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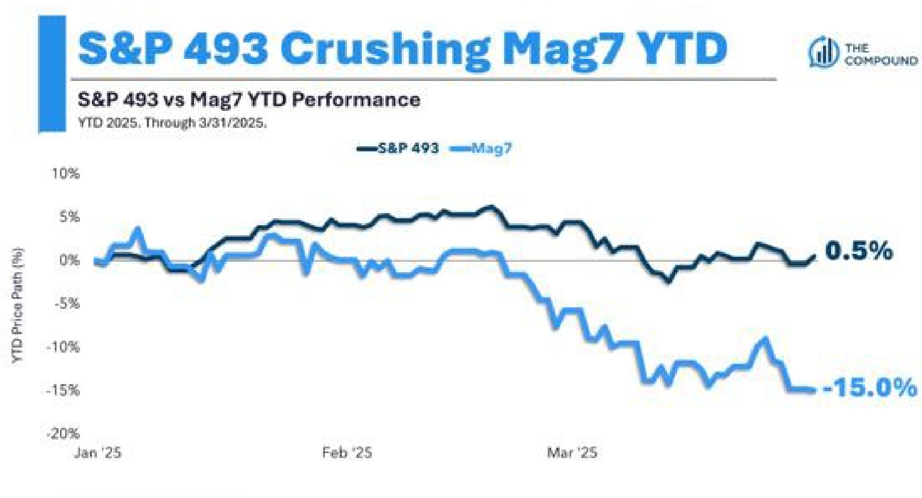
Market Commentary Q1 2025

The first quarter of 2025 saw volatility in markets, primarily due to concerns about slowing growth and the shifting tariff policies. Initially, the S&P 500 gained nearly 6% after Election Day, driven by optimism surrounding pro-growth policies.[1] However, later in the quarter, uncertainty about these factors and their economic impact led to a 10% decline from its peak.[1] By the end of March, the S&P 500 was down 4.3% for the quarter.[1]

Leading US Indices (Total Return)	3Q'23	4Q'23	1Q'24	2Q'24	3Q'24	4Q'24	1Q'25 (sorted)	TTM
S&P/Citigroup Value	-4.1%	13.6%	8.1%	-2.1%	9.1%	-2.7%	0.3%	4.2%
S&P 400 Mid-Cap	-4.2%	11.7%	10.0%	-3.4%	6.9%	0.3%	-6.1%	-2.7%
S&P 500 Total Return	**-3.3%**	**11.7%**	**10.6%**	**4.3%**	**5.9%**	**2.4%**	**-4.3%**	**8.3%**
S&P 100 Mega-Cap	-2.8%	11.7%	11.2%	7.1%	5.1%	4.6%	-6.0%	10.7%
S&P/Citigroup Growth	-2.6%	10.1%	12.8%	9.6%	3.7%	6.2%	-8.5%	10.5%
S&P 600 Small-Cap	-4.9%	15.1%	2.5%	-3.1%	10.1%	-0.6%	-8.9%	-3.4%
Russell 2000	-5.1%	14.0%	5.2%	-3.3%	9.3%	0.3%	-9.5%	-4.0%
Nasdaq	-3.9%	13.8%	9.3%	8.5%	2.8%	6.3%	-10.3%	6.4%

Strategas Securities, LLC – 04/02/2025

As seen in the media, key contributors to the selloff were the highly concentrated and over-valued stocks known as the "Magnificent Seven," which are included in the S&P 500 and Nasdaq among other benchmarks. These stocks saw significant declines of almost 15% in the first quarter.[1] As you'll see above, the Nasdaq was down over 10% for the quarter.[1] The chart below shows the rest of the market (S&P 493) versus those seven stocks through the end of the first quarter, highlighting a stark difference in what has worked in recent years.



