Vestor Capital
INVESTMENT & WEALTH MANAGEMENT

10 S. Riverside Plaza, Suite 1400
Chicago, IL 60606
T: 312.641.2400 | vestorcapital.com

Market Update

April 6, 2025

Equity Market Update

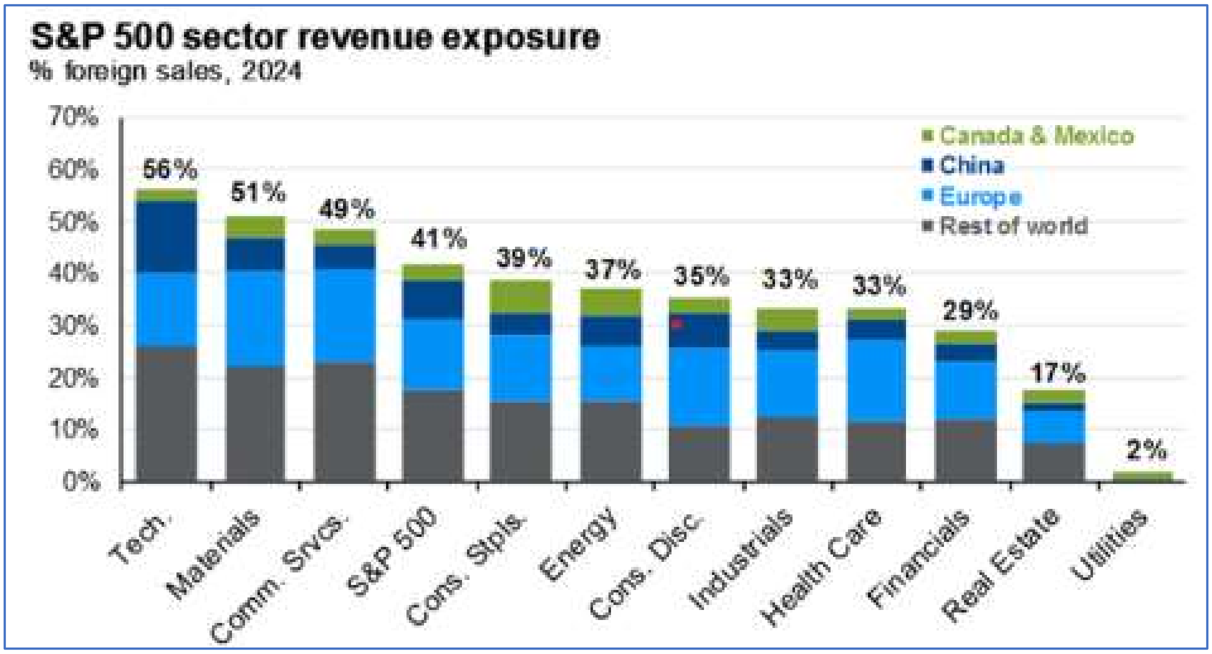
After posting strong returns in 2024, U.S. equity indexes pulled back in the first quarter of 2025. The S&P 500 and the NASDAQ indexes fell 4% and 10%, respectively. After leading markets the past few years, large technology stocks fell in the first quarter over concern that artificial intelligence (AI) spending will begin to slow. Developed international indexes have lagged the U.S. over the past decade, but are off to a good start as investors are heartened by the prospects of increased government spending, while the opposite is occurring in the U.S.

While we have just entered the second quarter, returns have fallen dramatically the first few trading days of April. Investors sold equities in response to the tariff levels that President Trump announced on April 2nd which were significantly higher than anyone expected. In response, China has announced higher tariffs, and other countries are likely to follow suit. It appears that we have entered a trade war which will negatively impact world economic growth unless these tariffs are reduced significantly. We will detail our thoughts in this letter but in summary, it is important to remember that anything this draconian is unlikely to stand. Unfortunately, no one knows when we will come out the other side of this and it is likely that market turbulence will remain over the near-term.

