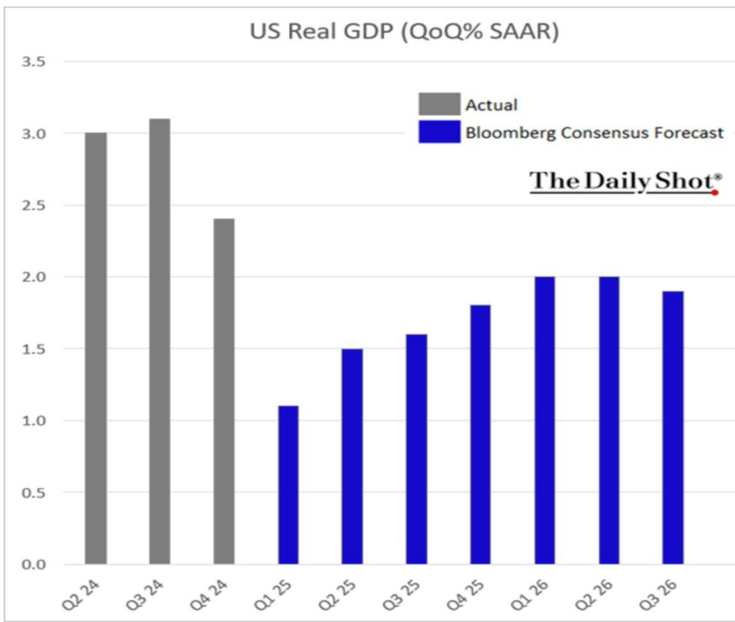
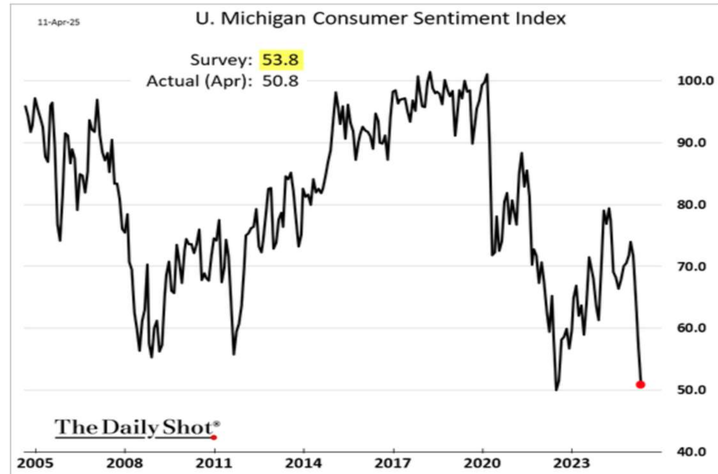
Q1 2025 Investment Update

Current Observations

The **ECONOMY** has begun to weaken as businesses and consumers are "***tariffied***" about the negative impacts from the Trump Tariffs. Announced only on April 2nd, the shock of substantial rates applied globally hasn't boosted confidence. Make no mistake. Donald Trump "***owns***" these tariff policies. Confidence is a fragile thing, and ramping up global uncertainty causes consumers and businesses to pull back from spending. The surprising thing so far is that economists are still not predicting a recession, as this chart demonstrates:



We'll see how accurate the Ph.D. economist crowd is when it comes to forecasting the economy. As we preach, it's almost impossible to know the short-term direction of the economy, even as it's much more predictable to discern the longer-term direction of the economy. The charts below tell us a different story that the average consumer is not feeling great about economic conditions right now:



Trump has believed for decades that the global trading system is rigged against the United States. While we do believe that there are trade practices that are discriminatory toward the United States, ***we must be careful that the cure is not worse than the disease.*** Global trade has become so intertwined over decades that trying to rejigger the system by yourself through punitively higher tariff rates is incredibly difficult.

