First Quarter Market Update

April 2025

PLAN WITH PURPOSE.

INVEST WITH CONFIDENCE.

POWER
WEALTH MANAGEMENT



Boston Light and Graves Light, Boston, MA

"There are decades where nothing happens; and there are weeks where decades happen."

President Trump made history on April 2nd as he announced tariffs in an apparent effort to re-orient global trade. Tariffs were much more aggressive than anticipated and led to a quick drop in US equities. Later, he announced a 90-day pause on higher reciprocal tariffs, while ratcheting up tariffs on China, and the S&P 500 saw its third best day since WWII. While the longer-term outcome of tariff actions is highly uncertain, and the landscape is quickly evolving, recent volatility highlights the wisdom of diversification, a guiding light in the Power Wealth Management investment philosophy. We also think that the recent market turmoil underscores the need for a thoughtful asset allocation and active management.

Q1'25 Market Performance, Key Drivers, & Go-Forward Outlook

The first quarter of 2025 saw total returns for US equities down 4.9%, while international developed equities were up 5.9%, and emerging market equities were up 2.3%. The US Aggregate Bond Index was up 2.8%. **See Figure 1.** for total returns in the first quarter and the year-to-date period*. Recent market volatility has demonstrated the value of diversification.

Figure 1. Market Performance, Total Return

	Q1'25	Year-to-date*
Equities		
US Total Market[1]	-4.9%	-9.3%
International Developed[2]	5.9%	2.1%
Emerging Markets[3]	2.3%	-3.1%
Fixed Income		
Aggregate Bond[4]	2.8%	1.1%

Source: Bloomberg; 1. S&P Total Market Index, 2. FTSE Developed ex US Index, 3. FTSE Emerging Index, 4. Bloomberg US Aggregate

**Year-to-date total returns are through 4/11/2025*

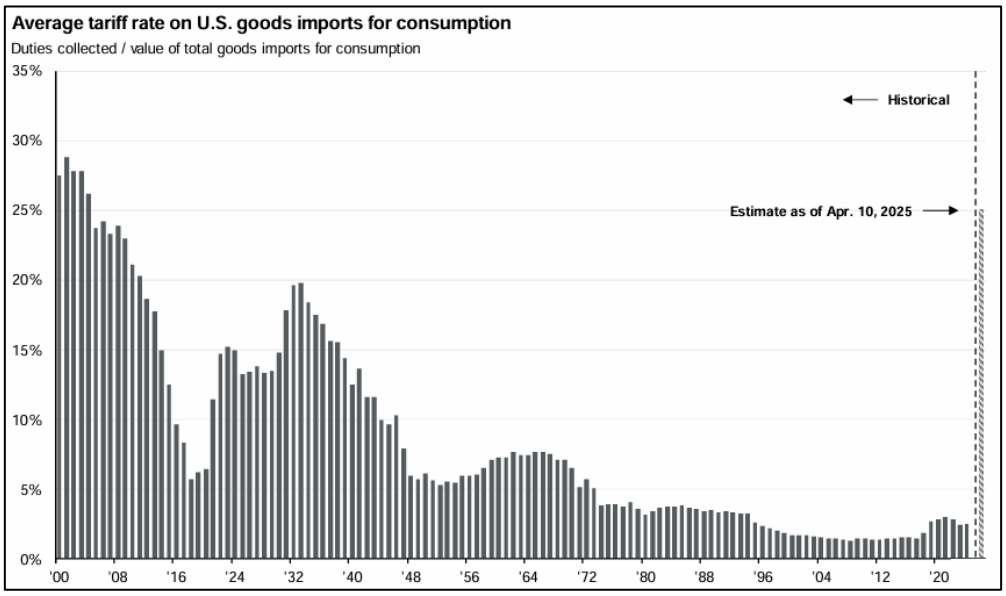
Since quarter-end, markets have moved dramatically, in response to tariff announcements from the Trump administration. While there's a diverse range of opinions regarding tariffs, with many supporters and detractors, the market has certainly expressed itself. Whether this is an opening move in the 'Art of the Deal' and will ultimately lead to fairer trade, a retreat to isolationism, or something in between, is highly uncertain. Elroy Dimson of the London Business School once said that 'risk means more things can happen than will happen.' In our view, the range of potential outcomes is unusually wide at the moment. Pragmatically, we deal with uncertainty by building diversified portfolios, including US equities, international equities, fixed income, real assets, and alternatives.

