CAIRN INVESTMENT GROUP

GREETINGS FROM THE NORTHWEST!

Here we are, two months into the new administration, and "uncertainty" is a word on everyone's mind. From a flurry of executive orders to unexpected trade tariffs, the White House is moving fast, and the markets are showing signs of stress. At Cairn, our job is to cut through the noise, protect your assets, and keep you on track toward your goals, so we can't get wrapped up in our own personal feelings, good, or bad, about these policies. While it feels like it's all about tariffs and the uncertainty they're causing, much more is at play here, as we'll discuss below.

We're possibly looking at a new economic landscape. The President's actions, on immigration, cost-cutting, and especially trade, signal a potential shift in how America engages with the world. Are these bold moves a negotiating tactic to reset global trade terms, or the start of a long-term reversal of decades of low-cost foreign manufacturing? If it's the former, we could see stability return in months. If it's the latter, the payoff (and the pain) may take years to unfold. Either way, change is coming, and how nations trade, invest, and collaborate is in flux.

Most Americans, including us, see value in a stronger domestic manufacturing base and fairer burden-sharing with allies. But unwinding a deeply entrenched status quo won't be quick or easy. The administration's "Gordian knot" approach, slashing through complexity with decisive action, rather than a slow and deliberate unwinding, promises disruption before progress.

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OF NOTE:

- :: Estimated taxes, IRA Contributions, and Tax Returns due on April 15
- :: Our ADV Firm Brochure is available on our website, or on request. A Summary of Material Changes is attached as is our Annual Privacy Notice.

MARKETS AND CAIRN CLOSED:

- :: Friday, April 18 – Good Friday
- :: Monday, May 26 – Memorial Day
- :: Thursday, June 19 – Juneteenth

Uncertainty tends to rattle markets, and we're seeing it now. Speculative stocks and growth-dependent sectors are taking the hardest hits, while safer assets show resilience. Your enclosed report reflects this dynamic, and the steps we've taken to shield your portfolio from the storm.

This is where we earn our keep. Patrick's update below dives into the market's twists and turns, but here's the bottom line: We're actively managing your investments to weather volatility and seize opportunities as they emerge, and we're keeping your long-term objectives in sight.

PATRICK'S PART

Volatility returned to U.S. stocks in the first quarter, with the S&P 500 Index declining 4.28% and small-cap stocks, as measured by the Russell 2000 Index, falling 9.48%. However, the recent trend of international stocks underperforming U.S. stocks reversed, with developed international markets gaining 7.03% and emerging markets rising 2.97%.

We have previously discussed the relative attractiveness of international equities, and a continued shift toward this undervalued segment of the market would be a welcome and healthy trend.

Last quarter, we highlighted the froth in market valuations and investor sentiment, cautioning that increased volatility could pose a short-term risk. While the recent selloff in U.S. stocks has helped normalize investor sentiment, the valuation concern remains. The S&P 500 continues to trade at levels exceeding those seen during the dot-com bubble, underscoring the ongoing challenge of elevated market valuations.

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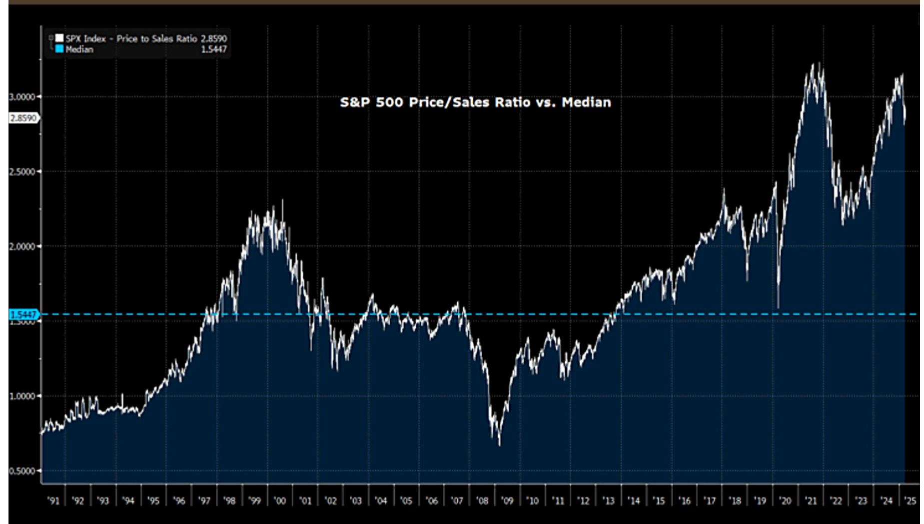
S&P 500 Price to Sales Ratio Remains Elevated



Source: Bloomberg

As I noted last quarter, the past three years have seen significant swings in equity prices – marked by dismal returns in 2022, followed by two strong years of gains. However, it's easy to overlook that, since the end of 2021, equities have barely outpaced the returns of a money market fund. With the negative returns in the first quarter, both the S&P 500 Equal Weight Index and the Russell 2000 Index have now fallen behind.

