

Week in Review

Equity Markets:

The markets ended the week on a negative note following the disappointing reading from the University of Michigan Consumer Sentiment Index. The S&P 500 fell 1.71%, and the Dow had its worst day so far this year, falling more than 700 points and closing down 1.69%. Prior to the sell-off to close the week, the markets were nearly flat as investors digested corporate earnings and various economic reports. Investors fled economically sensitive areas of the market. The Russell 1000 Growth Index fell 2.76%, while its value counterpart only finished the week down 0.96%¹. The Russell 2000 Index, which represents small capitalization companies, fell drastically by 3.69% for the week.

Earnings remain strong despite modest misses last week. So far, 85% of S&P 500 companies have reported earnings. 75.8% exceeded earnings expectations, a slight tick down from the week prior, and 63.8% have beaten revenue expectations².

Fixed Income Markets:

The bond market remained relatively stable for the second consecutive week. The 10-year treasury yield finished the week at 4.42%, a mere 0.05% lower than the week prior. The 2-year yield fell 0.07% and closed at 4.19%.

The Federal Reserve's most recent policy meeting minutes were released last week. A common theme continued in the policy minutes, concerns about current political policy on inflation. The FOMC members noted they feel the current policy rate, 4.25-4.50%, is sufficient until further progress is made on the inflation front.

Economic:

Home builders' confidence fell drastically this month as concerns about tariffs, higher rights, and inflation rose. The NAHB Housing Market Index fell five points to 42 this month. The leading economic index fell 0.3% in January following marginal gains in the previous two months. The "future conditions" portion of the index turned more pessimistic and was a major factor in the negative reading. The biggest surprise last week was the significant decline in the University of Michigan Consumer Sentiment Index. The index fell 10%, more than double the preliminary reading from just a couple of weeks ago. Consumers are concerned about how potential tariffs could keep inflation elevated. Inflation expectations for the next year spiked to 4.3% and the 5-year expected inflation rose to 3.5%. This is the highest expected long-term inflation reading since 1995³. An often overlooked report, S&P Global's Flash PMI, came in soft. This report provides more real-time insight into an economy's economic condition. The most recent report showed that the services sector of the economy unexpectedly fell into contraction due to uncertainty and disruptions from political policy.

Looking Ahead

Equity Markets:

We noted in last week's piece the year-to-date rotation into more "value" oriented companies. We believe maintaining a diversified portfolio that allows you to capture these shifts should be the foundation of your portfolio construction and asset allocation strategy. These style shifts also include geography. Very quietly, markets outside of the United States have significantly outperformed following multiple years of underperformance. The MSCI EAFE Index, which represents developed international, is up 8.2% so far in 2025, and the MSCI EM Index, which represents emerging markets, is up 6.9%¹. We believe this trend could continue if economic concerns remain top-of-mind domestically.

Admittedly, we don't know and believe nobody knows when a "value vs. growth" or "domestic vs. foreign" rotation will occur. This is why establishing strategic allocations is paramount to long-term investing success. These rotations can leave concentrated investors in the wind and potentially overexposed to a subset of risks that may not lie in other areas of the market. A thoughtfully developed strategic allocation not only allows investors to capture these shifts but also to establish a desired level of risk. Market sell-offs not only impact account balances but the emotional impact could be detrimental to achieving your long-term investing goals if the risk your current portfolio bears exceeds the established level of desired risk.

Fixed Income Market

The 4.5% level on the 10-year Treasury yield was an important level for us. Now that we have moved off of that level, we believe the bond market should stay range-bound in the 4.25-4.5% range in the near term. Despite the resurgence of inflation concerns, we believe policymakers have navigated the battle against inflation well. Inflationary risks remain, but the current policy rate is at a level at which we believe the FOMC will be able to make minor adjustments if the environment warrants action.

Economic:

This week's economic calendar will be light but will culminate with the PCE report being released Friday. Recent concerns over inflation will likely draw more attention to the Fed's preferred inflation gauge. The median forecast for the headline reading is an annual increase of 2.4%, and a 2.6% increase for the core reading, which excludes food and energy. Other notable reports include the second estimate for GDP, personal spending, and pending home sales.

**** See Important Disclosures on following page

Sources:

- 1)JP Morgan
https://am.jpmorgan.com/content/dam/jpm-am-aem/americas/us/en/insights/market-insights/wmr/weekly_market_recap.pdf
- 2) LSEG I/B/E/S
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- 3)Reuters.
<https://www.reuters.com/markets/us/us-consumer-sentiment-plunges-february-tariff-worries-2025-02-21/>

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