Despite the inauspicious start and tremendous intra-month volatility, April ended up being a flat month for domestic stock and bond indices. The S&P 500 fell 0.7 percent, the Dow Jones Industrial Average fell 3.1 percent and the Nasdaq gained 0.9 percent. The Bloomberg Aggregate Bond Index ending up gaining 0.4 percent for the month. So far in May – this was authored on May 5th – the rally has continued. Through Friday May 2nd, the major US stock indices have gotten close to even for the year with the S&P 500 down 2.9 percent, the Dow Jones Industrial down 2.4 percent and the Nasdaq down 6.7 percent. At the trough after the "liberation day" announcement on April 7th, the S&P 500 had declined 13.6 percent, the Dow Jones Industrial 10.4 percent, and the Nasdaq 19.0 percent. The rally/retracement since April 7th has been substantial – about 95% of the losses recovered.

While stock and bond markets ended flat for the month, the dollar generally weakened and stayed weaker. Consequently, international investments have continued to lead in 2025. Through Friday May 2nd, MSCI EAFE has gained 13.7 percent for the year, MSCI Emerging markets 6.3 percent, and the Bloomberg Global Ex-USD Bond Aggregate 7.5 percent. Gold has also performed well, up 22.8 percent year-to-date. Dollar weakening is a trend we expect may become secular – conversely, the last 15 years have been dominated by a strong and almost perpetually strengthening dollar. We are not gold bugs and regard precious metals as hedges rather than investments because in the long run gold begets no more gold – and thus does not offer the magic of compounding over time. That said, going forward, a reduction in trade deficits (the Trump administration's stated goal) necessarily portends a reduction in the capital account surplus (they are two sides of the same coin). Consequently, foreign demand for US dollars and US-dollar denominated assets (US stocks, bonds, real estate) will likely wane in lock step with a reduction in trade deficits. In times like these, gold will benefit as will foreign investments. But In more stable times, it's likely to be foreign stocks and bonds that continue to realize a little excess return.

As we head into the summer, our team would encourage clients to remain cautious in their short-term outlook. Just as we cautioned against giving up on 2025 and the television-confirmed certainty of doom in our note last month, we would also caution against believing "it's all over" this month. Our core belief remains that 2025 may offer decent returns to diversified investors, but that those returns will come at the cost of tremendous volatility. We continue to take the Trump administration literally when it claims its penultimate goal is structural changes to trade policy meant to reduce trade deficits over time. That cannot happen without significant upheaval in the global trade and monetary order. While the "pause" of reciprocal tariffs save China allowed breathing room for many countries and companies, not every country or company will achieve a permanent solution within the 90-day framework. It won't surprise us if tariff-related volatility returns this summer.

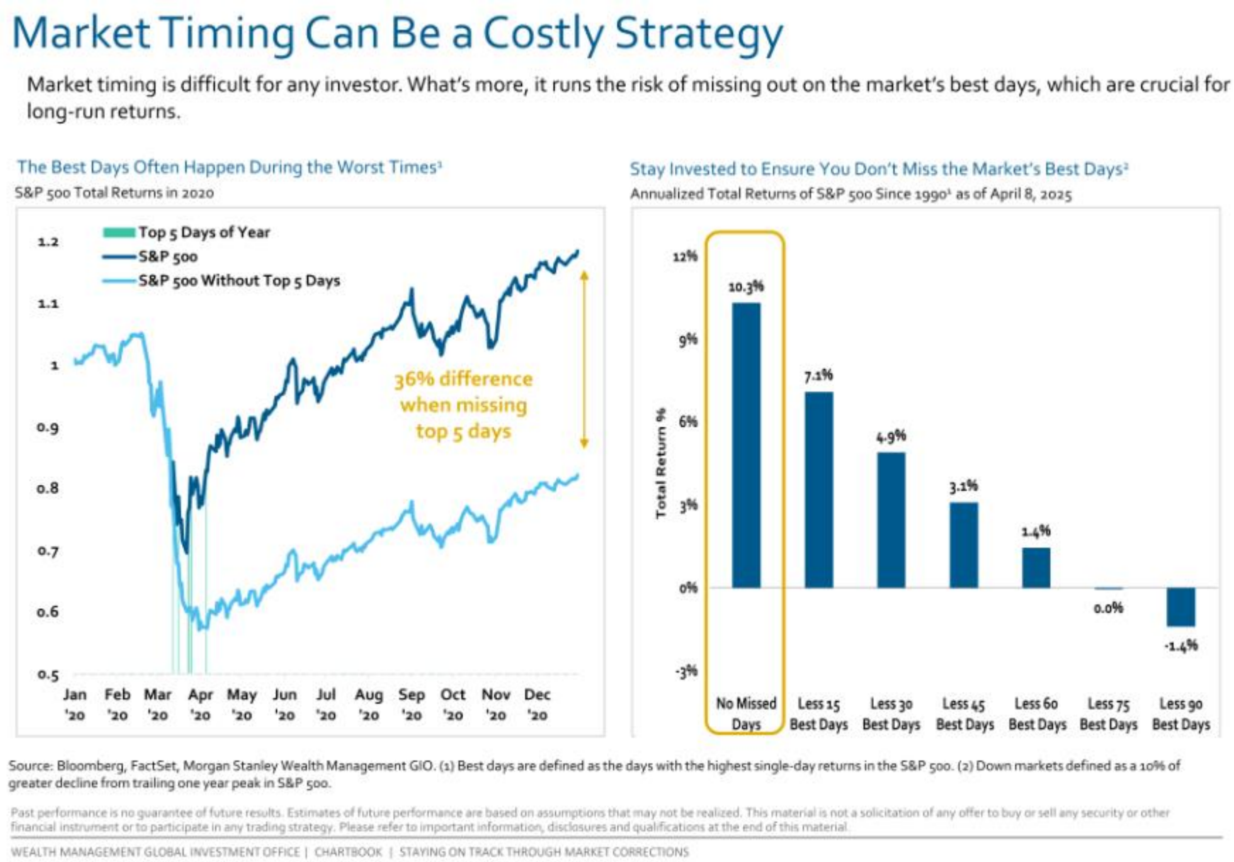
Furthermore, our team has correctly predicted since February the tariff- driven "inflation" many feared would be more muted and take longer to arrive than many thought. It's also worth noting that forward-looking inflation expectations have become incredibly partisan. Our inflation predications, however, are strictly economic and not based on personal political views. Much as we predicted, March CPI declined, not rose, by 0.1 percent. We think it's likely April CPI be up about .22 percent according to the Cleveland Fed's Inflation Nowcasting; but they also estimate May to rise by only 0.12 percent. In other words, in the three months since Trump initially placed tariffs on Canada and Mexico, inflation has been tame.

