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The Corner

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Can The Market Bear So Much Bullish News?

Surfing The Tariff Shockwave

Executive Summary

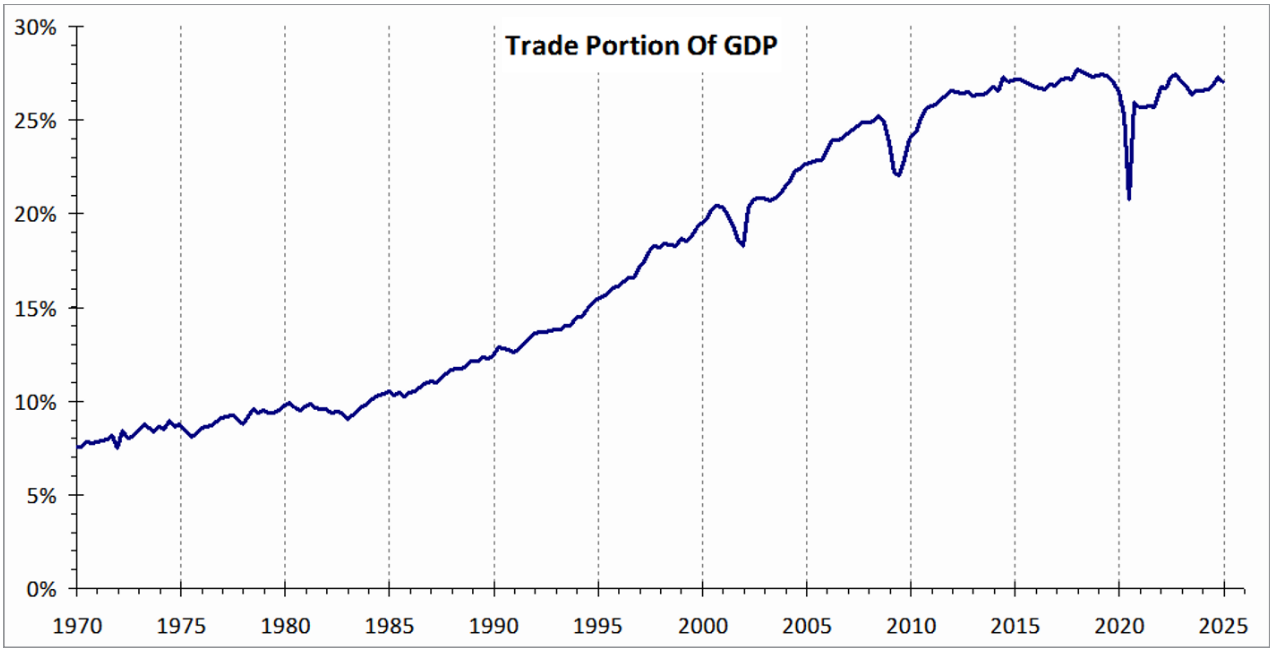
We believe the tariff shock of Liberation Day (April 2) was front-loaded. Most of the damage to the equity markets seems to have been completed after about a week, with the S&P 500 hitting a low of 4835 on April 7. Since then, the S&P 500 has not only rallied into resistance near 5600-5700 (just below its 200-day moving average), but it has broken above those levels to a modest gain year to date.

Despite previous rhetoric from Washington and Beijing, recent talks in Geneva between the U.S. and China have gone well, and the worst of the tariff excesses are now on a 90-day hiatus. Both countries need to resolve their trade problems, and while China may be more reluctant to agree to changes, the former situation could not continue indefinitely. We believe the pattern investors should anticipate is straightforward: good news on trade will likely drive market rallies. Given that much of the bad news appears to have been priced in already, any positive developments should provide a meaningful boost to equities, in our view. The current rally should continue into the summer. It is possible that the equity market will close with a gain for this year, and our 12-month target is 6550 for the S&P 500, which would be a gain of over 15% from recent levels.

A Brief Review Of The Trade And Tariff Issue

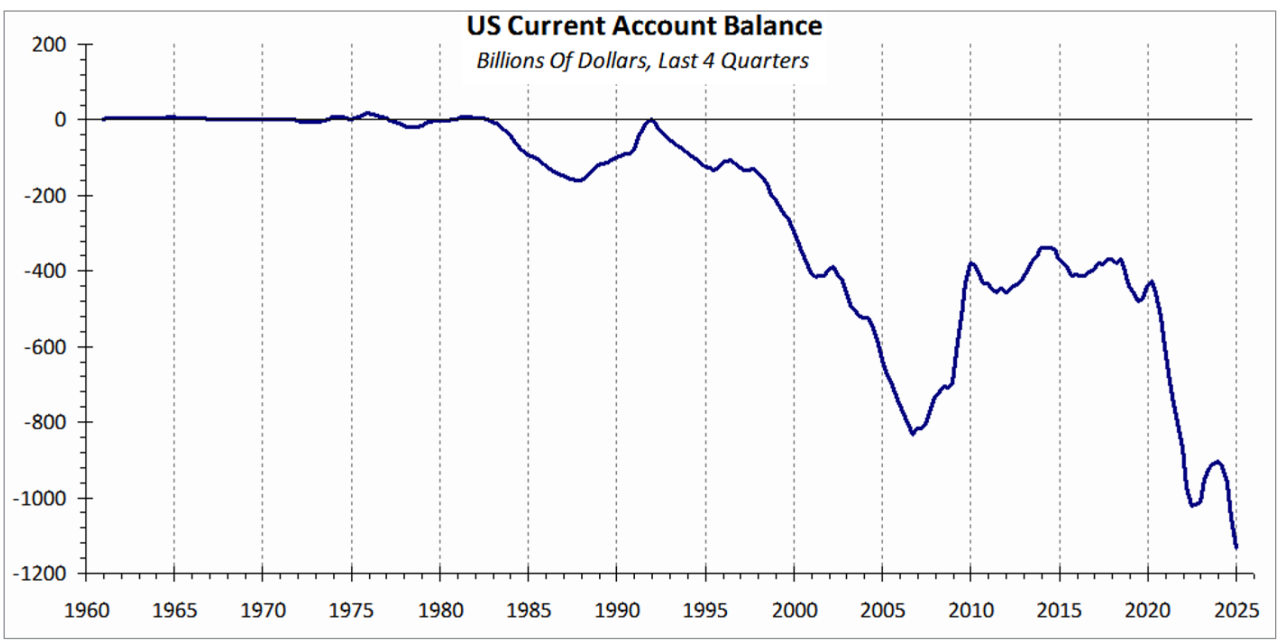
Not to beat a dead horse, but let's briefly review what's driving the tariffs. The U.S. dollar has been the reserve currency since World War II. Every other country needs to obtain dollars to settle international trade. As a result, every other country tends to underprice its products relative to U.S. domestic production, leading the U.S. to run a trade deficit. This is known as the "Triffin Dilemma," named for Robert Triffin, who first described the phenomenon 65 years ago.

