

## Market Update

### March 2025

The U.S. economy is showing signs of contraction as the first quarter of 2025 unfolds. The Atlanta Fed's GDPNow model projects a 2.4% decline in Q1. This adjustment follows weak January consumer spending data, which fell 0.2% instead of rising as expected. When adjusted for inflation, spending dropped 0.5%, reducing GDP contributions by a full percentage point.

The labor market presents a mixed picture. February saw the addition of 151k jobs, slightly below expectations of 160k, while the unemployment rate edged up to 4.1%. Gains were concentrated in healthcare, financial activities, and transportation, while government employment declined by 10k amid DOGE related cuts. Despite this, the unemployment rate has remained relatively stable between 4.0-4.2% since mid-2024.

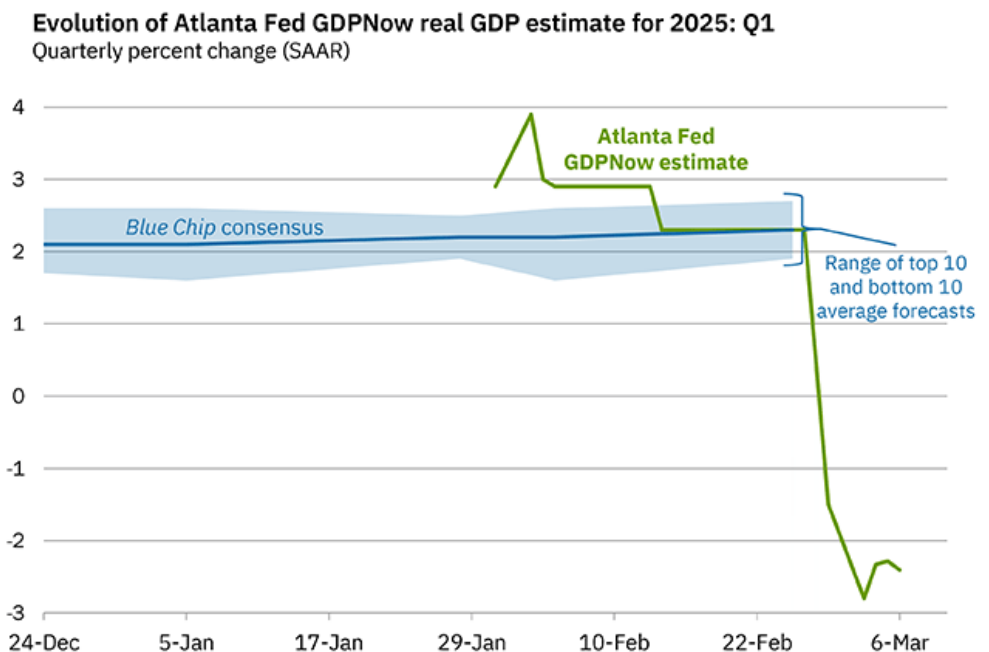
Inflation remains a persistent issue, particularly in housing. Zillow's rental costs rose by 3.5% year-over-year in January, with Bureau of Labor Statistics data showing rents up by an even higher 4.2%. Housing costs remain high as the ratio of house prices to rents has surged 20% since early 2020, nearing its 2006 peak. This imbalance poses risks for future inflation, as normalization could involve either falling home prices or accelerating rents.

President Trump's economic policies center on deregulation and tariffs. His deregulation efforts, particularly in energy, aim to boost investment and growth. Recent 25% tariffs on Mexican and Canadian imports, effective March 4, 2025, highlight his use of trade policy as a negotiation tool. We are already seeing signs of flexibility and strategic exemptions (e.g. autos) in response to industry concerns and ongoing negotiations.

The yield curve inversion between the 10-year and 3-month Treasury rates has returned, reinforcing its historical signal of a potential recession. Coupled with the GDP outlook, this has fueled speculation about Federal Reserve policy easing in the future. While pressure for rate cuts to counter the slowdown, persistent inflation complicates the decision-making process. The market's pricing of three rate cuts before year-end feels excessive, though not unreasonable. Ultimately, it will come down to consumer resilience and strength in employment.

Geopolitical tensions add another layer of uncertainty for markets. Expanding trade disputes threaten global supply chains and could exacerbate inflationary pressures while dampening growth prospects both domestically and internationally. Retaliatory tariffs from key trading partners remain a significant risk for U.S. exporters.

As multiple factors converge, market volatility is likely to remain elevated in the near term as investors reassess growth prospects amid shifting monetary policies and geopolitical developments. We see this volatility as an opportunity for investors.



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## Product Views

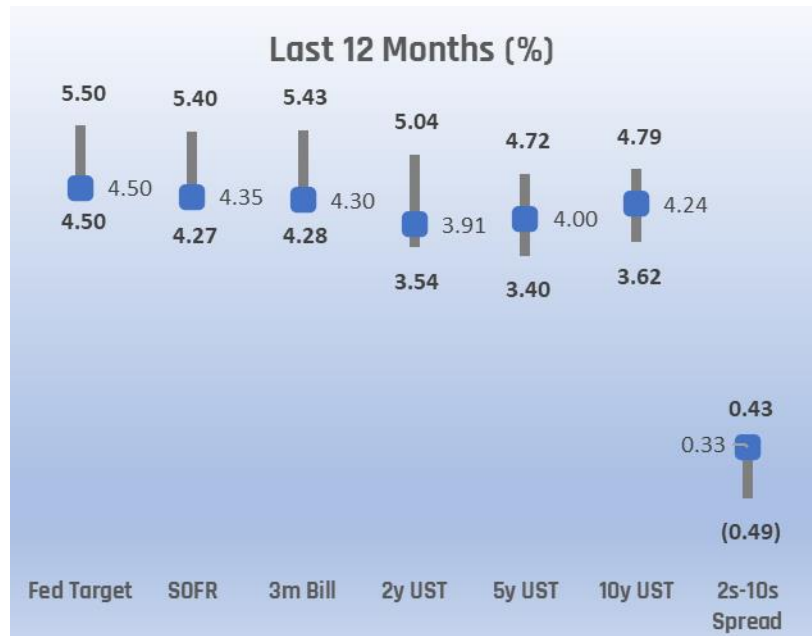
**Rates:** Treasury yields have been volatile in 2025, reflecting shifting economic expectations and policy uncertainties. The 10-year yield fell for seven straight weeks, dropping 22 basis points to 4.21% in early March, while the 2-year dipped below 4.00% for the first time since October 2024. Markets appear to be pricing in slowdown risks, potentially accelerating Fed easing.

The 2s-10s spread has steepened as investors weigh growth and inflation risks from new tariffs. Short-term rates remain anchored by Fed expectations, while long-term rates face opposing forces. We will look to use anticipated volatility to add duration in the front and intermediate parts of the curve.

**Credit:** Investment-grade (IG) corporate bonds continue to trade at historically tight spread levels despite recent volatility, recently widening to 87 bp amid a risk-off environment driven by uncertainty.

Credit fundamentals appear stable, though there is potential for increased debt-funded M&A activity. We are focused on Financials and Energy, which could benefit from deregulation, while maintaining caution on Consumer and Retail sectors, which may face margin pressure from tariffs and immigration policy.

**Securitized:** Commercial mortgage-backed securities (CMBS) have rebounded, posting the decade's highest excess returns. With the shift from remote work, the office market is stabilizing. We see targeted opportunities in Class A properties with proper credit assessment. Agency mortgage-backed securities (MBS) have led securitized assets. While nearing fair value, they remain a defensive play versus ABS, CMBS, and corporates while still generating excess returns.



12 month high  
Current  
12 month low

