Vivaldi Insights

Second Quarter 2025

Quarter in Review

In the second quarter of 2025, markets demonstrated remarkable resilience in the face of persistent volatility, geopolitical uncertainty, and evolving monetary policy. The quarter began with a sharp correction following President Trump's "Liberation Day" tariff announcement on April 2, which triggered the worst two-day performance for the S&P 500 since March 2020. During the month, major indices experienced significant volatility, with the S&P 500 falling nearly 14% at its lowest point before recovering to end down just over 0.5%, while the Nasdaq briefly entered bear market territory and the Dow also declined. The CBOE Volatility Index (VIX) spiked to 52%, placing it in the top 1% over the past 35 years. The tariff escalation was met with swift retaliation from China and the EU. While a 90-day pause was introduced mid-month, China was excluded, and tensions remained elevated.

Despite this, equity markets rebounded strongly over the remainder of the quarter. The Nasdaq gained 18.0%, the S&P 500 rose 10.9%, and the Dow added 5.5% for the quarter. From January 1 through June 30, 2025, the S&P 500 and Nasdaq Composite returned 6.2% and 5.9% respectively, while the Dow Jones Industrial Average gained about +4.5%. According to FactSet, 78% of S&P 500 companies reported positive earnings surprises for Q1, with a blended year-over-year earnings growth rate of 12.5% - marking the second consecutive quarter of double-digit growth. The forward 12-month P/E ratio for the S&P 500 rose to 21.3, above both the 5-year average of 19.9 and the 10-year average of 18.4, suggesting elevated market valuations.

Economic data throughout the quarter painted a mixed picture. In April, job growth exceeded expectations, with payroll gains surpassing forecasts and the unemployment rate holding steady at 4.2%. However, May data showed signs of softening, with rising jobless claims and slowing non-farm payroll growth, though inflationary pressures eased modestly. At the June FOMC meeting, the Federal Reserve decided to keep interest rates steady at 4.25-4.50%. The Fed noted that the economy is growing steadily, and unemployment remains low, though inflation is still somewhat elevated. Chair Powell emphasized a patient approach, signaling the Fed will wait before making any rate changes, particularly given ongoing tariff impacts and global uncertainties.

Fixed income markets were also volatile. Treasury yields initially fell in response to the tariff shock but rebounded as concerns mounted over the U.S. dollar's safe-haven status. By quarter-end, the 10-year Treasury yield settled around 4.16%. The bond market's traditional diversification benefits were questioned, as both equities and Treasuries sold off in tandem during the early-April turmoil.

Several alternative asset classes demonstrated resilience amid recent market volatility. For example, multi-strategy hedge funds delivered flat performance in April despite heightened market turbulence, while equity markets posted negative returns. Despite ongoing volatility and uncertainty, multi-strategy hedge funds as an asset class achieved positive returns for both the second quarter and year-to-date through June 30.

Private credit continued to deliver stable performance, supported by low volatility and robust risk management. The asset class remains attractive, with various sub-strategies - including direct lending, collateralized loan obligations, asset-based lending, and synthetic risk transfers - currently offering yields above 10%. A focus on high-quality borrowers, first-lien positions, and overcollateralized structures has supported the asset class's resilience in the face of broader market downturns.

Performance in private and growth equity remained muted, primarily due to ongoing challenges in the IPO market, including delays and tariff-related disruptions. However, portfolio companies continue to demonstrate solid fundamental progress. While the softer IPO environment has extended fund durations - as private companies opt to remain private until conditions stabilize - we remain confident in our managers' ability to execute high-quality exits over time.

Looking ahead, the interplay between trade negotiations, monetary policy, and corporate earnings will shape market direction. While the tariff pause offers a temporary reprieve, the path forward remains uncertain. The Fed's cautious posture and improving inflation trends provide some support, but geopolitical risks and policy shifts could reintroduce volatility.

As always, we remain committed to disciplined asset allocation and long-term planning. Diversification across traditional and alternative assets, combined with a focus on behavioral discipline, remains central to our investment philosophy. We continue to monitor developments closely and stand ready to guide you through this evolving landscape with a focus on your long-term financial goals.

