

# Invest Smarter. Live Better.

## Systemic Shock

Emotions have been running high since Inauguration Day. If you are feeling scared or uncertain, you are not alone. Markets have been behaving erratically in response to uncertainty about tariffs, DOGE and the constitutionality of executive orders. The volatility index has risen to the highest level since Covid lockdowns were beginning in 2020. In this letter, we want to acknowledge that fear is a normal response to uncertainty, but freaking out is not an investment strategy. While some losses are unavoidable at a time like this, we are taking action to mitigate the damage and prepare for the inevitable opportunities.

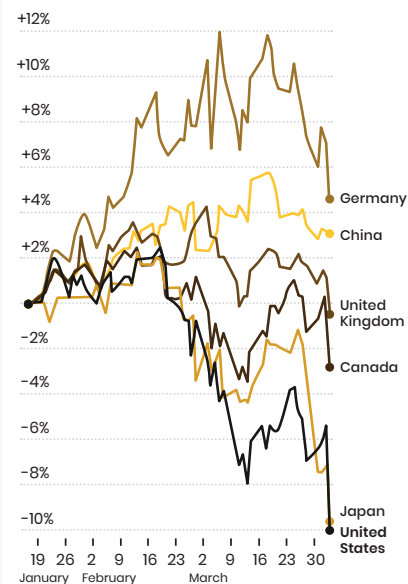
This April 3rd headline from the New York Times says it all, but tariffs are only part of the uncertainty that has been building this year.

As we sit down to write, here is an update of our key asset allocation benchmarks and their behavior since Inauguration Day. Given the breaking news, we are moving beyond just the first quarter data to keep you informed with more current updates in this most fluid situation.

### Trade War Sets Off 'Max Pessimism' in Global Markets as Stocks Plunge

The S&P 500 fell almost 5 percent on Thursday, its worst drop since June 2020, as President Trump's high-than-expected tariffs set off another round of economic worry.

#### Stock Markets Since Trump's Inauguration



Source: New York Times

# Asset Class Returns since Inauguration Day

Negative Total Return

Positive Total Return

## All Members

Rank	Asset Class	Total Return
1)	VANECK GOLD MINERS ETF	11.78%
2)	SPDR GOLD SHARES	9.52%
3)	ISHARES 20+ YEAR TREASURY BOND ETF	4.73%
4)	ISHARES CORE U.S. AGGREGATE	2.61%
5)	ISHARES MSCI EAFE ETF	-4.98%
6)	ISHARES MSCI EMERGING MARKET	-7.59%
7)	ISHARES US REAL ESTATE ETF	-7.66%
8)	SPDR S&P DIVIDEND ETF	-7.87%
9)	ISHARES NORTH AMER NATURAL RES ETF	-15.64%
10)	SPDR S&P 500 ETF TRUST	-16.30%
11)	INVESCO QQQ TRUST SERIES 1	-19.51%
12)	ISHARES RUSSELL 2000 ETF	-20.86%