Trade Is A Significant Part Of The U.S. Economy



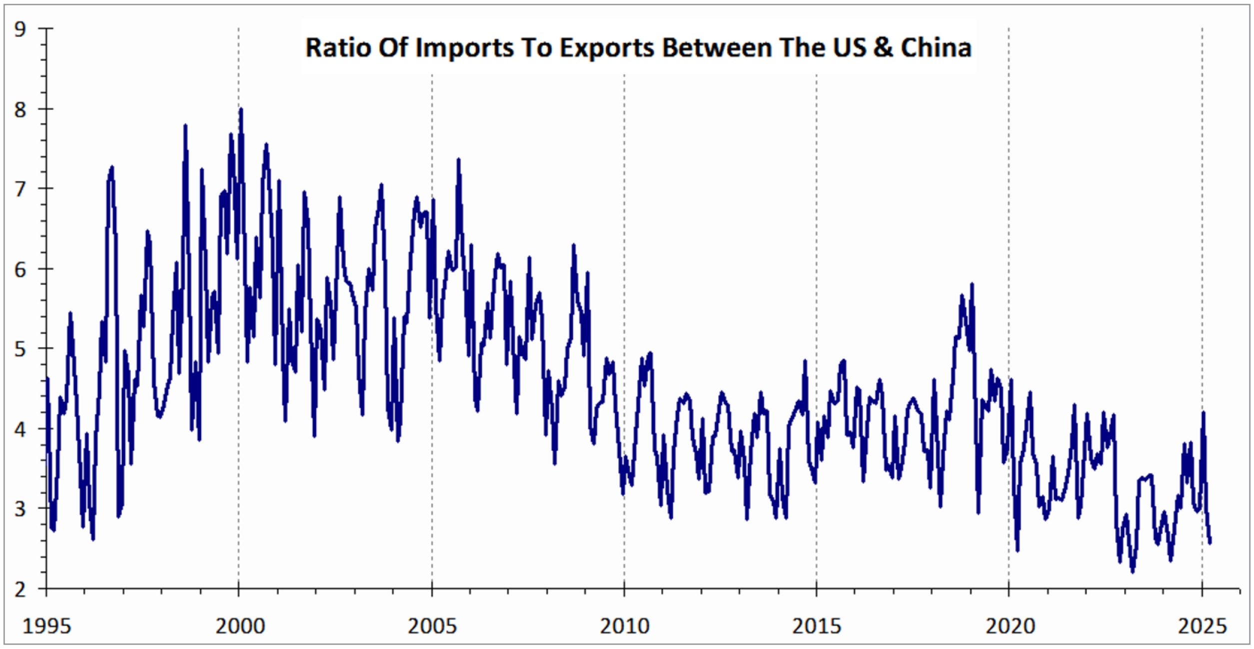
Source: Department of Commerce, Bureau of Economic Analysis, Sanctuary Wealth, May 7, 2025

The Deficit In The U.S. Current Account Balance Is Enormous



Source: Bureau of Economic Analysis, Sanctuary Wealth, May 7, 2025

The U.S. Imports From China Are 3 Times U.S. Exports To China

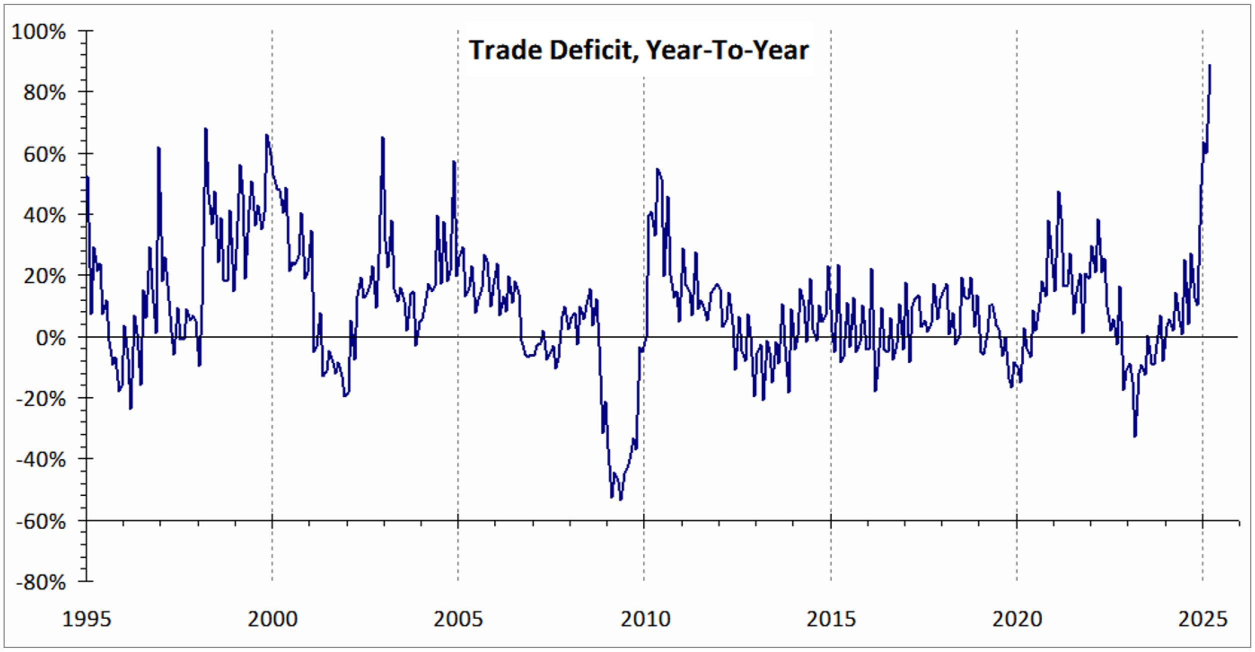


Source: Bureau of Economic Analysis, Sanctuary Wealth, May 7, 2025

Imports Ballooned In Anticipation Of Tariffs Even Before The April 2 Announcement

Savvy importers were better prepared for Trump's sweeping and punitive tariff announcements than the broader markets, which were initially caught off guard. These importers ramped up their orders, building inventory in warehouses to cushion the impact of higher duties.

Trade Deficit Exploded As Importers Warehoused Goods In Anticipation Of Trade Changes



Source: Census Bureau, Sanctuary Wealth, May 7, 2025

We Expect The Trade And Tariff Issue To Resolve Positively As The Year Goes On

We expect trade issues to get resolved as negotiations continue. Tariffs are likely to remain – just not at the rates first announced, in our view. Now the U.S.'s trading partners won't be happy about any changes to what had been the status quo – after all, those arrangements were quite profitable for them ; however, we do believe more equitable trading agreements are likely to emerge, and as they do, we expect stock markets to rally, especially in Europe and the U.S.

U.S. Stocks Have Completed A Bottoming Process And Are Recovering

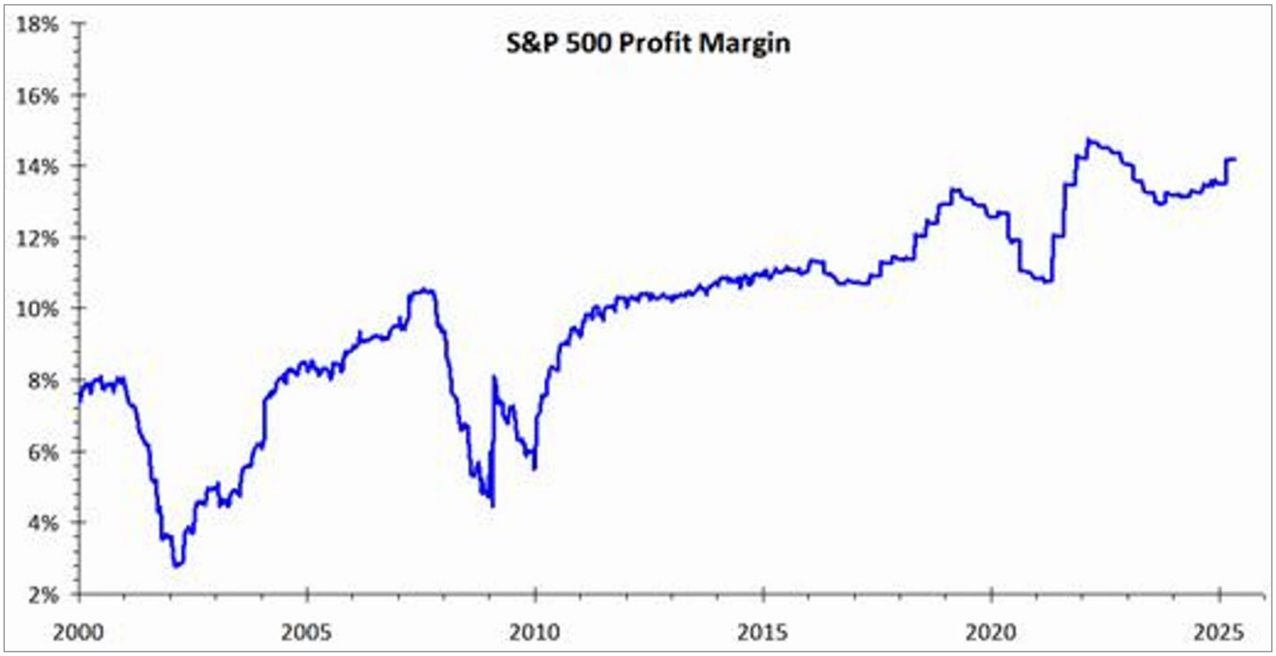
As noted earlier, we believe the S&P 500 should be able to reach 6550 or a 15% gain from recent levels over the next 12 months. Given recent news on the tariff and trade front and investors' positive reaction to it, the market is now unlikely to test its lows, in our view. We would be buyers on any pullbacks as we see the secular bull market remaining intact.

