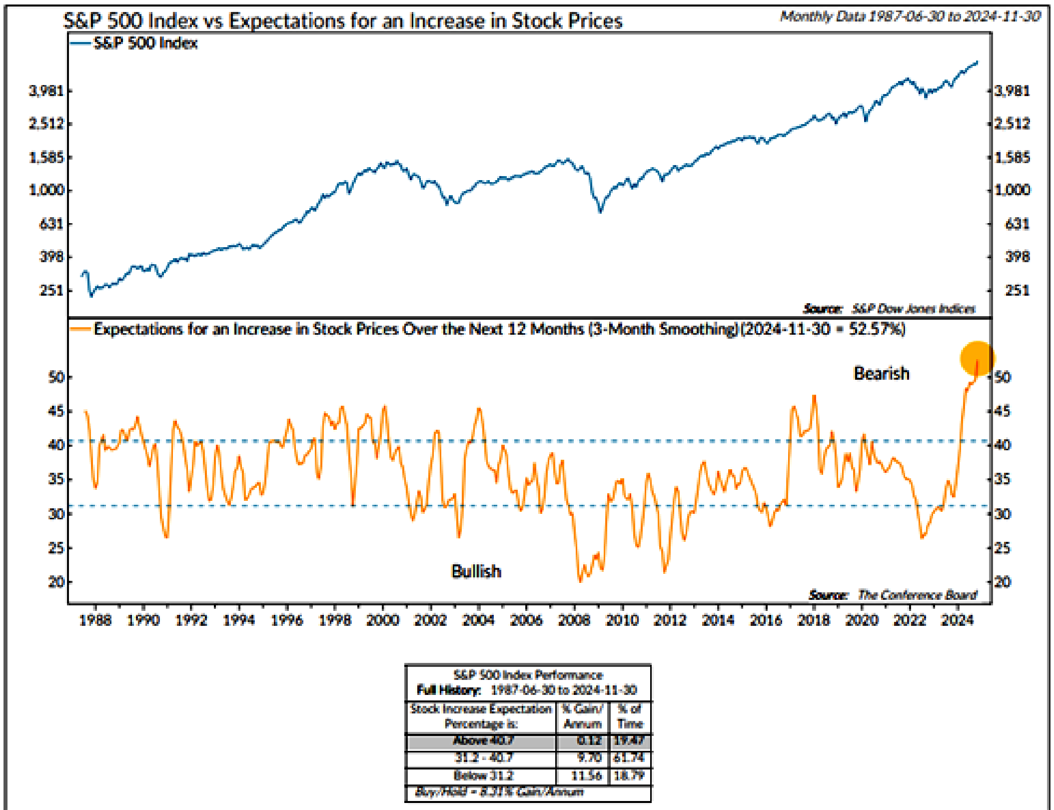
Next is the S&P price to book value ratio at an all-time high and ***this chart goes back to the 1920's!***



In conclusion, I see a sentiment/valuation bubble in stocks. When everyone turns bullish, the question needs to be asked, "Who is left to buy?" – NDR December 2024

The Conference Board surveys consumers about their attitudes toward stocks. The latest survey showed a record bullish outlook on stocks, which has historically been bearish for stocks. – Ned Davis Senior December 2024

The top of the market is the point of maximum optimism, as investors get fully invested. With this much optimism, one must ask how much liquidity is left around to buy. - NDR March 2025



S&P 500 Index Performance Full History: 1987-06-30 to 2024-11-30		
Stock Increase Expectation Percentage is:	% Gain/ Annum	% of Time
Above 40.7	0.12	19.47
31.2 - 40.7	9.70	61.74
Below 31.2	11.56	18.79
Buy/Hold = 8.31% Gain/Annum		

