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# MONTHLY MARKET PERSPECTIVE

FEBRUARY 2025 REVIEW

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## Overview

The volatile ride continued in February and there are early signs that the ups and downs may be taking their toll. Economic reports have been mixed; for example, in January the U.S. added 143,000 jobs, which was lower than the expected 175,000. However, the unemployment rate decreased from 4.1% to 4.0% and average hourly earnings increased by 4.1% year-over-year (YoY).[1] Even though employment remains strong and wages are rising at a reasonable pace, retail sales contracted by -0.9% month-on-month (MoM)—more than analysts expected—while retail sales excluding volatile autos and gas purchases also fell by -0.5% MoM where consensus expected a small gain.[1] And much to the Fed's chagrin, headline inflation (CPI) came in higher than expected in January and increased to 3.0% YoY from December's 2.9% YoY level. Core-CPI, which strips out volatile food and energy, also came in higher than expected in January rising to 3.3% YoY, which was higher than December's 3.2% YoY figure.[1]

In less than a month in office, the Trump administration has imposed a 10% tariff on over $400 billion in Chinese imports.  Trump also announced 25% tariffs on all steel and aluminum imports, effective March 12th. He also directed federal agencies to study how to raise US tariffs to match existing tariffs and certain economic barriers (typically import quotas) used by other nations to restrict US exports to their country. At month's end, Trump said his proposed 25% tariffs on imports from Mexico and Canada will go into effect March 4th and that China will be charged an additional 10% tariff on the same date.[2]

Amid the perplexing economic data and whirlwind of policy emanating from the White House, one should not be surprised that sentiment data has declined. The Conference Board's measure of consumer confidence declined for the third consecutive month, falling by 7.0 points—the largest monthly decline since mid-2021—to 98.3 due to concerns over inflation and future state of the economy, but it remains above the 50-year average of 95.4.[1] Meanwhile, the Small Business Optimism Index fell to 102.8 in January from December's 105.[1] but remains positive and is above its 50-year average (98) for the third consecutive month even as uncertainty has increased.[1] Although both sentiment indicators are above their long-term average, in the short run, the unease was reflected in poor equity market returns and the purchase of safety via U.S. Treasury bonds which drove interest rates lower.

[1] Bloomberg LP
[2] CNBC

## U.S. EQUITIES

| U.S. Equity Markets | | | | |
|---|---|---|---|---|
| **Index** | **1 Month** | **Quarter-to-Date** | **Year-to-Date** | **1 Year** |
| DJIA | -1.4% | 3.3% | 3.3% | 14.6% |
| S&P 500 | -1.3% | 1.4% | 1.4% | 19.0% |
| Russell 2000 | -5.4% | -2.9% | -2.9% | 7.5% |
| Russell 1000 Growth | -3.6% | -1.7% | -1.7% | 20.6% |
| Russell 1000 Value | 0.4% | 5.1% | 5.1% | 16.1% |

As of February 28, 2025

US equities endured the worst week of 2025 to close out February. Despite hitting a record high in February, the S&P 500 traded -1.3% lower over the course of the full month and shed over -5% in just the final seven days of trading.[1] US small caps (Russell 2000 Index) fared even worse, losing -5.4% in February. US small caps, are in fact, in a formal correction have dropped by -11.1% since its near-record high in late-November-2024. While most economic measures point to a good US economy and Q4-2024 earnings season was very positive, the sentiment among investors soured in the past few weeks as policy uncertainty reigned down from Washington DC and expectations for accelerating growth in the coming months faded. However, February was not all bad and several sectors gained during the month, including defensive sectors such as Consumer Staples (+5.7%) and Utilities (+1.7%). More rate sensitive sectors such as Real Estate (+4.2%) and Energy (+4.0%) also gained as expectations for Fed cutting rates by mid-year gained traction.

Investor sentiment can be a mercurial thing, but the fact remains that the S&P 500 has not experienced a formal correction—a loss of worse than -10%—since the period September to October-2023. After +25% returns in 2024 with only one significant draw-down in early August-2024 and below average volatility predominately since the November election, the odds of a drawdown in the S&P 500 in the near-term are building.[1] However, such intra-year drawdowns are normal and often set the stage for future gains.

