CAPITAL MARKET SUMMARY

Domestic Equity Markets

- The S&P 500 fell modestly during the first quarter of 2025 with the majority of the decline occurring in March. This ended a relatively long streak of positive quarterly returns.
- Small caps continued to underperform large cap equities.
- Sector dispersion has been more than 20% between the top and bottom sectors for the second quarter in a row. Perhaps a sign that active management will begin to reassert itself.
- Opposite of 2024, value-styled sectors have mostly led markets in 2025.

The S&P 500 Index® ended its streak of 5 positive quarters in a row as it fell by 4.27% during the first quarter of 2025. Growth and value styles have now been trading leadership for the most recent three quarters, as over the past three months the Russell 1000 Growth Index® fell 9.97% while the Russell 1000 Value Index® rose 2.14%. Growth is now outperforming value by less than 1% on a trailing 1-year basis. Mid and Small caps, represented by the S&P 400 and 600 Indices®, lagged large caps throughout the quarter. Mid cap stocks dropped 6.10% while small cap companies were lower by 8.93%. During the first quarter, sector returns continued to demonstrate significant dispersion. The weakest sectors were ones that had outperformed in recent years, Consumer Discretionary, Technology, and Communication Services which fell 13.80%, 12.65%, and 6.21%, respectively. The cyclical, but economically sensitive sectors, Industrials, Materials, Financials, and Real Estate delivered returns ranging from -0.19% to +3.58%. Defensive sectors were among the top performers as Utilities gained 4.94%, Consumer Staples rose 5.23%, and Healthcare popped by 6.54%. Somewhat unexpectedly, the Energy sector led the market with a return of 10.21% despite oil prices marginally declining at the same time. So far, the shifting momentum throughout the second half of 2024 continued into this year and we will be monitoring its progress or the lack thereof as the value style starts 2025 in the leadership position.

Fixed Income Markets

- Falling rates led to bond prices rising across the investment grade landscape.
- Longer duration and less credit-sensitive strategies outperformed.
- Most nontraditional asset classes provided positive returns, but failed to keep up with investment grade fixed income.

After yields rose sharply in the wake of the November presidential election, interest rates reversed lower throughout the first quarter of 2025, resulting in most asset classes of fixed income rising. This led to the benchmark Bloomberg U.S. Aggregate Bond Index® rising 2.78% during the first quarter. At the same time, credit spreads rose moderately which resulted in less interest rate sensitive areas of the bond

STRATEGIC ALLOCATION POSITIONING

Asset Class	Underweight			Neutral	Overweight		
	Max	Mod.	Slight		Slight	Mod.	Max
Cash					●		
Total Fixed Income				●			
Duration						●	
Credit		●					
Total Equity			●				
Domestic					●		
International			●				
Domestic Equity							
Large Cap		●					
Mid Cap				●			
Small Cap						●	
Growth			●				
Value					●		
International Equity							
Developed Markets					●		
Emerging Markets			●				

All data sourced from Morningstar.com

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market underperforming. Avoiding the rise in credit spreads, treasury bonds outperformed the aggregate index and finished the quarter up 3.19%. Despite rates falling, inflation expectations rose. This caused the Treasury Inflation Protected Securities (TIPS) Index to outperform treasuries and gain 4.17% over the prior 3 months. Municipal bonds declined 0.22% as they experienced widening spreads, and their lower starting yield limited their ability to profit from falling interest rates. Outside of the United States, yields fell to a smaller extent than domestically. This caused the Bloomberg Global Aggregate Bond Index to underperform US bonds despite still rising 2.64%. Finally, short-term T-Bills delivered 1.02% for the quarter due to their near-total resistance to interest rate changes. With interest rates heading lower, we continue to expect the future returns of T-Bills to become ever more muted. Lower duration (interest rate sensitivity) non-traditional fixed income asset classes lagged traditional bonds. Emerging market debt, buoyed by a falling US dollar, rose 2.93% during the quarter. Corporate high yield had another positive quarter, though with a muted return of just 1.00%. At the same time, high yield municipals gained 0.81%. Floating rate bank loans, unable to take advantage of falling rates and hampered by widening credit spreads, only gained 0.46% through March. The preferred stock asset class, which normally does well as interest rates decline, was eschewed by market participants, leading to a drop of 1.51% during the most recent quarter. Finally, the weakest nontraditional asset class for the quarter was convertible bonds (-1.76%), which were hindered by their sensitivity to equity market movements.