Y-Charts – 04/02/2025

Despite these losses, diversified portfolios and other S&P 500 stocks performed better, with seven sectors recording gains, which is largely where we are allocated. International stocks also outpaced U.S. stocks, supported by solid fundamentals in Europe. While bonds delivered steady returns, up almost 3%.[1]

S&P 500 Sectors (Total Return)	3Q'23	4Q'23	1Q'24	2Q'24	3Q'24	4Q'24	1Q'25 (sorted)	TTM
Energy	12.2%	-6.9%	13.7%	-2.4%	-2.3%	-2.4%	10.2%	2.5%
Health Care	-2.7%	6.4%	8.8%	-1.0%	6.1%	-10.3%	6.5%	0.4%
Staples	-6.0%	5.5%	7.5%	1.4%	9.0%	-3.3%	5.2%	12.4%
Utilities	-9.2%	8.6%	4.6%	4.7%	19.4%	-5.5%	4.9%	23.9%
Real Estate	-8.9%	18.8%	-0.5%	-1.9%	17.2%	-7.9%	3.6%	9.6%
Financials	-1.1%	14.0%	12.5%	-2.0%	10.7%	7.1%	3.5%	20.2%
Materials	-4.8%	9.7%	8.9%	-4.5%	9.7%	-12.4%	2.8%	-5.7%
Industrials	-5.2%	13.1%	11.0%	-2.9%	11.5%	-2.3%	-0.2%	5.6%
S&P 500 Total Return	**-3.3%**	**11.7%**	**10.6%**	**4.3%**	**5.9%**	**2.4%**	**-4.3%**	**8.3%**
Communication Services	3.1%	11.0%	15.8%	9.4%	1.7%	8.9%	-6.2%	13.6%
Technology	-5.6%	17.2%	12.7%	13.8%	1.6%	4.8%	-12.7%	5.9%
Discretionary	-4.8%	12.4%	5.0%	0.6%	7.8%	14.3%	-13.8%	6.9%

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U.S. GDP growth slowed to an annualized rate of 1.6% in Q1 2025, reflecting weakening consumer demand and cautious corporate spending.[1] Inflation continues to persist above 3%, driven by service sector price pressures and ongoing supply chain disruptions. The unemployment rate has edged up to 4.5%, indicating a softening labor market.[1]

Growth is slowing, inflation is sticky, and the labor market is holding up while soft data (surveys) is weak. The weakening consumer has been a topic of conversation for investors, and although slowing, we do not see a need for worry, currently. Retail sales came in lower than expected, expanding 0.2% m/m in February with downward revisions for January, but sales are still expanding 3.1% y/y.[1] Meanwhile, savings are up 4% y/y and wage growth is outpacing inflation.[1] Initial jobless claims are tame, and the labor market does not appear to be drastically weakening. Additionally, with bond markets rallying, mortgage rates have followed yields lower. February's housing starts rose 11.2% m/m, and existing home sales rose 4.2% m/m.[1] Lower mortgage rates will entice more home buyers to enter the market.

The U.S. fixed income market had a strong first quarter, driven by falling interest rates and a "flight to quality" amidst economic growth concerns. The Bloomberg Barclays Aggregate Bond Index returned 2.2% in the first quarter of 2025.[1] This reflects a strong performance in the bond market, driven by falling interest rates and a favorable environment for fixed income investments.

Municipal bonds lagged behind Treasuries, but tax-equivalent yields for high earners remained attractive. Overall, the fixed income environment was favorable, with higher yields providing durable income and a buffer against price volatility.

Inflation remains stubbornly above 3%, largely due to persistent service sector price pressures and supply chain disruptions tied to global trade tensions. The Federal Reserve ("Fed") left interest rates unchanged in its first meeting of the year with the Federal Open Market Committee ("FOMC") unanimously deciding to maintain the federal funds rate within the 4.25%-4.50% range. The Beige Book from the Fed showed modest gains in U.S. economic activity, but expectations for a rate cut are still low. However, the latest U.S. inflation figures could shift these projections.

US Yields	4Q'23	1Q'24	2Q'24	3Q'24	4Q'24	1Q'25	Q/Q Chg (bps)	Y/Y Chg (bps)
Fed Funds Target Rate	5.5	5.5	5.5	5.0	4.5	4.5	0	-100
3-Month T-Bill	5.4	5.5	5.5	4.7	4.4	4.2	-12	-121
2-Year Note	4.3	4.6	4.7	3.6	4.2	3.9	-35	-73
5-Year Note	3.8	4.2	4.3	3.6	4.4	4.0	-43	-26
10-Year Bond	3.9	4.2	4.4	3.8	4.6	4.2	-37	0
30-Year Bond	4.0	4.3	4.5	4.1	4.8	4.6	-21	23

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The next FOMC interest rate decision is on May 7 to assess economic conditions and determine any necessary monetary policy adjustments. Currently, it is seen as less likely to deliver interest rate cuts, with short-term rates likely remaining at the current level of 4.25% to 4.5%. However, the potential for rate cuts is growing, as policy whipsawing is causing dents in confidence and uncertainty for businesses and consumers alike.

