# The Volatility Begins
## Q1 2025 Commentary

The last several quarterly commentaries have been highlighting the narrow leadership in the Standard and Poor's 500 equity index, led by the Magnificent 7 stocks. The AI-focused technology names swelled to nearly 38% of the total market share of the 500 stock index while dominating the return dynamics. The first quarter of 2025 saw the beginning of a major breakdown of price and the extreme valuation placed on this narrow group. Market extremes are almost always corrected in a reversion, or return, to the means (averages).

Inauguration day on January 20th seems an eternity ago as the Trump administration hit the ground running with multi-pronged policy initiatives that created a frenetic news cycle and mixed market response. Financial markets dislike uncertainty almost more than a known negative event or policy action.


The graphic that I created above has been used in our market volatility podcast, available at https://www.raymondjames.com/thebrechnitzgroup/podcasts. It illustrates the numerous balls in the air, creating uncertainty not only in the equity markets, but also in interest rates (bond markets).

The negative volatility in response is the first correction (decline greater than 10%) since 2022. Typically, we have a correction on average every 18 months, so many investors were surprised and lulled into complacency. We often get questions during runaway bull markets, like the last two years, such as why we aren't keeping pace with the market indices on the upside. Our discipline and years of scars from past market declines has taught us to never chase excessive or narrowly concentrated periods, as they all have a season. Typically, when the season changes, there is much pain if you abandon your discipline.

In addition to equity market volatility that is rightsizing market valuation, the real stakes are being played out in the bond market. Many are unaware that the continued rolling of short-term US government debt by Janet Yellen and Co. has resulted in ~20% of our total debt maturing this year (Source: www.cbo.gov). One of the less visible objectives that the Trump administration has been trying to pull off is a slowing of the economic outlook to influence the interest rates lower. The desire is for the Federal Reserve to lower the Fed Funds rates (overnight bank lending), but more importantly, bring the longer-term interest rates lower, controlled by market forces. With a total national debt exceeding $36 Trillion, it is easy to see that every 1% drop in the re-financed debt burden saves America $360 billion annually!

The softening of inflation, and the threat and ultimate addition of tariffs on trade, was initially having the desired cooling effect on the economic outlook and bond market buying. The chart below shows the sharp decline in the government 10-year U.S. treasury yield in the first quarter. As you can see from the beginning of the year, the drop from just under 4.8% to under 4% was making the plan look like it was coming to

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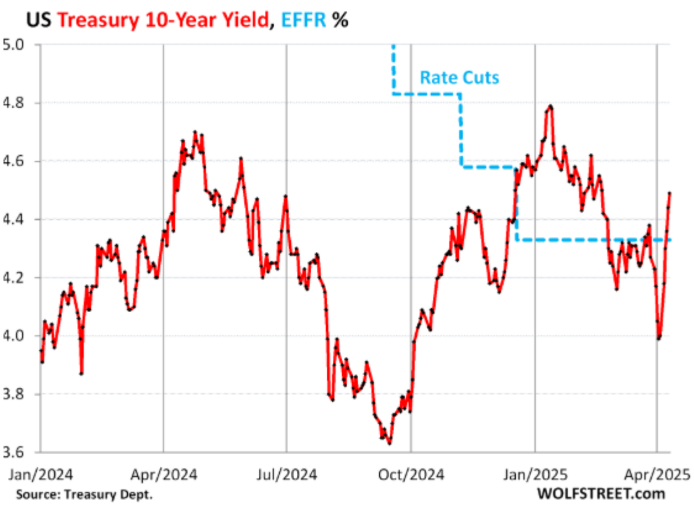
fruition. However, the beginning of April saw a sharp and dramatic spike in the 10-year treasury yield, sparked by fears of further inflation resulting from tariffs. The belief that the tariffs will create an inflation Genie that may be hard to put back in the bottle is a real concern.




Additionally, there is much speculation that foreign governments are selling their bonds to put negative pressure on the U.S. in retaliation for tariffs. Whatever the cause, we feel this may be the most important indicator to watch for both equity and bond markets.

We appreciate your confidence and trust.

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