Foreign Equity and Commodity Markets

- A weakening U.S. dollar resulted in significant outperformance for foreign equity markets.
- Emerging markets lagged developed markets but delivered positive returns contrary to U.S. equities.
- Commodities were very mixed, but higher as a group for the quarter.
- Precious metals continued to be the strongest commodity asset class.

An unwind of the US dollar rally that took place in the fourth quarter of last year led international equity to outperformance in the first quarter of 2025. For the quarter, developed international equity, represented by the MSCI EAFE Index®, rose 6.86%. The MSCI EM Index®, corresponding to emerging market equity, was left behind but still produced a gain of 2.93%. Still, over the past 5 years, emerging markets returned just 7.94% annually, approximately one third less than developed international equity's 11.77% annualized gain and less than half of the S&P 500's nearly 20% annual performance.

The S&P GSCI Commodity Index® gained 3.35% during the first quarter of 2025. Energy commodities were mixed as oil shed 0.33% while natural gas rose by 13.38%. Despite commodity prices being very volatile, it is interesting that over the past 15 years oil has been lower by 1.05% annually while natural gas is up by 0.42% per year. The Agriculture and Livestock Sub-Index was up 3.89% during the quarter, though many of its subcomponents were volatile as coffee prices rose 21.61% while cocoa dropped by 23.19%. Much of what drove the broader index higher for the quarter were components from both industrial and precious metals. Very economically sensitivity copper rose 11.05% during the quarter. And finally, precious metals continued to shine as gold and silver gained 19.28% and 17.33% respectively during the first three months of 2025. With these returns YTD, "boring" gold has now outperformed the S&P 500 Index by 8% annually over the past three years.

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Capital Market Outlook

The first quarter of 2025 started on a positive note with the S&P 500 Index® rising over 2.5% in January, reversing December's decline. However, in February the market slipped lower before dropping by 5.63% in March on economic concerns including the forthcoming tariff announcements. This caused the S&P 500 Index to fall 4.27% for the entirety of the quarter[1]. The small cap S&P 600 Index® trailed the large cap index as it fell by 8.93% over the same time period[1]. The MSCI ACWI ex USA Index® representing foreign stocks struggled in recent years relative to U.S. equities. In a reversal of poor prior performance, this index gained 5.23% over the past three months, as the US dollar declined by just shy of 4%[1]. Absent the fall in the dollar, foreign stocks would be closer to flat for the quarter. Lastly, the Bloomberg US Aggregate Bond Index® rose 2.78% over the quarter, which returned its three-year annualized performance to positive territory[1]. As we move further into the year, we will focus our attention on the Federal Reserve and interest rates, trade policy and tariffs, and global markets.

The Federal Reserve & Interest Rates

- Falling inflation has cleared the way for the Federal Reserve to lower interest rates.
- The Federal Reserve will need to balance economic growth, inflation, and the effects of domestic policy on foreign economies.
- The current administration seeks to increase exports, leading to our view of lower interest rates and a falling US dollar.
- Most categories of inflation are declining and may give the Fed more room to cut than the market currently believes.

After rising in early January, the 10-year U.S. treasury bond's yield has fallen steadily throughout the remainder of the quarter. This is despite the Federal Reserve's Open Market Committee (FOMC) choosing to only adjust the federal funds rate lower a single time in January[2]. Since then, the FOMC has kept short-term rates in a range of between 4.25% and 4.50%, and the 10-year bond yield declined from 4.57% at the start of the year to 4.25% at the end of the quarter[3]. The market is currently pricing in a series of interest rate cuts by the FOMC over the course of the remainder of the year. Now, the market is expecting a cut in June (with around a 40% chance that it happens in May) and 4 cuts by the conclusion of the Fed's December meeting[4].

