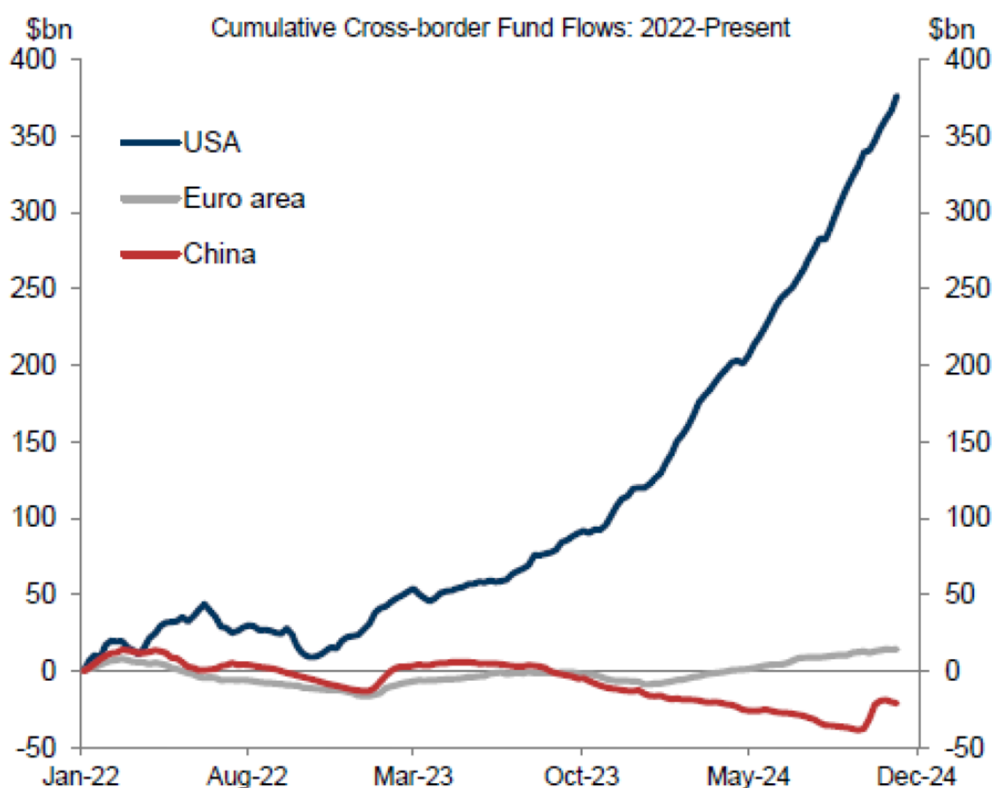
American Exceptionalism

In financial markets today, the term "American Exceptionalism" has gained momentum, and rightly so, as shown in the chart below as well as in U.S. equity market returns compared with the rest of the world. Still, it can be argued that valuation for the S&P 500 is far from *exceptional*.

The chart shows the amount of global capital that has flown around the world and landed in U.S. These flows into both private and public equities, real estate, and fixed income securities dwarf the amounts flowing to other countries, and the gap is growing.



Goldman Sachs, 11/18/24, 2025 Global FX, Stronger for Longer, pg. 1

In 2023 and 2024, the S&P 500 index did something it has done on only nine occasions since the end of the *civil war*: increase by 20%+ in two consecutive years.[1] (Of course most, if not all of these returns were generated by the largest capitalization technology stocks that make up the so-called 'Magnificent Seven'). More on this later.

There are many reasons for this *exceptionalism*. The executional excellence of the U.S. Technology sector, pro-business policy, rule of law, relatively free markets compared with the rest of the world, strength of the U.S. dollar, energy independence, a strong economy, relatively full employment, and moderately accommodative monetary policy, coupled with fear of regulation, leverage, and demographic structural issues in China, lack of acceptable growth in Europe, and wars across the globe. To a very large degree, arguably, flight of capital into the U.S., and the returns of larger capitalization companies has been well earned.

What is even more impressive, is that these returns were accomplished with interest rates and inflation well above averages of the past fifteen years, and with the Federal Reserve trying to temper the strength of the economy.

The stock market only tells one side of the story. In contrast, take a look at the bond market. The long-dated U.S. Treasuries have been selling off, and yields have been rising, even in the face of the Federal Reserve lowering interest rates by 1% over the past four months. As our Chief Investment Officer Robert Kleinschmidt wrote on November 28, 2022, *Thinking the Unthinkable*, is the volatility in the bond market partially the result of the world growing concerned of the debt pile mounting in the U.S. and starting to question the credit quality of the U.S.? Bond investors might be starting to think that maybe the U.S. is not that *exceptional*.

Time Required to Reach Total U.S. Debt Levels

Source: FRED, Strategas, Data as of 12/31/24

Of:	
$10 Trillion	232 Years
$20 Trillion	9 Years
$30 Trillion	4.5 Years
$31 Trillion	8 Months
$32 Trillion	8 Months
$33 Trillion	3 Months
$34 Trillion	3 Months
$35 Trillion	7 Months
Latest Level	***$36.15 Trillion***

Six months on average to reach each additional trillion in debt from $31 - $35.

Source: Strategas Research, “2024 Year-End Review in Charts,” page 5

At year end, the S&P 500 traded at nearly a 35% premium on a Price-to-Earnings (P/E) basis when compared to its long-term average. It is fair to say that a lot has been priced in. But upon closer inspection, most of the U.S. market is not so pricey. The valuation of these bottom, *not so magnificent*, 493 stocks is well within historical averages. Given the nature of the largest companies that sit atop of the index (Apple, Amazon, Microsoft, Google, Meta, Tesla, and Nvidia), much rests on the sustainability of the proliferation of Artificial Intelligence (AI), but for the rest of these companies, a strong economy, enlightened fiscal and regulatory policy, and solid execution can provide for a salutary investment environment.

Value can still be had in U.S. stocks, but sharpening the pencil is required. Value based stocks, healthcare, financials, commodities in general, among others, are trading at attractive valuations.

More chatter is heard through the crowd trying to compare today's environment in stocks to that of 1999. Visions of the future of AI is reminiscent of that of the early internet days. The major difference however is the companies leading the AI charge today are in fantastic shape from a balance sheet standpoint, are generating free cash flow once thought not possible, and are comfortably profitable and growing. Comparing today to past bubbles should be asked only if one believes investors are blindly buying U.S. stocks (and specifically the *Mag 7* for that matter) simply because the relative performance has been so strong over the recent past. AI is predominantly a U.S. story, and is indeed *exceptional*, however when asked if U.S. Tech stocks in particular are attractive from a valuation, the answer maybe far from exceptional.

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Source: [1] JP Morgan, Eye on the Market, 01/02/2025, page 12.

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