Quarterly Economic and Market Review

Q1 2025

David Lundgren, CFA
Executive Vice President & Chief Investment Officer

Stephen Morgan
Senior Vice President & Chief Investment Director

Paul Teten, CFA
Senior Vice President & Chief Investment Strategist

Martin Sirera, CFA
Senior Vice President & Director of Equities

Jeffery Tanguis
Senior Vice President & Director of Fixed Income

Richard Chauvin, CFA
Senior Vice President & Investment Director

Policy Blitz Sacks Stocks

David Lundgren, CFA

During the quarter, the spotlight shifted squarely back to Washington, D.C., as the Trump administration rolled out a rapid and aggressive policy agenda, shaking up the market narrative that had been largely focused on the Federal Reserve and inflation over the last two years. The administration's four policy pillars—taxes, tariffs, deregulation, and deportations—delivered a jolt to the political and economic landscape. This "policy blitz" introduced new layers of uncertainty that reverberated through markets, with the tariff agenda becoming a focal point for investors concerned about inflation, growth, and the durability of the current economic expansion.

To understand the significance of this moment, it is worth recalling where the economy stood at the start of the year. After two years of stellar stock market performance—driven heavily by large-cap growth names and AI enthusiasm—investors entered 2025 optimistic but cautious. The Federal Reserve had successfully helped guide inflation towards their 2% target by late 2024 and was on a path to policy normalization. Interest rate cuts were expected, and hopes for a soft landing were high. However, that optimism quickly ran into political headwinds.

POLICY SHOCKWAVES FROM THE WHITE HOUSE

The administration wasted no time in implementing its second-term agenda. On taxes, renewed efforts to extend and expand the 2017 tax cuts made headlines. While corporate America praised the prospects of lower effective rates, bond markets took notice of the implications for an already ballooning federal deficit.

Deregulation also picked up steam, particularly in the energy, environmental, and financial sectors. While this was met with applause from certain business constituencies, the celebration was limited as DOGE and other initiatives dominated the headlines.

Deportation policies and broader immigration restrictions introduced labor market uncertainty, especially in sectors reliant on migrant labor. From agriculture to hospitality, employers expressed concern about wage inflation and labor shortages. The deportation focus to date has been primarily on criminals and less productive members of communities leaving the broader labor market balanced and healthy with unemployment at 4.0%. However, immigration questions persist, and when combined with a slowing economy, cracks have emerged as job growth slows and wage pressures build.

TARIFFS AND THE NEW TRADE WAR ERA

Of the four pillars, tariffs were the most market-impactful and have quickly become the most economically consequential. While the stated intent is to protect American industries, the downstream effects have been anything but simple. The policy has introduced cost pressures across supply chains, reduced corporate margin visibility, and invited retaliatory actions and soured diplomatic relations from key trading partners.

Uncertainty around tariffs has already begun impacting economic behavior. Several multinationals have announced delays in capital spending and expansion plans, citing unpredictability in input costs and global demand. Consumer confidence fell sharply during the quarter, as evidenced by the Conference Board's index hitting its lowest level in more than a decade. Retailers and manufacturers alike have revised guidance downward, warning of margin compression and softening demand.

Perhaps most importantly, the tariff overhang has reignited inflation concerns. The Fed's preferred inflation gauge—the Core PCE index—ticked up to 2.8%. While still within a reasonable range, the sudden reversal and general stubbornness in inflation momentum has complicated the monetary policy outlook, leading some Fed officials to advocate a more cautious approach to rate normalization.

The S&P 500 experienced its first 10% correction since 2022 during the quarter but was helped by a strong start to the year finishing down almost 5% for the quarter.

MARKETS: FROM EUPHORIA TO VOLATILITY

After a blockbuster run for equities over the past two years, led by the so-called "Magnificent 7" growth stocks, the first quarter of 2025 brought increased volatility and difficult results. The S&P 500 experienced its first 10% correction since 2022 during the quarter but was helped by a strong start to the year finishing down almost 5% for the quarter. The Nasdaq Composite fared worse, dropping more than 10% for the quarter, its worst quarter since 2Q 2022. Investors used the quarter to reassess valuations that had become stretched by historical standards, especially given the increased macroeconomic and geopolitical uncertainty.

Developed international stocks—as represented by the MSCI EAFE Index—outperformed U.S. large-cap equities by a wide margin (over 11%) during the quarter. This marked one of the largest quarterly out performance by international developed markets relative to U.S. large caps in almost 40 years. This reversal comes after more than a decade of consistent U.S. outperformance. Several factors contributed to the out performance: renewed trade policy concerns following political developments in the U.S., stretched valuations in U.S. equities—particularly tech—and a weakening dollar, which improved returns for dollar-based investors in foreign markets.

At the same time, we witnessed a classic "flight to quality." With equity volatility rising and the economic outlook clouding, capital flowed into bonds, sending yields lower and providing a welcome tailwind to fixed income returns. After an uninspired 2024 for bond investors, Q1 2025 was among the strongest quarters for core bond portfolios in 25 years. Duration exposure paid off handsomely, and the diversification benefits of bonds were on full display.

AMERICAN EXCEPTIONALISM: AN OPEN QUESTION

Looming over all these developments is a renewed debate around American exceptionalism. Once considered an unshakable pillar of the global order, questions are being asked anew: Can the U.S. still serve as the world's anchor of stability? Can it grow robustly in a self-restricting trade environment? And does it still possess the political will and cohesion to lead globally in the face of domestic division?

These questions are not just philosophical—they have real market consequences. Capital flows, foreign investment, currency strength, and inflation expectations are all partially driven by confidence in U.S. governance and leadership. The events of Q1 suggest that investors may be recalibrating their assumptions. For the first time in years, we are seeing signs of concern not just about cyclical headwinds, but about structural ones as well. Hancock Whitney's Chief Investment Strategist, Paul Teten, dives deeper into this important discussion in the pages to follow.

For the first time in years, we are seeing signs of concern not just about cyclical headwinds, but about structural ones as well.

LOOKING AHEAD

As we move into the second quarter, the landscape remains murky. The Fed is navigating a more complex policy environment than it anticipated. Investors are parsing a White House agenda that seems poised to disrupt as much as it aims to reform. And the market is showing early signs of exhaustion after a long and impressive run. The coming months will test the resilience of both the U.S. economy and investor confidence in the American story.

In the following pages, senior leaders of the Hancock Whitney Asset Management team delve further into these topics, providing comprehensive analysis and insight into the evolving financial landscape. We are available to discuss these issues in greater detail, offering a nuanced understanding of the market dynamics and their implications for your personal financial situation.

Policy Rolls Out at Top Tempo[12-26]

Stephen Morgan

> "I got new rules; I count 'em."
>
> — NEW RULES (2017), DUA LIPA

NEW RULES

The second inauguration of President Donald Trump launched a flurry of federal executive activity at a scope and pace seen few times in U.S. history. Following a playbook likely developed during his interregnum, President Trump and his top advisors have pursued a program with the potential to reshape not only the executive branch but the relationship among the branches of government, and the economic and geopolitical world order. Between his inauguration and the end of the first quarter, Trump had issued over 170 Presidential actions including 109 executive orders, 24 proclamations, 27 Presidential memoranda and various nominations and clemency actions, already surpassing Franklin D. Roosevelt's first 100 days and dwarfing all others.