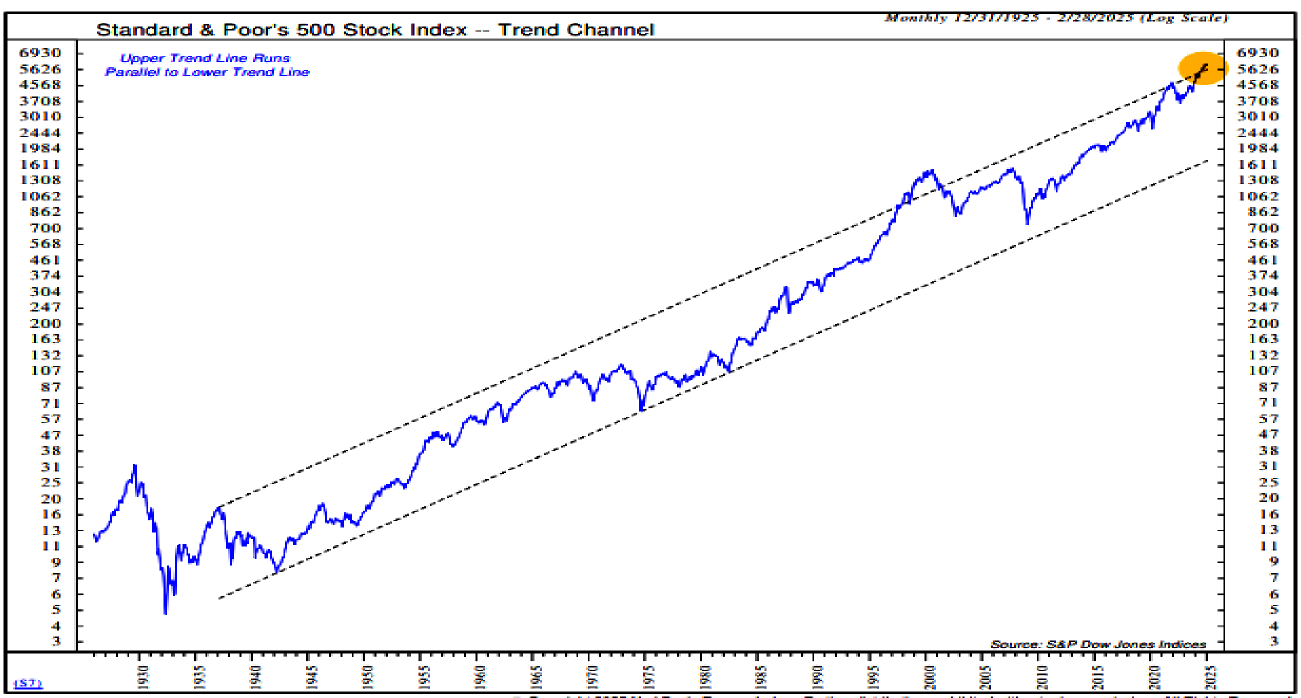
On the left you see investor's expectations over the next 12 months, which are the highest on record.

As the previous quotes from Ned Davis and myself points out this is typically a bad sign for the market.

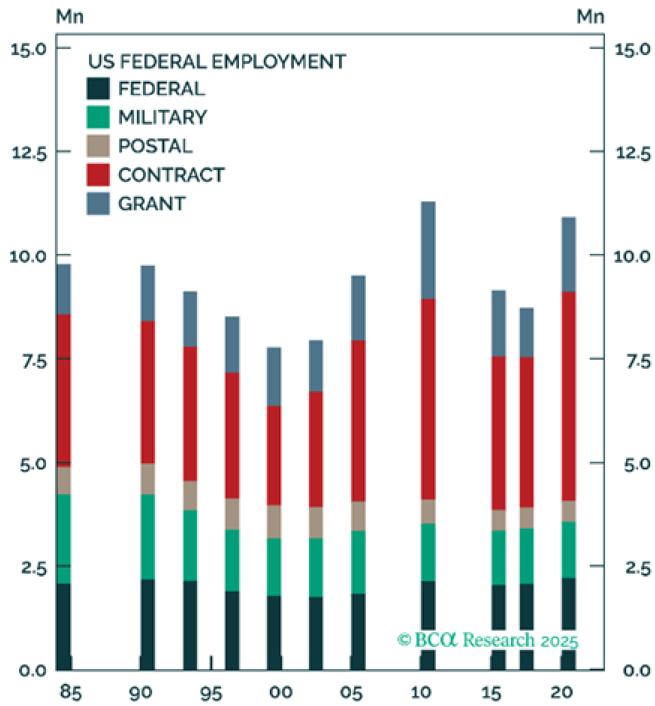
Excessive optimism frequently means that investors are "fully invested" and are not likely to continue to invest large amounts back into the market.

Typically this means a market correction is afoot or a bear market soon.

The final chart shows the S&P 500 trend channel going back to the 1920's. While nothing is ever certain about the market, the fact that the market has apparently peaked above the 100 year trend channel, leaves you to wonder how much more upside there is left in this cycle.



