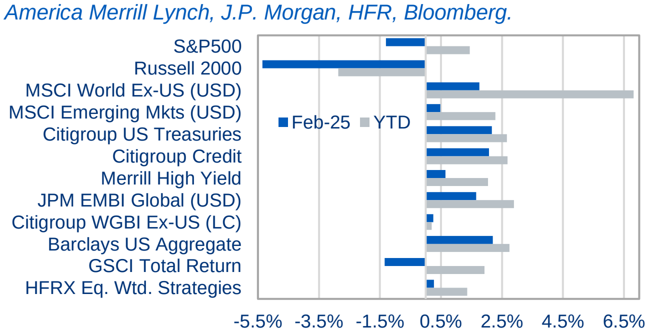
Global Market Review

U.S. equities fell in February amid heightened policy uncertainty, signs of slowing economic growth, fears of looming tariff-induced inflation, and a sharp deterioration in consumer and business sentiment. Small cap stocks and the Magnificent-7 led the decline. Non-U.S. advanced and emerging equity markets, in contrast, rose. European equities led advanced economy markets higher. The Chinese market outpaced all others, jumping 11.8%. U.S. Treasury prices also rose, especially at longer maturities. The yield curve re-inverted with the yield on 10-year Treasuries once again falling below the 3-month rate. The decline in yields was driven by a sharp fall in real yields which more than offset rising inflation expectations. Credit markets also registered gains, with investment grade bonds outpacing their high yield counterparts. The U.S. dollar index declined in February. Gold closed the month near record highs. Oil prices fell on concerns over economic growth and high inventory levels.

Performance of Major Market Indices

Sources: S&P, MSCI, FTSE Russell, Barclays, Citigroup, Bank of America Merrill Lynch, J.P. Morgan, HFR, Bloomberg.



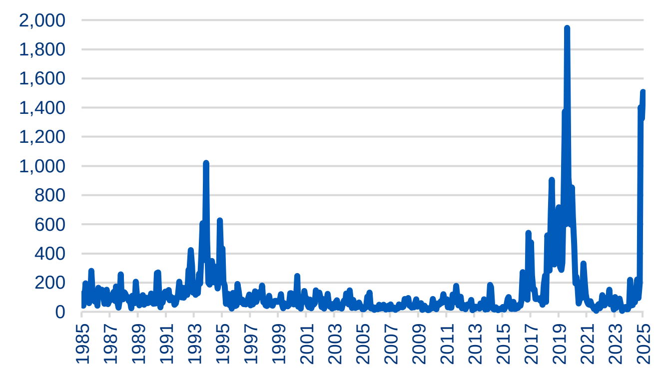
U.S. equities lag other markets in February.

Trade Policy Uncertainty Sours Sentiment

Business and consumer sentiment soured in February, largely reflecting uncertainty over the impact of tariffs on prices and spending decisions. The timing, scope, and level of tariffs that the U.S. will ultimately impose on imports and the extent of retaliation by trading partners remain in flux. Trade policy uncertainty is now well above the levels reached in the run-up to NAFTA in 1994 and is approaching the 2017-19 peak hit during the first Trump administration (Exhibit 1). The possibility that heightened uncertainty will stymy the spending plans of firms and households poses a risk to U.S. economic growth prospects and the richly valued U.S. equity market. The possibility that tariff-induced inflation will lead the Fed to keep rates restrictive is also weighing on sentiment.

Exhibit 1. Trade Policy Uncertainty Spikes

Source: Policyuncertainty.com. Index. Mean 1985-2009 = 100.



Small Cap and Mag-7 Drag Down U.S. Equity Market

Despite the high level of policy uncertainty, the VIX index of option-implied equity market volatility rose only slightly in February. The S&P 500 index lost 1.3% in February but remains up 1.4% so far this year. The decline was led by small cap stocks and the Mag-7, which both fell 5.4% (Exhibit 2). Tesla's 27.6% plunge was a major contributor to the Mag-7's poor performance. Growth stocks underperformed value in February, losing 3.7% versus value's narrow gain of 0.2%. So far in 2025, growth is down 1.8% while value is up 4.7%. Across sectors, consumer discretionary fell 9%, largely due to Tesla's plunge, while the telecom sector lost 6.6%. The consumer staples and energy sectors fared best, rising 5.6% and 3.2%, respectively.

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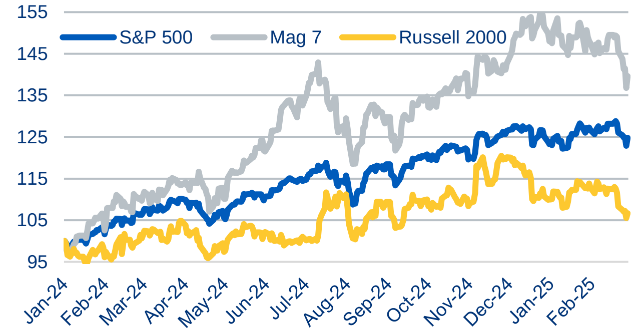
Exhibit 2. Mag 7, Small Cap Drag Down Broader Market

Source: Bloomberg. Index January 1, 2024 = 100.

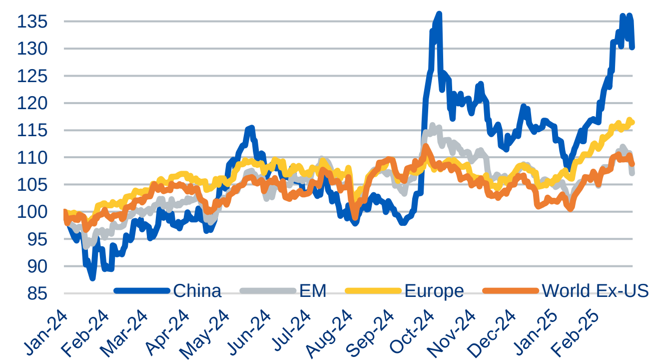


Non- U.S. Equity Markets Outperform the U.S.