International markets performed well in the first quarter. UK equities had their best returns since late 2022, driven by better-than-expected corporate results, especially in the banking sector, which posted significant earnings growth.[1] European markets benefited from Germany's approval of a €500 billion infrastructure fund, easing debt restrictions on defense spending, and stimulus measures from China.

International Indices (Price Chg)	3Q'23	4Q'23	1Q'24	2Q'24	3Q'24	4Q'24	1Q'25 (sorted)	TTM
Hang Seng (Hong Kong)	-5.9%	-4.3%	-3.0%	7.1%	19.3%	-5.1%	15.3%	39.8%
IBEX 35 (Spain)	-1.7%	7.1%	9.6%	-1.2%	8.5%	-2.4%	13.3%	18.6%
DAX (Germany)	-4.7%	8.9%	10.0%	-3.9%	6.0%	3.0%	11.0%	16.4%
Swiss Market Index	-2.8%	1.6%	5.3%	2.2%	1.5%	-4.7%	8.6%	7.4%
Bovespa (Brazil)	-1.3%	15.1%	-4.5%	-3.3%	6.4%	-8.7%	8.3%	1.7%
Bolsa (Mexico)	-5.0%	12.8%	0.0%	-8.6%	0.1%	-5.6%	6.0%	-8.5%
CAC 40 (France)	-3.6%	5.7%	8.8%	-8.9%	2.1%	-3.3%	5.6%	-5.1%
FTSE 100 (UK)	1.0%	1.6%	2.8%	2.7%	0.9%	-0.8%	5.0%	7.9%
Kospi (South Korea)	-3.9%	7.7%	3.4%	1.9%	-7.3%	-7.5%	3.4%	-9.7%
Shenzhen SE A Shares (China)	-6.8%	-3.8%	-4.9%	-7.4%	19.1%	1.6%	2.4%	14.7%
MSCI EAFE	-1.9%	4.6%	9.1%	0.0%	0.3%	-0.9%	2.2%	1.6%
S&P/TSX (Canada)	-3.0%	7.3%	5.8%	-1.3%	9.7%	3.0%	0.8%	12.4%
OMX Stockholm 30 (Sweden)	-6.7%	11.2%	5.1%	2.0%	2.2%	-5.5%	0.4%	-1.0%
Sensex (India)	1.7%	9.7%	2.0%	7.3%	6.7%	-7.3%	-0.9%	5.1%
MSCI AC World	-2.9%	9.0%	9.0%	2.9%	4.5%	1.0%	-2.5%	5.9%
All Ordinaries (Australia)	-2.1%	8.0%	4.1%	-1.7%	6.5%	-1.4%	-4.4%	-1.2%
Nikkei 225 (Japan)	-4.0%	5.0%	20.6%	-1.9%	-4.2%	5.2%	-10.7%	-11.8%

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The first quarter of 2025 brought a mix of challenges and opportunities for emerging market investors. Global trade policy uncertainty, particularly around tariffs, created headwinds for many markets. However, emerging markets equities outperformed U.S. stocks during this period, as investors sought diversification and value. Emerging markets benefited from a rotation away from U.S. growth stocks, which faced valuation pressures. Sectors like basic materials and energy saw gains, driven by global demand and favorable commodity prices. Additionally, bonds in emerging markets provided a safe haven for investors amid concerns about slower global growth.

China's economy showed unexpected resilience in the first quarter. Retail sales and industrial output were solid, contributing to strong asset market performance. The Chinese government implemented fiscal support and monetary easing through the People's Bank of China, which helped lift stock market valuations. However, challenges remain, particularly in the real estate sector, where weak property prices and excess supply continue to weigh on household spending and local government finances

As we write this commentary in early April, we wanted to touch on what the recent tariffs could mean for the market and investors (wish us luck)!