We think the American political system, and American business, is more self-correcting than many pundits anticipate. Historically, meaningful sell-offs have looked like buying opportunities. As we think about down-side risk, over the longer-term, in the event outcomes are particularly negative for Americans, we're hopeful that action would be taken well in advance of mid-term elections. There's also the potential for successful legal challenges, particularly related to the administrations use of the International Emergency Economic Powers Act (IEEPA). Businesses will also adapt where possible, which may include the re-arranging of supply chains and the on-shoring of manufacturing.

US Economic Trends

In our last quarterly letter, in addressing the agenda from the current administration, we highlighted the potential positive impacts of lower taxes and reduced regulation, offset by the potential negative impacts of tariffs and reduced immigration. To date, the administration has been more focused on the latter two. However, going forward, we think there is room for more positive news flow. This could come in the form of a tariff de-escalation, 'deals' with certain trade partners, or greater clarity on tax cuts. Importantly, in practice, tariffs may act as a funding mechanism for tax cuts, though this would likely take time play out. See **Figure 2.** for the estimated tariff rate on U.S. goods imports relative to history, assuming the 90-day pause expires. According to estimates from JP Morgan, this is a level not seen since the early 1900's.

Figure 2. Tariffs on U.S. Imports



Source: Goldman Sachs Investment Research, United States International Trade Commission, J.P. Morgan Asset Management. For illustrative purposes only. Estimates about which goods are USMCA compliant come from Goldman Sachs Investment Research. Imports for consumption: goods brought into a country for direct use or sale in the domestic market. The estimate does not consider non-tariff barriers, such as value-added taxes. Figures are based on 2024 import levels and assume no change in demand due to tariff increases. Forecasts are based on current data and assumptions about future economic conditions. Actual results may differ materially due to changes in economic, market, and other conditions. Guide to the Markets – U.S. Data are as of April 10, 2025.

All in, tariffs are viewed as 'stagflationary', which refers to an environment of lower growth and higher inflation. This combination puts the Federal Reserve in a potentially tricky situation, as they seek to achieve their dual mandate of promoting maximum employment and stable prices. For example, in a 'stagflationary' environment, if the Fed cuts rates to address high unemployment, it would also serve to stoke inflation. Additionally, if the Fed raises rates to reduce inflation, it would also serve to further weaken the labor market.

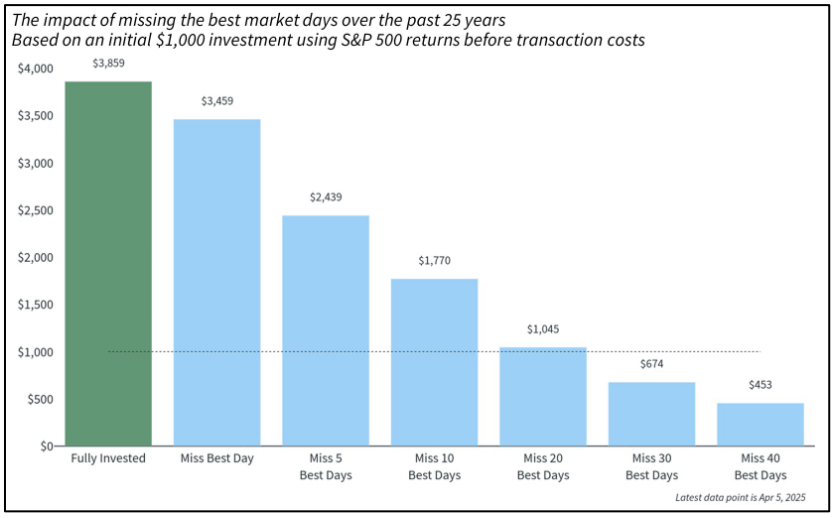
Most economists are now calling for a much higher risk of recession. To a large extent, we believe the duration of the shock will be the critical determining factor.

US Stocks

US stocks declined 4.9% in the first quarter, partly as a result of tariff concerns. Post quarter-end, those concerns were crystalized. The decline was even more dramatic for a number of big tech companies, as investors have grown more cautious on the AI theme, on the heels of an announcement that a Chinese AI company developed similar capabilities to ChatGPT at a fraction of the cost, as well as a reported slow-down in the build out of data centers. There's also concern that big tech is a potential target for tariff retaliation from abroad, presenting additional risk.