Is DOGE a Positive or a Negative?



SOURCE: PLEASE SEE PAUL C. LIGHT, "THE TRUE SIZE OF GOVERNMENT IS NEARING A RECORD HIGH," BROOKINGS INSTITUTION (OCTOBER, 7, 2020).

The stated goal of President Trump, Elon Musk and DOGE is to cut $1 trillion of spending out of the Federal government's budget. While I am all in favor of getting rid of corruption, waste, etc. and clearly this will benefit us over the longer term, in the short-run the layoffs involved will have a ***slowing*** effect on the economy.

Job losses lead to reduced consumer spending, as those persons laid off cut their budgets, and in turn reduced consumer spending slows the economy down. If Elon and Trump are successful in cutting a significant amount of jobs, waste, etc. ***$1 trillion in budget cuts amount to approximately 14% of the government's entire budget!***

In addition to the people who get laid off, is the ripple effect of others that will be directly affected by their job losses. Typically, economists estimate that for every one job lost, it will affect two or three other jobs as reduced consumer spending hurts other industries. In other words, one job loss equals the economic equivalent of three people not buying houses, cars, etc. The ripple effect of mass layoffs is quite stunning.

So, while these efforts, in my view, need to be applauded for the long-run, they will create uncertainty and a slower level of consumer spending in the short-run, likely helping facilitate a recession.

The chart above shows that estimates of the DOGE layoffs will not just affect the 300,000 federal employees that are being directly laid off or terminated. Private estimates are that this could affect up to 10 million people which is huge out of a U.S. workforce numbering 170 million.

If you factor in that laid-off workers will spend less money and that in turn affects all the people that they buy from, i.e. buying less expensive groceries, fewer times to go out to eat, no new car buying, or new houses, etc.

Thus, a large swath of layoffs of this magnitude will almost certainly have a much more negative effect on the economy than most people seem to be anticipating.

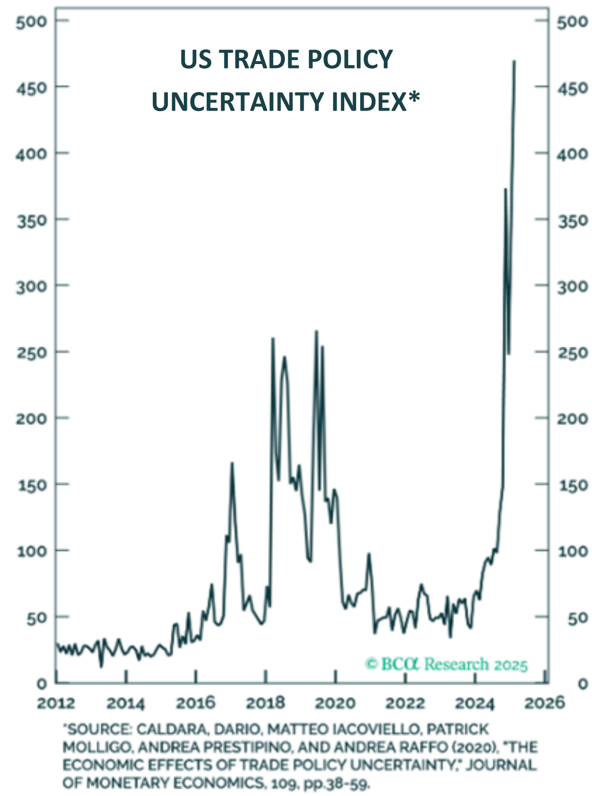
As previously stated, the bulk of these layoffs don't fully take effect until October, thus the rapid acceleration of the unemployment rate, which typically happens in a recession may not really hyper-accelerate until this fall.

In a Friday morning interview with CNBC, Treasury Secretary Bessent warned that the economy isn't as robust as it may appear to the naked eye. "Could we be seeing this economy that we inherited starting to rollover a bit? Sure. Look, there's going to be a natural adjustment as we move away from public spending by the government to private spending in the private sector."

In line with our view that the depletion of excess pandemic savings will eventually stifle a key tailwind, Bessent said, "The market and the economy have just become hooked, and we've become addicted to this government spending. There's going to be a detox period."

The shift in tone suggests that DOGE initiatives will continue full speed ahead. -BCA March 2025

Pending Recession?



