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WEALTH MANAGEMENT

Financial Market Update
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Stocks Fall on Trade War Concerns Despite Strong Jobs Report

Stocks fell sharply for the second day in a row following the announcement of broad-based tariffs on almost all US trading partners. While the announcement was expected, the magnitude of the tariffs surprised investors and raised fears of a trade war. The situation intensified today when China responded by announcing it was matching the 34% tariff imposed by the US.

Fed Chair Jerome Powell said in a speech this morning that the announced tariffs were higher than anticipated and could reasonably be expected to lead to higher inflation and slower economic growth. These factors create a dilemma for the Fed because the policy tools to respond to these problems are at odds with each other. In other words, high inflation would normally be fought with higher interest rates while high unemployment would normally be addressed with lower rates.

The market decline today comes despite the jobs report this morning which indicates that the economy is currently healthy. The disconnect between current economic conditions and the economic outlook is one of the biggest in recent memory.

The decline in equities has been substantial since the market high on February 19th. From that date, the S&P 500 Index is now down about 17% while the Nasdaq has fallen just over 22%. Not surprisingly, the concerning valuation levels which we wrote about last December are looking more attractive following the decline. In December we wrote that the stock market was 10-15% overvalued. Today those same measures show the market around 5% undervalued. To be clear, this doesn’t mean stocks won’t decline further. At their low in 2022, the overall market was about 20% undervalued.

A 20% decline is the (somewhat arbitrary) definition of a bear market. Since 1973 there have been eight bear markets (they are relatively rare). The average decline has been 35% and the average duration has been 10 months. A significant factor in determining the severity of a bear market is whether it is accompanied by a recession. Not surprisingly, the declines during a bear market accompanied by a recession are deeper than those without.

While it is an overused word, *uncertainty* is currently much higher than usual. Uncertainty about the level and duration of tariffs has given way to uncertainty about the economic outlook overall, with many economists having raised their odds of a recession in coming months. (Despite economists' poor record of forecasting recessions, it is worth noting their concerns in this case.) We will continue to update you as the outlook evolves in coming months.

Please feel free to call us at any time if you'd like to discuss your portfolio. Our client portfolios are designed with the knowledge that periods like the current one happen from time to time. While there are no guarantees in financial markets, history indicates that periods such as the current one are eventually followed by robust recoveries. Thank you as always for being a client.

Best Regards,

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