The MSCI World ex-U.S. index of advanced economy stocks rose 1.8% in February, bringing its gain for the year to 6.8%, handily surpassing the U.S. market's 1.4% gain. European equities continue to perform especially well (Exhibit 3). European economic activity, in contrast, is stagnant and expected to remain weak. The risks to Europe's economic prospects are tilted to the downside reflecting the uncertainties of the war in Ukraine and the prospect of U.S. tariffs. In response to these challenges and easing price pressures, the ECB cut rates in February and signaled further cuts ahead, helping to buoy the equity market.

Exhibit 3. Chinese Equities Surge, Europe Rallies

Source: Bloomberg. Index January 1, 2024 = 100.



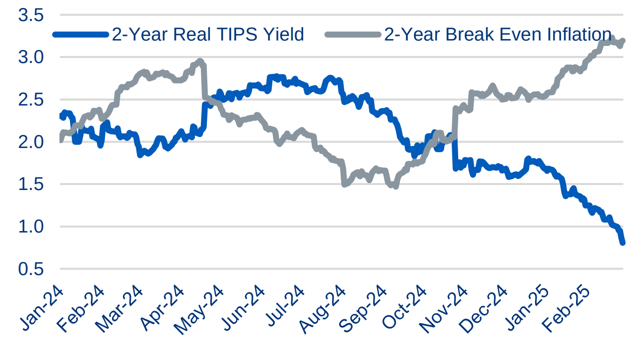
Emerging equity markets registered a small gain of 0.5% in February, while Chinese shares jumped 11.8%. The Chinese market's stellar performance reflects strong gains in the tech sector following a breakthrough in AI technology and the prospect of fiscal and monetary stimulus aimed at boosting both the broader economy and the share market. Latin American equity markets lost 1.8% in February, as tariff pressures loomed. Tariffs are widely expected to undercut growth prospects in the region and lead to currency depreciation. The Bank of Mexico, for example, has cut its economic growth forecast for 2025 in half, while each new threat of tariffs has sent the Mexican peso lower.

Real Yields Plunge, Inflation Expectations Rise

The real yield on TIPS and the breakeven inflation rate have moved steeply in opposite directions (Exhibit 4). Real yields have plummeted, and inflation expectations have risen equally dramatically. At the same time, the yield curve has reinverted with the 10-U.S. Treasury yield falling below the interest rate on the 3-month T-bill.

Exhibit 4. Real Yields Fall as Inflation Expectations Rise

Source: Bloomberg. Real yield on 2-year TIPS and associated break-even inflation rate in percent. Break-even inflation is a proxy for inflation expectations and is calculated as the differential between the real yield on TIPS and the nominal yield on a conventional U.S. Treasury with the same maturity.



Taken together, these moves could signal a rising risk of stagflation. The increase in inflation expectations reflects the growing likelihood of tariff-induced price pressures. Falling real yields and an inverted yield curve, for their part, often foreshadow an economic slowdown. This is far from an iron law, however, as evidenced by the prolonged inversion of 2022-24, which was followed by a period of resilient economic growth. While reading the runes of the yield curve is a highly speculative enterprise, its grim message on growth is echoed in recent declines in consumer and business sentiment and survey data pointing to slowing output. The increase in inflation expectations is similarly echoed in the latest data, including January's increase in year-on-year core and headline inflation of 3.3% and 3.0%, respectively.

Reflecting these yield shifts, U.S. Treasuries rose 2.2% in February, led by a 5.1% gain in Treasuries with maturities of 10+ years. So far in 2025, U.S. Treasuries are up 2.7%, with the long segment up 5.7%. U.S. credit markets also rose in February, with investment grade credit rising 2.2% versus a 0.6% gain for the high yield sector. So far this year investment grade and high-yield credit are up 2.8% and 2.1%, respectively.

Performance of Major Market Indices through 02-28-2025

Sources: MSCI, FTSE, Barclays, Citigroup, Bank of America Merrill Lynch, J.P. Morgan, S&P GSCI, HFR, Bloomberg.

	1-Month	QTD	YTD	1-Year	3-Year	5-Year
S&P500	-1.3%	1.4%	1.4%	1.4%	18.4%	12.6%
Russell 2000	-5.3%	-2.9%	-2.9%	-2.9%	6.7%	3.3%
MSCI World Ex-US (USD)	1.8%	6.8%	6.8%	6.8%	9.5%	6.3%
MSCI Emerging Mkts (USD)	0.5%	2.3%	2.3%	2.3%	10.1%	0.5%
Citigroup US Treasuries	2.2%	2.7%	2.7%	2.7%	5.0%	-1.1%
Citigroup Credit	2.1%	2.7%	2.7%	2.7%	6.6%	0.4%
Merrill High Yield	0.7%	2.0%	2.0%	2.0%	10.1%	4.9%
JPM EMBI Global (USD)	1.6%	2.9%	2.9%	2.9%	9.3%	3.0%
Citigroup WGBI Ex-US (LC)	0.2%	0.2%	0.2%	0.2%	2.5%	-2.2%
Barclays US Aggregate	2.2%	2.7%	2.7%	2.7%	5.8%	-0.4%
GSCI Total Return	-1.3%	1.9%	1.9%	1.9%	5.7%	3.4%
HFRX Eq. Wtd. Strategies	0.3%	1.4%	1.4%	1.4%	5.1%	2.5%