CAIRN INVESTMENT GROUP

GREETINGS FROM THE NORTHWEST!

Well, the calendar says it's Fall and I'm seeing some signs that it's true with some colorful trees, greener lawns, cool morning mists, and an occasional rain drop. If you don't live in the Pacific Northwest, you might be surprised by how dry it gets here in the late summer. The lawns are a dull yellow and the evergreens sag like they're begging for help. The shorter days and dewy mornings bring some relief, and then the rains arrive to finish the job. I know many of you share with me the sentiment that Fall is your favorite season. I'm not quite sure why it's better than spring, but it is. Maybe it's the anticipation of the Holidays or the excuse to cuddle up with a hot drink that's missing in the spring.

This will be a momentous fall season, with a high-stakes election and global unrest like we've not seen in a long time. We'll watch with interest, but as we've said before, we don't try to predict these outcomes or try to outsmart the hedge fund crowd by placing bets on such things. We have our data-driven process, and it will guide us through whatever these times present.

Speaking of data, you may have heard the witty and insightful quote attributed to Mark Twain, that "there are 3 kinds of lies: lies, damn lies, and statistics." Sometimes analysts are looking for an answer and they find it; other times they don't understand the nature of the data and present "findings" that are flawed. These are mistakes that we work hard not to make. In his part, Patrick will point out a situation or two where the answer being presented by the financial media may be the result of poor use of the available data.

On the home front, we have committed to a new lease for our Vancouver Headquarters, and with it comes a refresh of the office space and furnishings. We're not quite sure of the timing, but it should be in the early winter. While the construction is active, we'll be working much more out of the office than in and won't be having onsite meetings until it is completed. We're very excited for this next step in our evolution, and I hope that many of you will be able to come in and see the results next year.

OF NOTE:

:: Cairn Office Remodel TBD

IMPORTANT DATES:

:: **COLUMBUS DAY**
Monday, October 14: Bond market, banks and post office closed. No settlements.

:: **VETERANS DAY**
Monday, November 11: Bond market, banks and post office closed. No settlements.

:: **THANKSGIVING DAY**
Thursday, November 28: Stock market and bond market closed. Banks and post office closed.

:: **BLACK FRIDAY**
Friday, November 29: Stock market closes at 10:00 am PST.

:: **CHRISTMAS EVE**
Tuesday, December 24: Stock market closes at 10:00 am PST.

:: **CHRISTMAS DAY**
Wednesday, December 25: Stock market and bond market closed. Banks and post office closed.

One last thing before I hand it over. I have heard time and again how much you appreciate having a live person picking up the phone, and how having our Cairn staff available to answer your questions is so unusual and helpful. We are committed to continuing this level of service, as it's something that you deserve, and is increasingly rare nowadays. We're here to help you to navigate life's financial dilemmas, so please, call and ask to speak with any of our advisors when you're looking for a little help. It'll cost you nothing and you won't be disappointed.

With that, on to Patrick:

PATRICK'S PART

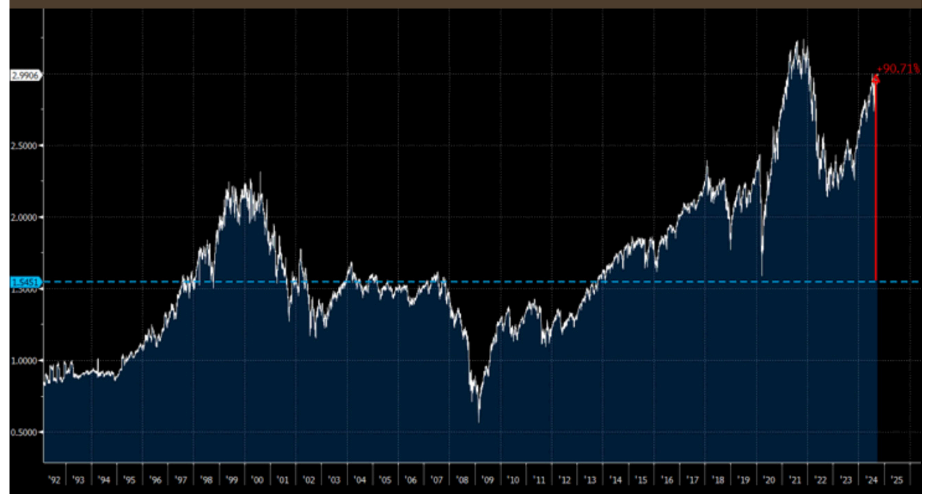
The third quarter continued to see strong returns across capital markets, as both stock and bond prices were supported by the belief that monetary policy was going to shift to be more accommodative. US stocks, measured by the S&P 500, returned 5.89%, and bonds returned 5.20%. International stocks had a nice tailwind during the quarter with the US Dollar weakening, returning 7.26%. Unlike the first half of the year, equity performance was quite broad, which is the one silver lining despite record high equity valuations.