President Trump's aim to use tariffs to help bring manufacturing back to the U.S. and address what he identifies as trade imbalances between the U.S. and the rest of the world is impacting markets. What the current trade and tariffs scenario could mean for investors can be viewed in the broader context of evolving policy and regulatory events, many of which are still unfolding. These include tax reform, immigration, and deregulation, among others. One thing that seems clear regarding the reciprocal tariffs announced on April 2 is that lingering uncertainty around them is the biggest risk. Are they essentially a starting point for negotiations or intended to be long-term? While the economic impact of these potential changes for the U.S. economy is expected to be moderate, market volatility is likely to remain elevated and the situation remains fluid.

Our early back-of-the-envelope calculation is that the effective tariff rate equates to over 20%; it has not been above 10% since the 1950s.[1] Here is what we know:

The administration announced a series of reciprocal tariffs on regions and countries with high trade deficits with the U.S., including China (34%), the European Union (20%), Vietnam (46%), Taiwan (32%), Japan (24%), India (26%), and South Korea (25%).[1] The U.S. announced a baseline 10% tariff on countries not specifically targeted, and 25% tariff on imported autos.

There is still considerable uncertainty around the holistic impact and true intent of the reciprocal tariffs. This uncertainty is a bigger risk than the tariffs themselves, given the lack of clarity around duration and who absorbs them (exporter, importer, consumer.) Uncertainty has led to a deceleration of economic activity and may increase the odds of an economic recession over time.

The stated goal of this action is a structural reset of the economy, aiming to rebuild domestic manufacturing by incentivizing production at home, enforcing fiscal discipline through smaller government and lower deficits, and driving corporate and consumer activity to boost domestic economic growth. This approach contrasts sharply with the global free trade model of the past several decades. The current turbulence reflects the economic pain of a possible transition.

With the odds of a recession increasing, investors should be aware that the market may remain volatile as tariffs remain a prevalent topic for businesses and the market. Market multiples (i.e., price-to-earnings ratios for the S&P 500 index) may continue to re-rate lower in this market environment.

The size and rapidity of the tariff announcements prevent firms from adequately addressing supply chain issues and therefore increase the near-term downside risks to growth and upside risks to inflation. In other words, the risk of stagflation rises. Given the uncertainty, we believe the odds of a more stagflationary environment have modestly increased and a more neutral versus fully risk-on positioning may merit consideration.

The impact on economic growth and inflation is dependent on how the "who will pay" breakdown plays out. For example, if supply chains absorb more of the costs, it may be more detrimental to growth (i.e., a lower U.S. GDP growth rate). However, if consumers end up paying more for imported items, that may result in a higher inflation rate.

To fully ascertain the net effects of this breakdown, knock-on effects must be considered. For example, corporate margin compression leading to layoffs may further slow economic growth (but likely would be disinflationary). Also, consumer behavior may lead to the consumption of alternative products not affected by tariffs, or they may seek out substitute products or altogether defer the consumption of a particular product.

The bottom-line impact of tariffs on economic and corporate fundamentals is challenging to conclude. Therefore, investors should remain vigilant and patient, focusing on diversification in their portfolios.

Looking ahead, investors remain cautious about tariffs, inflation, economic growth, and the Fed's potential response in upcoming meetings. Whether we will have a recession or not likely depends on the duration of this shock. Employment data and corporate earnings reports may provide clarity in the near term. While corrections like the 10% drop in the first quarter are normal, they can offer opportunities for long-term investors to rebalance portfolios.

The key is diversification and aligning portfolios with long-term objectives. Though market volatility is unavoidable, investors should remain focused on broader allocations to weather uncertain times effectively. History reminds us that emotional reactions to market volatility often lead to missteps. While no one can predict the future with certainty, we do know that long-term investment strategies have historically weathered even the most turbulent periods.

Our mission is to help you navigate financial complexity with confidence. We encourage you to stay informed, stay strategic, and above all, stay focused on the enduring mission of your organization. We're here to provide guidance and support, please don't hesitate to reach out.

To discuss this commentary further, please contact us at 914-825-8630.

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[1] Y-Charts – 04/02/2025
[2] Strategas Securities, LLC – 04/02/2025