Although our client letter generally covers the economy and markets over the past quarter, that feels a bit outdated as of this writing on April 11th, given the tariff news and market reaction of the last seven trading days. The first quarter did mark a turning point in markets, with a flip in performance amongst major asset classes. U.S. large cap stocks have been the toast of Wall Street for nearly 15 years, outperforming nearly every other asset class and geography over that time period, including 2024. That script has flipped in a big way so far in 2025. In the first quarter, the MSCI World excluding United States index (International Stocks) returned 6.3%, the Bloomberg Aggregate Bond Index (Bonds) returned 2.7%, while the S&P 500 (U.S. Stocks) fell 4.3%. The outperformance of bonds and international stocks versus U.S. stocks in the first quarter had been driven by an expectation of stimulus driven growth internationally and slowing growth domestically, as Inauguration Day passed and the Trump Administration began to roll out its policy agenda.

While less than 2 weeks have passed since March 31st, the first quarter feels like it was years ago for investors in financial markets. On April 2nd, deemed "Liberation Day" by the Trump Administration, the President announced wide ranging base and reciprocal tariffs on nearly every country across the globe. Market participants had been on pins and needles for the scheduled tariff announcement with hopes that "peak uncertainty" could be resolved, but the released details were more draconian than almost every scenario that had been anticipated by foreign governments, institutional investors, and global investment banks. The trading activity that has followed resembles the volatility of both the Great Financial Crisis and the COVID-19 pandemic. The benchmark S&P 500 index fell 10% on Thursday and Friday following the announcement, a $5 trillion loss in stock market value, the highest ever over a 2-day stretch. The up-and-down volatility continued this week, even within the normally safe haven Treasury markets. On Wednesday, April 9th, President Trump announced a 90 day pause on reciprocal tariffs for every country except for China. Stocks soared on the news, with the S&P 500 gaining 9.5%, its largest daily rally on a percentage basis since October 2008 but has since given back almost half of that gain.

The "Stock Market Vigilantes", a term coined by legendary strategist Ed Yardeni to describe the financial markets ability to punish government decisions, have spoken, and while they are skeptical of tariffs in general, they really do not like being surprised by an event with such an uncertain outcome. The stock market sees significant risks of stagflation, where the economy slows and inflation rises, or outright recession, where GDP contracts, unemployment rises, corporate profits decline and stock prices continue to fall. While the Trump Administration may have admirable goals of rebalancing global trade, reducing our dependence on China, and narrowing the budget deficit, the pathway for getting there without massively disrupting a delicate global supply chain is unclear. According to an analysis from JP Morgan, the Liberation Day tariff announcement would raise just under $400 billion in revenue, or about 1.3% of GDP, which, if passed on entirely to consumers, would be the largest tax increase on the economy since the Revenue Act of 1968. The tariffs could also raise inflation by about 1.0 – 1.5% this year, which may turn real disposable personal income growth negative for the year. Further, the uncertainty about the level and duration of each tariff makes for a difficult capital spending

environment for corporations. As we often write, corporations hate uncertainty, and this environment is about as uncertain from a policy standpoint as we have ever seen over the past 4 decades. If CEOs and CFOs see tariff policy as subject to change, how can they possibly approve large capital plans to build a factory that they expect to have a 40-year life? If we do tip into recession, the budget deficit is likely to get even worse, as it has expanded in nearly every recession in the modern era in the United States. While equity valuations and sentiment were frothy coming into the year and a well-deserved breather was certainly necessary, the recent tariff sell-off has turned a "breather" into a serious correction in just seven days.

Where do we go from here? The recent pivot by the Trump Administration is certainly a step in the right direction, as country by country negotiations offer the possibility of lifting various restrictions on the export of U.S. goods and lessen the likelihood of an extended halt to global trade. Economic circumstances, however, remain challenging. The size of the rally spurred by the 90-day pause was extreme, and historical rallies of similar magnitude have often been bear market rallies that were ultimately followed by continued volatility and losses. Tariffs still in place include 125% on Chinese imports and 10% on nearly all other imports, with those potentially going higher depending on the pace of negotiations over the coming 90-day period. While this is less of a shock than the initial announcement, the remaining tariffs will almost certainly have negative consequences for economic growth and corporate earnings, which investors will be watching closely over the coming month. Consumer and corporate sentiment were already falling in February and March surveys, even before the shock tariff announcements. If there has been any good news recently, it is that the hard economic data has remained solid so far this year. With the economy still steady, a policy induced downturn can be quickly reversed by a pivot from the Administration or the announcement of new deals with countries that eliminate uncertainty. However, the longer that the trade war drags on, the more we worry that a recession becomes inevitable as both corporations and consumers slow their spending dramatically.

We understand that many of our clients are concerned with recent events affecting financial markets. While we do not have a crystal ball to predict the future, we do know from history that selling when the fear is at its most elevated is usually a mistake over the long term. Setting appropriate long term asset allocation targets that allow investors to sleep at night, and careful rebalancing, especially when times are good, is almost always a better decision than "going to cash" when the world feels like it is ending. Investors that sit tight during the market turbulence, and gradually and methodically invest at good prices, tend to be rewarded. This does not mean that there is no further pain to come in the very near term, but that multi-year returns tend to be positive when measured from market panic events. As always, volatility is the price that equity investors must pay for superior returns, but we understand that moments such as this will test our ability to "sit tight" through the turbulence.

As always, please reach out to us if you have concerns about investment strategy or if you simply want to discuss recent events.