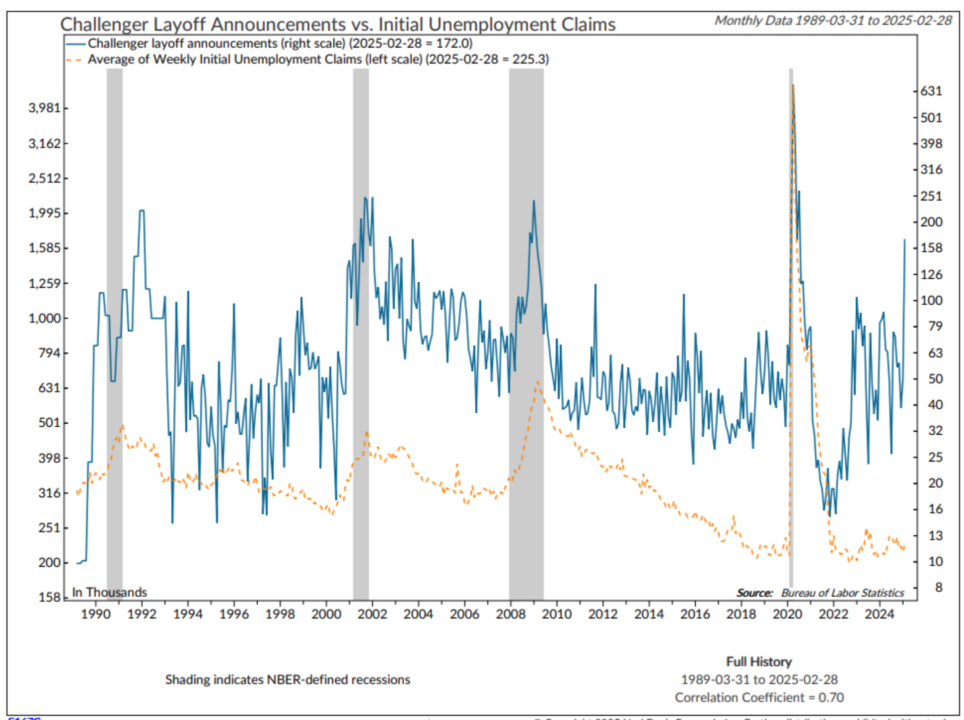
To the left you see a chart showing the full extent of the uncertainty created by President Trump's tariff war. I agree with him on most of the issues, it does appear that previous administrations have allowed other countries to take advantage of us in terms of tariffs, etc. There is no question that uncertainties and fears pertaining to these tariffs have a negative effect on the economy in the short run.

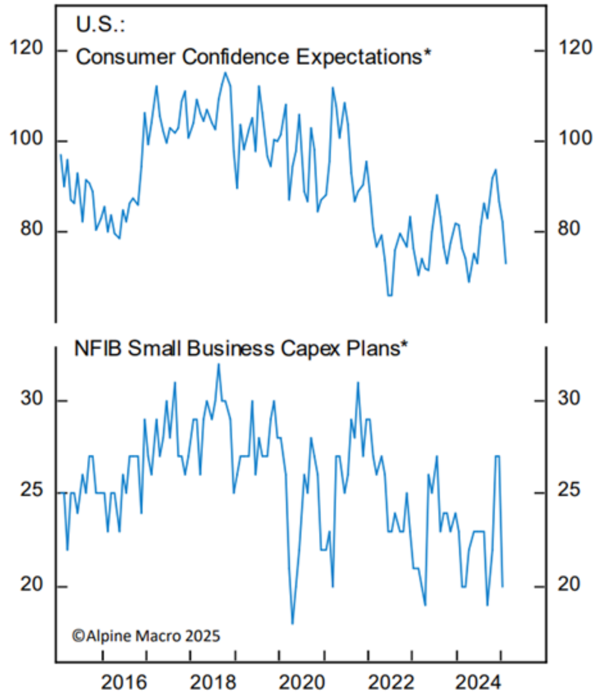
Consumers may decide not to buy a new home or new car. Corporations defer expansion plans or cancel them all together. In the short run, there is nothing positive for the economy and thus the stock market about a tariff war and President Trump appears to be ***dead set*** to take these other countries to the mat over the apparent iniquities of the present structures.

So while these ***adjustments need to be made for the long run,*** in the short run they are certainly negatives for the economy and the stock market.