S&P 500 Equal Weight Index to S&P 500 Index

Source: Bloomberg

Last quarter, I did a deep dive into valuations across the broad market and different asset classes so I won't spend too much time on the topic today besides saying that valuations remain extremely elevated.

S&P 500 Price to Sales Ratio v. Historical Median



Source: Bloomberg

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>
> ***—Tim Mosier***

The biggest event of the quarter was the change of monetary policy in the US, with the Fed cutting interest rates for the first time since 2020, on September 18th. The media and market participants immediately cheered the Fed's new policy stance, citing instances of previous interest rate cuts and subsequent market returns. As you know by now, we spend countless hours looking at data, and with any major shift in market behavior it's useful to look underneath the hood instead of relying on the media's constant cheerleading. Below is a table of previous interest rate cut cycles and subsequent one year returns for stocks. I've also included starting valuations when the Fed embarked on a rate cut cycle.

Fed Rate Cutting Cycles, Valuations, and Market Returns

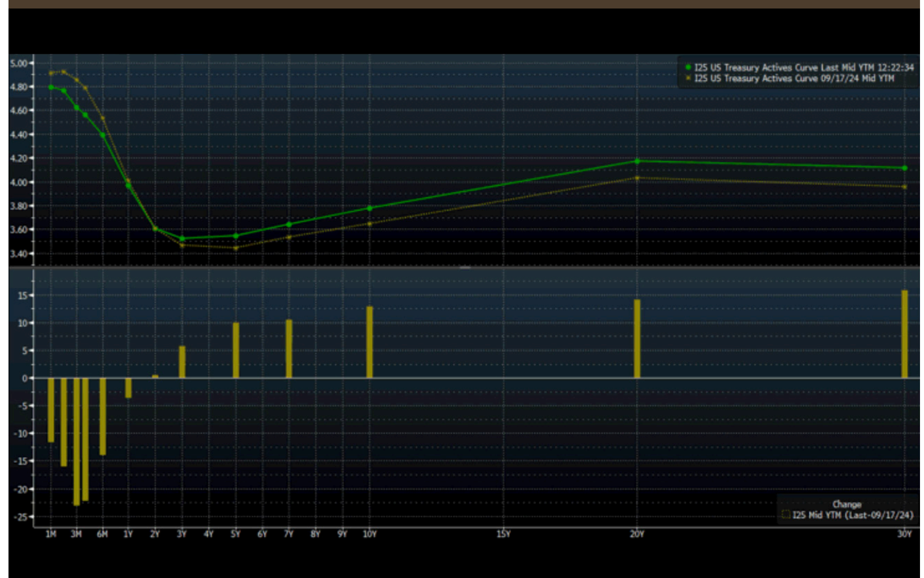
DATE	FED FUNDS RATE %	SHILLER P/E RATIO	S&P 500 1 YEAR RETURN
9/1/1971	5.12	16.9	15.93
7/1/1974	9.25	10.4	15.66
4/1/1980	11.5	7.8	40.56
11/2/1981	14	7.8	17.36
10/2/1984	10	9.6	17.52
6/5/1989	9.62	14.8	17.79
7/6/1995	5.75	23.4	21.42
1/3/2001	6	37	-12.38
9/18/2007	4.75	26.7	-18.85
3/3/2020	1.25	24.8	29.42
9/18/2024	5	36	??
	MEAN	19.56	14.43
	MEDIAN	16.9	17.44

Source: Bloomberg

When pundits and media personalities site the average return of stocks being strong after the Fed embarks on an interest rate cut cycle, they are not wrong, but looking at the data more closely paints a different picture. The starting level of valuation was a big driver of whether stocks did well or not after a shift in monetary policy. We do not know for certain what the next year brings, but we can say that outside of 2001, the S&P 500 has never been more expensive to start a rate cut cycle.

