QUARTERLY NEWSLETTER 2025.Q2

July 8, 2025

In our prior newsletter, we mentioned a long list of investor concerns that likely contributed to weaker market performance. These concerns included policy uncertainty, tariffs, stubborn inflation, signs of a softening job market, souring consumer sentiment, and recession fears. In our view, these are all still pertinent issues for investors. Add to these fears the continuing quagmire in Ukraine, a new conflict between Iran and Israel, and extreme political and social dysfunction domestically, it would seem investors had no shortage of reasons to sell during the last quarter. If only it were that simple.

From its low in April, the S&P 500 Total Return index surged nearly 25% before quarter-end[1]. The index has now risen 6.20% for the year. Not to be outdone, international markets continued their strong run, with the MSCI ACWI Ex-US index returning 12.03% for the quarter, bringing its yearly return to 17.90%. So much for bad news.

Solid returns were not unique to stocks, either. The Bloomberg US Aggregate Bond index increased 1.21% for the quarter to bring its year-to-date total to 4.02%. Boring, sure, but bonds have done a great job this year diversifying equity market volatility while still providing a reasonable return. In the not too distant past, interest rates were hovering near zero and fixed-income investors were left scratching their heads to find a reasonable source of return without undue risk. Even with the Federal Reserve telegraphing rate cuts before year-end, we think interest rates are high enough to justify meaningful allocations to fixed income for some investors.

Signal vs Noise

Determining what causes stock market moves over any time period is not exactly a precise science. Sure, there are daily headlines that play a role, and over longer time periods, there are trends that contribute to the returns of the overall index and its individual constituents, but there is also a lot of noise within the market. Sometimes, the most accurate response to "why was the market up/down today/last week/month/quarter" is "I don't know, and neither does anybody else."

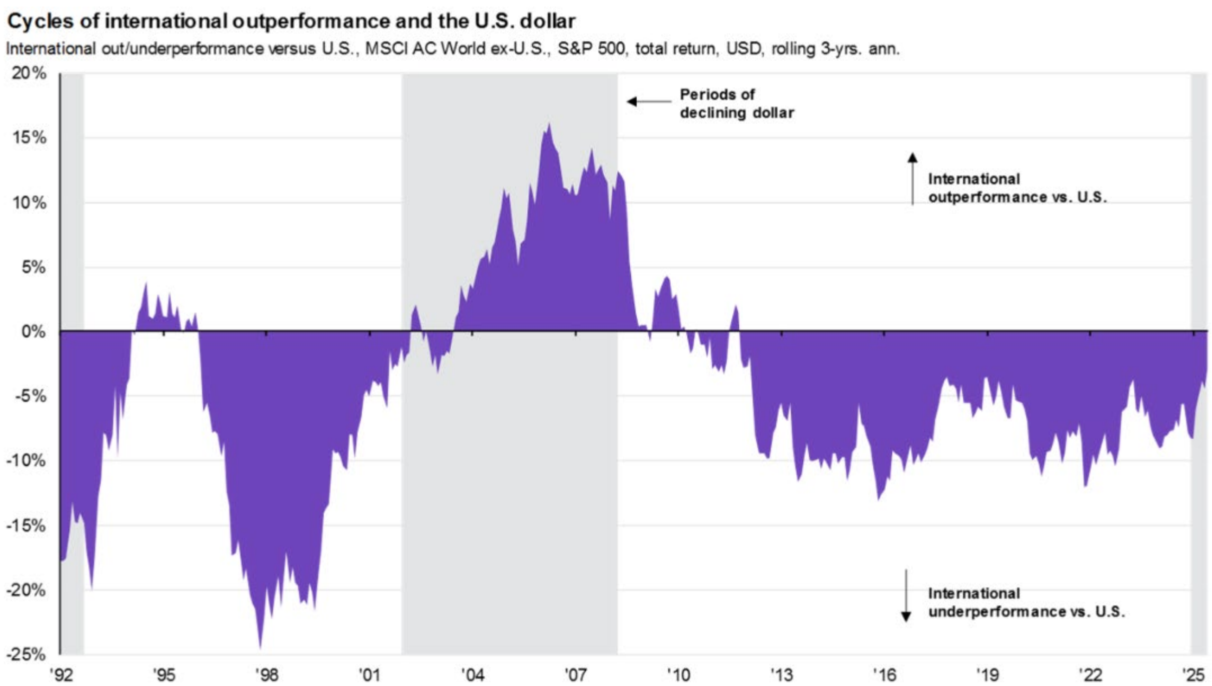
This past quarter is a great illustration. There was some progress made on tariff negotiations and trade agreements, inflation prints were somewhat improved, interest rates dropped slightly, and we are not officially in a recession quite yet, but how can that justify a 25% market surge in such short order? Tariffs are still a problem, inflation is still above target, interest rates are still elevated relative to recent history, and GDP growth was negative in the first quarter of the year. That hardly seems like a backdrop for attractive equity market returns, especially considering the stretched valuations we are currently experiencing.