Money Market v. Index Performance (12/31/21-3/31/25)

Source: Bloomberg

This is why it's crucial to remember that starting valuations play a significant role in determining future returns. No matter how high the quality of an investment, overpaying creates a headwind to performance. To mitigate this risk, we dedicate countless hours to analyzing the price we pay for every investment we make.

With the S&P 500 posting a negative return to start the year, U.S. stocks now face a historically challenging backdrop – elevated valuations combined with weakening price momentum. Investors are often reminded of the market's long-term average return of 10%, a figure supported by over a century of data. However, starting valuations play a crucial role in realizing those returns.

Looking back, since 1943, when valuations are high (CAPE Ratio above 20x) and the S&P 500 trades below its trailing 10-month moving average (indicating a declining price trend), average 12-month forward returns drop to below 2.5%, with a significantly higher risk of loss.

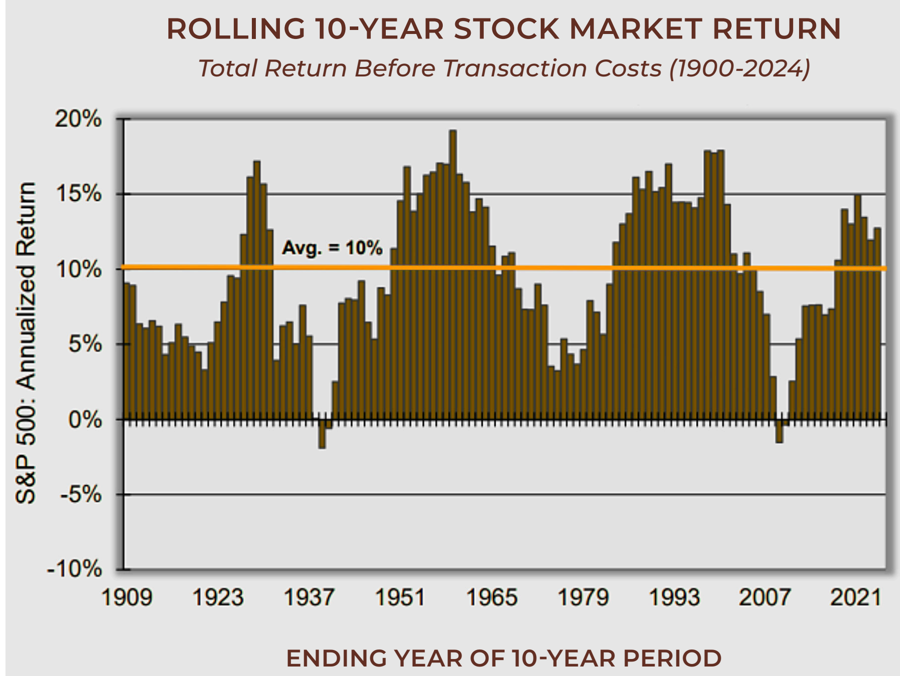
S&P 500 Returns When Expensive + Downtrend

Return: CAPE>20 and Negative Trend	2.37%
% of Time Taken Place	8.99%
Largest Drawdown	-44.76%
% of Time Negative	40.00%
Average When Negative	-20.88%

Source: Bloomberg

In fact, there have also been many longer-term periods (10 years) that stocks have experienced returns much higher and lower than the stated 10% average. As the chart below shows, rolling 10-year returns can vary widely. Starting valuations matter.

S&P 500 Rolling 10 Year Returns



Source: Crestmont Research

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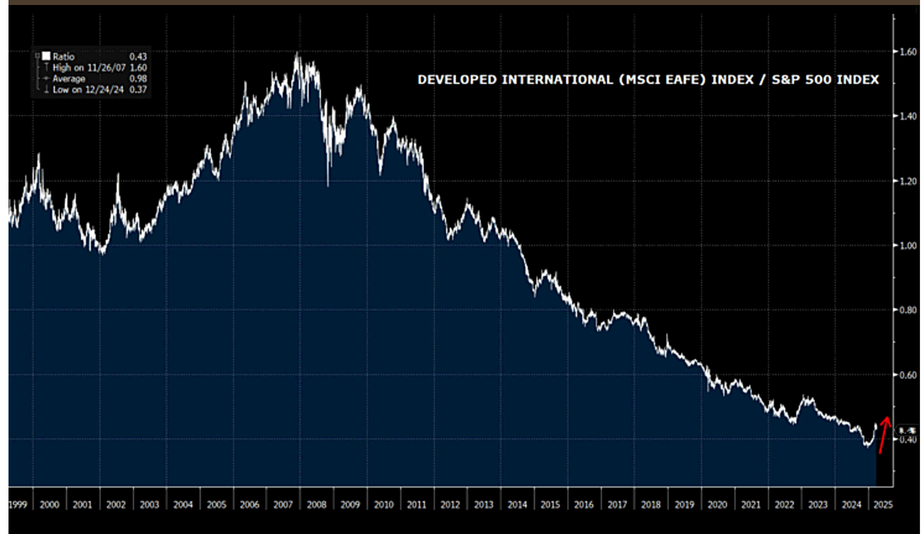
There are a few silver linings to the current backdrop, and we have the flexibility to invest where there is more compelling value. With the pullback taking place the large cap technology stocks, value has started to outperform which is a welcome environment for our investment discipline.