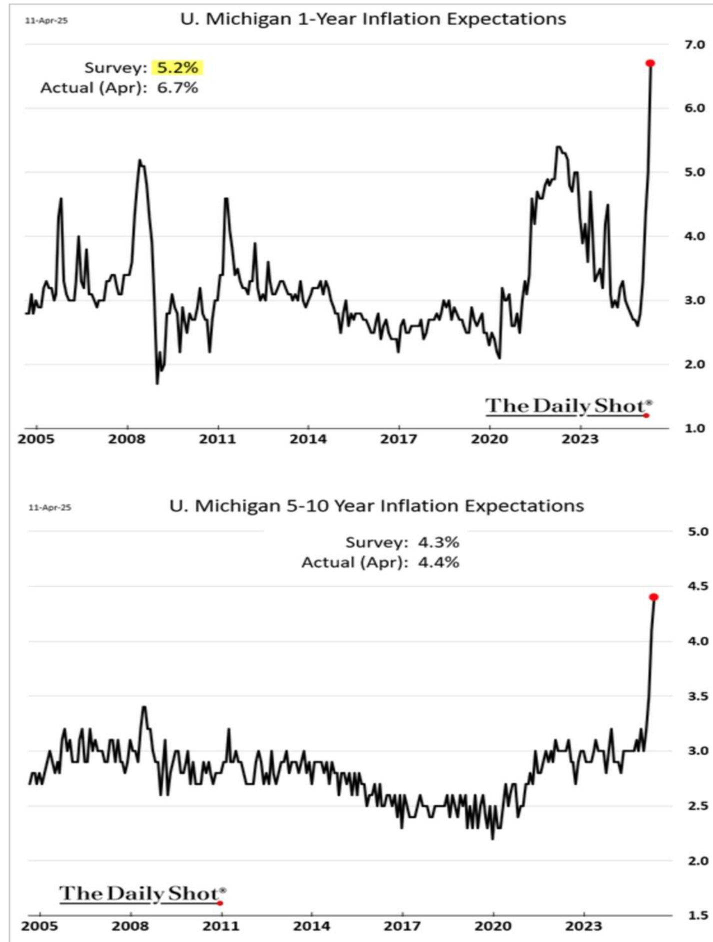
Trump wants a deal and needs a deal. In our opinion, Trump will get agreements in the next few months with most of our major trading partners. Except China. In fact, the Trump administration has told all our allies that it would like to make deals with them and then go to China in a unified front to strike a better deal with China.

China does have an unbalanced economy that is overly reliant on exports and much less on domestic consumption. The simple reason for this is the Chinese dictatorship can do what it wants and what it wants is to sell a lot of goods to the rest of the world—at the expense of its people not consuming the fruits of their own efforts.

The longer this trade friction persists the greater the pressure will be on Trump to cut deals. Trump claims not to be concerned about the stock and bond markets. We don't believe that. Trump watches hours of television daily and sees what's going on in both the stock and bond markets. And the demonstrations happening around the country.

Ultimately, we believe that global trade enhances the wealth of most nations and while the system needs reform, we'd all be worse off in a system where not much global trade happened. The good news is at least some of Trump's advisors understand this and hopefully they are going to win the arguments in the Oval Office.

INFLATION is likely to be higher in a world of much higher tariff rates. Again, Trump's advisors are aware of this. Consumers and businesses now expect to be paying higher prices for many goods. The chart below demonstrates how inflation expectations have recently risen significantly, from 3% over the next year to almost 7%, while five-year+ expectations have risen to 4.5%:



