SANJAC ALPHA'S QUICK TAKE

Staying Safe in a Max Volatility Environment

April 4, 2025

Recent days have delivered a jarring reminder of how markets can still be surprised by an event seemingly everyone knew was coming. U.S. stock markets experienced their most severe two-day decline in five years, with Wall Street's main indexes posting their largest one-day percentage drops since 2020 on April 3.

The catalyst? President Trump's sweeping tariff announcements, which sparked fears of an escalating trade war and a potential global recession. Inflation concerns and geopolitical tensions further fueled the sell-off, driving investors to seek refuge in safer assets like government bonds.

Bond markets, meanwhile, reflected a flight to safety. Yields on the 10-year U.S. Treasury dipped below 4% on April 4 as prices rose, signaling strong demand for fixed-income securities amid the equity rout. This shift came despite earlier volatility in yields, with front-end rates adjusting to expectations of more aggressive Federal Reserve rate cuts in response to tariff-induced economic pressures.

Investment-grade bonds have held up well, staying relatively tight through Q1, while high-yield bonds faced headwinds from tariff-related uncertainty. The bond market's resilience underscores its role as a potential stabilizer in diversified portfolios, though investors buying long dated duration should be mindful of inflation risks that persist into the near future.

While the tariff shocks are likely to be temporal as they can easily be added and removed, inflation and stubborn growth are more constant themes of 2025-26.

For investors navigating this max volatility environment, staying safe means leaning on diversification and discipline, and considering rebalancing and de-risking exposures to equities that have outsized gains over the past two years.

Previously we discussed the heavy equity allocations seen across both retail and institutional accounts with many asset managers heavily biased to equities. For instance, the BlackRock 80/20 Target Allocation Fund, a popular model, allocated 80% to equities (with roughly two-thirds in U.S. stocks) and 20% to fixed income.

SanJac Alpha Core Plus Bond ETF (NASDAQ: SJCP) offers an alternative portfolio structure, currently with treasury positions held with shorter term maturities balanced with investment grade credit positions. The short-term treasuries offer liquidity and a buffer against volatility, while the investment grade credit positions offer additional spreads while remaining at the less volatile end of the credit spectrum. This allocation should allow the investor exposure to enhanced yields while suppressing volatility.

SanJac Alpha Low Duration ETF (NASDAQ: SJLD) offers an even stronger bastion to volatility by currently holding a large position (now 80%) in short term treasuries, and a smaller exposure to investment grade credit. The credit portion targets the shorter-dated mortgage-backed securities (MBS) market that benefit from presently higher spreads and better value than other sectors. This profile should allow for investors to receive some additional spread over the treasury market while still remaining very defensive to rapid moves in rates or credit spreads.

SanJac Alpha continues to be active in its aims to mitigate risk and volatility in markets, and to achieve moderate positioning in investment grade bonds and mortgages to help generate an income to buffer pricing swings that commonly occur during these types of events.

Patience and a balanced approach will be key as markets digest this turbulence.