U.S. Tariffs and U.S. Equity Market Implications

The tariffs announced on April 2nd were much higher than even the most pessimistic forecaster anticipated. It seemed as if this was a delayed April Fool's joke but, unfortunately, it was not. It was previously announced that the U.S. would simply be matching the tariffs of other countries, which on the surface seemed inherently reasonable. However, final calculation included factors such as the total U.S. trade deficit by country along with other "soft measures" such as currency manipulation and state subsidies to name a few. The resultant tariff levels were, in some instances, 5-10 times higher than the published tariff of our trading partner countries. This caused investors angst and precipitated the sell-off of equities on April 3rd and 4th.

While it may be tempting to throw in the towel on equities at this time, it pays to pause and think about this in a longer-term perspective. As Herb Stein of the American Enterprise Institute once famously quipped "If something cannot go on forever, it will stop." We do not claim to be clairvoyant, but it is improbable that tariffs this high will stand in the long-term. However, it is certainly possible that they remain in the short to intermediate term which will continue to pressure equities. The chart below highlights the technology and communications services sectors, including companies such as Apple and NVIDIA, which generate a substantial amount of international revenue and stand to be negatively impacted. The odds of a recession, predicted by many economists, has now jumped to over 60%.



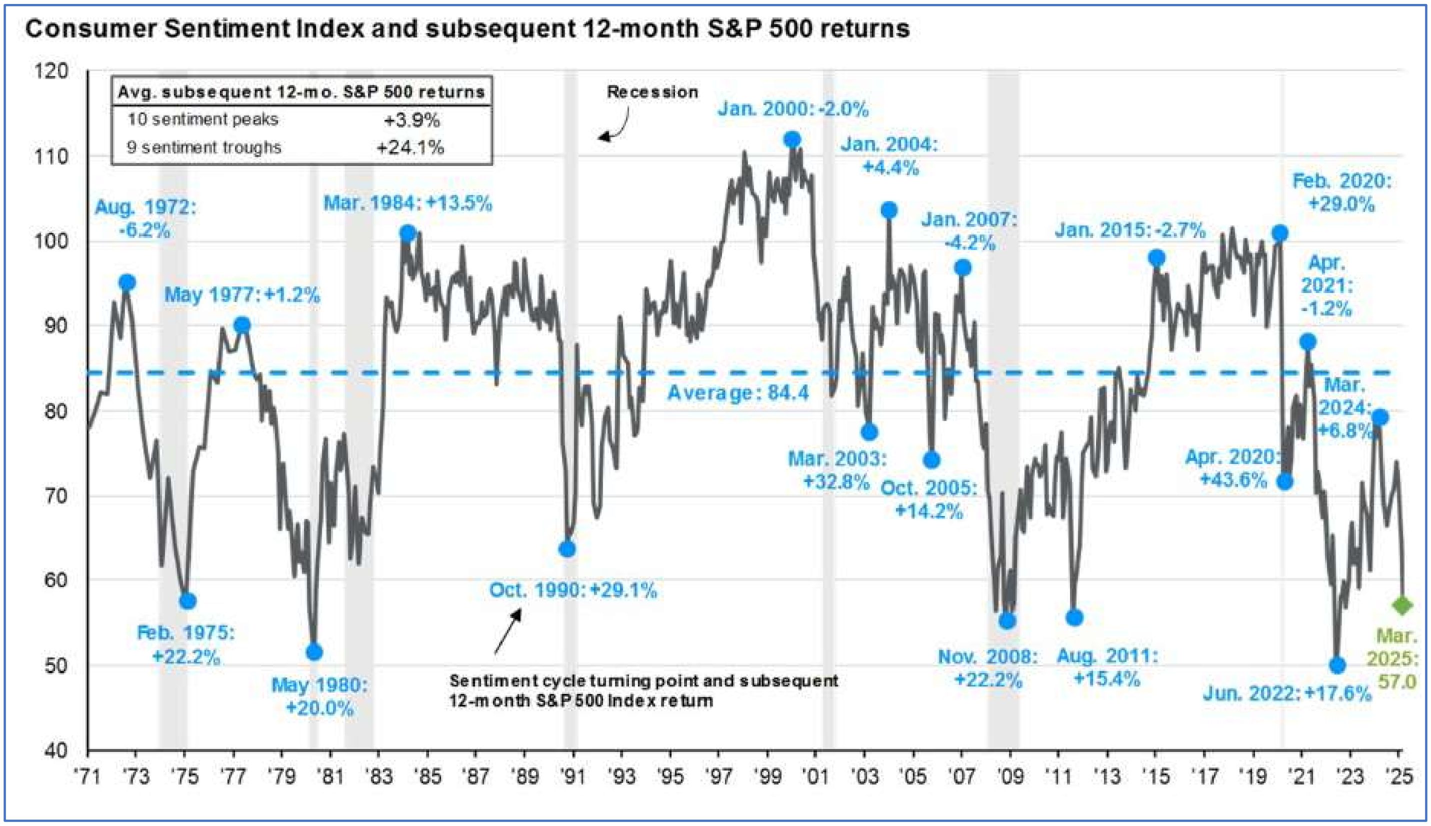
Source: JPMorgan Guide to the Markets 3/31/2025