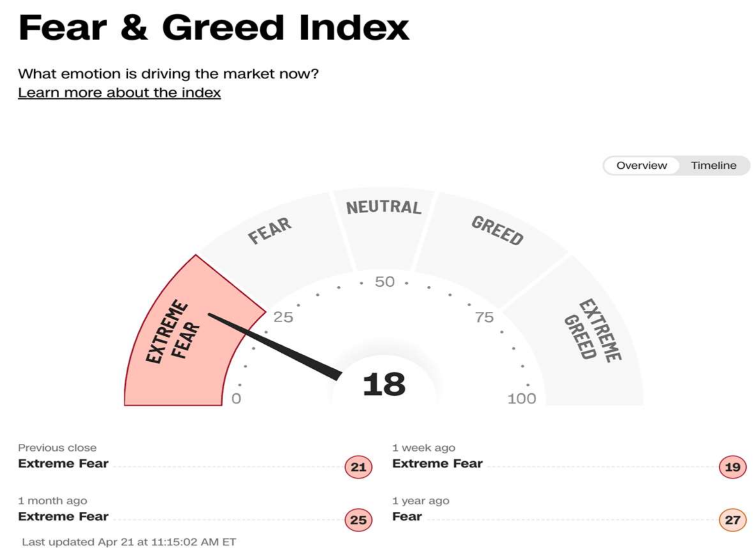
Unfortunately, the Federal Reserve Board feels boxed in as Trump wants interest rates reduced, but the Fed is expecting tariff-induced inflation to make rate cuts next to impossible. In response, Trump is threatening to fire Fed Chair Jerome Powell, which would likely lead to more financial market chaos as investors would rightly assume that a new Fed Chair would be Trump's lap dog. While some folks think that Trump is a brilliant businessman, we're pretty sure that he doesn't know much about monetary policy. Stay in your lane, Donald.

INTEREST RATES have increased since Trump's tariff announcements, as investors rightly conclude that longer-term inflation will go up and they seek higher interest rates to offset higher inflation. Higher interest rates don't help the economy as financed purchases of housing, automobile sales, furniture, business investment on plants, equipment, and other large outlays will likely be lower. Again, in our view, the clock is ticking on The Donald's tariff gambit.

Financial Market Conditions

The **STOCK MARKET** has been pummeled since the April 2nd tariff announcements. The shock of much higher tariffs and the uncertainty of the global tariffs' impact caused investors to dump assets such as stocks and bonds. While there is some short-term comfort in liquidating investments and sitting in cash, we continue to believe that predicting short term movements in Trump's brain, the economy, interest rates, stock markets and bond markets are just guessing games.

While the current economic and market situation may feel like unmitigated turmoil, in our opinion, the tariff situation will be resolved in months, not years. In the meantime, we don't have a lot to offer other than being patient and waiting for an eventual resumption of economic and market progress. Right now, investors are feeling very glum and that's reflected in current stock market declines. This CNN Fear and Greed Index pretty much sums up the prevailing investor mood, as investors vote with their feet and depart the stock market:



Unfortunately, many of the recent stock market departees will find themselves still sitting on the sidelines as the market eventually resumes its upward climb, and they find it difficult to reinvest, expecting another downward move, and a chance to catch the bottom. In our experience, it's unlikely anyone can do that. We believe it's much better to focus on a couple of important long-term financial considerations.

It's such an easy thing to talk about…yet difficult for so many investors to practice. We're talking about a LONG-TERM approach:

- Creating an investment plan based on your personal goals
- Selecting an appropriate asset allocation to meet those goals
- (Most importantly) sticking with the plan through the ups and downs that inevitably—always—occur over many years.

While we believe that market timing doesn't work, we also believe that at times the market can get too pessimistic, and too optimistic. We still believe that certain areas of the stock market continue to trade at what we'd call "**BUBBLE-LIKE**" valuations. We continue to steer clear of these areas and instead stay focused on real businesses, generating real sales, earnings, and significant free cash flow.

FIXED INCOME investments certainly look better now that interest rates are higher than they have been in many years. It's much easier for us to find higher levels of income in relatively attractive fixed income investments. Our focus is shorter-term maturities in case interest rates rise instead of decline. Since fixed income generally fluctuates less than the stock market these holdings can provide a buffer during particularly volatile economic and financial market conditions.

CASH holdings are no longer "trash" since money market yields are around 4% today compared to near 0% just a couple years ago. In this environment we don't mind having a little extra cash on hand as it's generating a decent yield while we wait for attractive investment opportunities.