Fundamentals in the markets also remain strong. The price-earnings ratio on expected earnings for the next 12 months has reached levels that have been attractive over the past 5 years, and profit margins are still expanding. These are positive indicators for the market going forward.

The Price/Earnings Ratio On The Next Twelve Months Earnings Per Share Is Attractive

Source: Standard & Poor's, Sanctuary Wealth, May 10, 2025

Profit Margins Are Still In A Rising Trend



Source: Standard & Poor's, Sanctuary Wealth, May 10, 2025

"Soft Data" Has Been Bearish

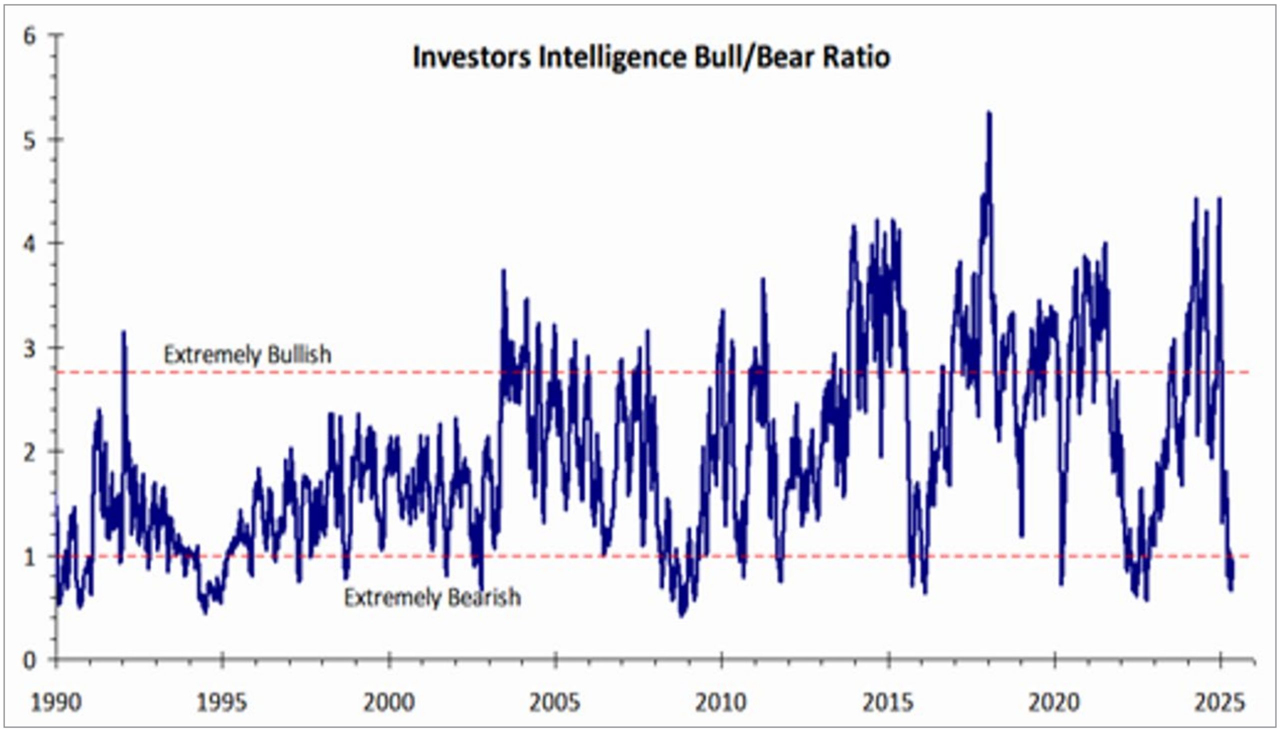
Soft data is survey data. The Federal Reserve (Fed) and its district banks, along with many private organizations, such as the National Association of Purchasing Managers (NAPM), the Conference Board, and the National Association of Realtors (NAR), survey their professional colleagues and consumers to assess expectations of future economic conditions. This data has been almost uniformly gloomy since the shockwave of tariffs was announced at the beginning of April.

The irony is that such gloominess is often a sign that markets can rally. This is a "contrarian" situation: Because too many people are on one side of a trade, the opposite happens. We have already noted that we believe the tariff situation is likely to improve over the coming weeks and months. This will push people who are not invested to go long, and it will force over-eager bears who have shorted the markets to cover (buy back their short positions) to avoid losses.

Bull/Bear Surveys

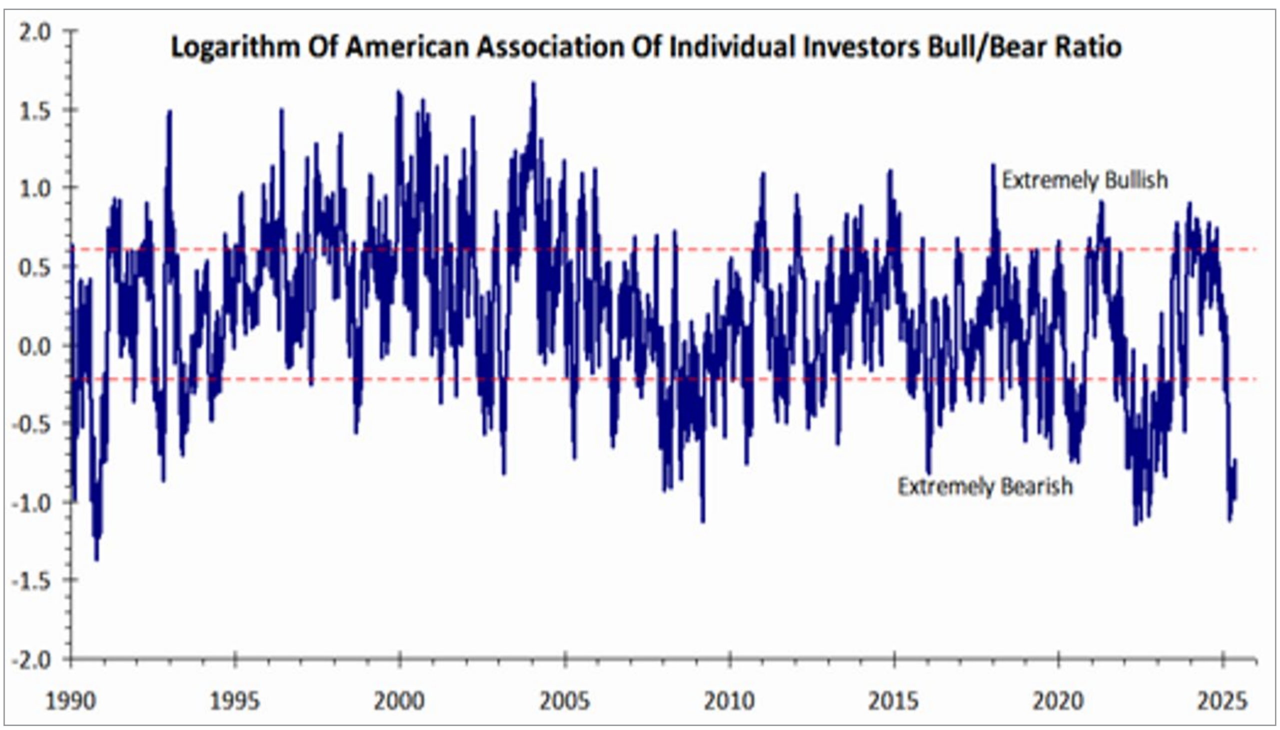
Investors Intelligence (II) and the American Association of Individual Investors (AAII) have maintained surveys of stock market Bulls and Bears. II's survey is based upon professional projections, while AAII surveys its members. We used the logarithm of the ratio of the AAII bull/bear survey, and later of the ratio of new highs to new lows and of the ratio of up to down volume, to make the data easier to visualize. While no indicator can define a market bottom, all of these are congruent with equity market bottoms.