We believe that there are many reasons why the market's view is likely to be correct. While there are numerous factors that affect interest rates, the two most prescient are policy preference and inflation. The US has historically had a policy preference for a stable dollar. Today, the current administration is explicitly seeking to increase domestic manufacturing, and thus exports. One of the easiest paths to this would be a weaker dollar. In recent years, the dollar has rallied as higher interest rates have made it more attractive compared to other developed market currencies, such as the euro or the Japanese yen. Therefore, it would seem logical that lower interest rates would be one path to weakening the dollar. Declining inflation is the second path. As inflation falls, the demand that investors place upon markets for the level of yield they require to invest in fixed income assets falls, as well. While we believe that the majority of the inflation decline has already occurred, over half of what is contributing to the current inflation readings comes from the shelter category. This category lags actual home prices, and therefore, is likely

[1] *Morningstar.com (March 31, 2025)*

[2] *Federalreserve.gov Federal Reserve Press Release (March 19, 2025)*

[3] *CNBC.com U.S. 10 Year Treasury. (April 8, 2025)*

[4] *CME Group. FedWatch Tool. (April 8, 2025)*

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to continue to head lower. Our evidence is in the monthly government Consumer Price Index (CPI) report which shows year over year inflation for shelter at 4.2%, yet over the last six months, the S&P CoreLogic Case-Shiller U.S. National Home Price Index declined slightly[5,6]. This implies that shelter inflation should follow in the coming months.

Summing it up, with our views of declining inflation, coupled with the administration's policy goals of lower interest rates and a less import-focused economy, we believe that it is highly likely that the Fed will continue their steady path of rate cuts as the year continues.

Trade Policy and Tariffs

- U.S. tariff policy initiated a correction in global markets.
- The U.S. administration is utilizing tariffs in multiple different ways.
- The tariff policy has been rolled out unevenly and with significant backtracking. This has led to difficulties in discerning exactly what the policy will be moving forward.

The primary impetus for the current decline in markets is uncertainty regarding trade policy. Tariffs, in some variety, are clearly en route, however, what their effect will be is being debated heavily by financial markets. The proof of this is visible in the decline in equity price multiples and wild gyrations within fixed income markets. The US administration initially decided to apply tariffs to countries with a minimum rate of 10% and higher rates depending on that nation's trade surplus with the United States. However, in the following days, much of this tariff increase was paused for 90 days to allow time for negotiation.

The US is wielding tariffs as a trade weapon in multiple different ways which we will bucket into two categories. First, we have coercive tariffs. These are geopolitical acts where the US is seeking to influence the policy of a foreign government. The clearest example of this type of tariff would be the fentanyl/border policy tariffs previously applied to Mexico and Canada[7]. This was a clear case of the US attempting to influence those nations to change their border policy with the promise that the tariff would be lifted if the policy changed. The second type is reciprocal. These are, theoretically, attempts at realigning trade relationships. The assumed long-term goal of this would be to reduce trade barriers between nations, but the US administration has not been clear on this. They have articulated expectations that this new tariff policy will both raise revenue for the government and increase GDP[8]. This claim has been met with significant skepticism[9]. We believe that the economic results are likely to be mixed. Could reciprocal tariffs result in lower trade barriers for all countries? Absolutely, but it is not a certainty. Will they truly be "reciprocal"? This remains to be seen. Will tariffs raise revenue? Undoubtably. But will that result in an increase in GDP? We are unconvinced because we remain skeptical that the most efficient use of resources is to move a significant portion of manufacturing to the U.S.

