GARDECAPITAL

March 2025

Market Update: Recent Market Volatility | Good News from Overseas and Bonds

The U.S. stock market has seen higher than normal volatility during the first quarter of 2025 as investors assess President Trump's policy implementation, developments in the artificial intelligence landscape, and mixed progress on inflation. The S&P 500 index of large U.S. stocks has declined -3.85% this year. However, non-U.S. stocks, as measured by the MSCI EAFE Index, have actually increased 9.45%, and bonds are once again serving as a key diversifier and stabilizer in portfolios with the Bloomberg Aggregate Bond Index up 2.08%. 10-year U.S. Treasury bonds now offer an attractive 4.31% yield. While this turbulence can be uncomfortable for investors, the recent results reinforce our belief that a disciplined approach of maintaining and rebalancing a well-diversified portfolio is key to weathering any market storm. Here we provide some additional insight into the key drivers of performance in each of these markets.

U.S. Stocks

While downturns are never comfortable, they are a normal part of the market cycle and evidence of a well-functioning market that is constantly assessing future economic and business environments. The recent reaction by the U.S. market coincides with Wall Street sentiment that Trump policy implementation may slow the U.S. economy in short term. Bank analysts' reported estimates show a reduction in 2025 U.S. GDP forecasts by approximately 0.5% to revised forecasts of 1.5-1.7%. And, while they report a higher chance of recession, their base case scenario is simply slower, but positive, growth.

U.S. markets have also been weighed down by some selling pressure in artificial intelligence (AI) related stocks. The technology/AI-heavy NASDAQ index is down -7.93% YTD and declined sharply in late January when a Chinese company named DeepSeek claimed to develop an AI model at a fraction of the cost reported by current leaders in AI. This news, coupled with the prospect of a slower economy and potentially lower investment in datacenters, pushed the NASDAQ lower. While AI lives in the Growth segment of the market, Value stocks have returned a positive 0.61% for investors this year, again reinforcing the importance of maintaining a balanced diversified portfolio.

Non- U.S. Stocks

International market returns have been helped by several factors. First, the threat and initial implementation of new U.S. tariffs has spurred a weakening of the U.S. dollar which helped non-U.S. assets like foreign stocks. Additionally, European defense and industrial company stocks spiked after the February 28th meeting between President Trump and Ukrainian President Zelenskyy on the market's expectation of more defense spending in Europe. Finally, since the pandemic, European banks have been playing catch up to recapitalize.

Good news regarding the European bank balance sheets this quarter added more tailwinds to European bank stocks and broader indexes. Finally, Emerging market stocks indexes, driven by China and India have also seen solid gains this year.

Bonds

The key 10-year U.S. Treasury yield has ranged from 3.6% to 4.8% over the past twelve months driven by varying expectations of sticky inflation and a flight to lower risk investments. Indeed, the Treasury Inflation Protected (TIP) bond market shows U.S. inflation expectations rising from 2.0% in September of last year to a high of 2.5% in February and back down to 2.3% today. The current 10-year Treasury yield is 4.31% which we find attractive relative to the 0.6% yield this bond offered 5 years ago and compared to money fund yields that have likely seen their highest point in this cycle. We are encouraged by the diversification that bonds have provided portfolios as yields are attractive and the yield curve continues to normalize.

Conclusion

The year to date results for the U.S. stock market, international stocks, and U.S. bonds reflect a complex interplay of factors. Currently, the markets are assessing and re-assessing President Trump's foreign and domestic policy implementation, developments in the AI sector, and ongoing guesswork on inflation.

As we look ahead at the rest of the year, we will continue to monitor the performance of these important components of our portfolios and the factors which drive them. These short term episodes of volatility can be uncomfortable, but remaining patient, thoughtful and disciplined is necessary to achieve the long-term portfolio returns that investors deserve.

As always, our mission at Garde Capital is to provide guidance on your journey to prosperity and peace of mind. Please reach out if you have any questions about the market, the economy, or your personal wealth management plan.

All returns represent total return for December 31st, 2024 through March 14th, 2025. Sources include: Bloomberg, Factset and JP Morgan Asset Management.

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