Investors Intelligence Ratio Of Bulls To Bears At Levels Associated With Market Bottoms



Source: Investors Intelligence, Sanctuary Wealth, May 9, 2025

The AAII Ratio Of Bulls To Bears Is Also At Low Levels Seen During Market Bottoms

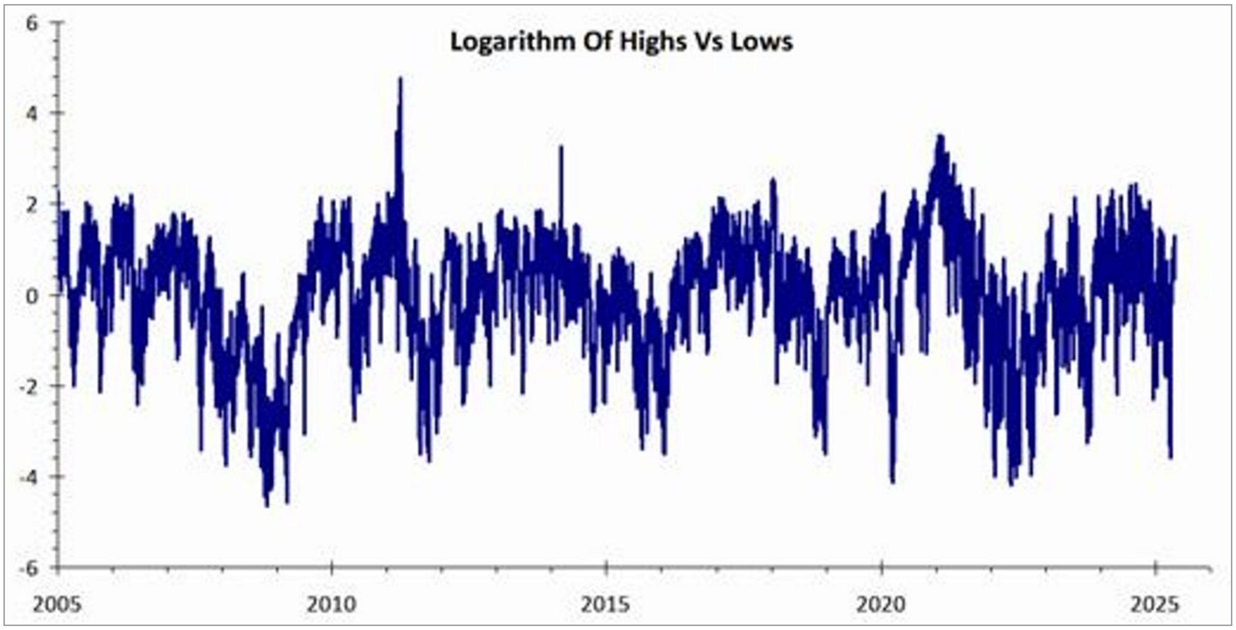


Source: American Association of Individual Investors, Sanctuary Wealth, May 9, 2025

New Lows Vs. New Highs And Volume Support A Market Bottom

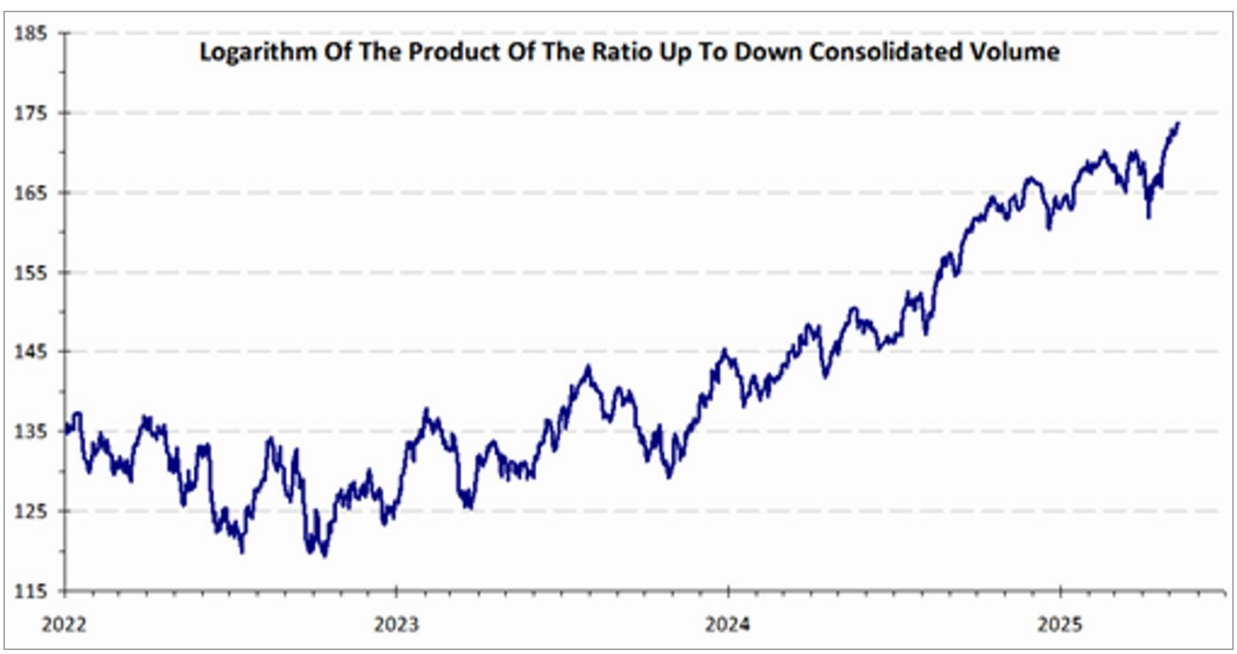
New 52-week lows normally exceed new 52-week highs at extremes around market bottoms. By the same token, rising volume exceeds declining volume when equity prices are rising, not falling, and the product of the ratio of rising volume to declining volume has reached new all-time highs. Finally, the advance-decline line for the S&P 500 has also reached all-time highs. New highs versus new lows are compatible with market lows, while rising volume compared to declining volume and the advance-decline line are compatible with rising markets. We believe the market lows have been set, and that the secular bull market has likely resumed.

