

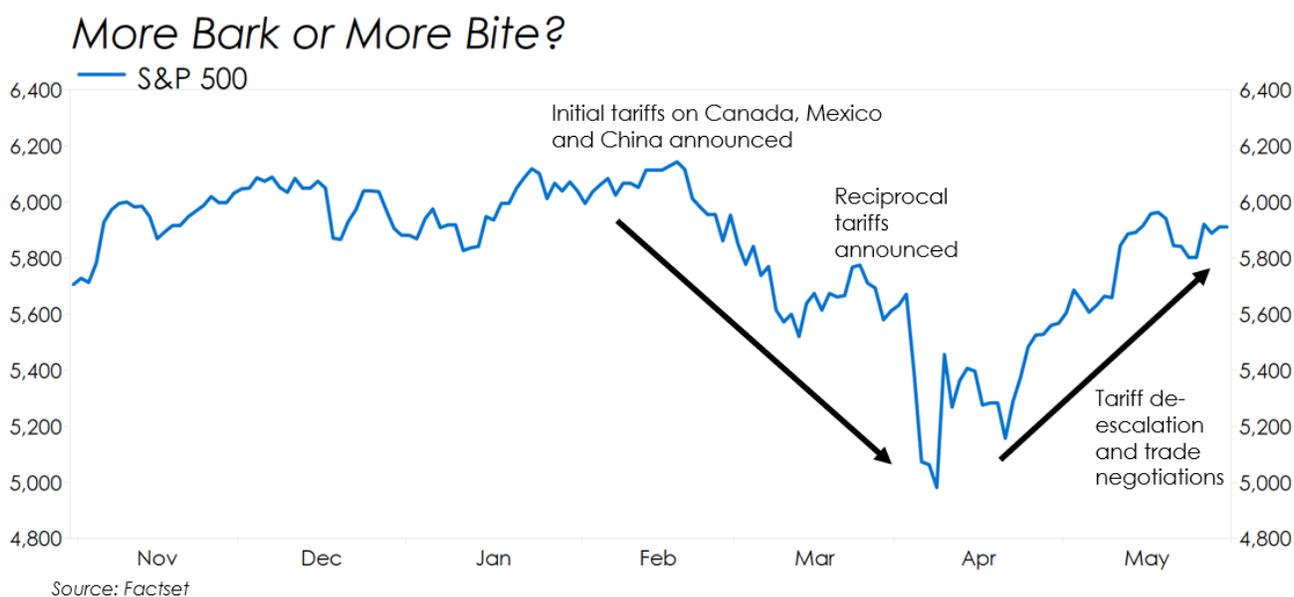
More Bark or More Bite?

“A little less conversation, a little more action please.”

– Elvis Presley (1968)

Pick your favorite four-legged friend of the canine variety. If you're a dog lover, you've probably encountered that lapdog pooch whose bravado greatly exceeds his physical dimensions. Unbeknownst to him, his bark might be worse than his bite.

Today's investing backdrop might be characterized in a similar fashion. As can be seen in the chart below – despite all the blustery trade headlines that seemed to bewilder investors for much of the first quarter, cooler heads prevailed in the back half of April and into May. Remarkably – at month end – the S&P 500 was trading back to levels seen at the beginning of the year. De-escalation in the form of lowered tariff rates and a 90 day stay certainly helped, but fundamentals holding up better than expected were probably more impactful to markets.



