

# Balancing Risk and Opportunity in Today's Market Environment

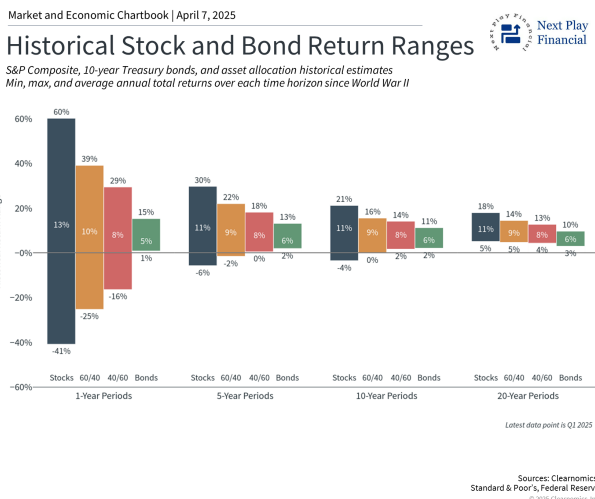


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April 7, 2025

Global markets have been roiled by escalating trade tensions and recession fears. As nations implement retaliatory tariffs, with China responding in kind, investors are increasingly concerned about a potential full-blown trade conflict. This uncertainty has driven declines across international markets while boosting traditionally safer assets like bonds.

## Strategic portfolio construction is critical in uncertain times



Successfully navigating markets requires both defensive positioning and offensive capabilities - much like in athletics. Defensive strategies focus on building resilient portfolios that can weather various market conditions. Given that market volatility and unexpected challenges are inevitable, maintaining strong defensive positioning is essential.

The offensive component involves capitalizing on opportunities that emerge during periods of market stress. While market uncertainty can be unsettling, it often creates attractive entry points for long-term investors. A well-constructed portfolio needs both elements. But how

should investors approach this balance in the current environment?

Long-term investing success relies heavily on diversification and patience, as illustrated in the accompanying chart showing historical performance ranges across different asset types. The data

demonstrates how these ranges shift with longer time horizons. For example, single-year stock market returns have ranged from +60% in 1983 as markets recovered from inflation concerns to -41% during the 2008 crisis.

Looking beyond one-year periods highlights the power of diversification and long-term planning. While diversification may limit maximum potential returns, it significantly reduces portfolio risk. This is clearly demonstrated by the balanced 60/40 stock-bond portfolio. While the S&P 500 has declined 13% year-to-date, a 60/40 portfolio is only down 4.6%.

The ultimate goal isn't maximizing returns at any cost, but rather optimizing the probability of achieving financial objectives. Diversified portfolios historically show more consistent outcomes, enabling better financial planning.

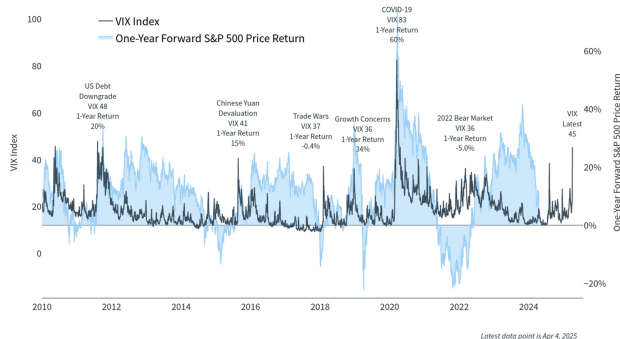
Time horizon extension can dramatically impact potential outcomes. Since World War II, there hasn't been a negative 20-year period for any of these portfolio types on an annualized basis. Many diversified allocations show similar results over 10-year periods. While past performance doesn't guarantee future results, this underscores the importance of maintaining a long-term perspective.

### Market uncertainty can create compelling opportunities

Market and Economic Chartbook | April 7, 2025

#### Volatility and Forward Returns

CBOE VIX Index and one-year forward S&P 500 price returns



Sources: Clearnomics, Standard & Poor's, CBOE © 2025 Clearnomics, Inc.

The VIX index, commonly called the market's "fear gauge," tends to spike during periods of market stress. These peaks align with significant market declines, as seen in 2008 and 2020. During these episodes, investor sentiment often reaches extreme pessimism.

Examining S&P 500 returns following these spikes reveals an interesting pattern. While no single year's returns can be predicted with certainty, history shows that some of the best opportunities emerge when fear is highest. This aligns with Warren Buffett's famous advice to "be fearful when others are greedy, and greedy when others are fearful."

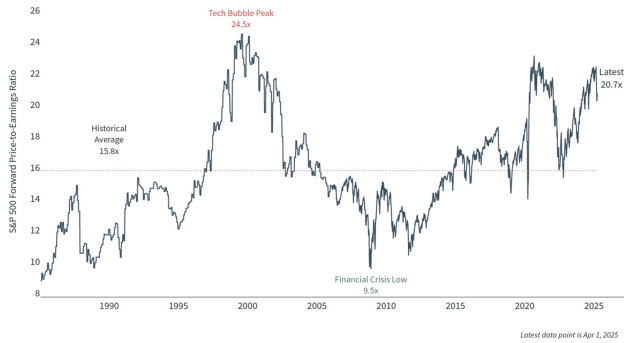
This is particularly relevant when markets face liquidity rather than fundamental challenges. Liquidity-driven selloffs occur when leveraged investors are forced to liquidate positions, potentially creating disconnects between prices and underlying value. These scenarios often present opportunities for patient investors.

However, this shouldn't be interpreted as advocating market timing. Even elevated VIX readings don't guarantee immediate market recoveries. Instead, investors should consider this within their broader portfolio strategy. Market declines often coincide with improved valuations, potentially warranting selective increases in exposure - though specific actions should align with individual circumstances.

### Market conditions have improved valuation metrics

## Stock Market Price-to-Earnings Ratio

S&P 500 forward P/E ratio using earnings estimates over the next twelve months



Latest data point is Apr 1, 2025

Sources: Clearnomics, S&P  
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In the current environment, bonds have provided valuable portfolio stability as yields have declined, helping offset weakness in other assets. Bonds typically exhibit lower volatility than stocks and often move inversely, providing valuable diversification benefits - hence the saying that "bonds zig when stocks zag." This uncorrelated behavior helps portfolios weather challenging periods.

After several years of strong equity performance, valuations have become more reasonable. While tariff impacts on earnings remain uncertain, the S&P 500's price-to-earnings ratio has decreased to 20.7x. Technology, Communication

Services, and Consumer Discretionary sectors have experienced particularly notable multiple compression.

Traditional safe-haven assets like gold have shown mixed performance recently. Despite reaching record highs earlier this year and delivering double-digit annual returns, gold prices have retreated amid broader commodity weakness. This reinforces the importance of maintaining a diversified portfolio rather than concentrating in any single asset class.

**The bottom line? Successfully navigating uncertain markets requires both defensive positioning and the ability to capitalize on opportunities. A well-constructed portfolio aligned with long-term objectives remains the most effective approach to achieving financial goals.**

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