The quickfire pace has left business leaders, political actors, and investors scrambling to respond to the rapidly shifting policy and economic landscape amidst a fog of uncertainty. Beyond "flooding the zone" to overwhelm opposition, the White House is harnessing the political momentum coming out of the President's November popular vote victory to advance its goals before the natural friction of governing sets in. Unsurprisingly, the action has touched all four pillars of President Trump's agenda that we have identified as key to the economy and markets, which we have dubbed the DT2 agenda: 1) Deportation and Border Security, 2) Tariffs and Trade, 3) Deregulation, 4) Taxes and Spending.

> "Do you ever wonder? That to win somebody's got to lose?"
>
> — AND THE BEAT GOES ON (1979), THE WHISPERERS

PICKING LOSERS

Among these, tariffs have clearly emerged as the central economic theme of the early days of the new administration. A regular drumbeat of trade policy news has moved from the business section to above the first page fold, spooking consumers and altering corporate strategies in the short-term and casting doubt across long-term plans (see Paul Teten's economics section). As the quarter closed, investors were anxiously awaiting the "Liberation Day" announcement of a broader, more comprehensive tariff regime. It turned out to be even more extensive than market participants had expected imposing near-universal levies of at least 10% on goods entering the U.S. with many countries – including traditional partners – facing substantially higher rates. The new tariffs are a depth charge to existing global trade foundations, raising the dual specters of higher inflation and lower growth but also creating substantial incentives for companies to shift production to the U.S. and leverage to boost U.S. exports to protectionist nations.

Analysts estimate that the already-announced levies will send the U.S.'s effective tariff rate vaulting from around 2% to 20% or more—the highest level since 1936, the pre-containerized era of the tramp steamer. They would also draw about $600 billion into federal coffers over a year, partially paid for by consumers, exerting upward pressure on inflation in the short-term as prices adjust to the new barriers. However, we also expect producing nations and companies will eat large portions of the cost in order to maintain market share.

However, these analyses assume that the tariff policy remains in place and that is not likely. We have seen, for example, tariffs threatened or announced but then reversed, delayed or suspended. There is also the threat of further tariff impositions – notably on imports of pharmaceuticals and semiconductors. That uncertainty may, in the end, pose the greatest economic risk from the restrictive trade policies. Companies will hesitate to make investments that may be undermined by future reversals, and consumers, hoping for a cheaper future, delay consumption.

Many nations have announced plans to impose retaliatory tariffs on U.S. goods and the European Union is reportedly considering taxes on digital services, targeting U.S. tech giants. These commercial conflicts – especially with long-standing allies – coupled with inflammatory rhetoric from President Trump, Vice President JD Vance, and others may well have broader impacts as Richard Chauvin discusses in the geopolitical update section.

> “I’m a peeping-tom techie with x-ray eyes.”
>
> — THE FUTURES SO BRIGHT I GOTTA WEAR SHADES (1986), TIMBUK3

BROTHER, CAN YOU SPARE A DOGE?

The magnitude of potential tariff revenue has linked trade to another of the President’s economic columns, the extension and expansion of the tax cuts that he views as a crown jewel of his first term. The tariff income estimated above would exceed total income from corporate income taxes, providing significant cushion for lower personal and corporate income taxes. That’s an important selling point for deficit hawks in Congress which holds the power to establish tax policies.

President Trump’s vision for a smaller executive branch with expanded Presidential authority also paves the path for lower taxes by trimming the spending side of cash flow. The headline effort here has been, of course, the informal Department of Government Efficiency headed by Elon Musk which has reached into various corners of the federal government, applying artificial intelligence and other technology to identify “waste, fraud, and abuse”. Musk’s efforts form part of a wider tapestry that would see a smaller federal workforce using updated technology.

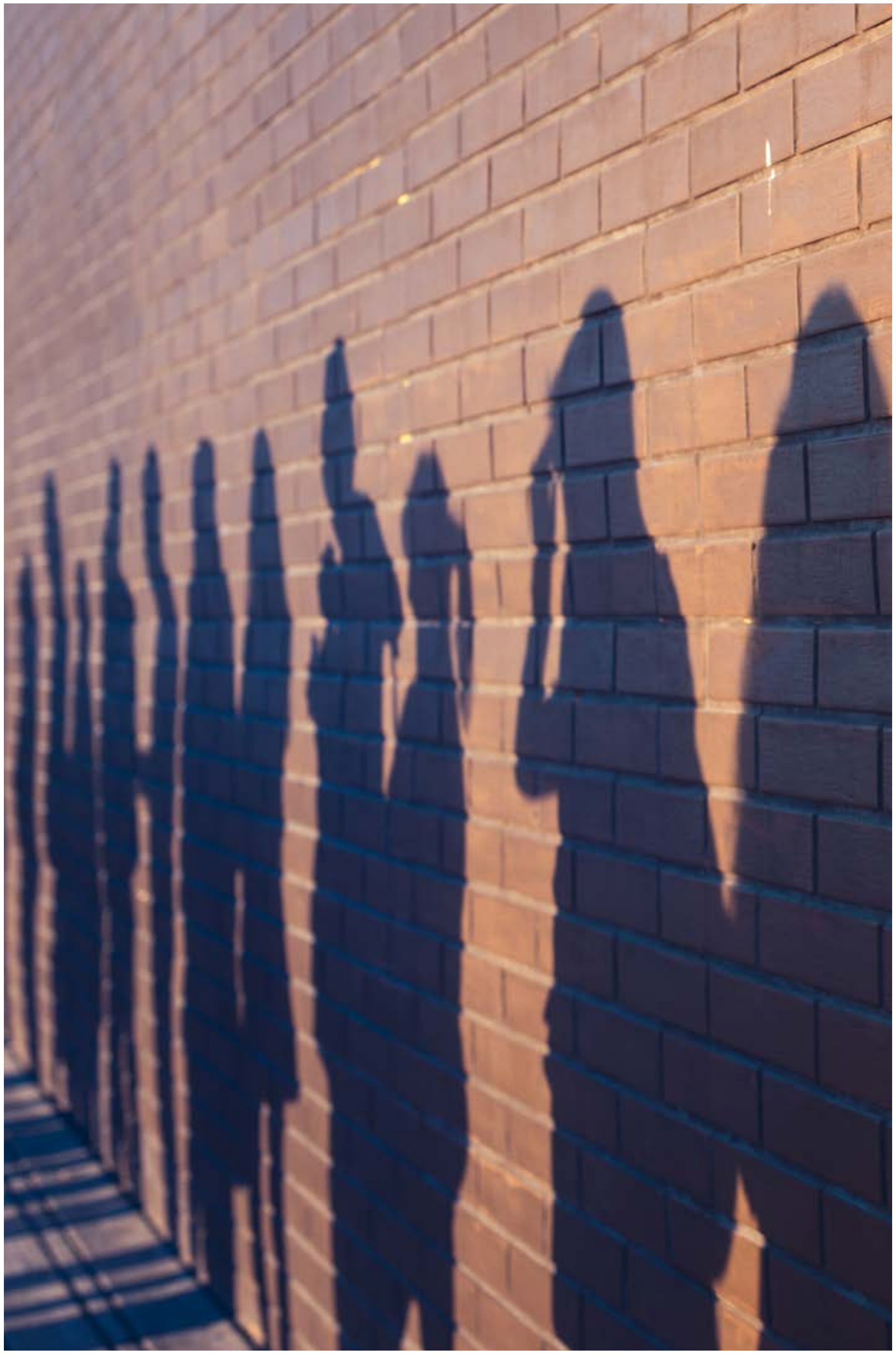
The administration has temporarily frozen some spending, moved to eliminate programs and agencies, and acted to slash federal payrolls. Many of these actions have invited questions about the limits of Presidential authority over spending directed by Congress, kicking off court battles. The White House has offered some deference to Congressional prerogative. After issuing an Executive Order for the Secretary of Education to take all necessary and legal steps to close her department, they noted that fully dismantling the department would require Congressional action. The speedy cuts also raise concerns about the level of analysis being applied and unforeseen risk.