Current trade and tariff policies in the United States are rapidly moving targets. Nearly every day over the past couple of weeks, the news on this subject has shifted. Because of that, we will remain committed to monitoring these changes and, if warranted, acting on them by making shifts to portfolio allocations. For the most part, the tariff policy has not altered our portfolio construction views but served to validate the cautious stance that we have taken. As winners and losers become clearer in the months ahead, this may change.

[5] *Bureau of Labor Statistics. Consumer Price Index - February 2025. (March 25, 2025)*
[6] *St Louis Federal Reserve. S&P CoreLogic Case-Shiller U.S. National Home Price Index. (March 25, 2025)*
[7] *Reuters. Emily Green and David Ljunggren. Canada, Mexico not subject to new global rates as fentanyl tariff still in place. (April 2, 2025)*
[8] *Whitehouse.gov. Fact Sheet: President Donald J. Trump Declares National Emergency... Security. (April 2, 2025)*
[9] *Taxfoundation.org. Erica York and Alex Durante. Trump Tariffs: The Economic Impact of the Trump Trade War (April 4, 2025)*

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Global Markets

- U.S. valuations remain elevated, despite having fallen from recent highs.
- Earnings growth is expected to be relatively robust.
- Domestic stocks have grown from 30% to 65% of global equity since 1987.
- Fixed income returns continue to look far more attractive on a forward-looking basis than in recent years.

With trade-related news dominating headlines, it remains important to gauge financial conditions, market valuations, and economic growth as we allocate portfolios across global markets.

At the end of March, the S&P 500 traded at a forward price to earnings (P/E) ratio of 20.2x[10]. While below the highs that it made in recent years, it remains a full standard deviation above its 30-year average of 16.9x[10]. Margins are also at elevated levels compared to prior decades[10]. Given the current slowdown in growth and weakening of sentiment, we believe that it is more likely that valuations and margins will revert toward their historical averages as opposed to elevating to new highs.

Looking to earnings growth, FactSet is currently estimating S&P 500 earnings to grow at a rate of 10.6% for 2025 on revenue growth of 5.3%[11]. These would be strong performance, if attained. However, we do find the high percentage of companies issuing negative guidance, as well as the low percentage of companies beating current earnings estimates to be somewhat concerning. Revisions to these estimates will be highly important to market pricing throughout 2025.

After the S&P 500 returned 13.2% annually for the last 15 years versus just 5.4% for stocks in other jurisdictions, U.S. stocks now account 65% of global equity (an all-time high) versus just over 30% in 1987 and 40% in 2008[10]. In recent years, a portion of U.S. outperformance was a result of a rising U.S. dollar. With the dollar moving in reverse in 2025, we will consider changes to our international allocations if we believe that they can take advantage of this movement. International stocks continue to trade at a very large discount to domestic equities[10]. While this can persist for a length of time, it is possible that the change in direction of the dollar will be the catalyst needed to see foreign stocks finally generate durable outperformance.

Finally, we examine the fixed income universe. The Bloomberg U.S. Aggregate Bond Index rose 2.78% to start 2025. This drove the yield of investment grade bonds from 4.91% at the start of the year to 4.60%. Further, we continue to expect fixed income assets to provide better ballast to equity portfolios than they have in years past. Though we find fixed income attractive, low credit spreads in most of the "plus sectors" such as high yield, bank loans, and convertible bonds continue to instruct us to shy away from excess risk[10]. Lastly, we will note that with a 4.60% current yield on the benchmark index, we would estimate an annualized return of approximately 4.7% over the coming 5-year period. This is a far superior starting point relative to the index yield of 1.60% as we entered 2022.

Conclusion

Last quarter we noted that, "Since 1950, there have been only 8 times when the market returned more than 20% in 2 consecutive years[12]. The recent returns of this manner, coupled with elevated market valuations and elevated growth expectations, are all reasons for taking a conservative stance within portfolio allocations." We said this with only limited foreknowledge of the current trade and tariff policy as the metrics for economic growth, corporate profits, and inflation have indicated a potential slowing of the broader economy for some time. Therefore, we believe that our current positioning has been and will continue to be appropriate for the market environment.