New 52-Week Lows Exceed New 52-Week Highs At Levels Associated With Market Lows



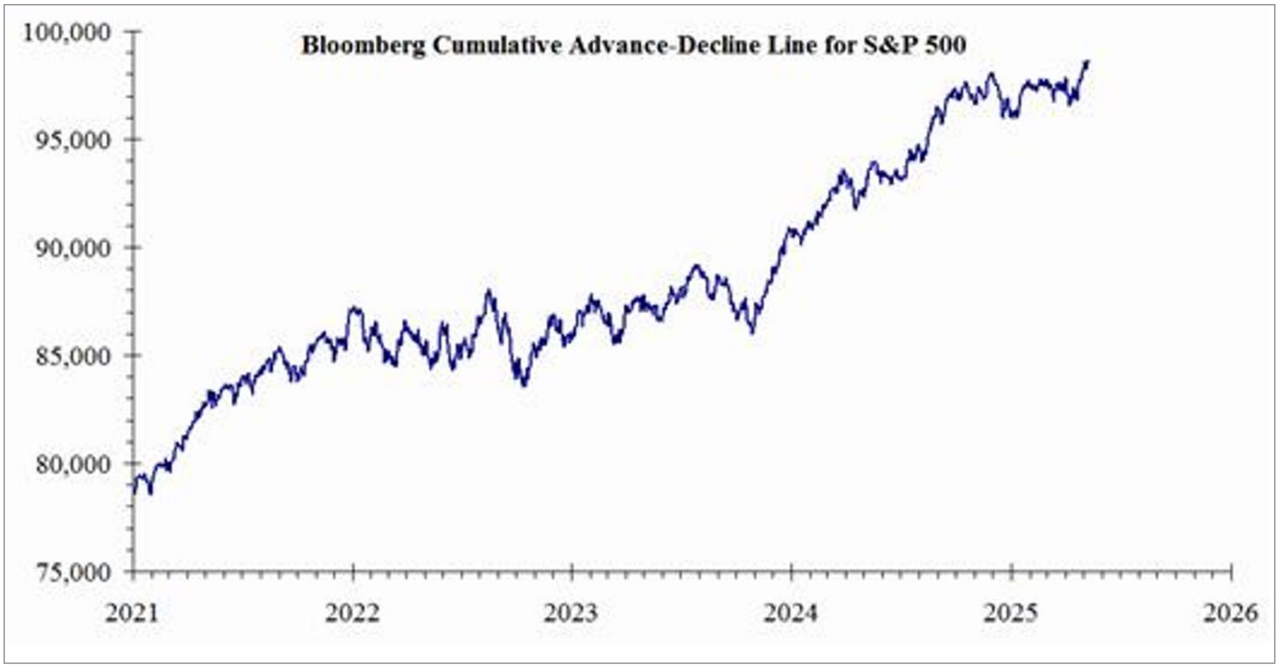
Source: Bloomberg, Sanctuary Wealth, May 9, 2025

The Ratio Of Up Volume On U.S. Exchanges Is Exceeding Down Volume Over Time



Source: Bloomberg, Sanctuary Wealth, May 9, 2025

The Advance-Decline Line For The S&P 500 Has Reached New All-Time Highs



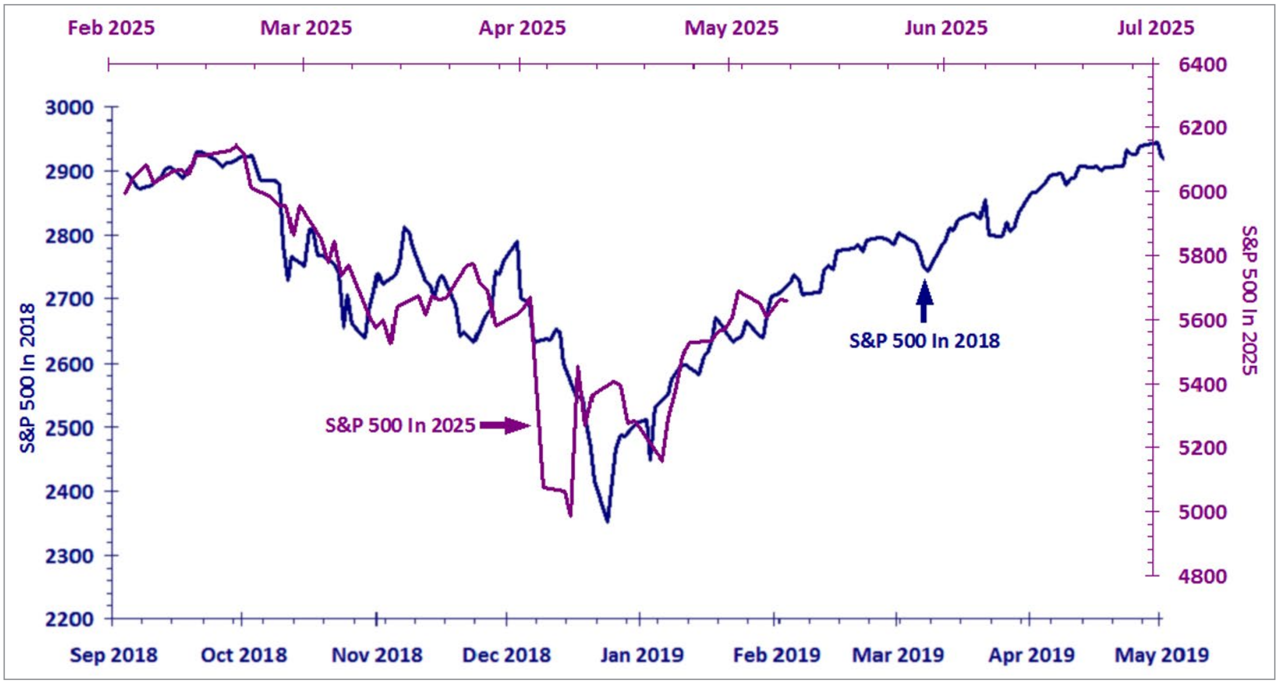
Source: Bloomberg, Sanctuary Wealth, May 9, 2025

Could This Equity Market Be Similar To 2018?

Every bear market correction has its own unique characteristics, but patterns among corrections can be similar. The current correction bears a striking resemblance to the 2018 bear market during President Trump's first term. In both cases, the market declined sharply without a retest and recovered swiftly, reaching a new high within four months. If today's market follows that pattern, we could be at new highs as early as August.

At this point, the S&P 500 has rallied into resistance near 5600-5700. We were expecting a test of the 200-day moving average (DMA) at 5746 and then the market could trade in a range between 5600 and 5800. This would form an inverted head and shoulders pattern that could set the stage for a test of the 6000–6100 level. On the China trade deal, the S&P 500 broke above the 200-DMA, forming an inverted head and shoulders. This breakout points to a test of the old highs near 6100. This would be one of the biggest surprises of the year *(not counting the tariffs!)*. If this is the case, the market could close out the year with a positive gain.

Comparison Of S&P 500 2018 Bear Market To Today



Source: Standard & Poor's, Sanctuary Wealth, May 10, 2025

Interest Rates

Breakevens mirror the bond market's inflation expectation. The breakeven is the difference between a Treasury bond yield and the comparable Treasury inflation-protected security (TIPS). For 10-year Treasuries, that level was 2.3% on May 9, and for 2-year Treasuries, it was 2.8%. This indicates that the market expected inflation to average 2.3% over the next 10 years but 2.8% over the next 2 years. These are not particularly onerous rates of inflation, in our view.

The 10-year Treasury yield appears to have support just above 4.0% and resistance around 4.6%. The Wall Street consensus is that the imposition of tariffs will cause at least a one-time, temporary slowdown in the economy. We consider the 2-year Treasury a better indicator of economic activity. The 2-year Treasury is near its 200-week moving average (WMA) of 3.57%.

Finally, there is the term premium on Treasury bonds, the extra yield investors demand to hold longer-term bonds rather than a series of shorter-term securities over the same period. The term premium on 10-year Treasury was 0.69% on May 9, which is historically quite modest.

None of these figures indicates that markets expect interest rates to rise sharply. We believe the secular trend in interest rates is rising, but we also think economic growth is likely to slow as tariffs stabilize and the economy adjusts to new international trade rules, keeping the short-term trend in interest rates down.