> “Do this. Don’t do that. Can’t you read the sign?”
>
> — SIGNS (1971), THE FIVE MAN ELECTRICAL BAND

CLEARING THE PATH

Deregulation featured prominently in the early days of the first Trump administration but has not gathered as much attention this year. While it is not gathering the same headlines, however, it is an emerging feature. The White House has frozen new regulation and the Environmental Protection Agency has begun the process to rollback over 30 currently effective regulations.

The President has also moved to limit the independence of agencies like the Federal Trade Commission and the Securities & Exchange Commission.



> “All the Federales say, they could have had him any day.”
>
> — PANCHO & LEFTY (1972), TOWNES VAN ZANDT

CLOSING THE GATES

Border security has remained a major focus for the President, and his administration has taken several highly visible deportations. However, so far, we have not seen a systematic program of workplace enforcement actions. Given low unemployment rates and the high incidence of undocumented workers in key sectors like construction and agriculture we have apprehension that an overly vigorous approach could raise consumer costs and impair economic growth. Meanwhile, encounters on the southern border have fallen off.

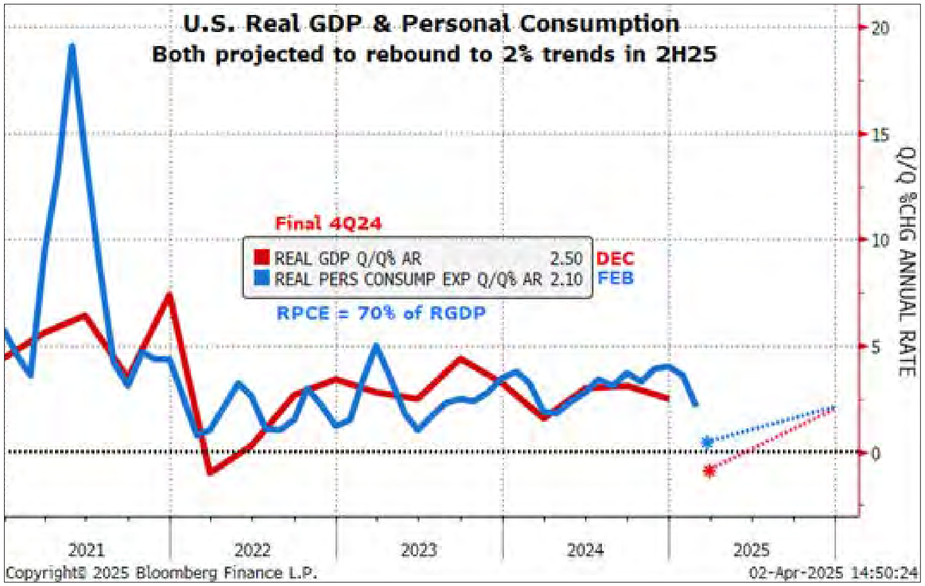
> “Oops...I did it again.”
>
> — OOPS, I DID IT AGAIN (2000), BRITNEY SPEARS

BUDGET BATTLES

Congress averted a government shutdown by passing a Continuing Resolution that mostly maintains spending at 2024 levels for the rest of the 2025 fiscal year which ends September 30. While this resolves the current year without passing a full budget, it leaves several open items. Most urgently, the Federal Government has hit its debt ceiling with the Treasury now taking its ordinary “extraordinary measures” to maintain spending. Those special measures are expected to run out in late August or September; absent Congressional action that could again trigger a government shutdown and eventually risk technical default on the debt. Late in the quarter Congressional GOP leaders agreed to address the debt ceiling in a budget reconciliation planned to enact tax reforms and other priorities. The effort to shape that legislation, though, still has some distance to go to gather enough support for passage.

Welcome back, President Trump, but please don’t blow up the U.S. economy![1,2]

Paul Teten, CFA



OFF TO A ROCKY START

1Q25 got off to a rough start with the Southern and Eastern seaboards buffeted by a polar vortex which froze economic activity for an extended period in January, while wildfire chaos on the West coast simultaneously flared in the nation’s 2nd largest metropolitan area. Household spending plunged, but the expected February rebound failed to materialize, presumably due to the billowing cloud of doubt surrounding the launch of the tariff agenda, prominent with the singularly irritating phrase for consumers: higher prices. Coupled with DOGE disturbances to several federal agency workforces and aggressive deportations of criminal migrants, hinting at the possibility of workplace interventions and disruption to the labor market, consumer sentiment plunged and there was no spending rebound in February and prospects for March do not look particularly hopeful. Our assessment is that real, inflation-adjusted, household consumption of goods and services, constituting 70% of Real GDP, will be close to unchanged in 1Q25, down from a brisk 4.0% Q/Q annual rate in 4Q24, qualifying as a screeching halt to consumer spending.

Simultaneous with the consumer funk, imports surged into the country in January and February to front-run the expected tariff implementation, which we estimate will exacerbate the U.S. chronic trade deficit and reduce the 1Q25 Real GDP Q/Q AR by a stunning 1-2%. An expanding trade deficit reduces GDP since the income from the consumption of imports is owned by foreign entities. Thus, the combination of stagnant consumer spending and the exploding trade deficit guide our estimate for 1Q25 Real GDP down from 1.5-2.5% Q/Q AR just a few weeks ago to a range from zero to -1.0.