[10] *JPMorgan. Guide to the Markets. (March 31, 2025)*
[11] *FactSet. Earnings Insight. (April 11, 2025)*
[12] *Yahoo Finance. Matthew Fox. The stock market's back-to-back gain of more than 20% may be setting the stage for another rally in 2025. (November 25, 2024)*

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As we conclude the first half of 2025, we will be keeping a close eye on equity and fixed income markets, global growth, and obviously, trade policy. Though recent years have implied otherwise, market volatility often takes a while to work through, and we look forward to cautiously navigating the waters of global markets with you throughout the remainder of 2025.

Economic Perspectives

Economic Growth & Profits

- Real gross domestic product (GDP) for the fourth quarter of 2024 according to the Bureau of Economic Analysis (BEA), climbed at a rate of 2.4%, 0.1% above the initial estimate. This represents a decline from the 3.1% growth experienced during the third quarter.[1]
- The increase in real GDP resulted from increases in consumer and government spending. This was partially offset by a decrease in private investment. A decrease in imports also slightly nudged the figure higher.[1]
- Nominal GDP (not inclusive of inflation) rose 4.8% on an annualized basis to $29.72 trillion.[1]
- Corporate profits from current production rose $204.7 billion during the fourth quarter of 2024 after falling by $15.0 billion during the preceding quarter.[1]

Interest Rate Policy

- The Federal Reserve maintained their interest rate policy by keeping the Federal Funds Rate in a range of 4.25% to 4.50%. The Committee believes that "Recent indicators suggest that economic activity has continued to expand at a solid pace. The unemployment rate has stabilized at a low level in recent months, and labor market conditions remain solid. Inflation remains somewhat elevated.[2]"
- Regarding the Committee's policy of reducing holdings of government, agency, and mortgage bonds on the Federal Reserve's balance sheet, they expect to slow the rate of reduction with regard to government treasury bonds only[2].
- In determining the appropriate monetary policy, the Committee will consider, "a wide range of information, including readings on labor market conditions, inflation pressures and inflation expectations, and financial and international developments" [2].

Employment

- Total nonfarm payroll employment rose by 151,000 in February. This resulted in a slight rise in the official unemployment rate from 4.0% to 4.1%. It remains 0.1% lower than at the end of November. The labor force participation rate fell slightly from one quarter ago to 62.4%. This is 0.2% below levels seen one year prior as well as being 0.9% beneath its pre-pandemic level.[3]
- In February, job gains were led by healthcare, financial activities, transportation/warehousing, and social assistance which gained 52,000, 21,000, 18,000, and 11,000

[1] U.S. Department of Commerce: Bureau of Economic Analysis - Gross Domestic Product 4th Quarter 2024 (March 27, 2025)

[2] U.S. Federal Reserve - Federal Reserve Issues FOMC Statement (March 19, 2025)

[3] U.S. Department of Labor: Bureau of Labor Statistics - The Employment Situation – February 2025 (March 7, 2025)

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jobs, respectively. Federal government and retail employment experienced declines of 10,000 and 6,000 jobs.[3]

- The average workweek for all employees on private nonfarm payrolls during February was unchanged since January at 34.1 hours. At the same time, average hourly earnings continue to rise, growing 10 cents during the month to $35.93, a level 4.0% higher than one year ago.[3]
- On a seasonally adjusted basis, the broader U-6 measurement of unemployment rose 0.5% since January to 8.0%, which is an increase of 0.7% over the past twelve months[3].

Inflation

- According to the Bureau of Labor Statistics, the Consumer Price Index for All Urban Consumers (CPI-U) rose 0.2% in February on a seasonally adjusted basis after rising by between 0.3% and 0.5% for each of the prior three months. This resulted in a total 12-month increase of 2.8%. The largest contributors on a year-over-year basis were transportation services (+6.0%) and shelter (+4.2%). Offsetting these were energy (-0.2%) and food (+2.6%). Food would come in even lower if not for the rise in egg prices which has since abated in March[4].
- The annual change in Core-CPI, a popular indicator that looks at all items except food and energy, remained elevated at 3.1% on an unadjusted basis. This category was pushed higher by services including shelter and transportation, while commodities, new vehicles, and airline fares pressured the index to the downside[4].