Value v. Growth Price Movement

Source: Bloomberg

Developed International v. S&P 500 Price Movement



Source: Bloomberg

After years of underperformance, international stocks have gained momentum since the start of the year. If this trend continues, our allocation to this asset class should remain well-positioned to benefit.

We are also still finding pockets of value in select companies and sectors that have not experienced the euphoric rise in prices of the past couple of years.

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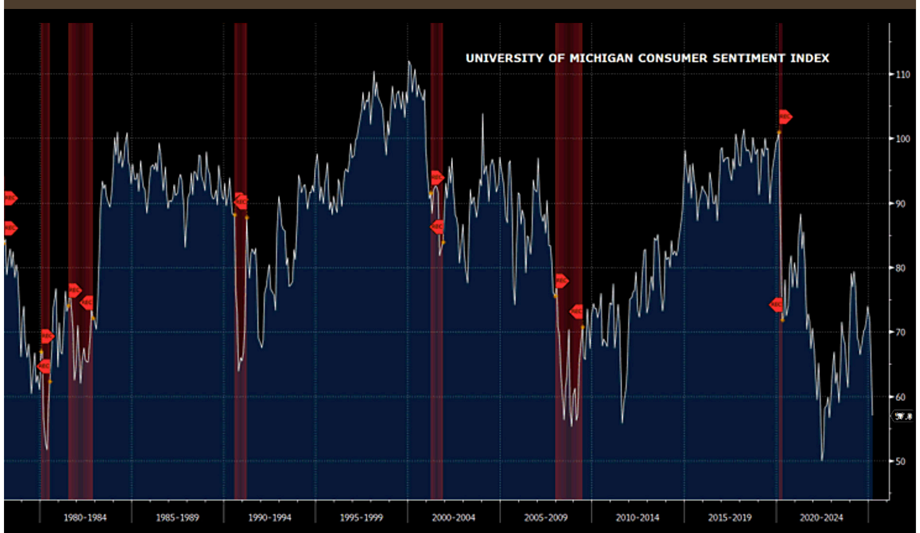
ECONOMIC BACKDROP

With the constant stream of headlines, it can be challenging to separate noise from meaningful trends in the data. While predicting recessions isn't part of our investment process, we do track economic activity to assess where we stand in the current cycle. At the start of the year, the consensus was that the economy would continue progressing at a measured pace, which would support equity prices and earnings. However, as the year has unfolded, opinions have become more cautious, especially with the growing concern over widespread tariffs. Consumer sentiment has already taken a hit, now at levels typically seen during recessions.

Consumer Sentiment Has Weakened



Source: Bloomberg

With nearly 70% of our economy tied to consumption, the mood of the consumer plays a critical role in shaping economic activity and trends. This is evident in many of the economic reports we track – where survey data (soft data) is showing much more weakness than hard data. We'll be closely monitoring whether this weakness in the survey data begins to affect the hard numbers in the coming months. However, the current trend suggests that the economy is likely in the later stages of this cycle, rather than at the start of a new expansion.

FINAL THOUGHTS

We continue to maintain a conservative approach to portfolio construction, given the still-elevated valuations and declining price trends in broad U.S. stocks. With a higher-than-usual cash allocation, we have the flexibility to pivot to a more aggressive stance if and when the data supports it. International and U.S. value stocks are offering more compelling value, and we're actively taking advantage of these underappreciated asset classes.

In our fixed income allocation, we remain focused on a short-maturity strategy with an emphasis on high-quality bonds.

Thank you for your continued support. Please feel free to reach out with any questions or concerns. —Patrick Mason

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Thanks, Patrick. As you read this, we're probably moving back into our newly remodeled office; a bit sparse on furnishings to start, but excited to be back in our space and looking forward to hosting meetings in the new and improved conference room.

Happy Trails,

Tim Mosier, President,
Cairn Investment Group, Inc.