IT ONLY LOOKS LIKE A RECESSION

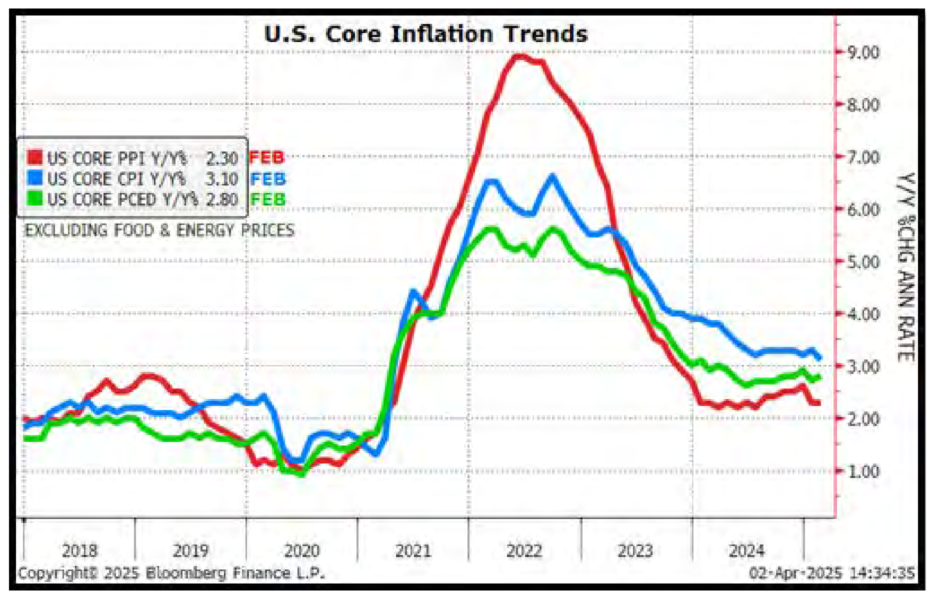
That's an astounding reversal of fortune, driven largely by behavioral shifts resulting from the shock and awe of the Trump agenda roll-out, which has singed consumers and markets alike. Now, in the wake of the unveiling of global tariffs on "Liberation Day" April 2, more economic disturbance appears likely in 2Q25, mostly resulting from global supply chain disruption. The bulge in the trade deficit is likely to reverse in the months ahead as imports normalize and perhaps recede below last year's levels if the tariff initiative turns out to be effective, potentially additive to GDP. The good news is that the suddenly weak economy is underpinned by solid fundamentals, including relatively full employment, strong consumer balance sheets, ample liquidity, downward trending interest rates and consumer purchasing power boosted by low inflation, which we anticipate will be only marginally impacted by tariffs. Our assessment is that while recession risk has risen, it is not a foregone conclusion, and the healthy and balanced U.S. economy is likely to power through the next few months in decent shape, with the more growth supportive initiatives of tax cuts and deregulation taking center stage in the fall.

The good news is that the suddenly weak economy is underpinned by solid fundamentals... which we anticipate will be only marginally impacted by tariffs.

A more pertinent risk to the macroeconomic outlook is the potential for labor market disruption from the DOGE downsizing of the federal bureaucracy and the deportation agenda. If the deportation initiative refocuses from prisons to workplaces, which may be a low probability due to capacity constraints, the potential for economic disruption would rise. Our assessment is that the now closed border will dry up the supply of cheap migrant labor which benefited economic growth from 2022-2024. The native-born workforce, accounting for 80% of the labor pool, is fully deployed has been exhibiting gradually deteriorating labor demand since mid-2023, characteristic of the late-cycle conditions in the U.S. economy. Our expectation is that a gradually rising unemployment rate is probable this year, and likely also to prioritize the Fed's attention toward its jobs mandate over its inflation mandate, which plausibly can be deemed acceptable under the circumstances.

THE DISINFLATION CYCLE IS ALIVE

We continue to maintain that the disinflation cycle engineered by restrictive Federal Reserve monetary policies is continuing and will slowly glide lower toward the Fed's 2% target for the core personal consumption expenditure (PCE) deflator this year. Critically, January and February reports for the Fed's designated inflation barometer have not repeated the disappointing mini surge seen in the same months last year, which is driving the key Y/Y growth metric down from 2.9% in December toward our expectation of 2.5% in March, based on the Federal Reserve's real-time tracking model. It's a big win in the inflation fight for the core PCE deflator to trend lower in the first quarter, which is prominently front-loaded with annual price increases. Unfortunately, the good news has been overshadowed by rising concern that the tariff agenda will swamp the disinflation cycle. Consumer surveys indicate widespread expectations that inflation rates will rise to 4-5% in the year ahead, which we regard as exaggerated fears. The Federal Open Market Committee (FOMC), the Fed's policy-making body, recently revised its forecast for core PCE Y/Y inflation this year from 2.5% to 2.8%, which is similar to what we see in market-based expected near-term inflation measures. It is not at all clear that tariffs will drive a significant and sustainable acceleration U.S. inflation, and we concur with the FOMC forecast that a limited, marginal increase is in the ballpark of likely outcomes.



AMERICAN EXCEPTIONALISM...

…is generally understood to be the benefits derived from a bedrock reliance on free market capitalism, entrepreneurial opportunity, low regulation and an educated workforce; including sophisticated financial markets and accessible capital, leading industrial innovation, productivity growth, strong economic growth among developed countries, typically low inflation, a high per capita standard of living, a stable currency and a resilient capability to recover quickly from economic recessions and other cyclical disruptions. All this despite a relatively open market domestically for trading partners to sell their goods to U.S. consumers, much to the foreign producers' benefit.

It has lately become fashionable among some financial market commentators to conjure an end to American exceptionalism, based largely on the Trump administration's America First themes and the cornerstone policy of an aggressive tariff agenda, presumed to be destined to levels not seen since the 1930s, with such abdication of free trade principles portending for those commentators a significant economic slowdown, in the U.S. at least, if not globally.

Our observation is that in order for there to be a substantial economically injurious result from the lack of free trade, free trade must first exist, which certainly is not the case, apart from the modest success of the North American Free Trade Agreement, launched in 1994 and modified in President Trump's first term in 2018, renamed the United States-Mexico-Canada Agreement (USMCA, note the dismissal of the phrase Free Trade). Otherwise, global trade operates under a patchwork of bilateral agreements and tariff treaties, a charade of free trade supervised by the World Trade Organization (WTO). The nominal protector of global trading rules since its launch in 1995, the singular achievements of the WTO have been the accession of China into the treaty in 2001 and the persistent denial since of U.S. claims of unfair Chinese trading practices which have had the effect of hollowing out U.S. manufacturing.

The Trump agenda is aimed at recharging and energizing the productivity and innovation at the core of America's economic leadership.

Our view is that the Trump administration's confusing, caustic and erratic ramp up of the tariff agenda, larded with bombastic taunts to historically close allies and trading partners, is the primary source of the uncertainty and risk aversion that has resulted in the stock market correction which began in mid-February. There has been a compelling case for an aggressive tariff imposition against China since they joined the WTO in 2001. President Trump started down that road in 2018, the Biden administration kept those tariffs in place, and in escalating the effort now, China is the raison d'etre for the Trump tariff agenda. The case is less strong against most other trading partners for a variety of non-tariff considerations, while there are significant tariff loopholes that need closing, see China's U.S. bound exports transiting through Mexico. The administration would be well advised to consider the wisdom in the law of comparative advantage, one example of which is that it is better to buy tequila from Mexico and sneakers from Viet Nam than make either. Following the big, beautiful reciprocal tariff announcement on Liberation Day, April 2, no joke unfortunately, we expect to see ongoing negotiations and a variety of accommodations to ease the tariff burdens for companies who see the value in basing operations in America.

Suffice to say our view is that American exceptionalism, while corroded in some respects from bureaucratic sclerosis, regulatory overreach and industrial policies, is alive and well. The Trump agenda is aimed at recharging and energizing the productivity and innovation at the core of America's economic leadership. Decoupling from China is overdue and the reshoring to America of high-value production destined to American consumers is likely to spur American economic growth and opportunity, facilitating global leadership.