Source: Bloomberg

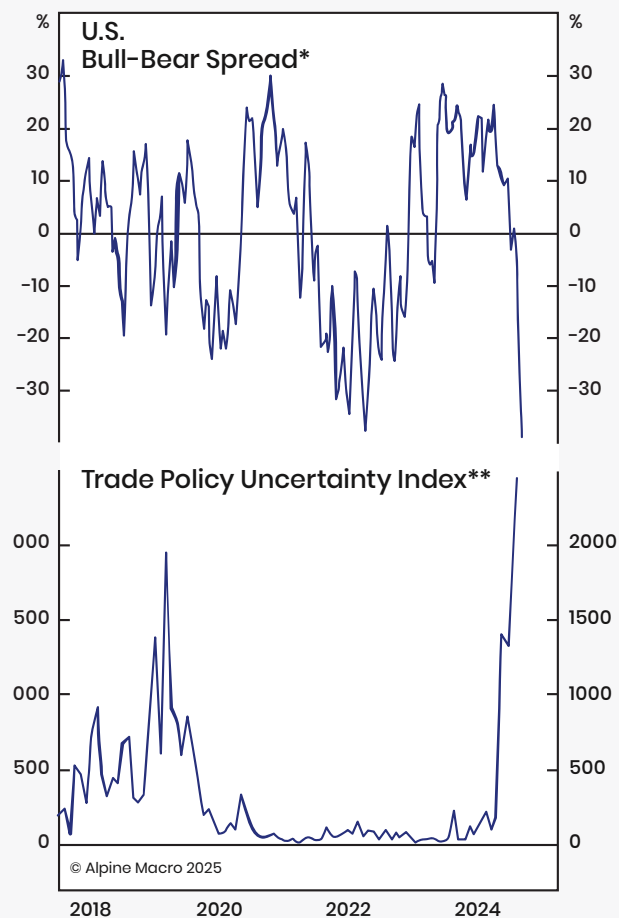
## U.S. Stocks – Resetting expectations

Going into the new year, American investors were looking forward to the promise of deregulation, business growth, and fiscal expansion; stock prices soared, bond yields rose, and the dollar was strong. In late January, the introduction of the Chinese AI company Deep Seek had a significant impact on stock performance in the technology sector, due to questions about overinvestment in AI and associated energy infrastructure.

As discussed in our fourth quarter strategy piece, *Precarious*, we anticipated the risks of an especially narrow market hinged on the performance of the “Magnificent 7” companies. As the quarter went on, the decline in this sector in conjunction with concerns around Trump’s tariff announcements, inflationary pressure, and continued geopolitical uncertainty, sparked a rotation of money flows out of U.S. equities.

Many assumed that the tariffs were going to be a negotiating tool. Instead, the blunt force nature of the actions has prompted retaliations, resulting in chaos. In response, there has been a waterfall decline in estimates and asset prices. Economists are lowering expectations for economic growth and raising inflation assumptions and analysts are lowering previously strong earnings estimates for the S&P500 to close to zero. “Liberation Day” has so far only liberated investors from their wallets.

**Chart 2 U.S. Equity Investors Are Resetting Their Expectations**



\*Shown as 4-week moving average; source: AAIL Investor Sentiment Survey

\*\*Source: Economic Policy Uncertainty

## Commodities

In the turbulent first quarter, we saw a few bright spots where Avalon portfolios were able to generate gains. Capital dispersion from U.S. equities bolstered gold, international investments, and sectors perceived as more resilient in times of economic volatility. Gold bullion was up more than 18% in its best quarterly performance since 1986, while gold mining stocks outperformed, up over 35%. Our investment analysis continues to support allocations to gold and gold mining companies as attractive in the long term, as central banks continue to divest holdings of U.S. Treasuries in favor of assets such as gold as a safe haven. Oil and other natural resources have declined significantly, indicating a potential for a tactical rally as an inflation hedge. Should recession odds increase due to the current tariff shock, the tactical trade for some commodity-related themes will stall. Should inflation begin to rise again, the secular base-building will likely extend, supporting the view that the 5-year to 10-year return prospects for commodities are still among the highest in our investment universe.

## International Markets - the End of American Exceptionalism

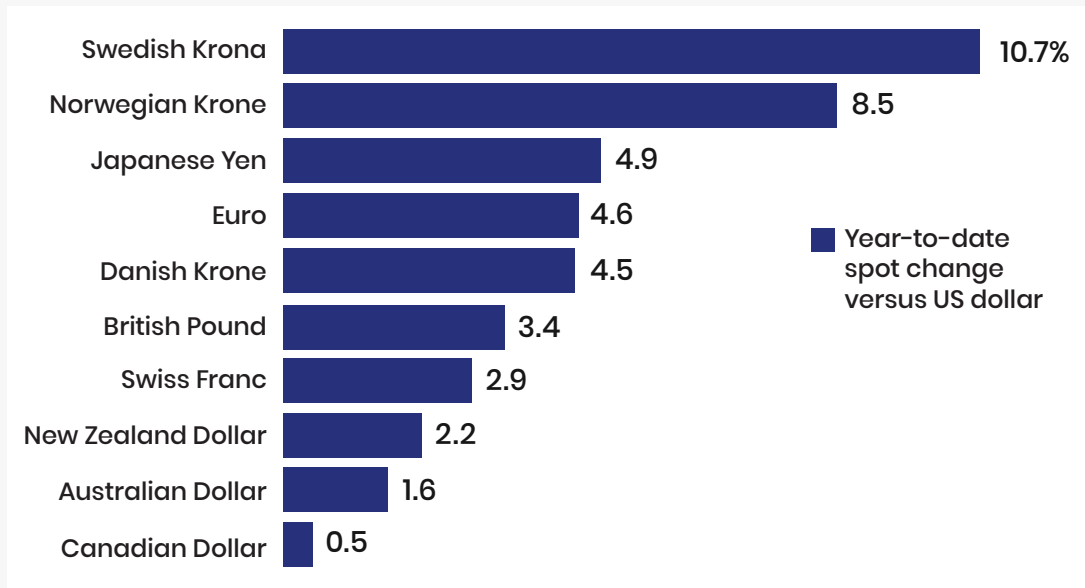
In late 2024, the “American exceptionalism” trade was booming post the election as investors poured money into U.S. investments. The Trump administration’s change in geopolitical strategy this year has disrupted U.S. dollar-denominated markets where strong outflows have depressed prices of stocks and improved foreign currencies like the Euro and Yen. International equities, particularly in parts of Asia and Europe, delivered their strongest quarterly performance in decades. The MSCI

