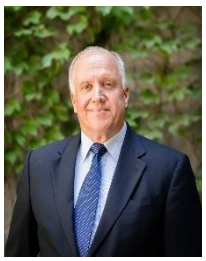
2025 – 1st Quarter Review & Outlook

Economic and Investment Review



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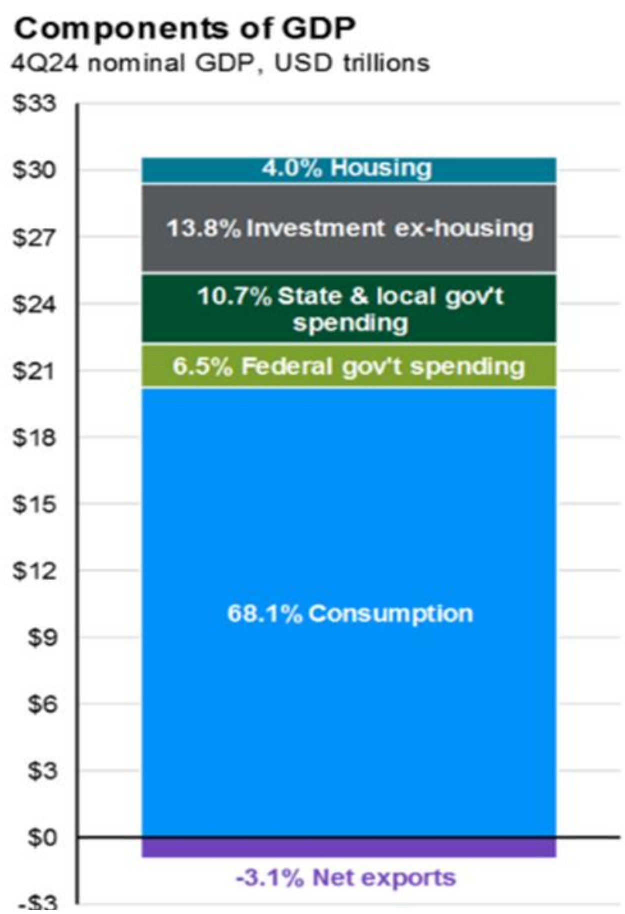
Economic Growth: Q1 GDP came in at -0.3% Q/Q, below the +0.3% consensus expectation. The decrease was primarily due to an increase in tariff-inspired imports and a decrease in government spending. The consensus forecast for 2025 GDP growth is currently 1.9%. Estimates peaked at 2.2% at the end of February and have been in the process of being revised down since that time. Economists and strategists have the impossible task of forecasting economic growth in the current volatile tariff environment.

Jan Hatzius, chief economist at Goldman Sachs, sees growth slowing to 1.3% for the year. Goldman identifies three developments that have impacted their growth outlook. First, financial conditions have tightened more aggressively than expected. Their Financial Conditions Index is calculated using a weighted average of funds rate, 10-year U.S. treasury yield, Baa credit spreads, the S&P 500, and trade-weighted dollar. Second, growth is trimmed due to declining foreign tourism and foreign consumer boycotts of U.S. goods. Third, policy uncertainty is extremely high which will likely result in less business fixed investment. In this scenario, Goldman expects the Fed to cut the Fed Funds target rate by 0.75% in 25 bp increments.

Eugenio Aleman, chief economist at Raymond James also revised their GDP forecast for 2025 down to 1.3% from 1.8% recently. The downward adjustment has been made in light of tariffs becoming more than just a negotiating tool. He identifies increased pressure on consumers and increased business concerns regarding the future of the U.S. economy as reasons for lower growth expectations. Raymond James is only looking for one 25 bp rate cut in the Fed Funds rate in 2025.

