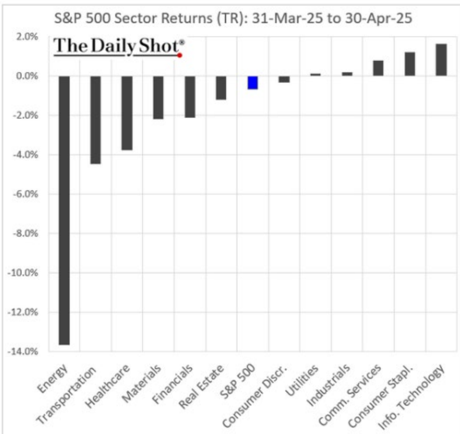
EQUITY MARKET UPDATE

As of 4/30/25 | Volume 14, Issue 4 | FFTAM.com

Stocks had one of their most volatile months on record in April. Investors were whipsawed by a crosscurrent of announcements from President Trump. On April 2nd, the President unveiled a list of tariffs against America's largest trading partners. The size and scope of the tariffs were far larger than markets forecasted. Stocks plunged at a rate not seen since the days of COVID and the Great Financial Crisis of 2008. Selling intensified as President Trump and China exchanged back-and-forth increases to tariffs on incoming goods. This negatively impacted the credit markets. Interest rates rose while the US dollar dropped in value. One week after the Liberation Day tariff announcement, President Trump calmed markets by pausing the implementation of tariffs for 90 days. However, downward pressure resumed after the President hinted that he may fire Federal Reserve Chairman Jerome Powell. Interest rates increased further while liquidity evaporated. A few days later, the President publicly stated he had no intention of removing Mr. Powell prior to his term expiring in May 2026. By month-end, stocks had recovered a good portion of their losses, but indexes were still down for a third straight month.

The S&P 500 fell 0.68% in April. Five of the eleven economic sectors were positive. Energy was by far the worst performer, dropping 13.65%. Interestingly, the index would have been flat for the month if you excluded the decline in shares of United Healthcare. These results were far improved compared to the 15% drop experienced in just three days earlier in the month. Year-to-date, the S&P 500 is down 4.93%. Defensive sectors like staples, utilities, and healthcare have posted gains. Meanwhile, the largest losses are taking place in communications, technology, and consumer discretionary, which serve as the homes to the Mag 7 tech stocks. Through April, the Mag 7 accounts for the entire decline in the S&P 500 (337.82 points of the index's 337.88-point drop).



The Dow Jones Industrial Average fell 3.08% for the month. Large declines in United Healthcare, Chevron, and Caterpillar weighed on results. Year-to-date, the Dow is down 3.92%. Less tech exposure, along with strong rallies from Amgen, Visa, and McDonald's, positively impacted returns compared to the S&P 500.

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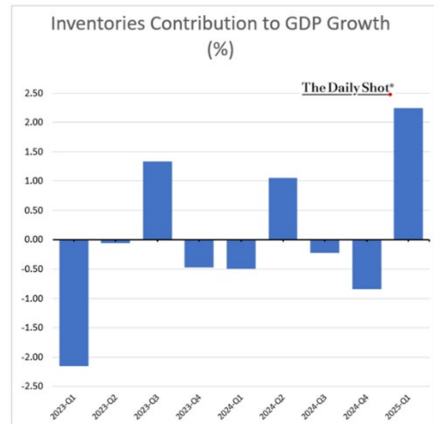
The NASDAQ was the only sole index to post a positive return in April, gaining 0.88%. Strong returns from Microsoft, Broadcom, Netflix, and Palantir lifted the index. Despite the good month, the NASDAQ is far underperforming both the S&P 500 and Dow in 2025. Fears about China gaining ground versus the US in artificial intelligence, along with elevated valuation and the apparent lack of interest rate cuts, have made this area of the market ripe for profit-taking. Year-to-date, the NASDAQ is down 9.47%. Mid and small-sized stocks also suffered significant losses. The S&P 400 Mid Cap (-2.25%) and S&P 600 Small Cap (-4.19%) indexes fell on concerns that the furious pace of announcements from President Trump on a large assortment of issues is creating fear and confusion among both business leaders and consumers that will negatively weigh on economic growth. With little movement on lower taxes and regulatory relief, along with interest rates remaining high, these stocks are down 8.22% and 12.75%, respectively, this year.