Breakevens - Market Inflation Expectations Are Not Extreme At 2.4%

10-Year Treasury Yield Is In Trading Range With a Downward Bias

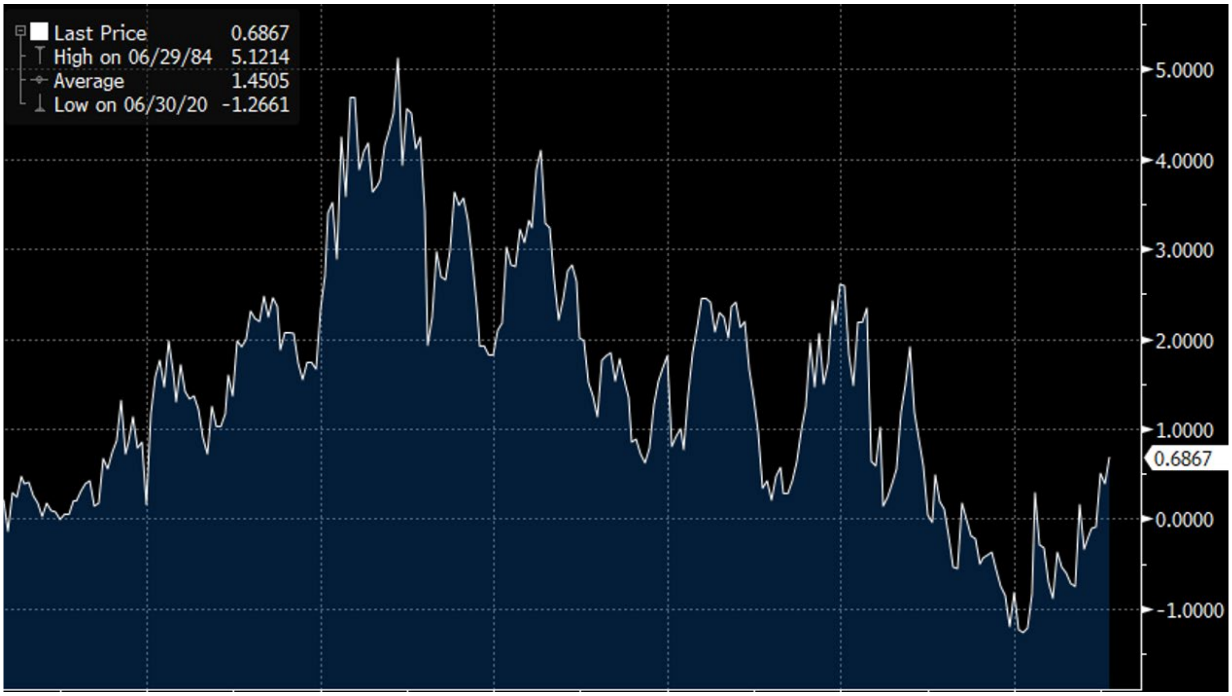
The past year has seen the 10-year Treasury yield trade within a tight range of 4.6% on the high side to 4.0% on the low end, with a short-term bias to the downside. Until we know the impact of the tariffs on the economy and inflation, rates are likely to remain range-bound.

10-Year Treasury Yield In A Range From 4.6%-4.0% Past Year

2-Year Treasuries A Better Indicator Of Economic Activity
2-Year Treasury Yield With 200-Week Moving Average (Top) And MACD (Bottom)

Term Premium For The 10-Year Treasury Is Just Shy Of 0.7%

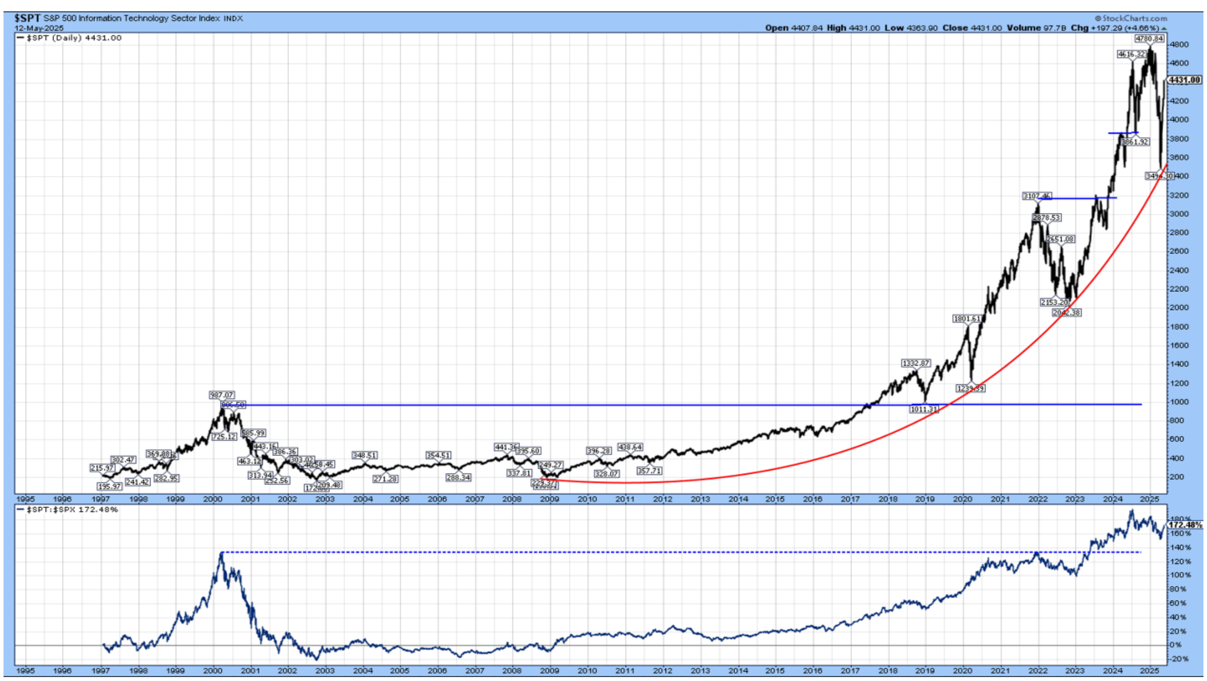
Term Premium For The 10-Year Treasury Is Still Quite Modest Historically



The Secular Bull Market Continues, And Tech Retains Its Leadership

The secular bull market remains intact in our view, and its long-term leadership is the Technology sector. Artificial intelligence (AI), blockchain, and Web 3.0 are spreading throughout the economy, just as computers, the internet, and smartphones spread in earlier decades, raising productivity and profitability. Cybersecurity stocks are increasingly important in this environment. Software companies are outperforming semiconductors, as we suggested they would as new technologies mature. IBM enjoys dominance in mainframes, along with AI applications in that space.

S&P 500 Information Technology Sector (Top) With Relative Price Vs S&P 500 (Bottom)



First Trust NASDAQ Cybersecurity ETF (CIBR) (Top) With Relative Price Vs S&P 500 (Bottom)

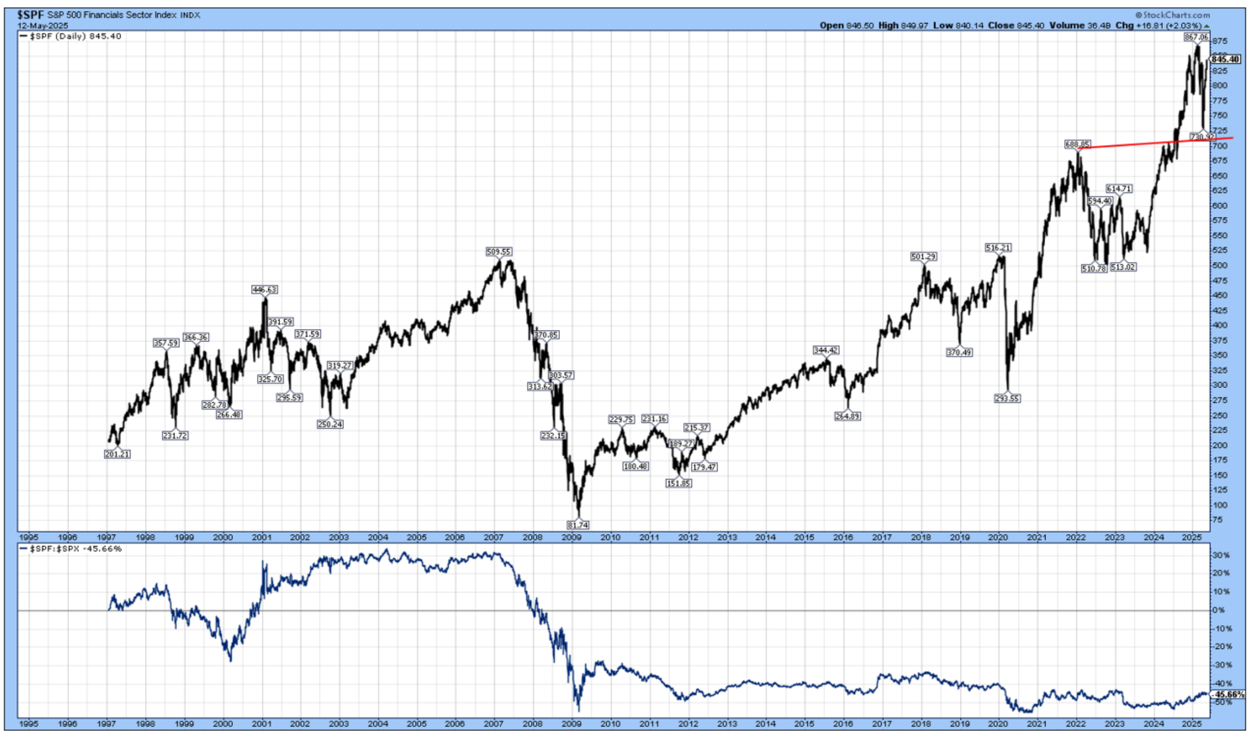
iShares Expanded Tech-Software Sector ETF (IGV) Vs VanEck Vectors Semiconductor ETF (SMH)