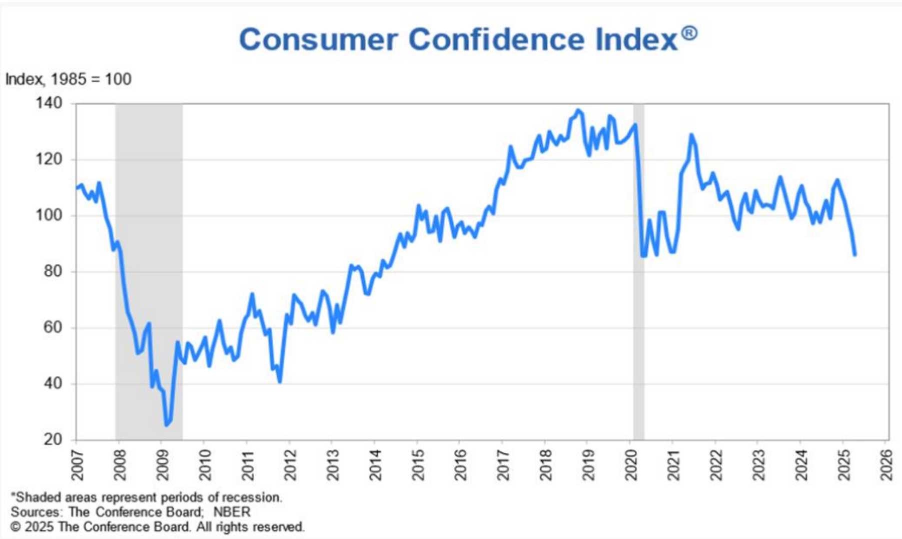
Neither firm is currently forecasting a recession but the lack of negotiated tariff settlements could lead to additional revisions in their forecasts.

The formula used to calculate Gross Domestic Product is GDP = Consumption + Investment + Government Spending Growth + Net Exports. The largest component of GDP is Consumption.



Source: JPMorgan Asset Management

Consumption will likely be reduced due to the impact of tariffs on business and consumer confidence. Businesses may delay hiring plans or even possibly reduce headcount. Consumers may become more conservative in their spending if they act on declining confidence. The Consumer Confidence Index fell to 86.0 in April from 93.9 in March and 100.1 in February. The April number was the lowest since 2011. The Conference Board's senior economist, Stephanie Guichard, stated that "the three expectation components – business conditions, employment prospects, and future income all deteriorated sharply, reflecting pervasive pessimism about the future."



If consumers are going to moderate their spending pace, they have yet to show it. Consumers may be trying to get in ahead of tariff-related price increases which could be pulling some purchases forward from future months. Retail sales surged 1.4% in March from a month earlier. Strong overall spending was somewhat of a surprise, but consumers may be altering their targeted spending. Bank of America analysis of debit- and credit-card spending shows decreased spending on Airlines and increased spending on electronics.

Investment or business capital expenditures related to AI were expected to surge in 2025. However, even if the AI-related investment holds up, it is likely to be more than offset by the delay in other investments due to the chaos caused by tariff announcements.

A deficit in consumer or investment spending may have been at least partially filled by an increase in government spending in the past but is not likely in the current cost-cutting environment. However, the continuing resolution passed in March will nearly maintain Biden-era spending through the remainder of the fiscal year. Additionally, state and local spending may have to be modified if tax revenues slow.

Inflation: Inflation was up 3.0% in 2024. Year-over-year inflation declined from 3.0% in January to 2.8% in February and 2.4% in March. The March number does not indicate how prices have been impacted by tariffs. However, the consensus estimate for 2025 has risen from 2.4% in December back up to 3.0% in April. Goldman Sachs forecast 3.4% for the year. Inflation will at least temporarily be impacted by tariffs and supply chain disruptions. Globalization had a positive impact on inflation and now if deglobalization becomes a reality, the reverse should be expected. The dreaded prospect of stagflation has been raised but softening demand due to a less confident consumer should work to help moderate any increase.

Interest rates: The Fed has been getting considerable pressure from the White House to cut rates. However, they do not want to respond to the pressure and desire to be cautious about cutting rates due to the possibility of rising inflation. The

Fed will be focusing attention on the labor market and the unemployment rate as they consider their timing for cuts in the Fed Funds rate. Chair Powell said that the tariff increases announced by the Trump administration were "significantly larger" than he expected and that tariffs were likely to slow growth and raise inflation. If the FOMC's maximum employment and price stability goals conflicted, Powell said the Fed would gauge how far the economy was from each goal, "keeping in mind that, without price stability, we cannot achieve the long periods of strong labor market conditions that benefit all Americans."

Source: FactSet

The European Central Bank and the Bank of England parted ways with the Fed in their recent moves. The ECB lowered its key interest rate to 2.25% from 2.5% on April 17 and the Bank of England lowered its interest rate by 0.25% to 4.50% in February.

The Fed reduced the Fed Funds rate by 1.0% in 2024 and the market expects the Fed to reduce the rate by an additional 0.75%, in three 0.25% increments later in the year.