With all the talk about equity market performance after the Fed's policy change, the reaction in the bond market was equally interesting. Intuitively, one would think that interest rates across all maturities of US treasuries would drop after an interest rate cut. The chart below shows how interest rates have moved since September 17th.

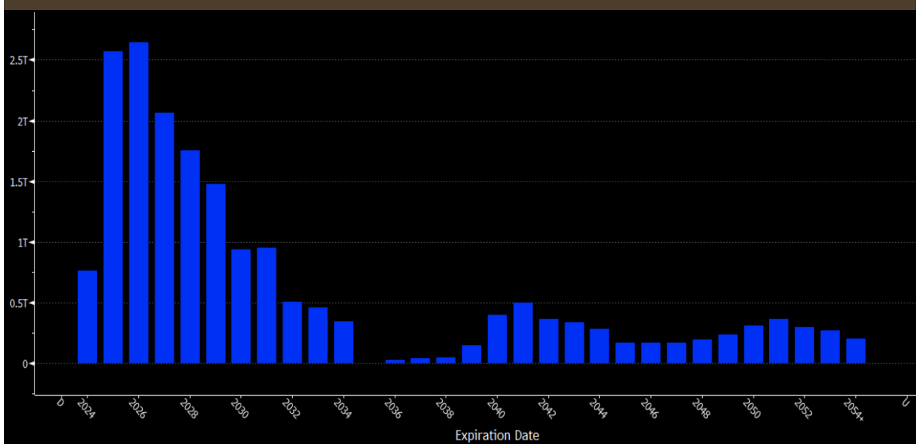
U.S. Treasury Yield Curve



Source: Bloomberg

As you can see in the bottom part of the chart, short maturity treasury bonds did see a drop in interest rates following the Fed's 0.50% interest rate cut. But when you look at the longer maturity bonds, interest rates increased in response to looser monetary policy. This seems to indicate that the bond market is not convinced the fight against inflation is finished, and looser monetary policy could reignite inflationary forces. The chart below shows the maturity schedule of the over $19 trillion in US government debt. Between 2025-2027 there is over $7 trillion maturing that will need to be refinanced. Suffice it to say, the US government does not want to see longer dated US treasury bond rates moving higher with the interest expense on US debt taking up over 30% of tax receipts 2023. I would imagine that number will increase when it is reported for 2024.

U.S. Debt Maturity Distribution



Source: Bloomberg

Longer maturity treasuries yields are sensitive to inflation and growth expectations in the economy. Currently, the data is still mixed on both fronts, with headline inflation numbers showing improvement, but survey inflation metrics and expectations still elevated. Economic activity data has started to show some weakness, so time will tell if a clear trend in either direction materializes.

Portfolio positioning has not shifted drastically over the last few months because opportunities are still scarce. We are still holding high levels of cash in money markets, as we view risks to be quite elevated and interest rates on cash are sufficient while we wait for a better risk / reward environment. When there have been opportunities to put some cash to work, we have taken advantage of them. We will let the data guide us on when a larger shift in portfolio allocation is warranted, but in the meantime, we still view risk management as being the largest priority, considering high valuations and euphoric sentiment.

We thank you for your continued trust and welcome any questions or comments you have on the economy, markets, or your portfolio. —Patrick Mason

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Thank you, Patrick. That was enlightening, as usual. We'll provide an update on the office construction as we know more, and hopefully get some firm dates that we can share. Until then, happy trails!

Tim Mosier, President,
Cairn Investment Group, Inc.

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