



Quarterly Investment Commentary

FIRST QUARTER, MARCH 2025

Things seem to be moving fast—so fast that we have decided to release our quarterly commentary ahead of schedule to offer more timely insights on developments and their potential impact. Of course, the markets have been digesting a series of rapid-fire policies coming out of Washington D.C. and what the implications are for the broader economy. At the heart of the matter are the on-again, off-again announcements of tariffs on some of the U.S.'s major trading partners. These tariffs are a response to what's seen as unfair business competition, lax border security, and to offset the growing trade imbalances. The tariffs are also presented as a way of taking the necessary steps in getting the country's fiscal house "in-order". It's a complicated situation and one where eventually other overseas trading partners could be targeted as well. As we see it, the administration's playbook is aimed at two potential outcomes: the short game or the long game.

• The Short Game

This approach involves leveraging influence, applying maximum pressure, and using negotiating tactics to strike a better deal for U.S. businesses. This includes less regulation on U.S. exports and would benefit multi-national businesses and farmers. A successful outcome in this scenario might include handshakes with other global leaders, a photo op, and a ceremonial press conference announcing the deal.

• The Long Game

This scenario is more complex and would likely involve higher tariffs becoming a more permanent fixture to trade policies. The end goal is to reorient the U.S. economy to be less reliant on imports while shifting a greater amount of burden for defense spending and aid to trading partners. A successful outcome here is that potentially, over time, idle manufacturing towns will be revitalized with new jobs, while foreign producers move operations to the U.S. to avoid tariffs.



While the final outcome remains unknown, attempting to predict it by analyzing every comment coming out of Washington may not be the most productive approach. The financial markets have been focusing on the broader implications of tariffs and the potential domino effect, which starts with higher prices.



The major concern is that a prolonged and escalating trade war will ultimately influence the direction of interest rates, impact the labor market and business production methods, and slow the economy or perhaps push it into recession.

It's also important to note that the U.S. is the largest consumer economy in the world and represents a significant portion of global demand for goods. While consumers in the U.S. will feel the pinch of higher prices on imported goods, the impact will be much greater on those countries targeted by tariffs. Hence the saying, 'No one wins in a trade war'—however, it is a powerful negotiating tool for the U.S., even if some of the actions being targeted have nothing to do with trade.

2018-2019

Let's not forget that during Trump's first term as president, we faced a similar situation with global trade tensions. Multiple rounds of tariffs were announced, then paused, then levied against Canada, Mexico, the European Union, and China. How did the markets react when these tariffs were announced? Pretty similar to today—not good.

As the table below illustrates, escalating trade tensions were a contributing factor in each of the notable sell-offs during the 2018-2019 period. It's also worth noting that stock indexes recovered remarkably quickly during this period, with price sell-offs only lasting a few weeks to a few months.

What Next?

While the enactment of tariffs came as no surprise (it was a campaign promise), the manner of execution has introduced some uncertainty, and uncertainty contributes to volatility. The tariffs announced today are also much larger than those imposed between 2017-2019. This, coupled with the announced government spending cuts, could translate to a larger impact on the U.S. economy. For reference, Goldman Sachs recently reduced its economic growth forecast and estimates that the average tariff rate will rise by around 10% this year, or about 5X the increase seen during the first Trump administration. While the situation has the potential of getting worse before it improves, any further tariff induced weakness could lead to a quicker resolution period. It's also easy to imagine that some of the proposed tariffs will stay in place while others end up being temporary, thereby lowering the overall price impact on imported goods.

Whatever the outcome, we are bracing for the increased volatility in the financial markets to continue. As an investor, the instinctive response to elevated uncertainty or volatility might be to run for the hills—sell stocks, raise cash. However, we view the current situation through a different lens.

Period	S&P 500 % Decline off Highs	Causes	Recovered
Oct- Dec 2018	-19.80%	Fed rate hikes, US-China trade tensions, Global growth concerns. Govt shutdown	Apr-19
May-June 2019	-6.60%	US-China trade tensions, bond yield curve inversion	Jun-19
Aug-Sept 2019	-6%	US-China trade tensions, China devalues its currency (Yuan)	Sep-19



While stock market volatility can be uncomfortable, it also presents opportunities to add exceptional businesses to an investment portfolio at attractive prices—something we welcome. Periodic rebalancing and repositioning during volatile periods also allows for adding to existing stock positions at more attractive price levels, which will assist in enhancing long-term returns.

What we do know is that trying to guess the short-term market swings through timing strategies or selling and then re-entering stock positions does not yield consistent results. The markets are influenced by many moving parts and short-term developments are too unpredictable to ensure any reliable outcome. As noted earlier, the tariff induced sell-offs during 2018-19 were relatively short lived. An investor would have had to sell stocks then almost immediately buy them back to avoid missing the subsequent rally.

Although short term market volatility can be an emotional roller-coaster, markets over time are resilient. As the Peter Lynch quote emphasizes, investors can inflict more harm by overreacting to downturns or potential downturns than by staying invested and sticking with a proven strategy. It's also important to note that trade wars can end as quickly as they arise. It only takes the stroke of a pen to reverse policies, ease restrictions, and restore market confidence.