Labor: The labor market remains reasonably healthy even with some corporate layoffs and government cutbacks. April nonfarm payrolls grew by 177K m/m vs the 130K consensus estimate. Unemployment remained at 4.2% for April and has ranged from 4.0% to 4.2% for the majority of the past year. The consensus estimate for the end of 2025 is 4.3%. However, Goldman Sachs and JPMorgan both expect the unemployment rate to exceed the consensus estimate at 4.7% and 4.5% respectively.

Global: The global economy is expected to generate real GDP growth of 2.4% in 2025 down from 2.7% expected at the beginning of the year. The Bloomberg consensus estimate for the Euro area is just 0.8% and is 4.2% for China.

Equity Markets

The U.S. large-cap equity market, as measured by the S&P 500, declined by -4.27% in Q1. The index peaked on February 19th at 6144 and then dropped by -18.9% to 4982 on April 8th in response to the Trump tariffs. The market has since rebounded to over 5600 but remains down by -4% on a year-to-date basis through May 5th (review date). Even with the recent downturn, the S&P is still up about 12% over the past 12 months. The Magnificent Seven was hit harder than the other 493 stocks as a group, declining by over 25% during the same period. The high flying group has rebounded significantly since that time but remains down -12% YTD. However, even with the large recent pullback, the group has returned nearly 20% on a 12-month basis.

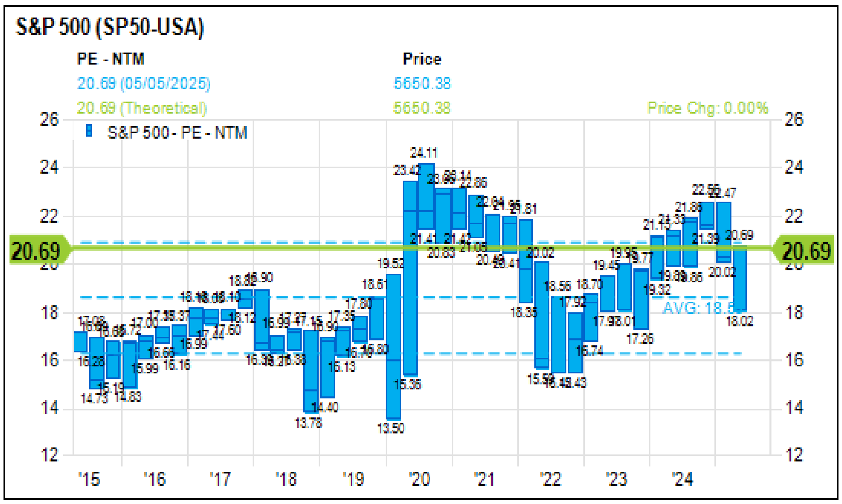
Value stocks held up better than growth stocks through Q1 but are nearly even on a YTD basis through May 5th. Small Cap stocks have been particularly weak, declining -8.9% in Q1. Small Cap stocks have also rebounded since April 8th but remain down -11.4% YTD and -4.1% for 12 months through the review date.

2025 Q1 Returns				
EQUITY	Q1 2024	YTD 3.31.25	1 Year 3.31.25	3 Years Annualized
S&P 500	-4.27	-4.27	8.25	9.06
S&P 500 Value	0.28	0.28	4.21	9.32
S&P 500 Growth	-8.47	-8.47	10.46	7.74
Dow Jones Ind Avg	-0.87	-0.87	7.40	8.75
NASDAQ Composite	-10.26	-10.26	6.37	7.60
S&P Mid Cap 400	-6.10	-6.10	-2.71	4.42
S&P Small Cap 600	-8.93	-8.93	-3.38	0.71
MSCI EAFE	6.86	6.86	5.00	6.05
MSCI Emerging Mkts	2.93	2.93	8.39	1.44

Source: FactSet

Developed international stocks have long lagged their domestic counterparts but finally proved their worth in diversified portfolios during the domestic downturn. The MSCI EAFE index was up 6.86% in Q1 and is up 14.1% YTD and 9.3% for 12 months through the review period. Developed international stocks have benefited from lower relative valuations, less reduction in EPS growth estimates and fiscal stimulus in a number of countries.

The S&P 500 currently trades at over 20x the next 12 months' earnings estimate. The PE multiple is near the 5-year average but remains well above the 10-year average of 18.6x.