Europe outperformed the S&P 500 by 18.4%, the widest margin in over 30 years. The best performers were European companies, mainly German, that stand to benefit from increased defense spending as the U.S. pulls back on international security commitments, especially as valuations had been depressed in this sector for quite some time. We will continue to monitor whether this trend is sustainable as European economies attempt to move toward a cyclical recovery, while the U.S. market is pricing for a growth slowdown. Our analysis shows that Emerging Markets will also continue to do well in this environment, particularly China, India, and Brazil. In the first quarter, Chinese stocks resumed their late 2024 recovery attempt, catalyzed by the Deep Seek announcement and the evidence that China is closer than originally thought in the artificial intelligence race. With stocks in China trading at significant discounts to the U.S., the natural response to the unexpected development has been a rally. With the Xi government now promoting higher stock prices, further rally is likely after nearly two decades of stagnant stock prices. Other emerging stocks are also attractive versus the U.S., however, in the short run, tariff uncertainty is likely to impact stocks everywhere even after a strong start to 2025.

## U.S. Dollar

Escalating tariffs and efforts to roll back decades of globalization has shaken confidence in the dollar, with the U.S. dollar index down more than 4% this quarter, dropping against all but a handful of the 31 major currencies over the last three months. The decline in the dollar has exacerbated the U.S market decline as investors shift to foreign repositories for their money. Avalon portfolio allocations to international equities, fixed income and cash have benefited from this shift.

## Dollar Down in 2025 Against All Group-of-10 Peers



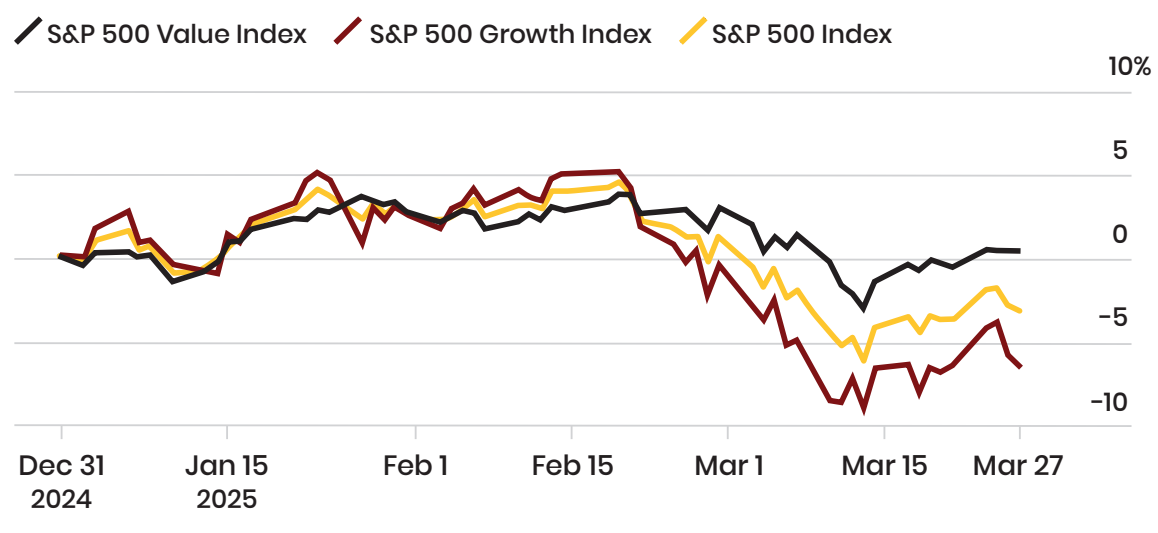
Source: Bloomberg

Note: As of March 28, 2025

## Value Investments

We have also benefited from investments in US Value stocks. Gains in dividend paying companies, consumer staples, and healthcare stocks helped the sector rise by over 4% during the quarter. In comparison, growth stocks declined over 6% this quarter. Value oriented companies tend to offer earnings and price stability in a fluctuating economic and market environment.