“Far more money has been lost by investors preparing for corrections or trying to anticipate corrections, than has been lost in corrections themselves.”

-Peter Lynch,

*Manager of the Fidelity Magellan Fund
1977-1990*

1st Quarter Recap

While the investment road has gotten bumpier during the first quarter, stock returns have been more of a mixed bag than the indexes might suggest. As of this writing, the S&P 500 stock index is down 6% and has declined 10% from the highs reached on February 19th. Although the broader indexes are in the red year-to-date, there are several more defensive sectors still in positive territory, which include health care, consumer staples, and utilities. The growing influence of the Magnificent 7 stocks* in the S&P 500 index and its impact on returns has been well publicized. Just as a pendulum swings both ways, the impressive AI-fueled rally of the past two years has finally shown some weakness. As illustrated in the chart on the next page, the Mag 7 stocks have led the downturn, while the average stock listed on the S&P 500 is down a more modest 3.5% so far this year.

**Magnificent 7 stocks include Alphabet, Amazon, Apple, Meta-Facebook, Microsoft, Nvidia, & Tesla.*

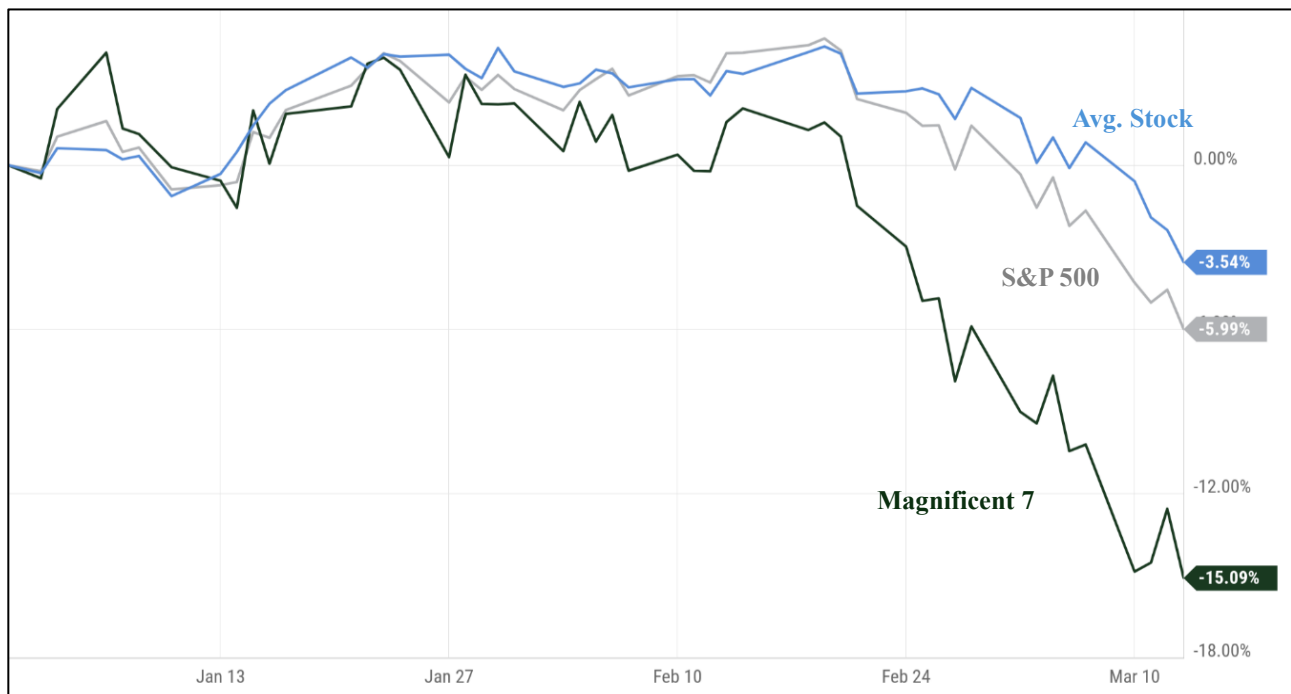


At this point, there is really nothing unusual about this correction. The brunt of the sell-off has been mainly confined to tech stocks that had risen rapidly under high public enthusiasm, which resulted in lofty valuations. Even with the recent downturn, it's important to note that the S&P 500 has still averaged over 20% per year the past two years, which is markedly higher from the long-term average investment experience. Despite the recent weakness in U.S. stocks, other asset categories are helping to stabilize the volatility, which demonstrates the benefits of a diversified portfolio. High-quality bonds have generated a total return of 1.6%, while International stocks have gained over 6% this year.

As noted in our previous commentary, our focus remains on broad equity diversification. This includes owning stocks outside of the most popular names, maintaining exposure to high quality bonds for income and a volatility offset, and owning some international equities, where valuations appear more attractive.

We will continue to keep a watchful eye on markets and make adjustments as needed. As active investment managers, we take a cautious approach with your assets and spend time focusing on the fundamentals despite the market volatility.

Please do not hesitate to reach out with any questions or concerns.



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