Morgan Stanley acknowledged some of the good news this month, writing in this Month's On the Markets that, "We are encouraged that thus far the real economy has exhibited general resilience, with both inflation and labor markets remaining stable even as growth has slowed. What's more, first quarter earnings have come in better than expected." The Morgan Stanley base case remains no recession in the next 12 months.

At some point however, inventories will run out (the GDP decline last month was very likely a mirage caused by companies building inventory in advance of tariffs; the poor number will likely be followed by a stronger second quarter GDP number as companies sell that accumulated inventory and await more policy certainty before restocking.) Once fully exhausted however, inventory must be replaced. Some goods will experience significant price upticks starting this summer when that process begins in earnest. We still believe the overall inflationary effect for the average consumer will be muted relative to expectations, which have become very political, but do anticipate an uptick in inflation from the current zero-inflation state from March through May. We think those looking for tariff-caused inflation will find ample opportunities to identify it this summer. We have no doubt the news will likely highlight those stories if for no other reason than a great many pundits will seek to highlight the accuracy of their March and April inflation predictions.

In short, we recommend caution today and are not giving an all-clear signal. As Lisa Shalett, Morgan Stanley's Chief Investment Officer wrote in her May 5th note, "after descending into bear market territory following "Liberation Day" tariff announcements, US equities spent April's final 10 days retracing more than 95% of the sell-off as investors seemed to "look through tariff noise." Emboldened by solid first quarter earnings, they also shrugged off both inflation and recession risks, hanging hopes on a responsive Fed, lower interest rates and progress on a tax bill. Such a relief rally ignores growing macroeconomic concerns and the damage that has already been done by tariff uncertainty. While recession is by no means certain, we are surprised that investors were quick to dismiss the first quarter's negative GDP report, deteriorating manufacturing orders, rising prices paid indexes, a spike in unemployment claims, weak consumer confidence and importantly, deteriorating forward earnings guidance. Solving the country's debt financing problem is far from clear, either. We remain focused on valuations, especially as deteriorating free cash flow growth may yet be the Achilles' heel of the Magnificent Seven."

Moving forward, at the margin our team is going to recommend – especially for more conservative clients – a mild increase in the proportion of foreign stocks and bonds. When we attempt to sort the noise from the underlying signal, we can't help but conclude dollar-weakening may persist at least until 2028 and perhaps for much longer than that. If we had to guess right now, the Fed will hold rates constant this week, and again June and July, but will lower rates this fall once or twice once the tariffs are fully digested into prices. Interest rates may fall quickly in that environment if inflation concerns wane. Consequently, bonds may fare well in the back half of 2025; but lower rates also generally invite further dollar weakness.



For new money, we continue to recommend dollar-cost averaging. For fully invested accounts, investors should remain true to their asset-allocation strategy and continue to rebalance accounts at peaks and troughs – trying to time the swings in a market driven by geo-political turmoil is a fool's errand that can be very costly (see attached slide.) Ultimately, we still see 2025 as likely to produce positive returns for diversified portfolios – it's just that we don't see US stock markets and the Magnificent 7 in particular as the source of that return in 2025.

As always, if you need anything at all, don't hesitate to reply to this e-mail or reach out to any member of the team.

For index, indicator and survey definitions referenced in this report please visit the following:
https://www.morganstanley.com/wealth-investmentsolutions/wmir-definitions

Bonds are subject to interest rate risk. When interest rates rise, bond prices fall; generally the longer a bond's maturity, the more sensitive it is to this risk. Bonds may also be subject to call risk, which is the risk that the issuer will redeem the debt at its option, fully or partially, before the scheduled maturity date. The market value of debt instruments may fluctuate, and proceeds from sales prior to maturity may be more or less than the amount originally invested or the maturity value due to changes in market conditions or changes in the credit quality of the issuer. Bonds are subject to the credit risk of the issuer. This is the risk that the issuer might be unable to make interest and/or principal payments on a timely basis. Bonds are also subject to reinvestment risk, which is the risk that principal and/or interest payments from a given investment may be reinvested at a lower interest rate.

Any type of continuous or periodic investment plan does not assure a profit and does not protect against loss in declining markets. Since such a plan involves continuous investment in securities regardless of fluctuating price levels of such securities, the investor should consider their financial ability to continue their purchases through periods of low price levels.

Rebalancing does not protect against a loss in declining financial markets. There may be a potential tax implication with a rebalancing strategy. Investors should consult with their tax advisor before implementing such a strategy.

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