Weak Stock Market Foreshadows Tariff Risk[3,4]

Martin Sirera, CFA

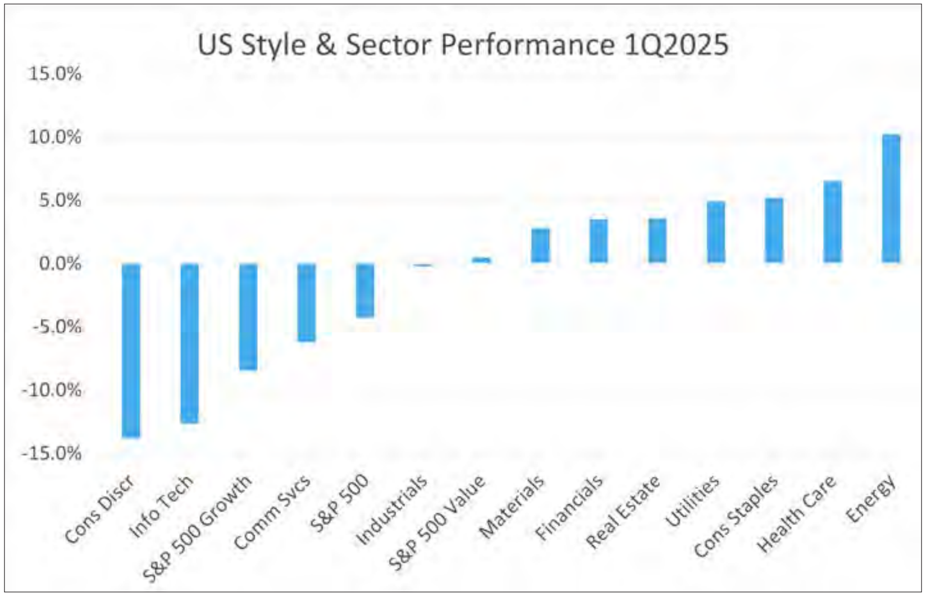
VOLATILE FIRST QUARTER

For equity markets, the first quarter of 2025 was like a roller coaster on cobblestones. First it was up, then it was down, and it was bumpy the whole way. The year opened with equity investors' psyches in pretty good shape. A new regime in Washington, D.C. was taking over and promising an environment more friendly to private sector production activities compared to the departing crowd. The promise of lower tax rates and lower regulatory burdens were enough to send global equity markets broadly higher across the first six weeks of the year. But as the economic policy conversation turned to much more of a protectionist focus, including tariffs and border controls, the jostling along the tracks sent investor moods tumbling. And for the first time in a while, there is competition for the performance lead among categories of stocks.

For the full first quarter, the S&P 500 Index posted a total return of -4.3%, the first down quarter since the third quarter of 2023, and the worst since the third quarter of 2022, which capped off the last meaningful bear market. The decline was driven by, and very much limited to, Technology sector stocks such as Apple, Microsoft, and Nvidia, but also including those not in the Information Technology Sector, such as Alphabet, Amazon, and Tesla. In fact, for the quarter, the Energy, Materials, Consumer Staples, Health Care, Financials, and Real Estate sectors all rose, while the Industrials sector was down only slightly. In general, Value stocks rose while Growth stocks fell.

Perhaps the most interesting aspect of first quarter stock market performance is that non-U.S. stock markets, particularly those in developed nations, outperformed the U.S. market by a wide margin. In fact, the difference between the MSCI EAFE Index and the S&P 500 Index for the quarter – 11.1% – was the largest since the fourth quarter of 1988.

Most other non-U.S. equity markets and categories posted positive results for the first quarter, so the first quarter decline was somewhat limited to the largest U.S. growth companies. For a change, equity diversification was helpful rather than harmful. The key dilemma for equity investors long accustomed to U.S. large cap dominance, is whether the markets are transitioning to a new cycle or merely experiencing a bump on the road (tracks).



DIMINISHING GROWTH EXPECTATIONS

While investor psychology has been challenged by the pace, volume, and seeming haphazardness of the new tariffs and other Trump Administration initiatives, the impact of the initiatives is being factored into expectations about near-term future growth. In the aggregate, investors are cutting back their forecasts for earnings growth here in the U.S. For the first quarter of 2025 (the results of which will be coming in corporate earnings reports over the next six to eight weeks), the forecasted growth rate for S&P 500 EPS has fallen about 40%, from a forecasted growth rate of 11.6% on 12/31/2024 to 7.0% on 3/31/2025.

The diminished growth expectations are mostly a function of higher expected expenses and the resulting thinner expected profit margins. Yet, revenue expectations are also declining. The forecasted growth rate for S&P 500 Sales for the first quarter currently stands at 4.2%, down about 17% from the 5.1% forecasted growth rate on 12/31/2024. Analysts have also adjusted their sales and EPS forecasts for the next few quarters downward, as well, but to a lesser extent.

This is quite rational and not merely the reaction of investors being spooked by the hyperactivity new administration. Tariffs are taxes, after all, and the imposition of them on the economy takes money out of the coffers of the private sector and puts it into government coffers. Expected growth rates, therefore, must be adjusted lower to account for not only the direct impacts – i.e,. higher expenses – but also the future compounding effects, like reduced incomes leading to reduced spending.

Consumers already have been reigning in expenditures. Economists' GDP estimates for the quarter just ended have been sharply reduced as a result mainly of these pullbacks. A significant risk to the overall economic situation is the potential for this consumer recalcitrance to extend further into the future. Should consumers become much less willing or able to spend in this volatile environment, recession risk grows.

Business behavior is also subject to the heightened uncertainty driven by this current environment. The first signs of concern are beginning to show up in CEO and CFO business optimism surveys. Capital expenditure growth is highly dependent on business outlooks and while optimism had been rising in the recent past, the most recent measures point to a little bit of doubt creeping in.

SIGNS OF UNDERLYING STRENGTH

Somewhat offsetting this fairly bleak picture of tariffs are the promises made by the President on the campaign trail: namely, that the corporate tax rate would be cut and that regulatory burdens would be lowered. Those things would be direct offsets to the cost of new tariffs. They would help businesses harmed by higher import-related costs. Unfortunately, the markets have observed no movement on the corporate tax issue yet. There are many signs of the positive movement in the direction of reduced regulations. However, the lack of a currently visible legislative initiative on lower income tax rates to offset the higher tariff taxes stands out as a cause of concern.

S&P 500 EPS are still forecasted to grow by over 10% both in 2025 and in 2026.

In the midst of the disruption of the tariffs, there are indicators of underlying economic strength in the U.S., economy. Real disposable personal income growth has recently been positive, that is, it has been outpacing inflation. And it has been gaining a little upward momentum lately. Payroll growth has been positive and has been steady since early 2023. Business investment, albeit with a little bit of a cloudy future as noted above, has been expanding lately. And even though profit growth expectations are being trimmed, S&P 500 EPS are still forecasted to grow by over 10% both in 2025 and in 2026.

