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MARKET COMMENTARY

While first quarter market performance may seem irrelevant at this moment in time, there were some changes worth noting. After a second straight year of strong, broad-based equity market returns in 2024, the first quarter of 2025 saw a significant pickup in volatility due to a continuation of geopolitical tensions, news surrounding cuts at both US government agencies and NGO's (non-governmental agencies), and most notably significant uncertainty related to US trade policy. After many years of domestic equity indices outpacing their foreign counterparts, there is a reversal of this trend. The S&P 500 fell 4.27% with US mid cap and small cap stocks falling slightly more, while developed international equities were up 6.86% and emerging market equities returned positive 2.93%. Broad-based US bonds had a positive quarter and served as a safe-haven against the volatility.

At the time of this writing (early April), equity market volatility has increased to levels that have not been seen since March of 2020.

It is well known in the investing world that markets hate uncertainty and the first week of April brought plenty of it. Financial markets had digested several of the Trump administration's early actions throughout the first quarter of 2025, as they were largely expected. This included securing the Northern and Southern US borders, focusing on government inefficiencies, and promoting a pro-business and deregulatory economic agenda. This is not a political endorsement nor criticism of the tactics and theatrics used, but simply a recognition that markets were not caught off guard and were generally well apprised of the end-goals. This changed on April 2nd when tariffs that the market expected to be reciprocal and targeted were announced as much larger and broad-based. As a result, we saw peak uncertainty.

We've written previously in our blogs and market commentary that markets, businesses and consumers alike can plan, spend, and invest accordingly when they know the rules of the game. At present, the rules of the game related to international trade are in-flux and negotiations over the next 1-2 months are likely to provide more clarity. As more clarity becomes available, our view is that markets will move away from their current state of peak uncertainty.

The most commonly used fear-gauge on Wall Street is the VIX. In most market environments, the VIX tends to remain below 20. At the height of the Great Financial Crisis in 2008, the VIX peaked at over 80 and in March of 2020 we saw a reading of more than 82. In the first week of April, the VIX hit 52. According to Franklin Templeton, over the last 30 years, anytime that the VIX has closed above 30, the average and median forward 3, 6, 9 and 12-month total returns for the S&P 500 has been positive. In fact, the average and median forward 12-month return is more than 20%. While historical returns are no guarantee of future results, a high VIX tends to be a bullish

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indicator for forward looking equity market returns.

The old Warren Buffet quote that "investors should be fearful when others are greedy and greedy when others are fearful" comes to mind during periods like this. In our Q4 2024 commentary, we mentioned that some market participants appeared to be overly euphoric, which had fueled rallies in speculative assets such as cryptocurrencies, companies with untested business models, and leveraged single-stock ETFs. Further, we saw many retail investors who had portfolios consisting almost entirely of 'Magnificent 7' tech stocks. At present, stepping into diversified equities with long-term money could prove to be prudent, given the level of fear that investors have exhibited.

One silver lining of the current market environment is that diversification has worked. While US stocks have been hit the hardest, international stocks have been hurt less, bonds have had a strong start to the year, and money markets continue to pay more than 4% interest. This is in stark contrast to the period from late 2021 through 2022 when interest rates were coming off of all-time lows and an aggressive Fed sent stocks and bonds both falling at the same time.

Going forward, there are several rules of thumb that will continue to be pillars of our process on behalf of clients. First, always hold a diverse portfolio of assets and maintain a risk profile that allows one to rebalance when equity allocations fall meaningfully below a targeted weight. Second, don't make short-term decisions with long-term assets. Have cash on hand for short-term obligations and own a ladder of bonds that will cover several additional years of spending. Predicting the direction of equity markets is nearly impossible in the short-term, but becomes much easier over the long-term. Allow the long-term portion of your portfolio to remain in place for obligations that are many years out. And finally, execute on actions that have a high probability of adding value with a relatively low probability of regret. Harvest taxable losses to help lower future tax bills, convert pre-tax IRA balances to tax-free Roth balances if you are in a low-income year, or consider locking in current interest rates for the next several years if you have significant amounts of low-yielding cash. Last but not least, if you find yourself with more equity market risk than you can comfortably handle, avoid making large emotion-based adjustments when volatility is high. Rather, make a plan to systematically reduce risk over time as volatility subsides. The old adage that patience is a virtue also applies to managing a financial plan.

We are acutely aware of how stressful market corrections can be. It is during times like these that we want to be fully available to our clients to address questions and concerns. Please do not hesitate to reach out to any of our advisors directly.

Christopher W. Frayne, CFA, CFP®

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