Source: FactSet

Higher than average PE multiples have been supported by strong sales growth, margin improvement, impressive earnings growth and the expectation for lower interest rates. It may be difficult to maintain the premium multiple as sales, margins, and earning will all be under pressure from the uncertainty caused by the tariffs and slower economic growth. There may be some support from lower short-term rates, reduced regulation and lower energy costs in the second half. Greater productivity and efficiencies may improve over the longer-term, which could also support valuations.

The consensus earnings growth estimate for 2025 has declined from a peak of 15.4% to 9.7% currently and is likely to be adjusted down further as we progress through the year.

Forecasts for the S&P 500 have been adjusted down markedly over the past few months. Forecasts for year-end range from 4,900 to 6,000. It is very difficult to make a forecast with any level of confidence in the current environment, but a range of 5600 – 5800 seems plausable. Goldman Sachs forecasts 5700, Raymond James forecast 5800 and Yardeni Research forecasts 6000. Additional upside from the current level likely hinges on trade deals being done with at least some of our major trading partners and a lower Fed Funds rate.

Sector returns year-to-date have primarily been lead by more defensive sectors. Consumer Staples, Utilities, Real Estate, and Financials have been the best performers. Conversely, the worst performers have been Consumer Discretionary and Information Technology.

Fixed Income Markets

Taxable fixed Income has played the traditional role of acting as an offset to a downward move in U.S. equity in Q1. During periods when stocks continue to move higher, many question the need for fixed income in their portfolios. Having an allocation to fixed income not only helps to provide income but also helps to manage downside risk in a balanced portfolio.

The Bloomberg US Aggregate Bond Index was up 2.78% in Q1 and was up 4.88% for one year through

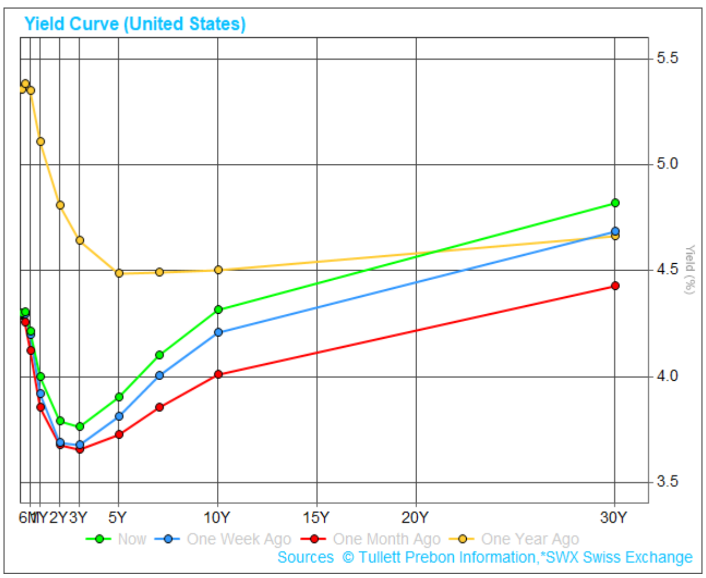
2025 Q1 Returns				
FIXED INCOME	Q1 2024	YTD 3.31.25	1 Year 3.31.25	3 Years Annualized
Bloomberg US Agg Bond	2.78	2.78	4.88	0.52
ICE AMT-Free Nat'l Muni	-0.51	-0.51	1.16	1.44
Markit iBoxx USD Liquid High Yield Index	1.15	1.15	7.97	4.79

Source: FactSet

March 31. Interest rates have moved slightly higher since the end of the quarter causing the index to move back down to 2.22% YTD. The index has returned 5.55% over the past year through May 5th.

Returns for municipal bonds have surprisingly been negative in Q1 and YTD. Paul Malloy, head of U.S. municipals at Vanguard gave three reasons for the slow start to the year including: 1) high relative valuations at the beginning of the year, 2) increased supply as issuers tried to get ahead of uncertainty related to economic policy, and 3) volatility across the fixed-income market, prompting outflows from municipal bond funds. There has been some concern that municipal bonds may lose their tax-exempt status in an effort to raise revenue. However, Malloy sees it as "a very low probability, given how critical a total municipal market is for every state (regardless of political affiliation) and the role it plays in infrastructure."

The U.S. Treasury Yield Curve has steepened over the past month in response to the potential for



higher inflation and fewer rate cuts. The Fed continues to project two 25 basis point rate cuts by the end of the year. The Fed has indicated that they are on hold and in no hurry to cut rates while they consider inflation and employment data. The first rate cut will likely be in July or September.