Tariff Implications for International Equity Markets

While international equity markets initially held up better than the U.S., they are now under similar pressure as U.S. Equities. There are no winners in a tariff war and we hope that cooler heads prevail. Many countries outside the U.S. have not resorted to as much fiscal and monetary stimulus as the U.S. since the COVID pandemic and now are beginning to loosen government purse strings while the U.S. is cutting government spending as evidenced by efforts of the DOGE team. Comparatively speaking, international stocks may hold up a little better due to more government stimulus and a lower weighting in technology and other high growth sectors. Nevertheless, we are sanguine about all equity markets in the event the tariff war lingers on.

Economy

The U.S. economy is still strong as evidenced by a better-than-expected March jobs report and a continued low unemployment level of 4.2%. However, cracks are beginning to form as the April PMI manufacturing index fell into a contractionary level and the ISM services measure showed modest regime, has been declining steadily since October 2024. As the graph below illustrates, consumer sentiment initially rose after the November elections but has since declined due to consumers feeling more unsettled. Paradoxically, when consumer sentiment hits a low, subsequent returns in the S&P 500 are typically strong. Given the unprecedented nature of the new tariff regime, it appears premature to look forward to a market rebound.



Source: JPMorgan Guide to the Markets 3/31/2025

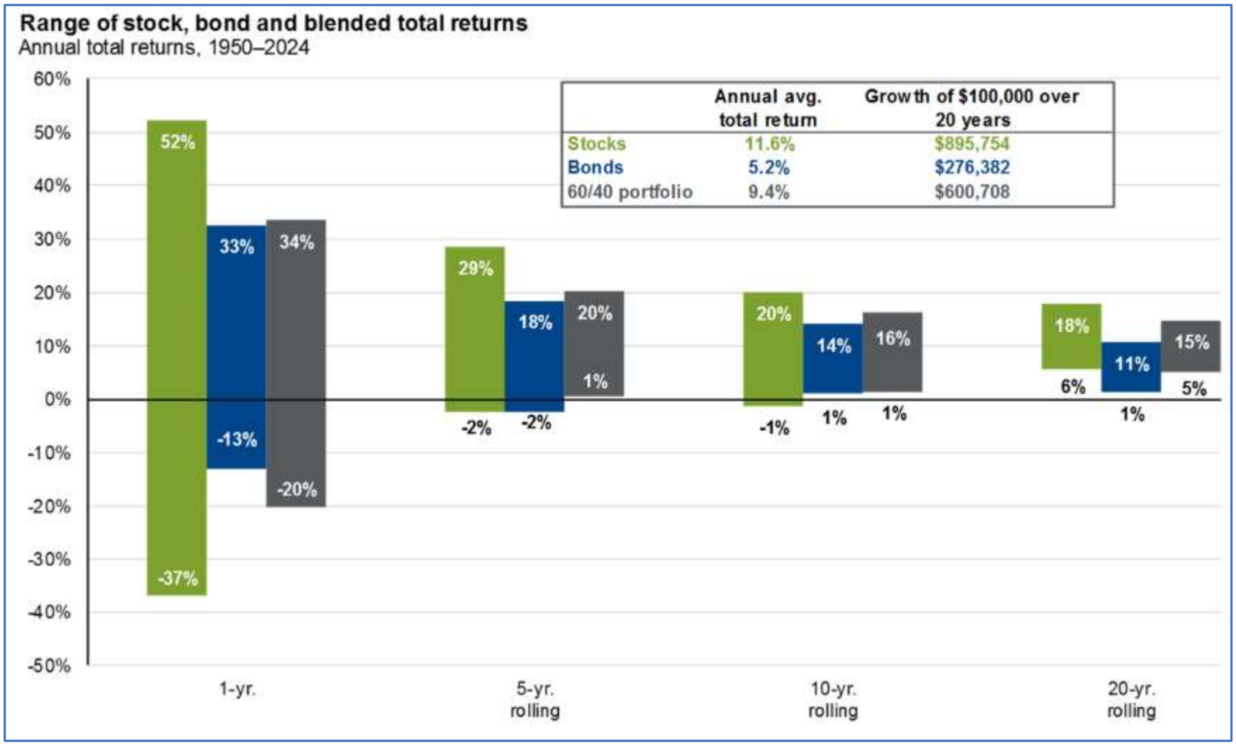
Inflation, Interest Rates & Fixed Income

Inflation levels are settling in at around 3% which is still higher than the Federal Open Market Committee (FOMC) led by Chairmen Jerome Powell would like. While modest additional tariffs would likely not have had a material impact on inflation, the proposed tariffs will likely bring inflationary pressure. Powell spoke on April 4th and expressed concern and indicated that it would be premature to lower interest rates due to inflation uncertainty. Of course, if unemployment rises due to tariffs, the FOMC would be in a bind as stagflation (stagnant economy coupled with inflation) is the one economic outcome that they fear the most.