OUTLOOK

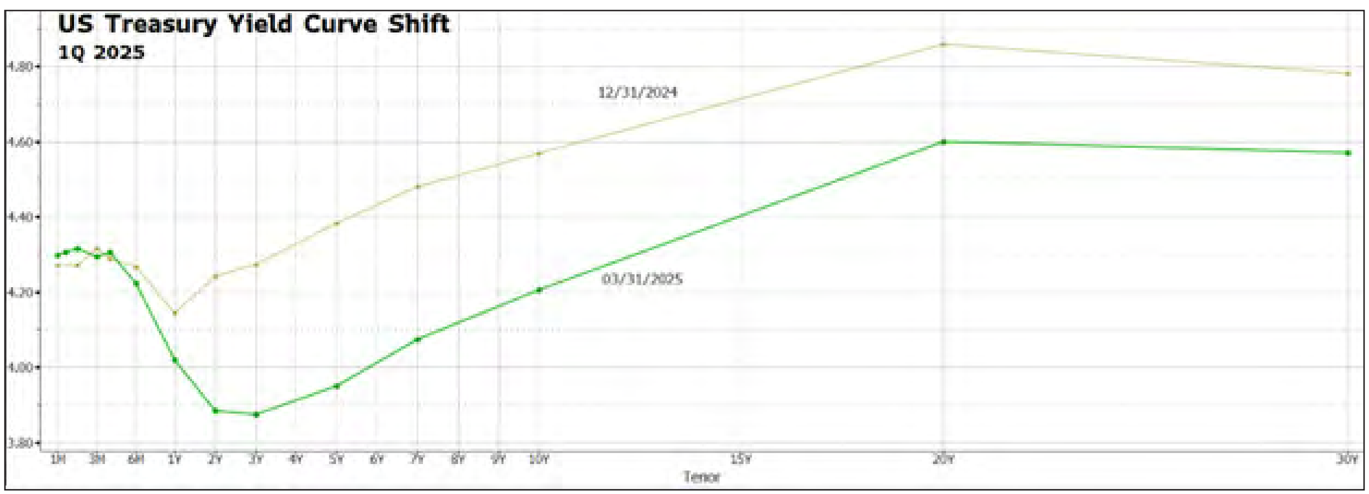
In this environment, volatility (risk) has risen. Measures of volatility have themselves been volatile. In the immediate aftermath of the November election, investors became extremely content. The VIX Index, which attempts to forecast near-term future S&P 500 volatility by measuring the cost of insurance, tumbled lower in November and December. Coupled with the rise in prices during that period, this indicated an strong sense of optimism about the future with the incoming Administration and Congress. However, U.S. stock market valuations were stretched even further. As the picture has become more clouded, those extreme valuation levels have contributed to a surge in risk. The VIX Index has spent the first three months of 2025 on a very volatile uptrend.

Investors are clearly anxious, and justifiably so. The near-term economic outlook is very important to consider to assess stock market potential right now. Unfortunately the tumultuous nature of the Washington D.C. environment adds to the overall level of uncertainty. In the most likely scenario, economic growth continues to slow a bit yet remains positive. In such an environment, should the markets be able to detect that negative tariff impacts will be offset by other policies like reducing tax rates as well as by positive impacts (i.e., onshoring manufacturing), stock prices are likely to have limited downside from here. In the less likely scenario of an extended period of consumer retrenchment driving the domestic economy into an actual recession, corporate sales will decline, profit margins will be squeezed, and profits suffer. In this scenario, mid-2025 could see more tumult in equity markets.

Safe-Haven Stampede Fuels Bond Market Rally[1]

Jeffery Tanguis

The bond market got off to a shaky start in 2025 before finding its footing in mid-January and chalking up sizable gains during the balance of the quarter. Demand from investors seeking refuge from the extreme volatility in the equity markets and a hedge against rising concerns over U.S. economic growth were the dual drivers of the safe-haven rally. Uncommonly erratic day to day bond market action was a hallmark of the quarter, a product largely of the bewildering impact of the Trump administration's shifting tariff policy on inflation and economic growth. Short to intermediate term maturity Treasury yields ratcheted lower during the period finishing down on average -35 basis points. The Federal Reserve gets little credit for the bond market rally. The benchmark federal funds rate was left unchanged during the quarter with the central bank sidelined by uncertainty and indecision. The intermediate term investment grade bond market as evidenced by the Bloomberg Intermediate Aggregate Bond Index generated a well above average total return of 2.61% for the 3-month period. Mortgage-backed securities were easily the top performing sector producing a 3.06% return. Intermediate term Treasury securities also shined in the flight to quality environment returning 2.49%. Intermediate investment grade corporate bonds trailed slightly under the prospect for a slowing economy but still returned a respectable 2.27%. By almost any measure the first quarter was a good one for bond investors and a textbook example of high-quality bonds providing welcomed stability to balanced portfolios during times of equity volatility.



BONDS START SLOW BUT FINISH STRONG

The quarter began with a brief run of better-than-expected economic reports that stoked inflation worries and kept bond buyers on the defensive. Wall street economist started pushing back Fed rate cut forecasts for 2025 following a surprisingly robust employment report in early January that contained an unexpected dip in the unemployment rate to 4.1%. An assortment of hot inflation indicators further spooked bond investors and sent interest rates higher. By mid-January market expectations were clinging to a single October Fed rate cut for the entire year, down from forecasting 3 cuts in 2025 late last year. Peak interest rates for the quarter occurred on Jan14th with the release of the December Consumer Price Index (CPI) which showed underlying disinflation trends remained intact. From that day forward interest rates would zig zag lower to close out the quarter. Cratering equity markets, falling consumer sentiment and daily headlines of federal government job and spending cuts cast a shadow of gloom that sent investors scrambling to buy safe-haven assets like investment grade bonds.

FEDERAL RESERVE SITS THIS ONE OUT

In atypical fashion the Federal Reserve played only a bit part in the strong bond market performance during the quarter. The policy committee met twice during the quarter and both times elected to leave rates unchanged. Chairman Powell made clear the policy committee's unanimous desire to take a "wait and see" approach toward Trump's tariff proposals and their potential inflationary impulse. Powell repeatedly drove home the point throughout the quarter that the Fed "does not need to hurry" to lower interest rates. Inflation will continue to get a lot of lip service from the Fed, but a rising unemployment rate is what really keeps Chairman Powell up at night. The Fed is on record forecasting a rise in the unemployment rate to 4.4% by yearend. Look for the Fed to fast-track rate cuts if unemployment gets anywhere near their forecast. At the March Fed meeting Powell opined that not all tariffs cause persistent inflation, and the Fed might choose to look past a one-time blip in tariff generated inflation. The comment brought painful flashbacks of the 2021 episode of "transitory" inflation. Also at the March meeting, the policy committee maintained its December forecast for two rate cuts during 2025. Both the equity and bond markets breathed a sigh of relief at the news. The Fed did take one important action this quarter though not technically a monetary policy move. Policymakers took a big step toward ending quantitative tightening, a program geared toward returning (shrinking) the Fed's massive balance sheet back to more normal pre-Covid levels. The move effectively halts the draining of liquidity from the global financial system and ensures ample reserves in the banking system while adding capacity for additional Treasury debt purchases, something Treasury Secretary Scott Bessent will surely appreciate.

