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Where are Equity Markets Going from Here?

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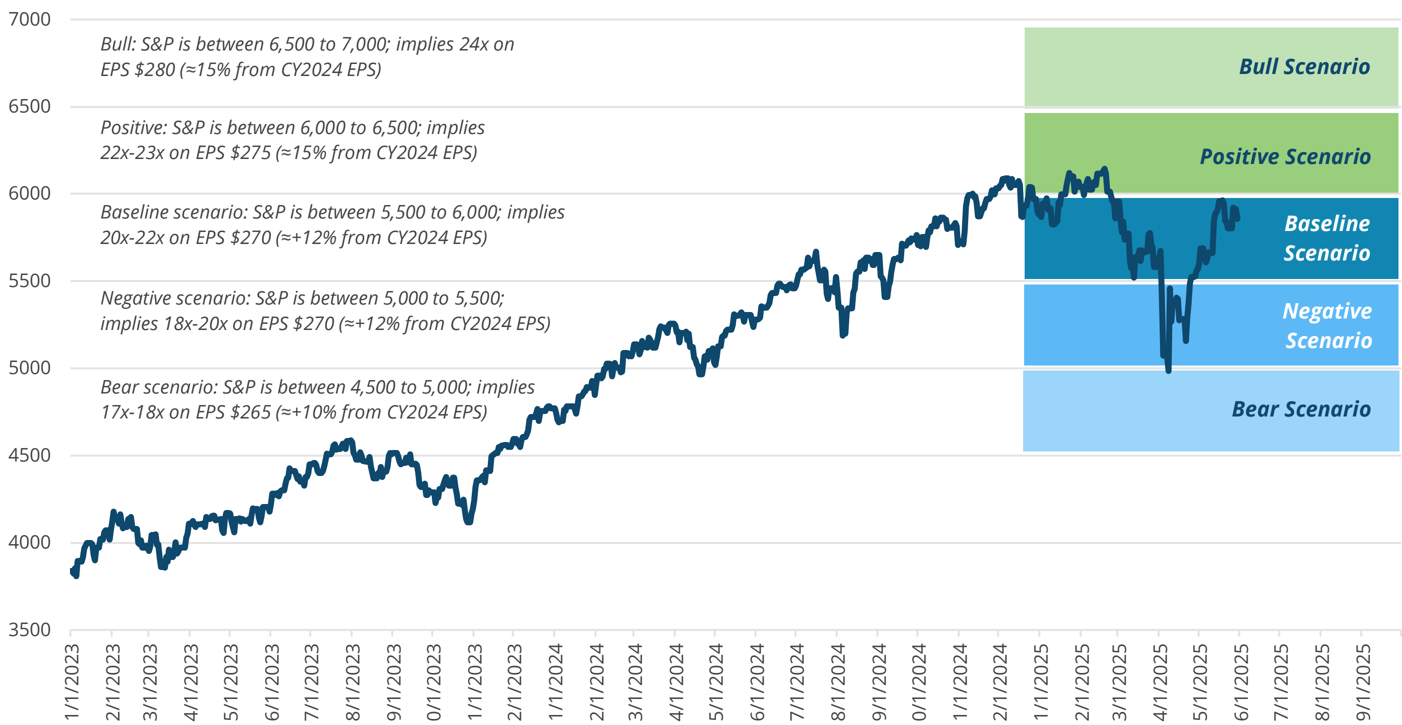
Introduction

The first five months of the year have been eventful. After charting a new historic high in mid-February, the S&P 500 sold off, then corrected (down by more than -10%), and got within a hair's breadth of a bear market (down by -20%) just after the Trump administration announced higher tariff rates on nearly every US trading partner than in any time in the past 100 years. There were signs of panic selling in the market. But just as markets looked the worst, the Trump administration announced a 90-day pause to most of these tariffs and the equity market began to improve.

Just after the Trump administration announced the reciprocal tariff (Liberation Day) regime, numerous market indicators began to suggest that a recession would be increasingly likely by the end of the year. This recessionary risk stemmed from the anticipation of slowing global trade, slowing global growth, and some rise in the price level for goods and some services in the US as higher priced (tariffed) imported goods worked their way into the US economy. However, the Trump administration's successful negotiation of a trade deal with the UK as well as some progress to deescalate the trade war with China (see RC 12-May), eased market concerns. Given these developments, many market indicators of recession risks have declined in recent weeks.