IBM (Top) With Relative Price Vs S&P 500 (Bottom)

Financials Earning Positive Returns

Financial stocks are generally performing well, led by big diversified banks and many insurance stocks, particularly Property & Casualty Insurers.

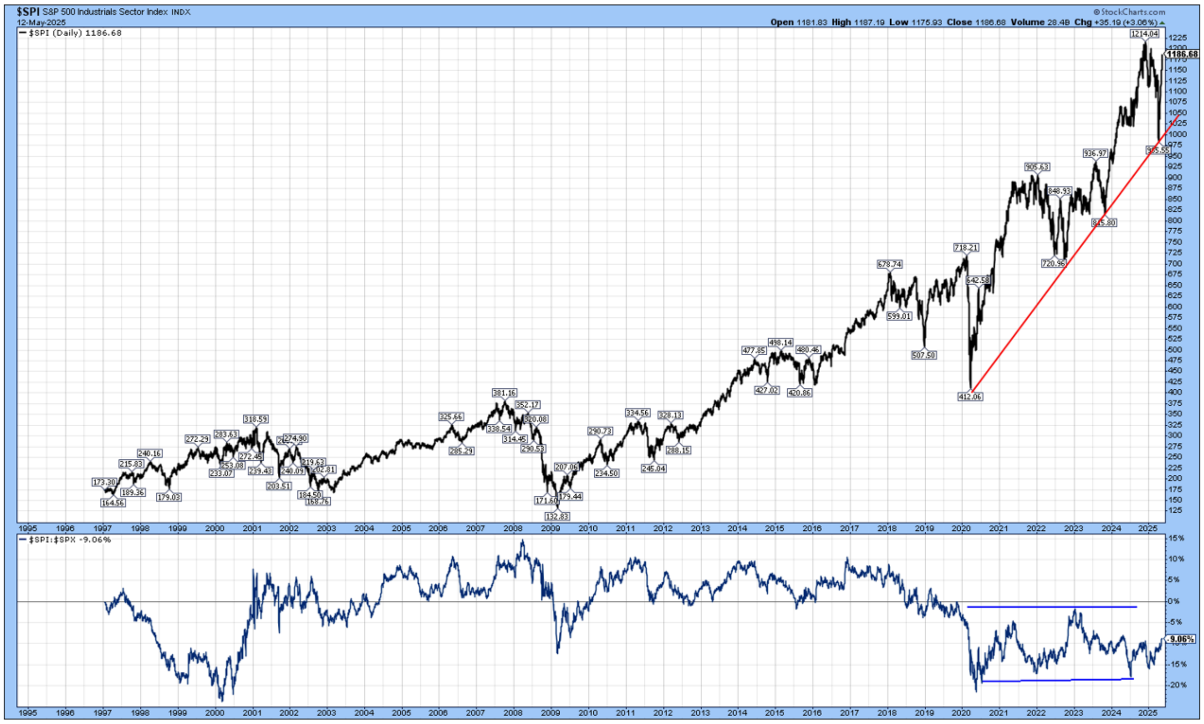
S&P 500 Financial Sector (Top) With Relative Price Vs S&P 500 (Bottom)



Industrials Are Industrious

Industrial stocks have held their uptrend and appear to be forming a relative price bottom.

S&P 500 Industrials Sector (Top) With Relative Price Vs S&P 500 (Bottom)



Energy Sector Is Low On Energy

The energy sector is not a market leader. Oil prices have declined as OPEC increases output in a global economy that may slow, due to reduced international trade.

West Texas Intermediate Crude Prices Have Fallen Below $65/Barrel To As Low As $55

S&P 500 Energy Sector (Top) With Relative Price To S&P 500 (Bottom)

Not All Energy Stocks Are Weak, However

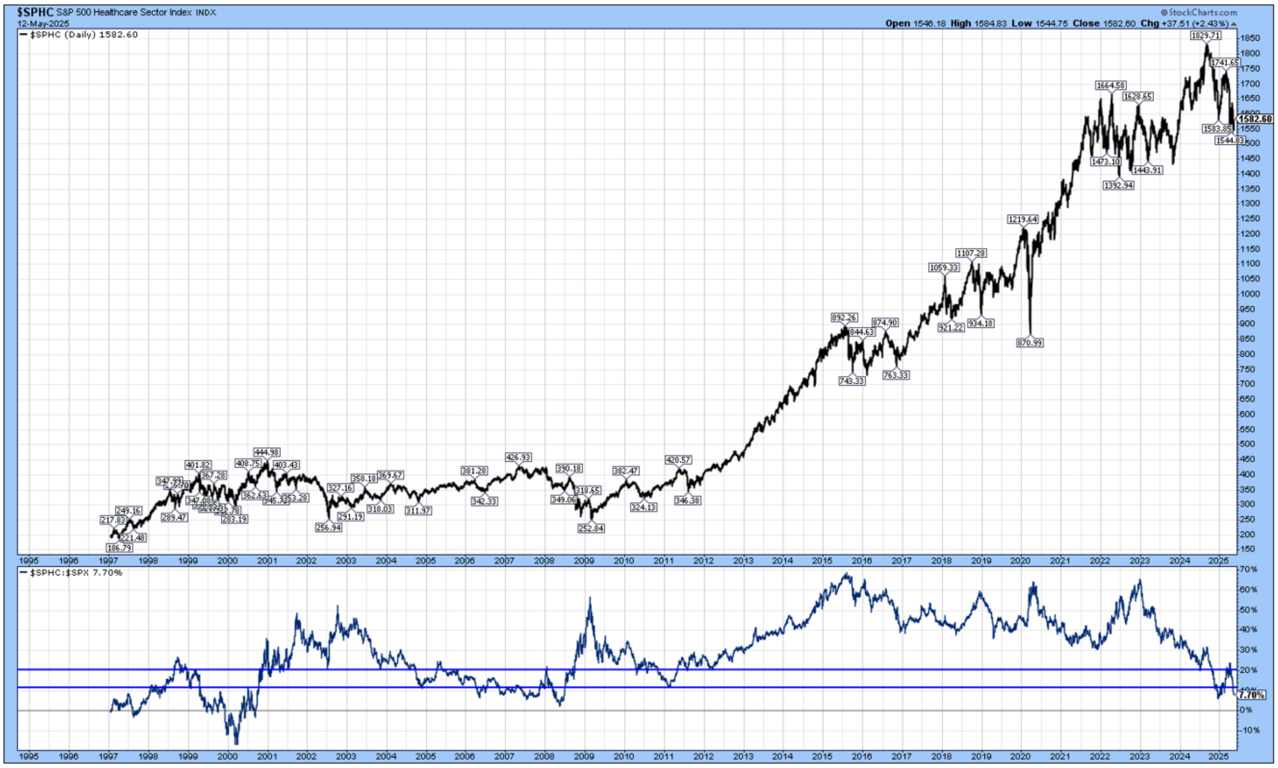
Some liquefied natural gas (LNG) stocks are performing well. Not only is LNG a clean source of energy, but rules barring new contracts for exports of LNG have been lifted.