With an unusual amount of concentration in the S&P 500, particularly from the 'Magnificent 7', we continue to highlight the importance of diversification and encourage investors to focus on the long-term. Again, we think America is more resilient than many pundits anticipate, and in fact, draw-downs have historically presented strong buying opportunities. While historical results are certainly no guarantee of future performance, investing in the S&P 500 after a 20% draw-down has on average generated a double-digit return one-year later. Additionally, we think that fearful investors who choose to liquidate and wait for an 'all clear' will likely end-up missing out on the rebound. Note that an investor who missed just a few of the best days over the last 25 years would have fared materially worse than a 'buy and hold' investor. See **Figure 3.**

Figure 3. The Importance of Staying Invested



Source: Clearonomics, Standard & Poor's

On a year-to-date basis*, there has been a wide divergence in performance across sectors, highlighting the need for active management. Information Technology for example, is down ~15%, while more defensive sectors, like Healthcare, are approximately flat. As a reminder, we added a Healthcare ETF to many accounts in the fourth quarter, and recently rebalanced portfolios, in an effort to position clients more conservatively.

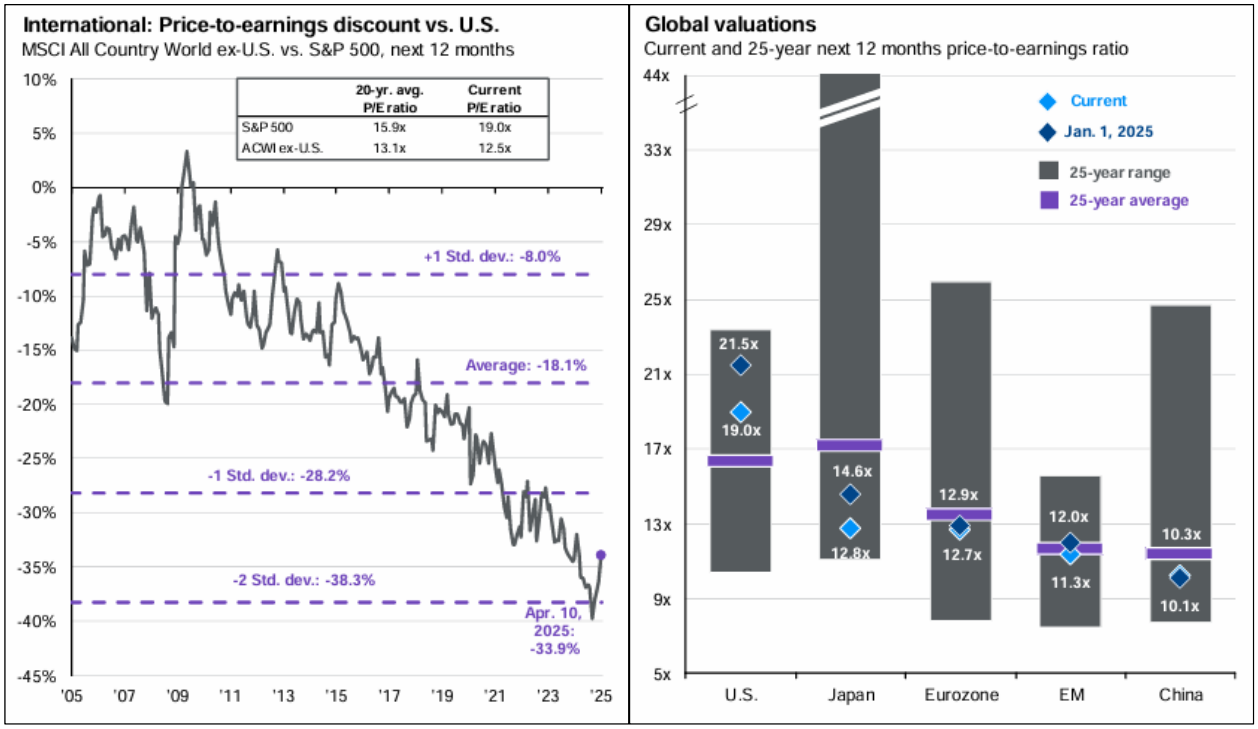
**Year-to-date returns are through the end-of-day April 11th, 2025*

International Stocks

International Developed and Emerging Market stocks generated total returns of 5.9% and 2.3%, respectively, in the first-quarter. Additionally, international stocks have held up relatively better year-to-date. There are a number of variables at play. First, in response to a shifting relationship with the United States, and threats from abroad, Germany has committed to increase spending on defense and infrastructure by up to €1 trillion. This is expected to stimulate growth in Europe. There are also early signs that Europe is getting more serious about enacting market friendly policies (e.g., bank de-regulation) that could further stimulate growth. International stocks are also benefitting from a weaker dollar. There are a number of moving parts, but as foreign currencies become stronger relative to the dollar, international businesses that generate more profit overseas, are by definition, more valuable to an American investor.