The next chart shows anticipated layoffs announced by Challenger, which deals with the private sector. Note, this has ***nothing to do*** with the government sector due to DOGE, ***but private sector employees***. Note as well that the layoff announcements are now approaching 2008 levels, certainly not as high as the brief Covid job's crash, but historically extremely high and if these announcements manifest as expected these levels are ***only*** hit during recessions.

Trump has said that he is "not looking at the stock market" and admitted that the economy will need to undergo a "period of transition" to adjust to higher tariffs. – BCA March 2025





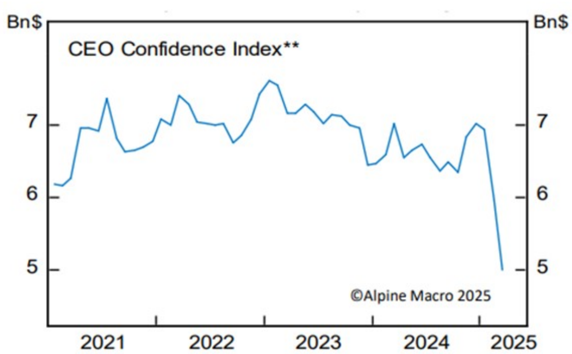
*Next three to six months
Source: Conference Board

The next chart shows consumer expectations which have tanked, small business expansion plans which have tanked, and CEO confidence which has also tanked.

Not to be outdone, the University of Michigan Sentiment Index has returned to recessionary levels. Thus, everything that I'm seeing is pointing towards ***imminent*** recession starting in the next few months.

My guess would be that unless there is an EXTREME situation developing between Iran, Israel and the U.S. in the Middle East this could be a mild recession.

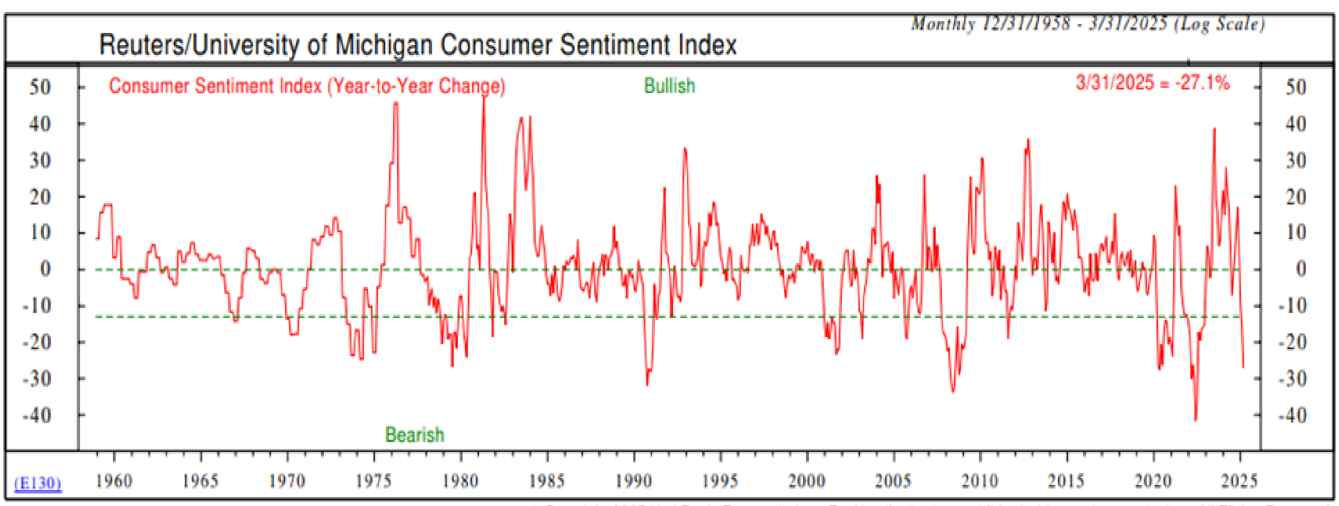
But predicting exactly how the situation might turn out in the Middle East is not something I'm prepared to do.



**Source: Chief Executive Group

Note: that the Michigan Consumer Sentiment Index has now fallen to the lowest levels since Covid and the 2022 recession.

These low levels of consumer sentiment, which help determine whether they buy a new house, new car, etc. are amongst the lowest in 40 years. - Jerry Tuma March 2025



Israel vs Iran 2025?