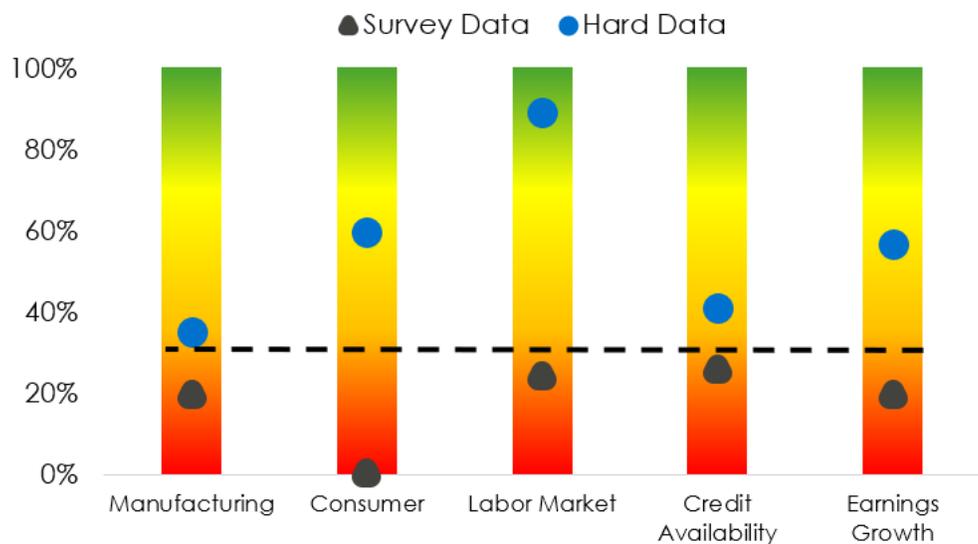
One observation made among investors is that the so-called hard data is holding up much better than the soft or survey data. Hard data is often referred to as that which can be verified as factual whereas soft data is quantified based on surveys of opinion. Investors tend to think about soft data as that which businesses or consumers might say they're doing while hard data refers to what they're actually doing.



In evaluating comparable datapoints across both the soft and hard data divide, one might conclude that the bark has, indeed, been worse than the bite. As can be seen in the chart below, we used comparable metrics (see the footnote for more detail) in each category and plotted where these current measures ranked (by percentile) across common overlapping time periods. Relative to the hard data, the survey data scored consistently worse across each dimension. In short, participants might be feeling worse than they're behaving. So as the fundamental data has come in better than feared, investors have breathed a collective sigh of relief.

This begs the question, if there can be such big disconnects why does one pay attention to the survey data at all? While participants may not always do what they say, the survey data tends to be more timely and therefore can be more predictive of the hard data. As a result, many leading indicators originate from the survey data. Even still, we're reminded as investors that analyzing the fundamentals tends to be both a science and an art. As an example, there are nuances to the current dynamic. The tariff headlines have likely caused some degree of a pull forward of demand as companies pre-ordered in anticipation of higher prices. This might have the effect of stronger actual results in the first half of the year than in the second half of the year, as a consequence. Of course, there's nothing to suggest that the hard data has to definitely "catch down" to the survey data, but within the context of the rally in risk assets, we can't help but wonder if the market has already priced in some degree of improvement in the survey data regardless.

More Bark or More Bite?



Source: Factset. Data series represent the percentile rank across overlapping time periods within each category as defined by the following: Manufacturing - Survey Data: ISM Manufacturing / Hard Data: Industrial Production 12/1962-Current; Consumer - Survey Data: UofM Consumer Sentiment / Hard Data: Core Retail Sales % 1 Yr 1/1993-Current; Labor Market - Survey Data: Conference Board Labor Differential / Hard Data: Jobless Claims 4 Week Average 6/1977-Current; Credit Availability - Survey Data: Senior Loan Officer Opinion Survey C&I Credit Standards Net Tight/Loose / Hard Data: C&I Loan Growth % 1 Yr 4/1990-Current; Earnings Growth - Survey Data: S&P 500 EPS NTM 3 mo Rev / Hard Data: S&P 500 EPS LTM % 1 Yr 4/2003-Current.

In summary, so far, the bark has been worse than the bite though we remain on the lookout for any graduation from Puppy Dog to Alpha Dog.