[3] *U.S. Department of Labor: Bureau of Labor Statistics - The Employment Situation – February 2025 (March 7, 2025)*
[4] *U.S. Department of Labor: Bureau of Labor Statistics - Consumer Price Index, February 2025 (March 12, 2024)*

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Disclosure

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Index Returns Table

Index	Total Return (%) 3 Mo (Mo-End) USD	Total Return (%) 1 Yr (Mo-End) USD	Total Return (%) Annualized 3 Yr (Mo-End) USD	Total Return (%) Annualized 5 Yr (Mo-End) USD	Total Return (%) Annualized 10 Yr (Mo-End) USD
DJ Industrial Average TR USD	-0.87	7.40	8.75	16.20	11.43
S&P 500 TR USD	-4.27	8.25	9.06	18.59	12.50
S&P 400 Mid Cap TR USD	-6.10	-2.71	4.42	16.91	8.43
S&P 600 Small Cap TR USD	-8.93	-3.38	0.71	15.09	7.52
MSCI KLD 400 Social GR USD	-6.90	2.78	7.30	17.66	12.12
MSCI EAFE NR USD	6.86	4.88	6.05	11.77	5.40
MSCI EM NR USD	2.93	8.09	1.44	7.94	3.71
Bloomberg U.S. Agg Bond TR USD	2.78	4.88	0.52	-0.40	1.46
Bloomberg Global Agg Bond TR USD	2.64	3.05	-1.63	-1.38	0.61
S&P GSCI Spot	3.35	-2.47	-7.77	17.32	3.66
S&P Target Risk Cons. TR USD	1.38	5.70	2.98	4.83	4.02
S&P Target Risk Mod. TR USD	1.09	5.89	3.59	6.33	4.77
S&P Target Risk Aggr. TR USD	-0.08	6.65	5.96	12.38	7.63
Source: Morningstar® as of March 31, 2025					

The Dow Jones Industrial Average is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange (NYSE) and the NASDAQ. The MSCI U.S. Broad Market Index is comprised of nearly 100% of the total market capitalization of U.S. stocks traded on the NYSE and the NASDAQ. The S&P 500 Index is a market capitalization free-float adjusted index of the prices of 500 large capitalization common stocks traded in the United States. The S&P 400 Mid Cap Index serves as a barometer for the U.S. mid-cap equities sector and includes stocks with total market capitalization that ranges from roughly $750 million to $3 billion. The S&P 600 Small Cap Index covers a broad range of U.S. small cap stocks and is weighted according to market capitalization covering about 3-4% of the total market for U.S. equities. The MSCI KLD 400 Social Index is a free float-adjusted market capitalization index designed to target U.S. companies that have positive environmental, social, and governance (ESG) characteristics. The MSCI EAFE Index is a market capitalization weighted index and is designed to measure the equity market performance of developed markets (Europe, Australasia, and Far East) excluding the U.S. and Canada. The MSCI EM NR USD Index is a free-float adjusted market capitalization index that is designed to measure the equity market performance in the global emerging markets. The Bloomberg Aggregate Bond Index is a market-capitalization weighted index that is considered to be representative of U.S. traded investment grade bonds. The Bloomberg Global Aggregate Bond Index includes government securities, mortgage-backed securities, asset-based securities and corporate securities to simulate the universe of bonds in the market. The S&P GSCI Spot is a composite index of commodity sector returns which represents a broadly diversified, unleveraged, long-only position in commodity futures. The S&P Target Risk series of indices comprise multi asset class indices that correspond to a particular risk tolerance with varying levels of exposure to equities and fixed income intended to represent stock and bond allocations across a risk spectrum. The market indices referenced are unmanaged. You cannot invest directly in an index.

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