BUCKLE UP AND ENJOY THE RIDE

The path ahead for bond investors over the balance of 2025 will continue to be bumpy but generally rewarding. The U.S. economy is likely downshifting into slower growth over the coming quarters given what we now know about the initial phase of tariff policy and the cutbacks in government spending. Unemployment is likely to creep higher as layoffs announcements gain steam. Disinflation progress may continue to stall but inflation is not likely to rebound materially in the tepid growth environment. The wild card is Federal Reserve rate cuts amid uncertain tariff policy and a slowing economy. The Fed's base inclination is to defend the U.S. labor market, so we believe 1or 2 cuts this year are likely and will provide a nice tailwind to favorable bond market returns in 2025.

Connecting Geopolitics to Markets – A Current Day Example[5-11]

Richard Chauvin, CFA

With what may be the understatement of the year so far, the new Trump administration has fostered a high degree of geopolitical uncertainty since taking office through a flurry of announcements and orders regarding trade, immigration, energy, and technology. In the section of this report authored by Steve Morgan, there is a detailed account of some of the policy pronouncements.

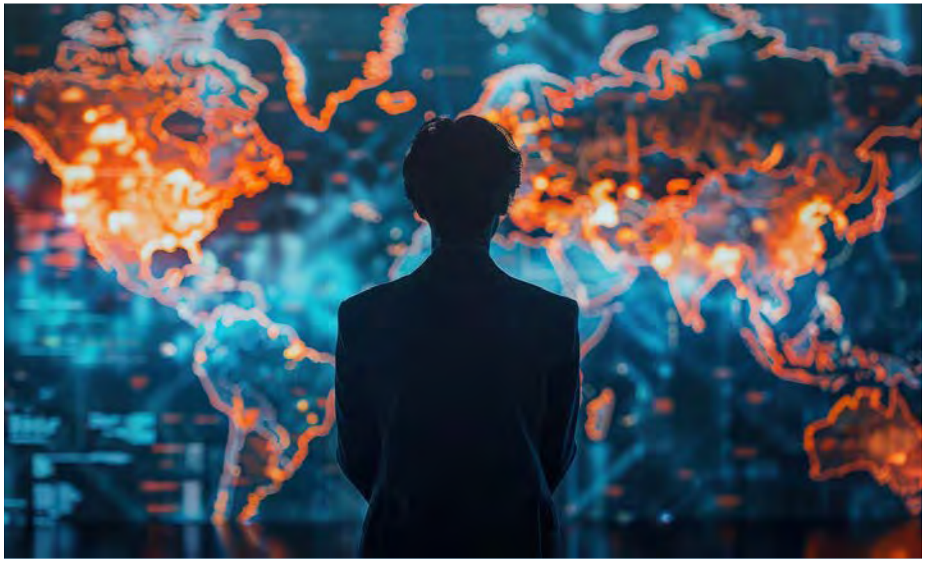
In prior geopolitical updates we postulated that in contrast to the short-term effect of geopolitical events on financial markets over the Cold War and post-Cold War periods, geopolitics has taken on elevated importance in influencing macro-economic policies. We continue to expect geopolitics' effect on market behavior is likely to be structural and sustained in this new multi-polar world.

We aim to support this view by describing a recent example of the elevated importance of geopolitics in influencing the outlook for the macro economy and financial market trends. Our focus is on how Trump's comments, policies and actions regarding the Russia-Ukraine war, NATO and tariffs have created a significant shift in investor sentiment and behavior towards European equity markets.

AMERICAN EXCEPTIONALISM IN DOUBT

Over the decade ended December 31, 2024, the S&P 500 Index produced a total return of 13.07% annual return, exceeding the MSCI EAFE Index by 7.86% per year. EAFE is the most recognized international stock market index representing developed economies other than the U.S. There are a number of factors that contributed to this large performance disparity, but the key factors include Europe's stifling bureaucracy, a lack of innovation and entrepreneurial spirit, and the expense of a social safety net that is more generous than the U.S.'s. The consistent performance disparity over such a long period fostered a strong consensus view that the MSCI EAFE Index, of which Europe is a dominant member, would consistently underperform in the future and should be priced at a significant discount the U.S. market, even on a sector-neutral basis.

The consensus view began to change as the new Trump administration began to unveil its foreign policy priorities. The three major policy areas in which Trump has affected the way investors think about the investment opportunities in Europe are tariff policy, U.S. support of NATO, and the funding of Ukraine's defense against Russian aggression. While the President's views on these topics were well-known before he took office, the aggressiveness with which he spoke of them alarmed EU leaders. They suddenly realized that key industries, such as auto production were at risk, as was the security of the continent should the U.S. cut its support of NATO. The U.S. has been the largest single donor of aid to Ukraine. Though Trump has declared that he expects a near-tern end to the war, European nations are worried they will be saddled with the full expense of Ukraine's defense support should the U.S. back away.



EUROPE HAS A PLAN, BUT CAN 27 COUNTRIES AGREE?

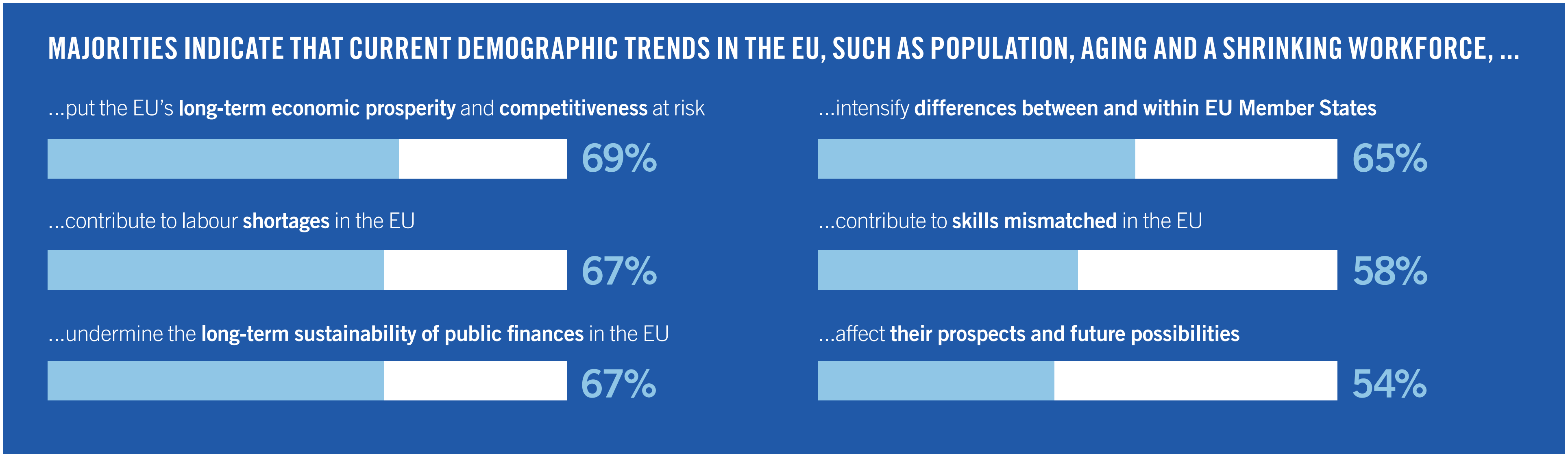
In response to the pressure Trump has placed on Europe's economy and potentially on its security, European leaders have reacted with several actions that investors find encouraging.

