

Highlights

- **The Economy: *Jittery investors sell off S&P 500 stocks***
The index dipped into negative territory YTD in mid-March
- **Food for Thought: *Measuring happiness ... is it even possible?***
A high-profile annual survey says Finland has the world's happiest citizens
- **Offbeat Investments: *The risk characteristics of owning luxury watches***
Looking for an asset class very uncorrelated to stocks? It might be time for watches. (This is NOT investment advice!)

Headwinds for Stocks: S&P 500 Suffers a Correction

On March 13, the S&P 500 closed down more than 10% since its all-time high set on Feb. 19 – meeting one definition of a correction. The total return of the index was down 5.9% YTD through March 13, after rising 25.0% last year.

Some market observers suggest that a significant factor behind the recent decline in stock prices is uncertainty stemming from Trump's tariff policies, noting that tariffs have at times been abruptly announced and subsequently withdrawn. Such unpredictability influences the discount rates investors use when evaluating future cash flows. However, other factors are also likely influencing market movements.

Additionally, some equity strategists have argued over recent months that stock valuations appeared elevated compared to historical averages, and thus a correction reflecting a reversion to the mean was likely to occur eventually.

Moreover, some forecasts of recession probabilities jumped sharply in the past month. A closely watched quantitative GDP forecasting model, the Atlanta Fed's GDPNow, suffered a sharp drop off in its estimate of Q1 GDP, which is now negative. The GDPNow model, which forecasts only the upcoming quarter, is based on recent economic reports. On March 18 it forecast -1.8% GDP annualized for Q1, down four percentage points from three weeks ago. A recession is two straight quarters of negative GDP growth. Our proprietary model, which forecasts the probability of a recession six months from now, shows about a 10% chance now vs. a 2% chance just several weeks ago. It predicts a 40% chance in 12 months.

Bloomberg's forecasting model now predicts a 25%-20% chance of a recession, up from 10% at the beginning of the year. Bloomberg's SHOK model also predicts a significant hit to GDP in the second half of the year from tariff costs and DOGE spending cuts and layoffs. JPMorgan Chase's chief economist puts the recession likelihood at 40%.

The latest consumer inflation report (CPI) was better than expected. Currently, the expectation based on Fed funds futures prices is for another 25 bps interest rate cut no later than the Fed's mid-June policy meeting (CME FedWatch forecasting tool, March 14). The CME FedWatch tool indicates at least two 25-bps rate cuts by year end, with an 80% probability. The probability of three rate cuts is about 30%, and four cuts, 15%. This is a reset of recent expectations for a slower pace of rate cuts and presumably reflects the increasing prospect of recession.

The benchmark 10-year Treasury yield has lost 30 bps so far this year and stood at 4.27% on March 13. The 2-year yield has also lost 30 bps and is at 3.94%.

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Headline inflation stands at +2.8%. Consumer demand is strong, but jobs and housing are sputtering

Headline inflation (CPI-U) rose 0.2% in February vs. a disturbing +0.5% in January. The 12-month trailing rate is now 2.8%, down from +3.0% in January. Core CPI, leaving out volatile food and energy prices, rose 0.2% and stands at +3.1% over the last year.

In February, the shelter component of CPI was responsible for half of the monthly increase. The price of gasoline fell 1.0%, and the cost of the energy component is -0.2% over the last year. The price of food, much in the news lately especially because bird flu sent the price of eggs soaring, is actually up only 2.6% over the past year, less than the overall inflation rate.

The CBOE VIX, the so-called “fear index” which tracks the volatility of S&P 500 futures, had been bound in a range of 14-20 since the beginning of the year, fairly low relative to the long-term average. But it spiked higher to around 25 on the early-March tariff news, and has stayed around that level.

Stocks outside the U.S. (iShares MSCI ACWI ex-US ETF) rose in both January and February and were up 6.1% YTD through Feb. 28. For full year 2024, they had a 5.2% gain, significantly underperforming U.S. markets. Emerging markets overcame late 2024’s headwinds, with the iShares MSCI Emerging Markets ETF up 3.3% YTD through Feb. 28.



Non-U.S. stocks are up 6% in 2025, while U.S. stocks have tumbled

The first read of Q4 2024 U.S. GDP was +2.3% annualized. Robust consumer spending compensated for a downturn in investment compared to the previous quarter when GDP rose 3.1% annualized. The trade balance (imports & exports) had little effect on GDP.

Other U.S. economic reports have been mixed. Factory orders plunged 0.8% in December but rose 1.7% in January. Durable goods orders were up 3.1% month-over-month in January, and nondefense capital goods orders ex-aircraft—a proxy for business investment—rose +0.8%.

The February jobs report was so-so, with 141,000 new jobs added, little changed from January. Headline unemployment remained at 4.1%. Average hourly earnings rose a bit in February to \$35.93. They’re up 4.0% over the past year, significantly higher than the rate of headline inflation.

The residential housing market is sputtering as lower interest rates have mostly not translated to lower mortgage rates, according to the National Assn. of Realtors®. Existing home sales were down 4.9% month-over-month in January, but +2.0% year-over year. January new home sales fell 10.5% month-over-month and were 1.0% less than a year ago. The average sale price of a new home is now \$510,000.