Given the seismic shift to global commerce from President Trump's tariff announcement and executive orders, many firms have materially increased the odds for a recession. Thus far, economic data is pointing towards a different "r" word—resiliency. Although the US economy has softened in recent months, nothing outside of sentiment surveys indicates a recession is at the doorstep. Consumer spending is firm, but it is primarily coming from the highest income households. For months, many metrics have shown financial stress building among lower-income households, and recent consumer sentiment surveys indicate the potential for higher prices from tariffs is front-of-mind. Labor, which has been the bright spot for the past two years, appears to be returning to more normalized conditions. April payrolls showed that another 177,000 jobs were created. Unemployment held steady at 4.2%. Wages were up 3.8% from one year ago, an amount that continues to exceed both the Fed's expectations and the pay raises seen pre-COVID. The labor market is tight, but competition to recruit and retain employees has obviously waned. The JOLTS report showed that there are 7.19 million jobs open but unfilled, a sizable decline from the previous month. There are currently 1.1 job openings for every unemployed person. This is below the levels seen pre-COVID, and it indicates that getting a new job is becoming harder for people on unemployment. Encouragingly, the weekly reports on the number of new people filing for unemployment are tame.

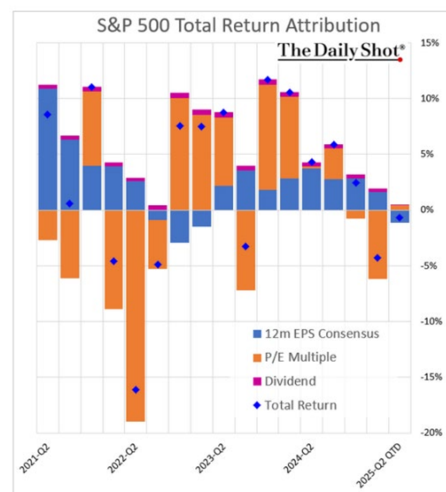
Consumer inflation continues to be stubborn, with prices increasing 2.4% from one year ago. Core inflation that removes food and energy softened to 2.8%. PCE data, the Fed's preferred measure of inflation, showed total prices climbing 2.3%, while prices ex-food and energy rose 2.6%. These statistics are much better than the high-water marks seen in 2022, and they are within reach of the Fed's 2% target. However, the large debate among investors is how much room does the Fed have to lower interest rates, especially if the threatened tariffs push prices higher.

Despite wage growth and relatively low unemployment, clouds are forming over select segments of the consumer population. Personal income grew 0.5% in April. Total spending rose 0.7%, while retail sales gained 1.4%. With spending outstripping income, many wonder if consumers are overspending to buy goods prior to tariffs taking effect. Consumers have increasingly funded their expenditures with the use of debt. Credit card balances are at record amounts, and debt delinquency has climbed from one year ago in both credit cards and auto loans, especially among people with lower credit scores. Until President Trump provides greater details on his economic policies, monthly job reports and weekly unemployment claims are vital pieces of information to watch to gauge the strength of the consumer.



Business investment took another step backwards in April. The ISM Manufacturing PMI Index was 48.7. This index has contracted 27 of the last 30 months. Employment data (46.5) contracted once again. Manufacturing jobs have fallen in 23 of the last 27 months, something that historically happens only during recessionary periods. New orders (47.2) improved after last month's collapse, but the reading is still in contractionary territory. This data, along with a spike in the trade deficit the past two months, is providing skeptics with fuel that businesses are ordering products and components before the proposed tariffs take effect. Unfortunately, prices paid (69.8) increased again to their highest level since June 2022, adding to fears that inflation from proposed tariffs could be bubbling. Services have been the engine powering the economy, but it too has slowed in recent months. The ISM Service PMI Index expanded with a reading of 51.6. Service employment (49.0) dropped for a second month, which could spell trouble for future payroll releases. New orders (an indicator of future demand) improved to 52.3. Just like its manufacturing cousin, prices paid for services (65.1) was really hot.