Other Current Topics

While our investment focus is still in the United States, we also pay attention to international events as the current geopolitical situation is the most difficult and dangerous since perhaps World War II.

The Trump Administration will likely stay focused on a couple of primary themes over the coming months. We've already touched on tariffs, which will be front and center until agreements are made. We believe it's a matter of months for the tariff situation to be resolved.

Immigration is another Trump focus and border crossings at this point have ground to a halt. We'll see what happens in the future, but you gotta admit Trump hit his goal of reducing illegal border crossings significantly. Next up, Trump is hoping to cut taxes and renew his expiring tax bill. Trump is also hoping to reduce spending to offset the tax cuts. We're not sure about the tax bill or ability to reduce spending.

Lest we forget, we still have plenty of global adversaries, including China, Russia, Iran, North Korea, Venezuela. Other trouble spots include the broader Middle East, and of course, the ongoing war in Ukraine. In addition, China is threatening to take over Taiwan by 2027, which could result in a United States response—and a global recession—given the importance of Taiwan to the technology industry.

What actions are we taking in the current environment? First, we don't panic. We certainly continue to monitor your investments to ensure that each company has the wherewithal to make it through the current difficulties and come out the other side in good shape, or in some cases in better shape. Great businesses have a way of taking advantage of difficult conditions to improve their business results. We own many wonderful businesses.

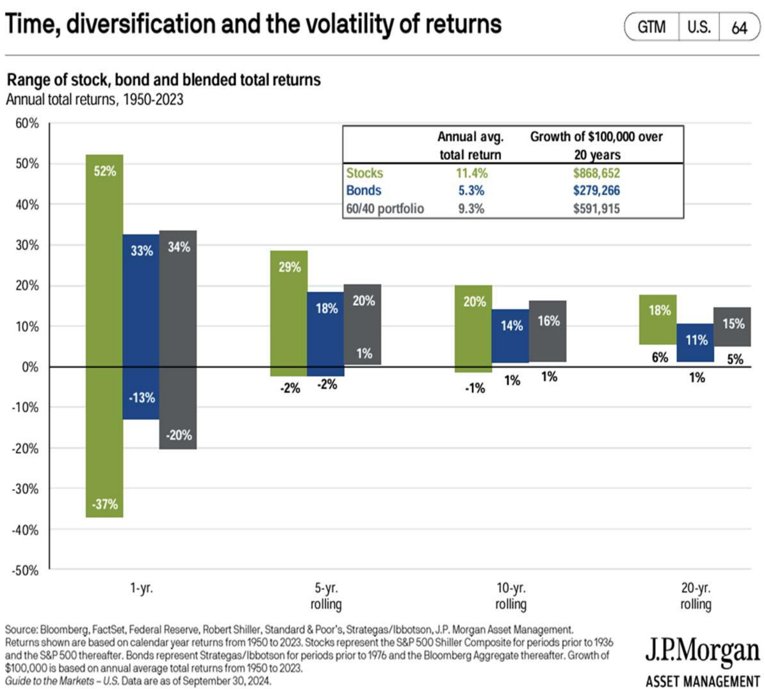
The other thing we're doing is looking for opportunities to invest in great businesses that we've been monitoring for years but haven't purchased because we felt that the asking prices were too high. In declining markets, all investments go down—it's just a question of how much. If we can find a fantastic business, that's now trading at a much more attractive valuation then we won't hesitate to invest. The big idea here is not to sit on your hands unnecessarily but continue to look for smart opportunities. You can be sure that we are doing this now.

Let's conclude with some important long-term investment ideas.

We think it's helpful to periodically remind ourselves that investment progress comes ONLY over long periods, as the short-term fluctuations of the economy and markets tend to be smoothed over time. The chart below demonstrates that ***as you extend your investment time horizon, the probability of earning a positive return increases***.

