

MARKET SIGHT LINES



Don't Wait for the Pullback: Steps to Take in a Resilient Market

By Michael O'Keeffe, *Chief Investment Officer*



Last week, we discussed how markets may react negatively if the [Federal Reserve dissappoints](#) and cuts rates less quickly, or less deeply, than investors expect. We've also discussed optimism around artificial intelligence, and how it is playing a key role in our [long-term investment themes](#). 2025 has been an interesting year, where markets declined in April around tariff worries, then recovered and surged against a backdrop of a resilient economy and earnings environment. Now equity valuations are quite elevated, primed for a possible pullback, whether from the Fed disappointing or some other catalyst. In this Sight|Lines, we review the environment and identify what an investor can do today to prepare for any negative volatility.

THE TAKEAWAY: THE ENVIRONMENT HAS BEEN RESILIENT, AND IT'S A GOOD TIME TO PREPARE FOR A MARKET PULLBACK

The economy continues to grow, and markets have moved higher, making this a good time to prepare for a potential market retrenchment. In summary:

- Second quarter GDP was strong, and a positive third quarter points to a solid 2025.
- Despite a decline in April, equity markets have recovered this year.
- Market valuations are now quite elevated, perhaps more susceptible to a pullback.
- For putting money to work, lean on the reliable approach of dollar cost averaging.
- If you are fully invested and overweight stocks, consider rebalancing.
- Some investors may be interested in derisking their investment strategy, especially those moving closer to retirement – and this is a good time to do that.
- Popular stocks like the Magnificent Seven (Alphabet, Amazon, Apple, Meta Platforms, Microsoft, Nvidia, and Tesla) may have seemed out of reach, and a market decline will likely be a good time to establish or add to a position.
- For investors worried about a more severe negative outcome, consider some [black swan](#) ideas to increase diversification and protect wealth in an extreme environment.

IN-DEPTH: THE ECONOMY AND MARKETS HAVE BEEN RESILIENT, AND THIS IS A GOOD TIME TO GET READY FOR ANY MARKET DECLINE

While the economy continues to grow and markets seem to keep moving higher, we'll have a market pullback at some point – making this a good time to prepare for such a move. Going deeper:

- A strong GDP in second and third quarter points to solid economic growth in 2025:
 - GDP is estimated to have grown in the second quarter at an annualized rate of 3.8%.
 - The Atlanta Fed GDPNow, a real-time growth estimate, is also at 3.8% for third quarter.
 - The consensus GDP 2025 growth rate is at 1.8% and has been moving higher.
- Equity markets are higher this year, even with a big decline in April around tariff worries:
 - Year to date, the S&P 500 fell -19% through April 8 but is now up about 15%.
- Markets today are more susceptible to a pullback, given elevated valuations:
 - The S&P 500 P/E ratio is 25% higher than its 10-year average.
 - Solid profits and earnings growth are supportive of higher levels, but only to a degree.
- The classic dollar cost averaging approach can be particularly helpful for investors putting money to work:
 - While each situation is different, consider a longer investment horizon, like 12-18 months.
- If you're fully invested and are now overweight stocks compared to your target, consider rebalancing.
 - A stock/bond portfolio at "60/40" to start the year may now be about "63/37."
- For those investors looking to "derisk," this is a good time to begin to lower their stock allocation:
 - For example, investors approaching or in early retirement may want to reduce equity exposure.
- Some investors feel like they may have "missed out" on investing in stocks like the Magnificent Seven, and a market decline may well create a "buying opportunity":
 - In 2022, while the S&P 500 declined -18%, the Magnificent Seven declined -45%.
 - And earlier this year, the Magnificent Seven declined -25% through April 8.
- Some investors may be worried about a more severe negative outcome, perhaps anchored in the U.S. [Fiscal Trajectory](#) or the polarized political environment – those may consider [black swan](#) ideas:
 - Precious metals: Assets like gold and silver tend to perform well during periods of market stress and uncertainty.
 - Natural resources real assets: Provide essential services and infrastructure that typically remain in demand regardless of economic conditions.
 - Foreign assets and currencies: Exposure to high-quality non-USD sovereign bills and selective foreign exchange can offer diversification against USD-centric shocks.

CONCLUSION

2025 has been an interesting year, with markets declining in April around tariff worries, then recovering and moving even higher given a resilient economy and earnings environment. With equity valuations quite elevated, the market is primed for a possible pullback, whether that be from the Fed disappointing or some other catalyst. But given positive markets, this is a good time to take action to get ready for any market pullback we might experience.

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