Despite the recent outperformance, international stocks are still meaningfully cheaper than the United States, both on an absolute basis, and relative to their own histories. See **Figure 4.** for the relationship of price-to-earnings ratios for international stocks vs. US stocks since 2005, as well as current valuation levels relative to historical averages. We continue to view international equities as an important source of diversification.

Figure 4. International Valuations



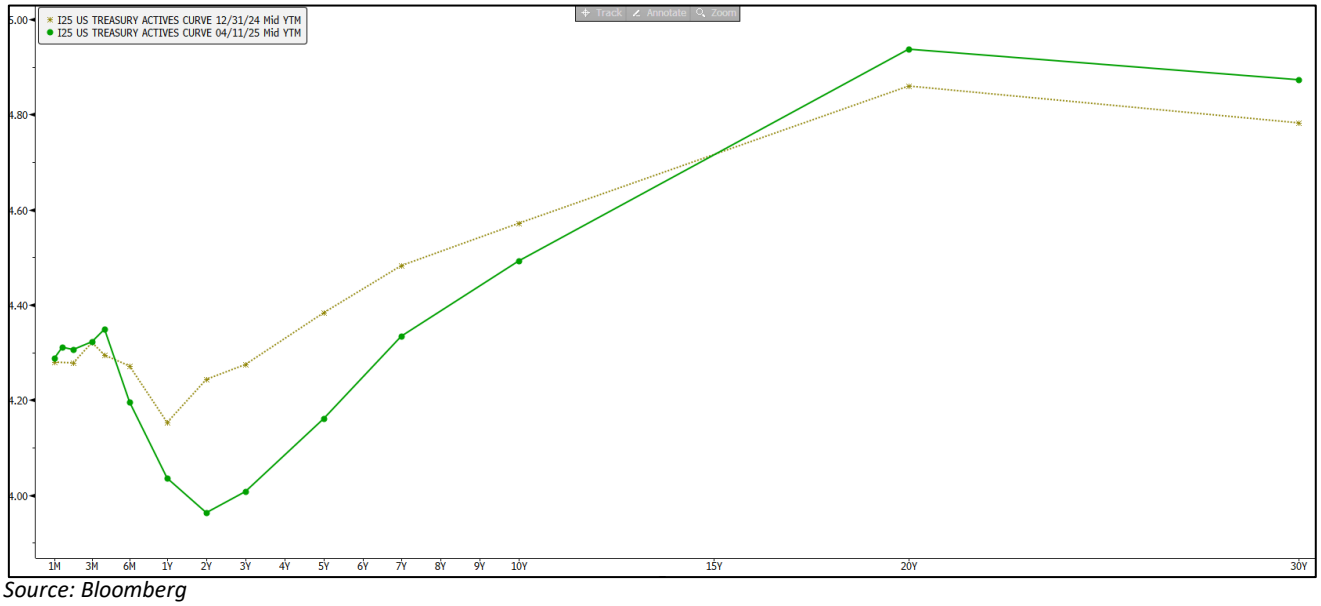
Source: FactSet, MSCI, Standard & Poor's, J.P. Morgan Asset Management; purple bars for EM and China show 20-year averages due to lack of available data. Data is as of April 11th, 2025

Fixed Income

The US Aggregate Bond Index generated a 2.8% total return in the first quarter. The Federal Reserve also held fed funds, or short-term rates, steady at 4.5% for the second straight meeting in March. However, given recent events, the futures market is now pricing in four cuts this year. In our view, this assumes the Fed reacts more aggressively to weaker economic growth than higher inflation.

The yield curve also 'steepened' in the year-to-date period, meaning shorter maturity bonds rallied, while longer maturity bonds sold-off. See **Figure 5.** As a reminder, yields and prices move inversely to one another. As recession-risks rise, the textbook outcome is for investors to flock to the safety of US Treasuries and for bonds to rally. It was unusual to see long-term yields rise, and this could be the result of some combination of foreigners selling Treasuries, or high volatility driving excessive trading activity, which may be more akin to 'noise' than 'signal'. Encouragingly, our fixed income sleeves are typically shorter duration relative to the US Aggregate Bond Index.