(Editor's Note: The following is an excerpt from Jerry's radio interview with ***Bank Credit Analyst*** senior political strategist Matt Gertkin. Go to our website at www.cornerstonereport.com for the full interview.)

Jerry: Let's jump into something explosive. I literally did a double take, having to go back to reread what you said. You've never been a sensationalist. Your analysis has been spot on and extremely accurate.

You discussed the odds of a ***black swan event*** — something you can't necessarily predict — but if it happens it has an outsized impact on the world economy.

When I read your ***Five Black Swans for 2025*** newsletter, the cover shows Iran's nuclear program taking flight. I'm not a nuclear expert, but before Trump took office in 2016, it looks like they were around 300 or 400 nuclear centrifuges ***and now they have 12,000 of them!***

You said the ***odds of Israel attacking Iran in 2025 was 75%***, that's where I did the double take. I've never seen you put that high of odds on anything. After reading, I agree with your analysis. Please elaborate on what is going on here. It looks like we could have an ***existential problem*** in parts of the Middle East right now.

Matt: Yeah, thank you. I've been following this story my whole career, 18 years of watching this Iran saga about whether Iran can obtain a nuclear weapon. From their perspective, they believe they need a nuclear weapon to secure their regime over the long term, to make the Islamic revolution permanent. That was the logic that other states used in obtaining nuclear weapons, including China, and most recently we've seen North Korea obtain nuclear weapons after a series of negotiations with the U.S. As soon as the U.S. looked the other direction, North Korea would keep marching in the direction of their strategic objective, and they ultimately obtained it. Now, the dynamic is that the Iranians have learned from this process. They learned that if you're Pakistan or you're North Korea and you really stick to your guns, you will eventually obtain a nuclear weapon.

On the other hand, if you trade it away on promises, you end up looking like Libya or Ukraine, both of which ***gave up nuclear weapons only to be invaded later.*** So, the Iranians have a very clear strategic calculus bent on deterrence. They are also going through some internal problems as well. Ali Khamenei, the supreme leader, is in his mid-80s, he's not going to last very long and is jockeying his son to be his successor. That's a very sensitive time for any regime to be having a succession and simultaneously be under attack by Israel. ***They chose to pursue a conflict with Israel during that sensitive period.*** So there was a question, would they retreat into their turtle shell and sort of hide from the world while they did a power succession? Or would they be aggressive?

Well, we know the answer, because Hamas and Hezbollah and the Houthis have been very active. And that's what provoked Israel to go on this offensive. Well, Israel's now got the upper hand, not only by decimating Hamas and pushing back Hezbollah, but also, ultimately, we saw Syria collapse, which was a keystone to the Iranian strategic agenda in the region. And what this means is that Iran is ***extremely vulnerable*** and the Israelis have a huge opportunity. From Israel's point of view, this is the chance to reassert what is called the Begin Doctrine, to prevent other countries in the region from obtaining nuclear weapons, set back that nuclear program, and also undermine the regime and try to make sure that when this succession process happens in Iran, that it's not just business as usual. Perhaps they will be an opening for real political change in the country. And Israel would be very reluctant to miss this opportunity, and certainly Benjamin Netanyahu would be. But I like to emphasize for listeners, this isn't all about personalities.

If Netanyahu falls from power because of internal political machinations, and suddenly you have a new prime minister of Israel, they still have an historic strategic opportunity to set back Iran and make sure they don't get a nuclear war. And the Americans are involved in this, obviously, because first of all, in order to truly cripple the nuclear program, Israel needs American support. But the U.S. has also said it's a red line that Iran doesn't get nuclear weapons, and that's been under multiple presidencies.

So the issue is that President Trump is interested in negotiating with Iran. He wants to freeze their nuclear program, but he has to start by enforcing the oil sanctions, which President Biden was not enforcing. Then he's putting maximum pressure on Iran. The Supreme Leader said, well, I don't want to talk to Trump. He's not reliable. And Israel's point of view is that it's probably better to ask for forgiveness than permission, meaning that they could escalate the conflict and draw the Americans into the conflict, even more likely if Iran is behind the attempt on President Trump's life.

So, I think this is a true crisis point. I do put a date on it when saying it's in our 12 month forecast that this will be a major crisis. The crisis can be resolved by diplomacy. I would never say never. I would never say that there's no diplomatic solution. But the trends that I've witnessed in the past have convinced me that the diplomatic solution is a lower probability, and that's specifically because the U.S. and Iran did work out a nuclear deal, and it collapsed. From Iran's point of view, the Americans betrayed it.