Collectively, the data shows the Fed is winning the battle with inflation, although as stated above, the proposed tariffs from President Trump insert a high degree of uncertainty for future prices. The FOMC held interest rates steady at 4.25% to 4.50%. Dot plots indicate the central bank believes rates will be between 3.75% and 4.00% by the end of 2025, implying rates will only be cut twice in 2025. The Fed is holding on to their wait-and-see position given the uncertainty surrounding the President's threatened use of tariffs against major trading partners.



The S&P 500 currently trades at 20.2x forward earnings estimates. This is in line with one year ago, and it is above the 5-year (19.9x) and 10-year (18.3x) averages despite the higher interest rate environment. The equity risk premium that compensates investors for the excess risks associated with stocks compared to bonds remains thin.

We are in the thick of earnings season. So far, 72% of S&P 500 companies have reported, and year-over-year profit growth is 12.8%, well ahead of Wall Street expectations. However, investors should note that major earnings beats from Alphabet and Microsoft are heavily skewing results. A new item we are seeing this quarter is many companies suspending forward guidance given the uncertainty surrounding tariffs. Analysts have taken this as bad news, and they are downwardly revising their future profit expectations. The consensus forecast calls for 2025 earnings growth of 9.5%, a significant drop from last month's 11.3% view given concerns about a slowing economy.

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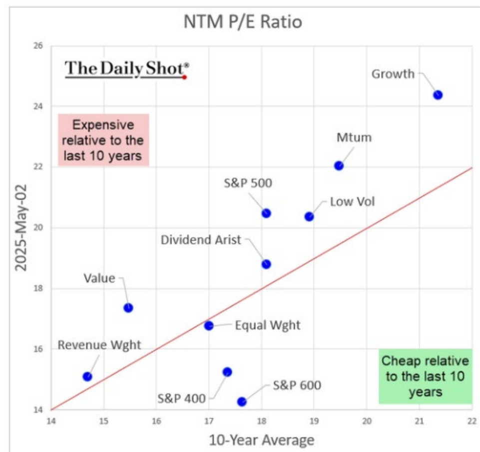
With the market trading above valuations of the past decade, stocks are vulnerable to headline risk from the White House. All major economic reports are also being closely scrutinized for signs of weakness. Coming into 2025, the S&P 500 experienced two years in which returns exceeded profit growth, resulting in back-to-back years of PE multiple expansion. This told us investors were fully convinced that inflation and interest rates would be coming down while overall demand for goods and services would remain intact (i.e., soft landing or “Goldilocks” scenario). This view has become clouded due to the lack of clarity from President Trump on the use and implementation of tariffs, along with mixed messaging on the duration in which tariffs would remain in place.

The sell-off over the past three months has been very deep in some pockets of the market. Investors are taking chips off the table given the elevated valuation entering the year, along with the whirlwind of fiscal, tariff, and monetary policy announcements coming out of Washington DC. It appears there are simply too many items in motion for investors and business leaders to ascertain the end result. This has weighed on near-term sentiment for both investors and consumers as mentioned above. However, we believe the clouds hanging over the market will lift once Congress presents substantive facts regarding taxes and regulatory relief. Any announced trade agreements with major trading partners will also calm fears since completed deals could serve as templates for the countries still negotiating with the Administration.

For months, we have written about the large difference in valuation between the big tech companies at the top of the index and everybody else. Currently, if you equal weight the names inside the S&P 500, the forward PE ratio drops from 20.2x to 17.0x. Although the margin remains wide, it has closed significantly in 2025 on the combination of strong earnings from big tech mixed with falling share prices. When you factor in future growth opportunities, select pockets within technology look attractive at current levels. We also remain bullish on financials, utilities, and parts of industrials attached to re-shoring and AI infrastructure. Defensive positions have outperformed so far in 2025, but they possess limited future growth potential. This makes these areas vulnerable should investor sentiment shift. Finally, our preference for quality companies with strong balance sheets and growing dividend streams to enhance performance remains strongly intact.



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