## INTERNATIONAL EQUITIES

| International Equity Markets | | | | |
|---|---|---|---|---|
| **Index** | **1 Month** | **Quarter-to-Date** | **Year-to-Date** | **1 Year** |
| MSCI ACWI ex USA | 1.4% | 5.5% | 5.5% | 9.9% |
| MSCI EAFE | 1.9% | 7.3% | 7.3% | 9.0% |
| MSCI Emerging Markets | 0.5% | 2.3% | 2.3% | 10.3% |
| MSCI EAFE Small Cap | -0.3% | 3.1% | 3.1% | 6.7% |

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International markets fared much better in February. Developed international equity markets (MSCI EAFE Index) gained +1.9% during the month and emerging market equities (MSCI EM Index) gained +0.5%. International developed equities have been boosted, in part, by optimism that there may be a ceasefire for war in Ukraine in the coming months as well as the recent elections in Germany will lead to a new German Chancellor who will usher in reforms to boost German spending on infrastructure and defense as well as reduce regulations and pursue other pro-growth economic policies.

Emerging markets were buoyed, in part, by Chinese equities which gained almost +12% in February ahead of the economic focused "Two Sessions" policy meetings which begin in early March. These meetings, which are led by Chinese Premier XI Jinping, are the main policy setting meetings for the year and will allow Chinese leadership to announce key reforms, economic stimulus plans, and goals for Chinese economic growth for 2025.

## FIXED INCOME

| Fixed Income Markets | | | | |
|---|---|---|---|---|
| **Index** | **1 Month** | **Quarter-to-Date** | **Year-to-Date** | **1 Year** |
| Bloomberg US Aggregate | 2.2% | 2.7% | 2.7% | 6.0% |
| Bloomberg Global Aggregate | 1.4% | 2.0% | 2.0% | 3.2% |
| Bloomberg US High Yield | 0.7% | 2.0% | 2.0% | 10.2% |
| JPM Emerging Market Bond | 1.6% | 2.9% | 2.9% | 9.6% |
| Bloomberg Muni | 1.0% | 1.5% | 1.5% | 3.1% |

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In February's risk-off environment, it is not surprising that interest rates significantly declined – U.S. Treasury 2-year yields declined by 21 bps (4.20% to 3.99%) while 10-year yields declined by 33 bps (4.54% to 4.21%). High yield bond spreads, the percentage difference in current yields between high-yield bonds and U.S. Treasury securities, increased from 261bps to 280 bps as investors found more comfort owning "risk free" U.S. Treasury bonds during this challenging environment.[1]

The good news is that the bond market, in general, performed well, but quality was reflected in the month's top performers. The Bloomberg Aggregate index, a broad-based benchmark that measures the investment grade US dollar denominated, fixed-rate taxable bond market, gained 2.20% while the Bloomberg High Yield index gained 0.67%. High yield's underperformance was not due to declining prices, but the flow of money into the bond market sought the safety of U.S. Treasury securities over lower quality high yield corporate bonds. This is a positive sign that fixed income investors have not been overwhelmingly selling their high yield securities during this volatile period.

## CONCLUSION & OUTLOOK

As stated last month, it is breathtaking to see President Trump's governing style in action. Surprising media pundits and politicians on both sides of the political spectrum, he has been implementing the policies he ran on during his presidential campaign. Given all the activity it is wise to stop and evaluate where we are today. Yes, the S&P had a challenging month, but it is only down 3.05% from its all-time high on February 19th. Interest rates have significantly declined (10-year U.S. Treasury yields went from 4. 79% on January 14th to 4.21% on February 28th) but remain well within a trading range (U.S. Treasury 10-year yield 3.3% to 5%) that we have witnessed for the last 2½ years. With almost 97% of the S&P having reported Q4 earnings, 75% of firms had a positive earnings surprise—on-par with the 10-year average (75%) but behind the 5-year average (77%)—while Q4 earnings growth for the index ended up at +18.2% YOY, which is the best quarterly earnings growth since Q4-2021.3[3]

The U.S. economy appears to remain vibrant, is the envy of our trading partners, and is the destination of choice for entrepreneurs. The President's policies may be controversial and implementation graceless, the objective, in general, is for a more efficient government and pro-growth business environment, which should be good for financial assets. The potential for further volatility will persist as the government faces shutdown in mid-March, while negotiations over a new spending, tax, and debt ceiling bill will continue to evolve. We have repeatedly said that 2025 was likely to be a volatile year and, so far, that is exactly what we have witnessed and will most likely continue to observe.

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[3] FactSet Earnings Insight 2/28/2025