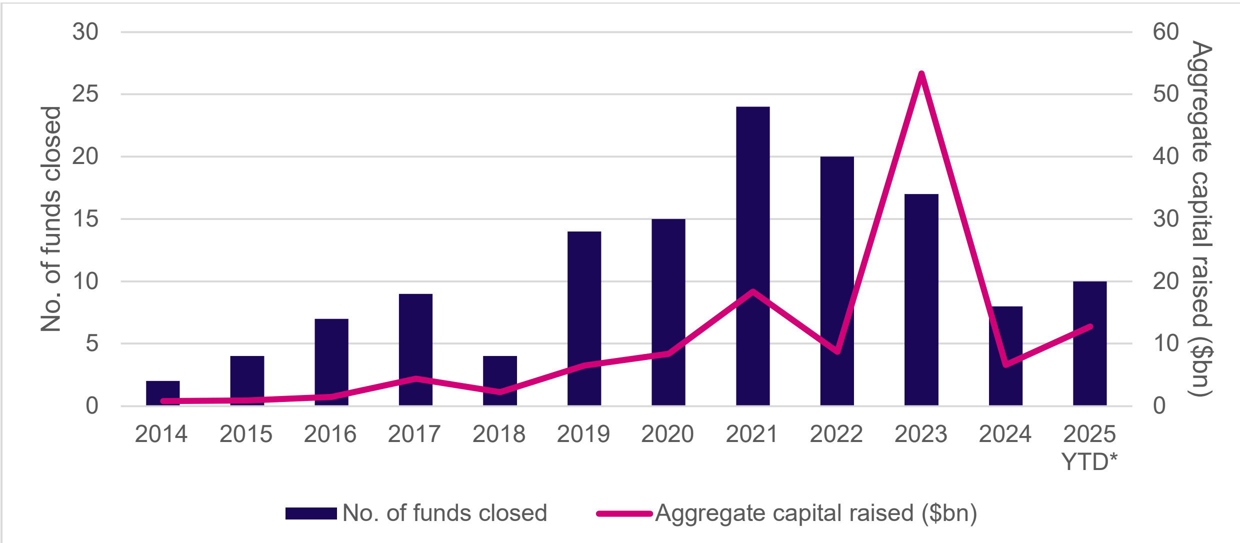
Exploring Opportunities in Private Real Estate and Data Centers:

Investing in private real estate, especially through non-traded Real Estate Investment Trusts (REITs), provides compelling diversification benefits beyond stocks and bonds. Private REITs invest in a wide range of property types, including residential, commercial, industrial, and increasingly data centers, which are becoming a valuable asset class. This variety helps reduce risk and smooth out portfolio ups and downs, while also offering the potential for steady income from rent and property sales. Over time, rising property values and smart acquisitions can also support long-term growth.

Private real estate offers strong risk-adjusted returns, with a 7.99% annualized return and a relatively low standard deviation of 6.25%. This makes it a compelling alternative to more volatile investments. By comparison, the S&P 500 returned 9.06% annually over the past three years but with much higher volatility (17.05% standard deviation). Private real estate also adds valuable diversification, with low or negative correlations to traditional assets like U.S. Core Bonds (–0.16) and Global Stocks (0.02)[1].

For most non-traded REITs, generating consistent cash flow remains the primary objective. Several of the larger players in the space are delivering attractive yields ranging from 5% to 6%. When factoring in their tax-equivalent yields, the income potential becomes even more attractive.

Fundraising for real estate funds focused on data centers reached its highest point in 2023, both in terms of the number of funds closed and the total capital raised.



Source: Preqin, YTD as of May 2025

Private real estate also tends to be less volatile than public markets since it isn't traded daily. It may offer tax advantages, like deferring income taxes and reducing capital gains through return of capital (ROC). Non-traded REITs are especially opportunistic, often seeking out new and attractive real estate sectors like data centers or logistics hubs, where demand is rising. These investments can also help hedge against inflation, offer tangible value, and benefit from supply-demand gaps in fast-growing or underserved markets.

Financial Planning - One Big Beautiful Bill Act Financial Planning Implications:

On July 4, 2025, President Trump signed into law the One Big Beautiful Bill Act (OBBBA) following narrow approval by both chambers of Congress. A substantial portion of the bill permanently extends key provisions of the 2017 Tax Cuts and Jobs Act (TCJA). While discourse around the legislation continues, we want to highlight several provisions with meaningful implications for personal financial and estate planning.

Key provisions include:

- Lifetime Gift and Tax Exemption: Previously set to sunset from $13.99 million to approximately $7 million in 2026, the exemption has now been permanently increased to $15 million per individual, indexed annually for inflation beginning in 2026. This presents a valuable opportunity for high-net-worth individuals to revisit gifting strategies and long-term estate plans.
- Qualified Opportunity Zone (QOZ) Program: The QOZ program, originally set to expire on December 31, 2026, has been granted permanent status under the OBBBA. Investments made prior to the 2026 deadline must still recognize deferred gains by that date. However, investments made on or after January 1, 2027, will benefit from a 10% step-up in basis on deferred gains after five years, as well as 100% exclusion of appreciation if held for ten or more years—reaffirming QOZs as a powerful long-term planning tool.

Other notable provisions include:

- A permanent boost to the standard deduction to $15,750 for single filers, $23,625 for heads of household and $31,500 for married individuals filing jointly
- A temporary increase in the State and Local Tax (SALT) deduction cap from $10,000 to $40,000 from 2026 through 2029, with the increase phasing out at higher income levels
- A permanent extension of the individual tax cuts enacted under the 2017 Tax Cuts and Jobs Act (TCJA), which were set to expire in 2025
- Elimination of income tax on tips and overtime, subject to certain limitations
- A new charitable income tax deduction for non-itemizing taxpayers, allowing deductions of up to $1,000 for single filers and $2,000 for joint filers

We are actively monitoring the implementation of these changes and will continue to provide timely insights to help clients optimize planning strategies in this evolving tax landscape.

Thank You

We reiterate our closing statements from our Q1 letter. We are here to provide guidance and advice throughout challenging times. We thank you for your trust and confidence in Vivaldi Capital Management. We continue to work each day to maintain that confidence.

Please contact us with any questions, comments, or concerns - clientservice@vivaldicap.com

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1. Source: eVestment, NCREIF. Data begin date 3/31/1995 – 12/31/2024, most recent data available.