Figure 5. US Treasury Yield Curve, Dec 31st & April 11th



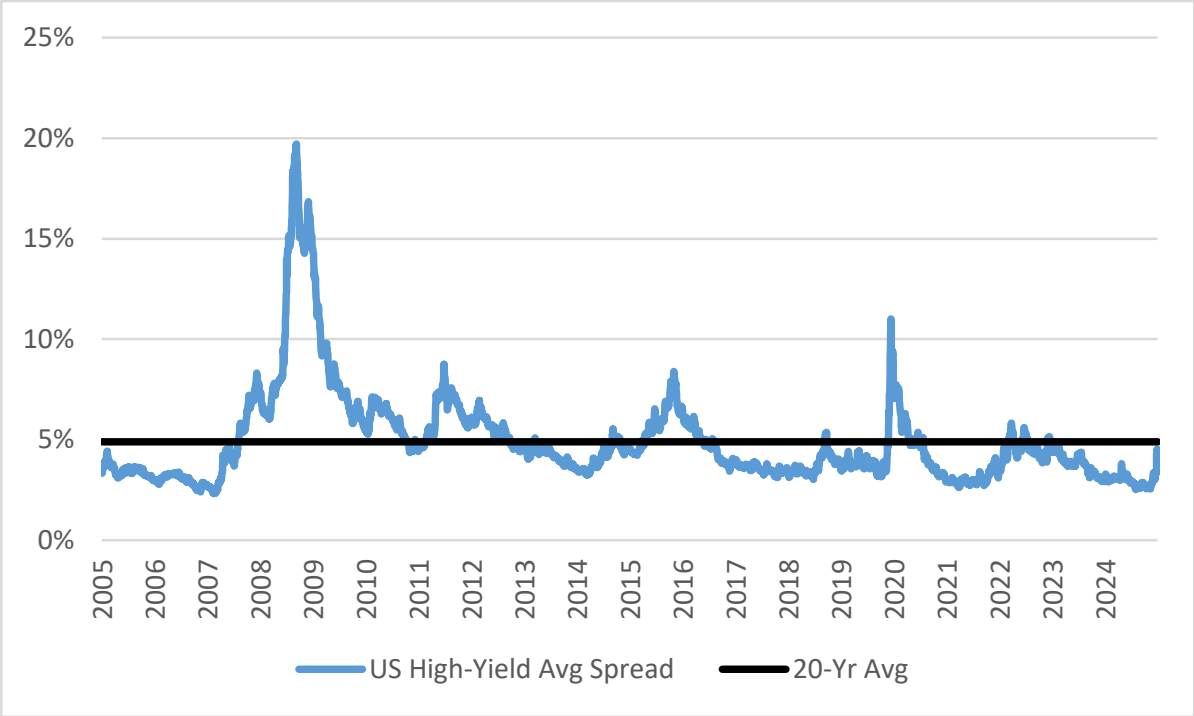
Source: Bloomberg

In regards to budget deficits, and related to that, the necessary issuance of Treasuries, there's debate around the 'Department of Government Efficiency', or DOGE, cutting an estimated ~$50B of spending from the federal government. While this may carry a modest benefit in regards to reducing the deficit, this can also be viewed as a form of austerity, and as a result, represents a further drag on the US economy. Additionally, as many commentators have pointed out, $50B of savings hardly puts a dent in our budget deficit, which is estimated to be ~$1.9T by the Congressional Budget Office. At the same time, there's a great deal of uncertainty regarding tax policy going forward and the extent to which DOGE savings will be offset by tax cuts.

Additionally, credit spreads, or the extra yield investors earn in riskier fixed income has increased year-to-date, but is still far from 'panic' levels. Note that wider credit spreads are associated with investors perceiving a greater risk of default, and vice versa.

'High-yield' bonds started the year with particularly narrow spreads, and even after widening 130 basis points (i.e., 1.3 percentage points) year-to-date*, spreads are still below their 20-year average. See **Figure 6**.

Figure 6. Bloomberg US Corporate High-Yield Spreads



Source: Bloomberg; US Corporate High Yield Option-Adjusted Spread

Thematically, over the longer-term, we think fixed income serves a number of roles in portfolios, including 1) ballast in the event of an economic downturn, 2) capital preservation, 3) liquidity, 4) income, and 5) the potential for capital appreciation.

Given the higher levels of uncertainty, and our view that fixed income is primarily about 'defense', we continue to lean more heavily into 'quality'. This includes US Treasuries, skewed to the shorter-end of the yield curve, as well as agency mortgage-backed securities, and investment grade corporate bonds. Going forward, we will look to add exposure to higher-yielding, and thus riskier, fixed income securities, should credit spreads widen beyond levels justified by the go-forward economic environment.

**As of April 11th, 2025*

As always, we continue to monitor financial markets and invest on your behalf, with a long-term orientation, consistent with the PWM investment philosophy. We continue to emphasize financial planning, and take a holistic approach to helping you manage your wealth. We consider it a privilege to help our clients reach their financial goals.

Thank you for your continued trust, and as always, we remain available to address any questions or concerns.

Sincerely,

Power Wealth Management

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