## Value Stock on Pace For Biggest Outperformance Since 2022



Source: Bloomberg

# Fixed Income

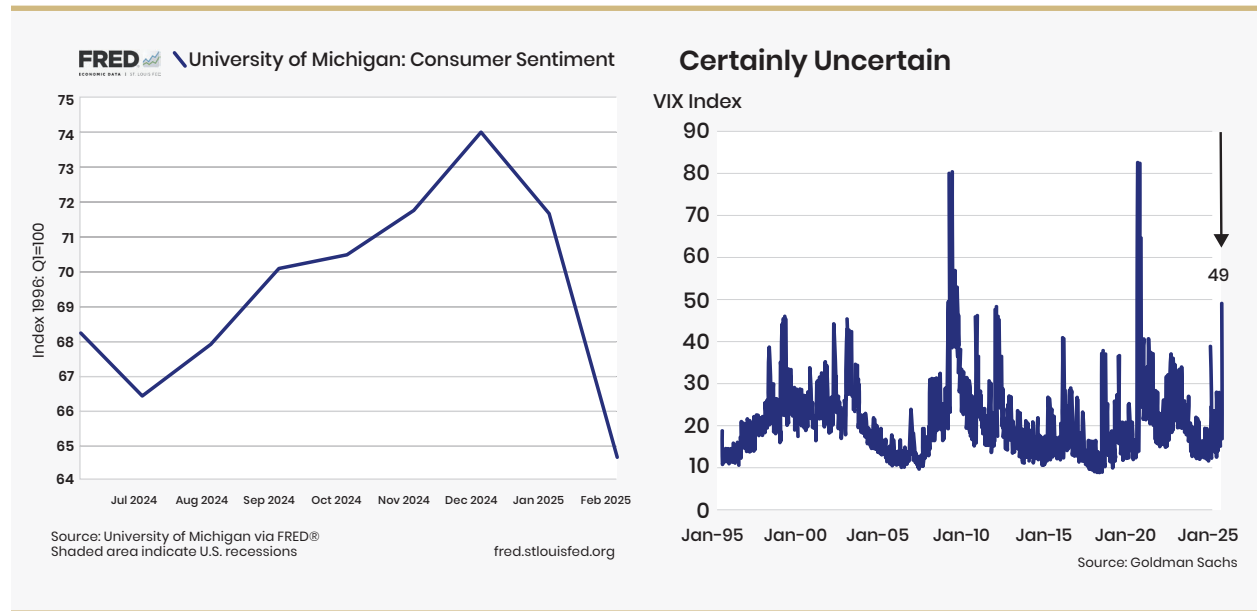
Fixed income was also a strong performer in the first quarter, with long-term U.S. Treasuries and U.S. Treasury Inflation Protected Securities (TIPS) among the best performers. Our analysis supports an allocation to U.S. TIPS and international fixed income as a hedge against a potential resumption of inflation should the economy avoid recession.

# Sentiment

2025 has been marked by widespread uncertainty and economic pessimism as reflected in most measures of Consumer Sentiment. The Consumer Confidence Index fell 28% over the past year, marking the lowest sentiment level since the depths of COVID. The Index of Consumer Expectations, reflecting the short-term outlook for income, business, and labor market conditions,

dropped by more than 30% since November 2024, a 12-year low. Business sentiment was less pessimistic but is now turning negative as well. JP Morgan's CEO criticized the new tariff policy and said that it would likely send us into a recession. Small businesses, perhaps impacted more by tariffs and the potential for increased inflation, were equally cautious.

The only thing markets dislike more than uncertainty is unexpected shocks. Think of the current moment like a natural disaster where the evacuation warnings came with only minutes to spare. With U.S. growth fully priced as we entered 2025, we have protected against the risk of near-term cross currents due to global trade uncertainty, inflationary pressures and capital flow shifts out of the United States. These ideas predate April 2 and will likely return as themes when markets settle down.



# Here for you

We began by saying we know that you might be shaken by recent developments. Even in uncertainty, once the information is better digested, markets are likely to resume some of the trends we have highlighted and to present new opportunities we've been waiting for in the form of better

valuations. We are watching and waiting and encourage you NOT to look minute by minute at your portfolio values or the news. This is why we are here. Should you need some extra time to discuss our unfolding analysis, please don't hesitate to contact us. We are always here for you.



Clara Basile



Ross Revenaugh



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