Interest rates have been declining the past month and the pace accelerated last week as investors fled to the safety of high-quality bonds. Bonds are performing as expected providing ballast to a diversified portfolio of equities and fixed income. However, floating rate and lower credit quality bonds have been pressured somewhat as investors price in the risk of a recession coupled with lower interest rates. Nevertheless, the attractive yields of floating rate and lower quality bonds provides a high level of income to cushion the decline in price.

Summary

The chart below highlights that portfolios, which have a blend of 60% equities and 40% bonds over rolling five-year periods dating back to 1950, have always posted positive returns. While the unprecedented nature of these tariff increases may throw a wrench in these historical returns, it does provide some needed perspective during unsettling times. Investing requires risk taking and a strong stomach to generate attractive long-term returns.



Source: JPMorgan Guide to the Markets 3/31/2025

We have enjoyed strong equity returns over the past 10 years and we believe some of this correction is a normal recalibration of valuations after an extended bull market. What was needed was a catalyst and that came in the form of a tariff war. History has shown that rash investment decisions made during times of market stress typically result in subsequent regret. Reviewing your allocations between equities, fixed income and alternatives is certainly a useful exercise. In times like these, rely on your trusted financial advisor to walk you through the maze of negative headlines to help you make the right decisions. This is not the first “black swan” rodeo that we have been through and there is a lot of collective wisdom among Vestor’s seasoned investment professionals. We are in this together with Vestor employees owning the same investment strategies as you. We will keep you posted on our thoughts as the tariff situations evolves over the coming weeks and months. As always, we appreciate the trust you have placed with us.