There has been a vibe shift to a more positive sentiment in the markets over the past few weeks and the eventual tax bill winding its way through Congress could further boost investor sentiment over the summer months. The S&P 500 now trades once again at above its 200-day moving average and the VIX—the so called "Fear Gauge"—has moved lower and is near its long-run average. While this shift in sentiment is welcome, it may not last. Trump is always a wildcard, and it is difficult to anticipate the full range of policy actions or pivots that may come over the remainder of the year. The Trump administration may enact policies to help boost equities or they may enact policies that weigh on equities—only time will tell. Clearstead would caution, however, that while the risks of a recession have lessened, they remain elevated and another "growth" scare could loom later this year if the positive momentum in these bilateral trade talks does not translate into actual trade deals by mid-summer. Furthermore, the S&P 500 is expensive on a price-to-earnings basis and the prospect that adverse economic or policy news would be a catalyst for the S&P 500 to retest April's lows cannot be ruled out. Nonetheless, thus far earnings have remained strong, the economy resilient, and gauges of sentiment from households to business as well as market indicators of risk appetite have moved in a positive direction. Additionally, there are credible reasons to believe that the US economy is less-cyclical than in decades past and its more service-sector oriented economy may be more resilient to recessionary downturns than when the manufacturing sector was a larger share of the economy.

S&P 500 Index | H1-2025 PERFORMANCE & Q3-2025 OUTLOOK



Source: Bloomberg LP, Clearstead, daily data as of 5/30/2025; Past performance is not an indicator of future results

As we move into June, the S&P 500 is up slightly on the year (total return as of 5/30/2025 the S&P 500 is 1.1% YTD) and it has fully recovered its losses from Feb-April period. We are now being asked by clients—where do we go from here?

Well, the short answer is there are still a lot of unknowns to contend with and, unfortunately, we still have more lingering questions than definitive answers. The most likely near-term dynamic is a volatile and sideways market as the range of outcomes, both positive and negative, for the US economy and markets have widened out for the year. Nonetheless, we are advising clients to stay the course and rely on the security of their portfolio construction and not to lose sight of their long-run investment goals. Clearstead recommends diversified portfolios structured with the goal of withstanding volatility and outperforming the market over the long-term. We hope that today's volatility does not distract clients from the benefits of a strategic asset allocation and the power of compounding returns over time.

Given the uncertainty and unknowns that loom this summer—Will tariffs go up or down from here? Will the tax bill pass Congress? Will the labor market remain strong? What actions will the Fed take?—on the margins we are favoring things we can control. For instance, dividend paying stocks have historically been less risky and speculative than companies relying on multiple expansion or lower interest rates to make further gains, and shorter duration fixed income with reasonable yields look attractive. We believe that risk assets are likely to remain volatile this summer, but as the first five-months of the year have shown, investors that do not panic and are focused on their long-run goals usually come out ahead.

CY2025 S&P 500 EPS growth disappoints; negative earnings revisions broadens and deepens; P/E contraction	**CY2025 S&P 500 EPS growth surprises; earning revisions move to neutral-to-positive; P/E expansion**
Downside Catalysts	***Upside Catalysts***
US consumer pull-back in spending in H2-2025 as many goods and services see price increases	US consumer proves resilient; spending gradually improves in H2-2025 due to tax incentives
Corporate sector pause for CapEx and hiring as global supply chains shift; margins are squeezed	Corporate sector hiring and CapEx accelerate due to tax incentives, AI productivity, and deregulation kick-in; margins stable-to-expanding
Housing market weakens amid growing inventory and little new homebuyer foot-traffic; rental vacancies increase	Fed is able to cut rates as inflationary pressures from tariffs prove negligible; rates drift lower
Fed remains on the sidelines seeking clarity on inflationary trends; US interest rates drift higher	Weaker US$ and positive terms-of-trade boost US exports; foreign tourism to US stabilizes
Reduced foreign tourism in US; weak US export growth due to slowing global growth	Non-performing loans are minimized and confined to niche areas/credit segments
Non-performing loans increase broadly in banking sector—CRE, auto loans, credit cards, and small business loans	Bilateral trade talks with China, EU, Mexico and Canada deliver; effective average tariff rate ≈ 15%
Bilateral trade talks with China, EU, Mexico and Canada disappoint; effective average tariff rate ≈ 20% or higher	

Source: Clearstead 5/30/2025