Cheniere Energy (LNG) (Top) With Relative Price Vs S&P 500 (Bottom)

Health Care Stocks Are Unwell

Health Care stocks are weak in the market, led by Pharmaceuticals, which face increased bureaucratic scrutiny.

S&P 500 Health Care Sector (Top) With Relative Price Vs S&P 500 (Bottom)



Growth Returning to Dominance Over Value

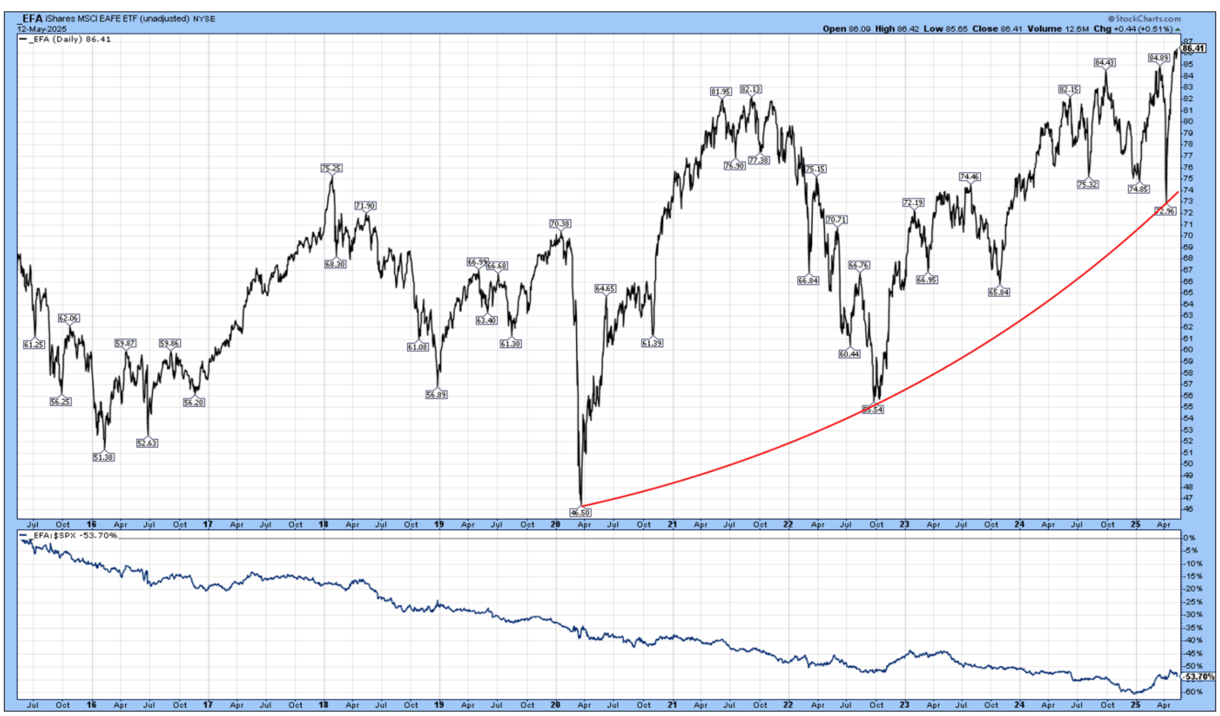
Value stocks have performed well so far this year as Growth stocks retreated from overbought conditions. Growth stocks, however, do well during periods in which profit expansion is not widespread, and we believe these conditions are likely to return as the economy adapts to the new international trade regime.

iShares Russell 1000 Growth ETF (IWF) Vs iShares Russell 1000 Value ETF (IWD)

Is It Time To Consider International Stocks?

U.S. stocks have outperformed the rest of the world for 18 years. It may be that the new international trading regime will reverse some of this. It is certainly the case that Europe is about to begin a massive rearmament, led by Germany, which has pledged €400 billion in new military spending and €400 billion in new infrastructure spending.

iShares MSCI EAFE ETF (EFA) With Relative Price Vs S&P 500 (Bottom)



STOXX Aerospace & Defense Sector Price Index And 200-Day Moving Average(Top) With Stochastics (Middle) And Moving Average Convergence-Divergence (Bottom)

iShares MSCI Germany ETF (EWG): Secular Bull Market Breakout!

Gold And Gold Miners

Levi Strauss made a fortune selling durable canvas pants to hopeful participants in the 1849 California Gold Rush. It isn't always the speculators who win in a rush, but the people who sell them the tools they require. In this environment, Gold Mining stocks are rising as global demand for the precious metal also rises. Our 2025 price target for Gold is $4,000 per troy ounce, but the price of Gold appears temporarily extremely overbought and has entered a correction, so the mining companies might be a better position for now.

Gold Prices Have Risen Sharply, Leaving Gold Overbought

VanEck Vectors Gold Miners ETF (GDX) (Top) With Relative Price Vs S&P 500 (Bottom)

Stablecoins Go Mainstream

Stablecoins are cryptocurrencies whose value is pegged, or tied, to that of another currency, commodity, or financial instrument. Stablecoins aim to provide an alternative to the high volatility of the most popular cryptocurrencies, including Bitcoin (BTC), which has made crypto investments less suitable for everyday transactions. USDC (issued by Circle) is a fully collateralized, dollar-backed stablecoin pegged 1:1 to the U.S. dollar and available on multiple blockchain networks. USDC was estimated to be $240B–$250B in size at the end of April. For comparison, that is about 4½% the size of demand deposits at banks, 11% the size of currency in circulation, almost 12% the size of retail money market funds, and nearly 25% the size of small time deposits in the banking system.

On April 28, Mastercard announced that it is teaming with several crypto providers to settle in stablecoin. Just as Americans can go to the UK or Japan and use a Mastercard for purchases, a Mastercard user can pay in either dollars (or other local currency) or with the stablecoin USDC, and the vendor can receive in payment either their local currency or USDC.

This is an extension of Mastercard's tokenization program that began in 2013 using blockchain, so the backbone, or structure, has been around quite a while and is well-tested. (Tokenization is how Mastercard enables one-time purchases without revealing the card number. This is why you can use your smartphone to buy a cup of coffee, for instance.) Only the crypto partners and the selection of the USDC stablecoin are new: the ecosystem is stable and reliable.

PRESS RELEASE

Mastercard unveils end-to-end capabilities to power stablecoin transactions – from wallets to checkouts

APRIL 28, 2025 | PURCHASE, NEW YORK

Latest partnerships with OKX and Nuvei will unlock a 360-degree approach where consumers can spend stablecoins and merchants can receive them, creating a seamless ecosystem

decrypt

Mastercard Jumps Into Stablecoin Trend With New Crypto Payment Offering

The payments giant wants crypto holders to be able to spend their stablecoins.

Apr 28, 2025

By Mat Di Salvo

MasterCard (MA) (Top) With Relative Price Vs S&P 500 (Bottom)

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Last Words

We believe the secular bull market remains intact and can rally on good news regarding trade and tariffs going into the summer months. The secular bull market's Technology leadership also remains intact, and its overbought condition from earlier this year has corrected. Financials are performing well, too. Europe is performing quite well. We would consider taking positions in Europe, particularly in Germany. We would prefer Growth over Value as markets continue to recover from the tariff announcement shock. We continue to believe that Treasury yields can decline on a cyclical basis. Inflation expectations continue to remain anchored, and term premium is historically quite modest.

While we believe that a summer rally has started early and it's onward and upward for the markets, the risks to our outlook are:

- Inflation pressures return, keeping rate cuts at bay or forcing the market to price in higher rates (especially on the 10-year Treasury yield).
- A sharp pullback in consumer spending, though we see no clear signs of this yet.
- U.S.-China tariffs return after the current 90-day hiatus.

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