- NATO military chiefs and European defense ministers met in Paris in March and again in London to create a European "coalition of the willing" aimed at enhancing European security cooperation outside NATO and EU structures. Its purpose is to create a flexible, mechanism that allows willing European states to pool resources, coordinate defense strategies and ensure consistent military and financial support for Ukraine without the institutional barriers that come with existing alliances. The coalition's goal is not to replace NATO or the EU but to serve as a parallel mechanism that ensures military aid gets to Ukraine regardless of the changing political dynamics.

- Friedrich Merz, Germany's chancellor-in-waiting following recent elections, gained approval of a massive €1 trillion spending package. The changes loosen the country's borrowing restrictions to allow unlimited defense spending and create a special €500 billion vehicle to modernize the country's infrastructure. The package signals Germany's goal to accelerate its rearmament and could jump-start the Eurozone's largest economy out of years of stagnation.

- The EU is preparing to increase its defense industry with a major stimulus plan. Called "ReArm Europe Plan/ Readiness 2030: the plan to finance EU defence", the plan aims to finance an €800 billion package mostly by allowing member states to increase their defense budgets by 1.55 of GDP. The EU expects the financial tools it will create will have positive effects on the economy and competitiveness. This includes building new factories and production lines essential for generating good jobs in Europe.

- In Europe, more than anywhere else, regulators have pushed ESG mandates, enforceable through the Corporate Sustainability Reporting Directives (CSRD), which affect companies operating in the EU even if headquartered elsewhere. These are controversial among U.S. companies, but have also seen growing opposition in Europe, given that they place a significant regulatory burden on companies, increasing costs and placing them at a competitive disadvantage. President Macron of France recognizes this and has called for the EU to postpone these requirements indefinitely, recognizing that such regulations are a prime example of what Mario Draghi meant when he described the factors causing the EU's lack of economic competitiveness. The report was commissioned by the EU and was issued in September of last year. While many investors may have assumed the report's prescriptions for economic growth might not be embraced by the EU bureaucracy, its publication months before the Trump administration began to place greater pressure on Europe may be having the effect that Draghi hope for.



Source: European Union

From December 31, 2024, through March 31, 2025, the EAFE index has performed much better than the S&P 500, rising 8.11% while the US index declined 4.33%, a 12.44% performance advantage over a three-month period. There are certainly other factors involved than those described above that influenced this remarkable reversal in relative performance. It's notable that the valuation difference between the two indices had grown to a record – the S&P 500 became very expensive relative to the EAFE. However, the geopolitical environment has been the catalyst for this reversal of fortune.

The question for investors is whether Europe will find enough cohesion to embrace the necessary changes in economic policies to sustain its ability to outperform the U.S. stock market. There remain several obstacles to that achievement, including political instability, most notably in Germany and France, and poor demographic trends, including an aging population, fertility rates below the replacement rate and a shrinking working-age population. Investors must also be cognizant of ongoing geopolitical risks of a trade war and a possible new migrant influx from the Middle East.

Sources

[1] Bloomberg, [2] Wall Street Journal, [3] Ned Davis Research, [4] St. Louis Federal Reserve, [5] Blackrock Geopolitical Dashboard; February 2025, [6] Geopolitical Futures, [7] Financial Times, [8] European Commission, [9] "The Future of European Competitiveness: Report by Mario Draghi," [10] Real Clear Wire, [11] European Union; Demographic Change in Europe, [12] Strategas Research Partners, [13] The Hill, [14] Politico, [15] Roll Call, [16] Punchbowl News, [17] Piper Sandler Research, [18] Associated Press, [19] Reuters, [20] BBC, [21] The Economist, [22] The Washington Post, [23] Ballotpedia, [24] House.gov, [25] Senate.gov, [26] Whitehouse.gov

About the Authors

David Lundgren, CFA

Executive Vice President & Chief Investment Officer

David Lundgren, CFA is the chief investment officer at Hancock Whitney. He is responsible for directing the bank's investment approach; the delivery of asset allocation solutions to institutional and high net worth clients; the management of a platform of client-focused internal and external money managers; and ensuring the bank meets all regulatory requirements.

Additionally, he has been in the banking industry for almost 30 years.

Prior to joining Hancock Whitney, he was a portfolio manager at First Commerce Corporation. David has a Bachelor's Degree in Finance and a Masters in Business Administration from the University of New Orleans, and holds the Chartered Financial Analyst designation.

Martin Sirera, CFA

Senior Vice President & Investment Director

Martin Sirera is an investment director at Hancock Whitney, where he is responsible for management of Equity Strategies and client relationships; for participation in firm Asset Allocation decisions. Martin has been in the banking industry for 28 years. Prior to joining Hancock Whitney, Martin worked for Capital One and Hibernia Corp. He has a Bachelor's of Science in Finance from the University of New Orleans and holds the Chartered Financial Analyst Designation. Martin is a Past President of the CFA Society of New Orleans, has served as a Grader for CFA Exams, and is a member of CFA Institute and Chicago Quantitative Alliance.

Stephen Morgan

Senior Vice President & Investment Director

Stephen Morgan is the investment director at Hancock Whitney, where he facilitates a team of investment professionals focused on delivering superior investment strategies and client outcomes. Stephen has been in the investment industry for 25 years. He joined Hancock Whitney as part of the acquisition of Capital One Asset Management LLC. Prior to joining Capital One, Stephen worked at Morgan Stanley, efolio.com, Hibernia Bank and Waterhouse Securities. He has a Bachelor of Mathematics from Carleton College and a Master of Mathematics from the University of Wisconsin.

Jeffery Tanguis

Senior Vice President & Investment Director

Jeffery Tanguis is an investment director at Hancock Whitney, where he is responsible for developing and implementing fixed income strategy and serves as a portfolio manager for high net worth clients. Additionally, Jeff has been in the banking industry for 37 years. Prior to joining Hancock Whitney, Jeff worked with Hibernia Bank as a senior fixed income portfolio manager. He has a Bachelor's of Science in Finance from Louisiana State University. Jeff is a MSRB registered Series 55 Municipal Advisor.

Paul Teten, CFA

Senior Vice President & Chief Investment Strategist

Paul Teten, is a chief investment strategist at Hancock Whitney, where he supervises the formulation and implementation of proprietary equity and fixed income strategies. Paul has over 40 years of experience in the finance industry. He joined Hancock Whitney as part of the acquisition of Capital One Asset Management LLC. His prior experience includes portfolio management for the Bank of America Private Bank and fixed income trading and portfolio management at Criterion Investment Management in Houston. He earned his Bachelor's Degree in Finance and Masters of Business Administration from the University of Texas at Austin. Paul is a Chartered Financial Analyst and remains active at the College of Natural Sciences at the University of Texas and serves on the Board of Visitors of McDonald Observatory.

Richard Chauvin, CFA

Senior Vice President & Investment Director

Richard Chauvin, CFA is an investment director at Hancock Whitney, where he is responsible for investment research and strategy, and serves as a portfolio manager for high net worth personal and institutional clients. He has been in the banking industry for over 30 years. Prior to joining Hancock Whitney, Richard served as the Chief Investment Officer at Capital One and was a Senior Portfolio Manager at Hibernia Bank. He has a Bachelor's Degree and a Master's in Business Administration from Louisiana State University, and holds the Chartered Financial Analyst designation.