From the American point of view, the Iranians never intended to really fulfill it in a good spirit, and so I think there's a lack of trust, and I think obviously Israel believes that, especially in the wake of what happened with Hamas. So all of this leads to a critical juncture: conflict. The only way to stop it would be if President Trump uses military, overwhelming military threats to force Iran to freeze their nuclear program. So that means that we should expect the U.S. at some point to threaten Iran in a really significant way, looking as if we are going to attack them. The other thing is that President Trump would also have to restrain Israel saying, "look, I've got this, I'm in control. I can cause Iran to freeze their nuclear program and then that way you don't have to go and do anything unilaterally." And Trump has to do both of those things in order for us to avoid a really major conflict this year. I think the takeaway for investors is, first of all, we'll have the fire and fury when Trump is threatening Iran. Second, Iran will conduct strikes against oil facilities on at least a minor basis to show the risk of confronting Iran. And then third of all, if if things go wrong, well, we may well end up with a big oil shock.

Jerry: Sounds fairly likely. Obviously, we want to always leave room for something to work out. But go back, you said two things have to happen. What are those two things again?

Matt: Trump has to threaten Iran, with a credible threat that the U.S. is willing to conduct airstrikes so that they freeze their nuclear program without us having to do that. And then the second part is he has to restrain Israel. He has to tell Israel, look, the United States is in control of the region and we are going to stop them from getting a nuclear weapon and therefore you do not need to take unilateral action. Those two things are critical and that's going to blow the whole world up this year or maybe not.

I'd just say one thing about methodology and forecasting. Obviously, none of us know what's going to happen in the future. The key thing in putting timeframes on this is what we see is that the Iranians have enough highly enriched uranium to build 10 nuclear devices in one month if they want to. They have not yet made that decision to do that. We also see that conflict has already erupted in the region with Israel and with Iran.

So there are direct hostilities already between the two players. Iran is expanding rather than freezing its nuclear program. And the new U.S. administration is generally quite supportive of Israel and quite hardline on Iran. So those are the ingredients here. Here, whether this all materializes is an open question. But I would say that the urgency is a critical part of the analysis where if Israel misses this opportunity if they wait around for five years, they might have a less friendly U.S. administration. They might have a new regime in Iran. You know, if Iran has a succession process and they've got a new young leader where they're all feeling a lot more confident and Iran might get more weapons support from Russia, and China over that time period...so, that's where we have a window of opportunity that says that this is really a more urgent issue for this year or maybe next year, as opposed to kicking the forecast down the line and saying, oh, at some point there will be a conflict.

Conclusion

In all, it looks to me like we're headed for, what I hope to be a garden variety recession and bear market, not something more severe. Historically, there are no exceptions to the fact that bear markets for stocks accompany recessions. Some bears are worse than others depending on how overvalued stocks are at the beginning and how much leverage is in the system. Other bears can be milder.

Considering that we have hit extremely high levels in terms of valuations and leverage, this could end up being more severe than a 30-35% crash. But right now that would be my best guess. I reserve the right to change my opinion later. ☺

The ***unpredictability of this bear is extreme*** due to unprecedented geopolitical issues in the Middle East. If Israel decides to take Iran's nuclear facility out, there will be ***enormous*** ramifications worldwide.

First, will Israel be successful in a "surgical" strike taking out their nuclear capabilities without extensive damage to the Iranian people and their country? The regime is very unpopular with a high percentage of Iranian citizens, some of which would like nothing better than to see the regime taken out.

Secondly, if it's not a perfect "surgical" strike how much damage will the Iranian regime be able to inflict upon the rest of the world? This could be represented by missile attacks on Israel, but given their poor success ratio in previous attacks it may be better for the regime to close the Straights of Hormuz, a 90-mile stretch of ocean just south of them, where 20-30% of the world's oil supply travels daily.

Thirdly, what other damage/terrorism will Iran's proxies, such as the Houthis and Hezbollah, be able to inflict on others.

Finally, would the Iranian regime be able to survive such an attack if it were a successful? Or would there be another Iranian revolution and a new government installed?

While all of these issues pale in comparison to the potential for World War III between the U.S. and China later this decade or next, this potentially ***represents the biggest geopolitical events of my lifetime.***

As the old Chinese proverb says, "may you live in interesting times," it certainly appears that we do.

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