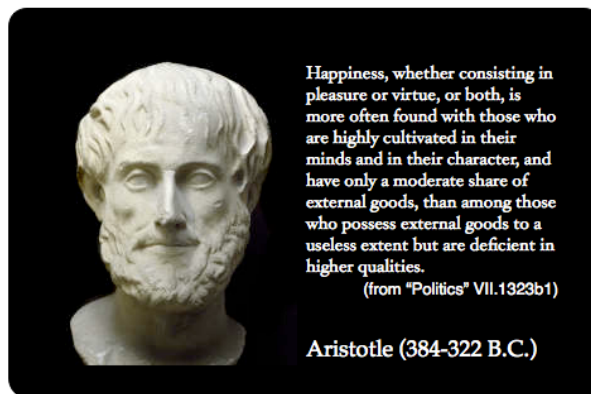
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Food for Thought: Those Happy Finns

The annual World Happiness Report always gets plenty of media coverage, usually, in this country, because the U.S. does relatively poorly compared to the Scandinavian countries which consistently top the survey. This year, Finland was the world happiness winner once again. Denmark, Iceland, and Sweden round out the top four, the same as last year.

The U.S. came in at #24 this year, with citizens less happy than in Costa Rica (#6), Israel (despite the war with Hamas, #8), and Mexico (#10).

The consideration of happiness – what it is, how to measure it, and how to achieve it – has been an absorbing topic since antiquity. The most famous philosophical definition of happiness is Aristotle’s: He believed it’s a state of flourishing and living well, achieved through cultivating virtues and engaging in activities that align with human potential, rather than fleeting pleasure.



Aristotle wasn’t a rich man, and he believed that the virtuous rather than the rich had the best shot at happiness. But prosperity is easier to measure than virtue. Since happiness is an emotional state, its measurement is necessarily subjective. Moreover, we haven’t come up with a method of measuring “happiness,” as such, better than asking people if they’re happy.

As discussed by political scientist Yascha Mounk (“The World Happiness Report is a Sham,” March 20), the method Oxford University researchers use to harvest data for the report is suspect. The rankings are based on the answers to a single question, the so-called Cantrill Ladder:

“Please imagine a ladder with steps numbered from zero at the bottom to ten at the top. Suppose we say that the top of the ladder represents the best possible life for you and the bottom of the ladder represents the worst possible life for you. If the top step is 10 and the bottom step is 0, on which step of the ladder do you feel you personally stand at the present time?”

Mounk concludes, “[P]erhaps the biggest problem with the World Happiness Report is that metrics of self-reported life satisfaction don’t seem to correlate particularly well with other kinds of things we clearly care about when we talk about happiness.

“At a minimum, you would expect the happiest countries in the world to have some of the lowest incidences of adverse mental health outcomes. But it turns out that the residents of the same Scandinavian countries that the press dutifully celebrates for their supposed happiness are especially likely to take antidepressants or even to commit suicide.”

Offbeat Investments: Luxury Watches

There are several reasons to own a luxury watch, only one of which is wearing it. Collecting watches is a popular hobby, even though no more than one may be worn at a time, and a collector might not even want to wear a prized rarity. Not to mention the risk of wearing a costly watch and getting robbed of it by knowledgeable thieves.

As a high-profile hobby for the very rich, collecting luxury watches might be said to have replaced the traditional hobby of owning racehorses. Worn for prestige and display by the likes of Mark Zuckerberg with his \$1 million Greubel Forsey, or Beyoncé with her \$5 million diamond-studded Hublot, the “super-watch” may turn out to be a good investment. Lesser timepieces like the relatively humble Rolex Submariner can also appreciate in value.



Record \$17.75 million for Paul Newman’s Rolex Daytona

The investment characteristics of luxury watches, as an asset class, are promising. A recent academic study estimated the size of the luxury watch secondary market worldwide at \$24 billion, a third of the total market for luxury watches. In January, Swiss scholars Philippe Masset & Jean-Philippe Weisskopf (unaffiliated with any watchmakers) published the first study of the investment characteristics of the secondary market.

The authors concluded that “luxury watches increase portfolio diversification and reduce risk.” Returns over time for the five years ending in 2024 were less than for stocks, but with lower volatility. Luxury watches did outperform fixed income and real estate. For the five years 2019-2024, the overall return of luxury watches was 5.68% annualized. The MSCI World index returned 12.85% annualized and gold 13.06% over the same period. The authors calculated the correlation to stock returns as 0.04 and zero to negative for other asset classes.

Now comes the most interesting part of the paper, at least to most collectors and investors: Which watch brand had the best returns? Among the brands tracked in the data, Hermès did best with a 27.72% annualized return. Rolex, by far the largest luxury brand in overall sales, returned 6.94% annualized and Patek Philippe returned 10.92%. The lowest performer in the group was Swatch, not usually thought of as a prestige brand, with -3.01% annualized.

Philippe Masset & Jean-Philippe Weisskopf, “Time is Money: an Investment in Luxury Watches,” SSRN (Jan. 2025).