Credit spreads have widened for both investment-grade and high yield bonds recently as the economy has slowed. Yields remain well above the 10-year median for most fixed income sectors.

Money market fund assets remain at record levels as rates remain relatively attractive and due to the spike in volatility in the equity markets. As the Fed continues to reduce the fed funds target rate, investors may look for better opportunities which would add support to other asset classes.

Real Assets

The Dow Jones Real Estate Index was up 3.34% YTD and 9.63% for one year through March 31st. U.S. real estate securities rose in the quarter amid falling interest rates and generally healthy real estate

2025 Q1 Returns				
REAL ASSETS	Q1 2024	YTD 3.31.25	1 Year 3.31.25	3 Years Annualized
Dow Jones U.S. R/E	3.34	3.34	9.63	-0.89
S&P GSCI	4.89	4.89	3.83	1.25

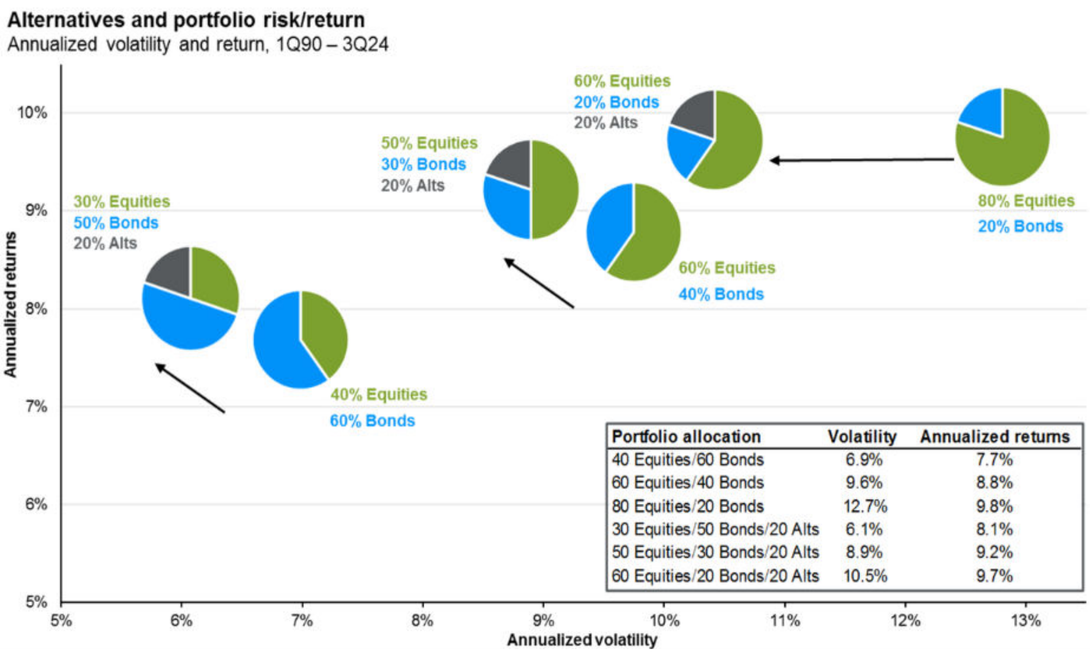
Source: FactSet

fundamentals. The index has given up about 1% of the YTD return through May 5th; however, one-year returns are now in excess of 15%. REIT managers are generally cautious about more economically sensitive sectors but believe that real estate stocks are less likely to feet the brunt of negative tariff impacts.

The GSCI commodities benchmark was up 4.89% YTD and 3.83% for one year through March 31st. However, energy has dropped significantly since that time pushing the index to -4.58% YTD and -4.23% for one year through May 5th. Energy accounts for about 60% of the S&P GSCI commodities index. Crude Oil WTI has declined from $73/bbl. at the beginning of the year to under $59/bbl. currently. Precious metals remain elevated due to market uncertainty and geopolitical concerns. Gold is at all-time highs at $3,438/oz. and is up over 30% YTD.

Asset Allocation

We have been conditioned to be buy-the-dip equity investors and over the long term it has proven to be a valuable strategy. However, caution is advised due to ongoing premium valuations for U.S. large cap equities. Don't overlook more attractive valuations in Developed International equities, less volatile fixed income, and alternative options. The inclusion of alternative assets to a balanced portfolio has shown to improve returns for a given level of risk over time.



Source: JPMorgan Asset Management

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