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## **In Brief**

April was characterized by continued resilience in equity markets, albeit with increasing divergence beneath the surface. The S&P-500 advanced approximately 10.4% over the course of the month, marking one of its strongest monthly gains in recent years, with Communication Services and Information Technology leading performance. The index was supported primarily by a narrow group of large-cap technology and AI-related companies, while broader market participation remained more subdued. Periodic volatility persisted, driven by geopolitical uncertainty, particularly ongoing tensions involving Iran and disruptions around the Strait of Hormuz, which continued to support elevated energy prices, inflation expectations and shifting expectations for monetary policy, but overall market behavior remained orderly. This is notable given elevated valuations and the concentration of performance of a limited number of names. Fixed income markets remained under pressure as Treasury yields stayed elevated, reflecting ongoing inflation concerns and a more cautious outlook on the timing of policy easing. At the same time, higher yields have enhanced the attractiveness of fixed income from an income perspective, particularly in high-quality segments. Overall, April reinforced that markets continue to be supported by earnings and liquidity, and the stability in price action suggests that investors remain confident in the current economic backdrop, even as underlying conditions gradually soften.

## **Economy**

The U.S. economy continues to show signs of gradual deceleration but remains broadly resilient. Growth is moderating toward a more sustainable pace, with GDP expected to expand in the range of approximately 1.5% to 2.0% this year. Consumer spending is holding up, although early signs of fatigue are beginning to emerge. Manufacturing activity remains weak, reflecting softer global demand and tighter financial conditions, while the services sector continues to provide support. Overall, the data is consistent with a late-cycle environment in which growth is slowing but not contracting; however, this outlook remains sensitive to energy prices, particularly if disruptions around the Strait of Hormuz persist and keep inflationary pressures elevated.

## **Labor Market**

The labor market continues to provide underlying support to the economy, although signs of gradual normalization are becoming more apparent. Job creation has slowed from earlier elevated levels, wage growth is stabilizing, and continuing claims have begun to trend modestly higher. Despite this, overall employment conditions remain solid, with unemployment expected to remain in the range of 4.0% to 4.3%, while layoffs remain low by historical standards and labor demand continues to exceed supply. Concerns that rapid advances in artificial intelligence would lead to immediate and widespread labor displacement have begun to moderate, as adoption remains gradual and largely complementary rather than disruptive. This suggests a transition from an overheated labor market toward a more balanced environment rather than a sharp deterioration, although a more pronounced weakening would represent a key downside risk.

## **Monetary Policy**

Monetary policy remains a central factor for financial markets, with the Jerome Powell-led Federal Reserve maintaining a cautious and data-dependent stance. Inflation continues to trend lower, but remains above target, particularly in core components, limiting the scope for near-term policy easing. As a result, markets have adjusted expectations, now anticipating rate cuts later in 2026 rather than in the near term. Policy remains restrictive, but stable, providing a degree of visibility for investors while avoiding additional tightening pressure. At the same time, elevated energy prices, particularly if disruptions around the Strait of Hormuz persist, represent an upside risk to inflation and could delay the timing of any policy easing further. With the succession of the Fed Chair now

largely defined, markets are not anticipating a meaningful shift in the policy framework, reinforcing expectations of continuity. At the margin, however, a shift in communication strategy may emerge, as Kevin Warsh has indicated a preference for more limited and disciplined Federal Reserve communication, which could reduce forward guidance and increase market sensitivity to incoming data.

### **Corporate Earnings**

Corporate earnings continue to provide the primary support for equity markets, with growth remaining positive and showing signs of improvement. S&P-500 earnings are currently expected to grow in the range of approximately 8% to 10% this year, led by large-cap technology and communication services, where earnings growth is materially higher due to continued investment in AI and related infrastructure. In contrast, more cyclical sectors are delivering mid-single-digit growth, reflecting the impact of slower economic activity. Importantly, the current environment is characterized by a divergence between earnings trends and broader economic momentum, with corporate profitability holding up despite a gradual slowdown in growth. Historically, such periods have typically been resolved in favor of earnings, supporting equity valuations, although the narrow concentration of profit growth remains a key area to monitor.

### **Thoughts**

One of the more notable features of the current market environment is the contrast between underlying strength in corporate earnings and a cautious investor posture driven by geopolitical risk. While headline indices remain resilient, positioning suggests a degree of hesitation, particularly given the concentration of performance and sensitivity to macro developments. This dynamic likely overstates underlying fragility, as fundamentals remain solid. At the same time, the current level of uncertainty appears elevated relative to potential outcomes. A key variable remains the situation around the Strait of Hormuz. Should disruptions ease or the strait reopen more fully, energy prices would likely stabilize, reducing inflation concerns and improving the outlook for monetary policy. In such a scenario, equity demand could reaccelerate quickly, leading to a broader-based rally and a rotation beyond the current narrow leadership. Political considerations may also play a role. In the run-up to midterm elections, there is typically limited tolerance for sustained market weakness, giving the feedback loop between financial markets, confidence, and economic activity. While not a primary driver, this backdrop may support efforts toward stabilization. Importantly, current earnings trends provide a strong foundation for equity markets. With earnings growth remaining robust, a reacceleration in equity demand would not require a fundamental shift in the economic backdrop, but rather a reduction in uncertainty. In that context, a rally would be justified not only by improving sentiment, but also by the continued strength in corporate profitability.

Overall, the market appears more constrained by perception and positioning than by fundamentals. Should key uncertainties begin to be resolved, equities have the potential to respond quickly, allowing prices to realign more decisively with underlying earnings strength.

### **Market Outlook**

The market outlook remains cautiously constructive, supported by positive earnings momentum and stable liquidity conditions, although risks have become more evenly balanced. Equity markets continue to benefit from resilient corporate profitability, but elevated valuations and narrow leadership increase the potential for periods of volatility. While higher bond yields have improved the nominal attractiveness of fixed income, the case for corporate investment-grade credit as a true alternative to equities remains less compelling on a real basis, particularly if inflation proves more persistent. In such an environment, real returns in fixed income could remain constrained, while equities retain a relative advantage through earnings growth and pricing power. The path forward is, therefore, likely to be less linear, with markets increasingly sensitive to incoming economic data, developments in energy prices, and the timing of monetary policy easing. Overall, the fundamental backdrop remains supportive but reinforces the importance of a selective and disciplined approach to equity exposure.

Best regards,

Your Terra Nova Team!