In simple terms, anything can happen over one year, whether it's big gains or big declines. As you extend out to 5-, 10- and 20-year rolling periods, we've seen positive results in just about every period under consideration since 1950. Something to remind yourself the next time the financial media talking head screams at you to dump your investments. That's a road to financial disaster, in our opinion.

The other important consideration is that a ***sizable portion of your nest egg*** could be inherited by children, grandchildren, relatives or charitable organizations, so ***the lifespan of your funds is very likely measured in years if not decades beyond your own lifetime.***



And finally, this chart reminds us that progress never occurs in a straight upward path. But investors have been rewarded over time despite enduring numerous but inevitably **SHORT-TERM** crises, pandemics, natural disasters, recessions, political upheaval, rising interest rates, hot wars, tariff wars, terrorism, market declines, inflation, deflation, etc.

The stock market has historically provided **above-inflation returns**—which means real, after inflation, growth of your wealth, which can maintain or increase your ability to spend far into the future. ***Long-term success can result for those who remain patient, realizing that periodic volatility in economies and markets is an inevitable part of long-term business progress, and stay focused on their personal long-term goals, not what the stock market did today.***

General Principles

Together, we are **long-term, goal-focused, planning-driven investors**. We've found in our experience that the best course for you is to formulate a financial plan—and to build portfolios to serve the plan—based **not** on a short-term view of the economy or the markets, but on **your most important lifetime financial goals**.

- Since 1960, the S&P 500 Index has appreciated approximately **76 times**; the cash dividend of the Index has gone up about **33 times**. Over the same period, the Consumer Price Index has increased **10 times**. So historically, **equities have functioned as an extremely efficient hedge against long-term inflation and a generator of real wealth** over time. We believe this is likely to continue in the long run, hence our investment policy of primarily owning successful companies rather than lending to them.

- We believe that **acting continuously on a rational plan**—as distinctly opposed to reacting to current events—offers the best chance for your long-term investment success. The best recent example of sticking to the plan was seeing the market's reaction to COVID. Simply stated: **unless our goals change, there is little reason to alter your financial plan**. And if our portfolio is well-suited to that plan, we don't often make significant changes to that, either.

- **We do not believe the economy can be consistently forecast, nor the markets consistently timed**. We're therefore convinced that the most reliable way to capture the long-term return of equities is to ride out their frequent but ultimately temporary declines. In practice, this means being mentally prepared to handle roughly 15% short-term declines annually, and roughly 33% declines every 5 years or so.

- **Avoiding costly changes in reaction to short-term volatility provides you the potential to earn higher long-term returns.**

- The performance of your portfolios relative to their benchmark(s) is irrelevant to your investment success as we define it. **The benchmark we care about is the one that indicates whether you are on track to achieve your financial goals**. **One of the biggest goals is making sure you don't run out of money during your lifetime.**

- Our investment philosophy is to **invest in businesses with a history of providing essential products and services**. We **prefer significant management ownership** to create an alignment of interests with us. We seek to invest at reasonable prices and hold these exceptional businesses for many years. Assuming no nuclear annihilation or World War III…we expect this approach will do well over long periods.

As always…please keep us updated with any changes to your financial situation that might suggest altering your asset allocation and investment portfolio and let us know if you'd like a current copy of our Form ADV Part 2.

Your LOYALTY and PATIENCE remain our secret weapons. We value our relationship with you and appreciate the opportunity to continue to serve you and your family.

Thank you for being our client. It is our privilege to serve you.

Sincerely,

John Heldman, CFA　　　Dave Hutchison, CFA

April 21, 2025

"The best way to measure your investing success is not by whether you're beating the market but by whether you've put in place a financial plan and a behavioral discipline that are likely to get you where you want to go. In the end, what matters isn't crossing the finish line before anybody else but just making sure that you do cross it."

-Benjamin Graham, <u>The Intelligent Investor</u> (and Warren Buffett's mentor)

"Forecasts are highly uncertain. Forecasting is very difficult. Forecasters are a humble lot with much to be humble about."

-Jerome Powell, Federal Reserve Board Chairman

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