Domestic vs International

[1] All index return data from YCharts

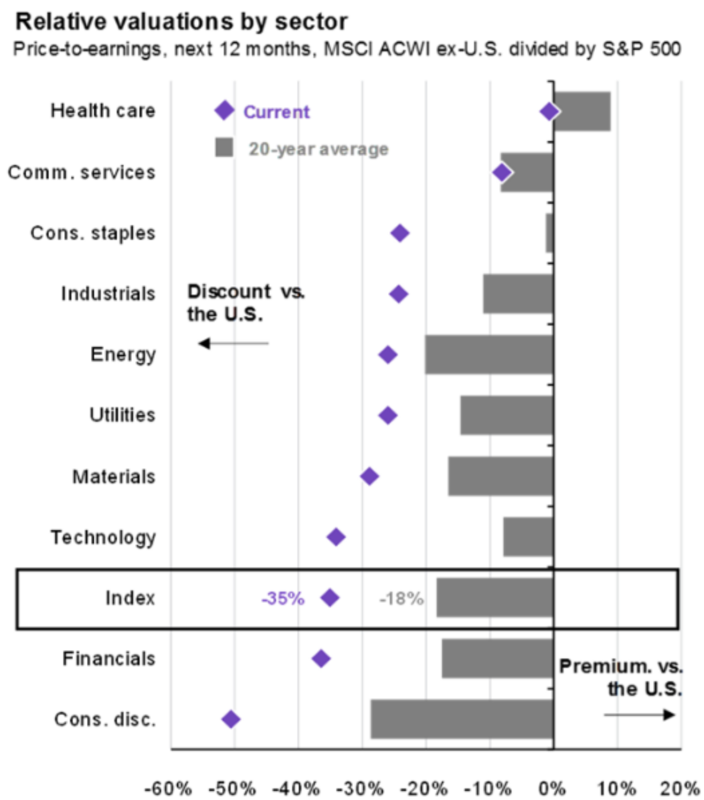
So, what is a diligent investor to do? As we mentioned in our last newsletter, we have allocated assets to areas of the market that still look attractive. In general, we have moved funds away from the domestic stock market and towards international markets, both developed and emerging.

In our view, the US still has, by far, the most innovative, robust, and resilient economy of any country in the world, but the valuation gap between it and the rest of the world has become too large to ignore. After more than a decade of underperformance, international stocks have outperformed the S&P 500 for the year, and we think that trend has more room to run. Historically, periods of relative performance between the US and international equities have lasted multiple years[2]:



And though we've shared similar charts in the past, it's worth mentioning, international markets are historically cheap relative to the US[3]:

[2] JP Morgan Chase "Guide to the Markets" as of June 30, 2025
[3] JP Morgan Chase "Guide to the Markets" as of June 30, 2025



This is not to say we have given up on US stocks. In fact, we still own more US stocks than international stocks, but that gap has tightened significantly over the course of this year.

Pessimists vs Optimists

We hope we aren't telling the reader anything groundbreaking here, but there will *always* be bad news. It's human nature to focus on everything wrong in the world, but our overarching belief is that the world will continue to improve. Call us naïve, but the ability for humans to innovate and make incremental improvements to their lives and those around them is astonishing. We don't think that ingenuity is going anywhere anytime soon, and it's the central reason we think owning stocks is a good idea – it's a bet on a growing and more prosperous worldwide economy.

Over the course of our careers, we have heard from clients and prospects many times something to the effect of: "I'll start investing when things calm down." We grant there are times when news flow is higher than normal and volatility in the market can be elevated, but there will always be *something* going on to give investors pause. We'll repeat it: there will *always* be bad news. You can't time it, and you're better off jumping in than waiting for the perfect moment that may never come.

One of our favorite quotes is from investor Nat Friedman in May 2020, during the height of the COVID crisis: "Pessimists sound smart. Optimists make money." As much as we would love to sound smart, we think our clients would appreciate the latter of those options.

Please contact us if you have any questions, we are honored to manage your accounts.

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