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WEALTH MANAGEMENT
NORTHWESTERN MUTUAL PRIVATE CLIENT GROUP

# Q1 2025 Quarterly Market Commentary

***The more intensely we feel about an idea or a goal, the more assuredly the idea, buried deep in our subconscious, will direct us along the path to its fulfillment.***
***-Earl Nightingale***


As we head into 2025 it is very easy to see how well markets have been doing. The S&P 500 had a return just shy of 25 percent last year and risk-on assets like Bitcoin have been on a tear, to name a few. However, with these higher returns have come higher valuations and stocks at these levels have given us a reason to be a little more cautious as we head into the new year. There are several questions that can be asked on how exactly we should deal with this reality and hopefully by now the answer will come as no surprise. There is a common saying in the industry that, “Bull markets don’t die of old age,” and at Patterson Andrews Wealth Management, we know the pitfalls of trying to prove or disprove markets in the short run. With that being said, we aren’t putting blinders on, either and now would be a good time to talk a little bit more about our investment philosophy in fixed income.

Equities and the broader economy in general may get all of the headlines and I seriously doubt that any of you are clamoring to talk about bonds at social events, but the importance of this asset class cannot be understated. There is also no shortage of fixed income strategies and overall philosophies of how fixed income should be incorporated into a portfolio. Hopefully we can help provide you with our framework so that the next time that you do hear of the asset class you can translate that into how your portfolios are being invested here. At Patterson Andrews, we believe that the fundamental purpose of fixed income in a portfolio is safety. Bonds should be the shock absorber for the portfolio when the equity markets are doing poorly and act as a ballast. With safety in mind, lets discuss our three-tiered pyramid approach since I believe that this is the easiest way to articulate what we are trying to do.

The base of that pyramid functions in the way that I just described above. It should have the highest overall weight in the portfolio because it serves the chief purpose of the asset class. Within the base of the pyramid are a few different types of fixed-income securities that should be included here, all of which will give you that solid and stable foundation on which to build the overall portfolio. We are not reaching for yield in this part of the pyramid, and this should almost always be the most boring part of your portfolio. In fact, if this part of your portfolio stands out in your statements, then that is likely going to mean bad news. Remember, if markets are behaving normally, and we have achieved our goals in fixed income, this part of the portfolio will do well when the rest of your portfolio isn't.

As we move up from the foundation of the pyramid, we get into some of the more sophisticated fixed-income strategies (and the most fun for me to research). Keep in mind that although these strategies may seem complicated, and these portfolio managers are some of the smartest in the industry, they are doing all these fancy things just to ensure an optimal risk/return tradeoff. What do I mean by that? They are finding ways to give you a return that's slightly higher than core, foundational fixed income, without taking on excess risk. The result is going to be marginal, but material to the overall returns in fixed income. Strategies in this part of the pyramid will just have a wider dispersion of returns, all else equal, than the base of the pyramid but are still considered safe.

Lastly, the top of the pyramid, which will also have the lowest overall weight in the portfolio, is the place where we find it appropriate to look for return-enhancing opportunities in fixed income. It is also probably the easiest part of the portfolio to understand. High-yield bonds and their substitutes reside here.

Put it all together, and you should have a highly diversified, well-structured fixed-income portfolio that will be the ballast that the portfolio needs in times of stress. If you have any additional questions, I'd be happy to discuss our fixed income strategies in more detail.

Regards,

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