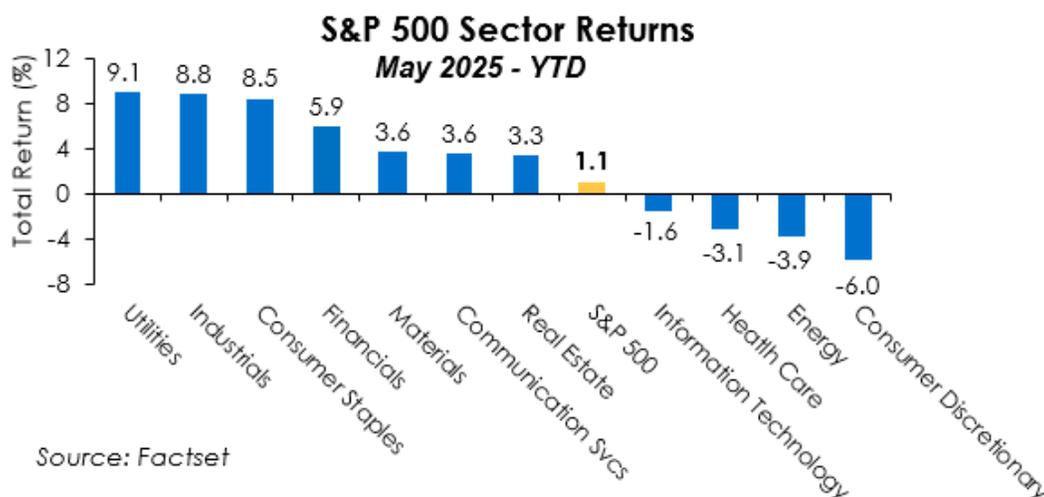
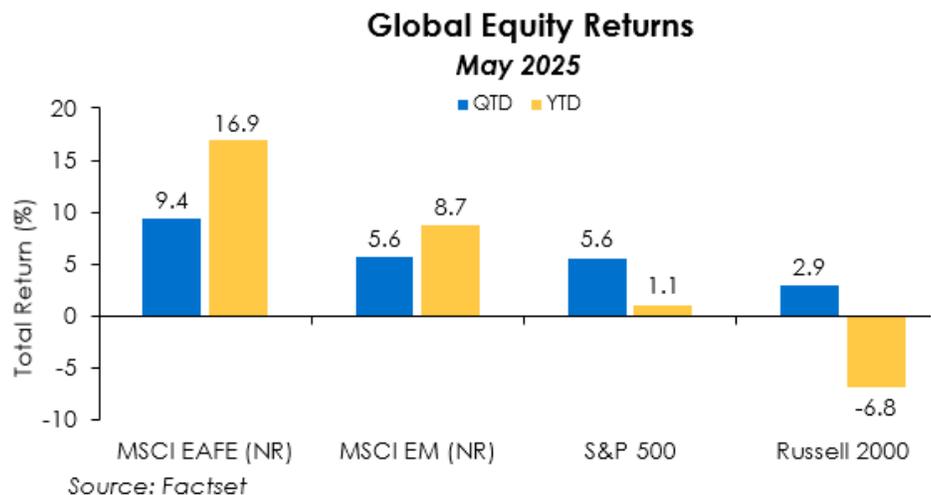


US Stocks saw a bounce back rally in May with the S&P 500 turning in its best month since November of 2023. Still, negative equity returns from February through April leave the S&P 500 with its most subdued YTD return since 2022 (albeit still positive). REITs turned the corner into positive return territory in May. Meanwhile, Overseas Stocks continued to perform strongly. Finally, Bonds and Commodities have softened over the past couple of months after the latter turned in leading returns in the first quarter.

Stocks

International Markets (MSCI EAFE and MSCI EM) remain in the lead for both the second quarter and the year. Returns have benefited from dollar weakness and as investors look to increase portfolio diversification. Meanwhile, US Stocks (S&P 500 and Russell 2000) have underperformed

amid trade and stagflation fears though concerns eased in May as these laggards became leaders. From a sector perspective, performance has been broader year-to-date with a combination of defensive and cyclical value sectors outperforming (Utilities, Industrials, Staples, Financials, Materials). However, that trend reversed in May with cyclical growth sectors leading in the month (Tech, Discretionary, Communication Services).



Bonds

Policymakers pivoted to an easing bias by reducing the Fed Funds rate by 50 basis points at their September meeting and another 25 basis points each at their November and December meetings (Fed Funds at 4.25-4.50%). While this easing bias is the first in over four years, policymakers left rates unchanged at the January, March and May

meetings. Since December, the Fed has reduced the number of expected 2025 rate cuts from four to two (25 basis points per) and indicated they expect slower

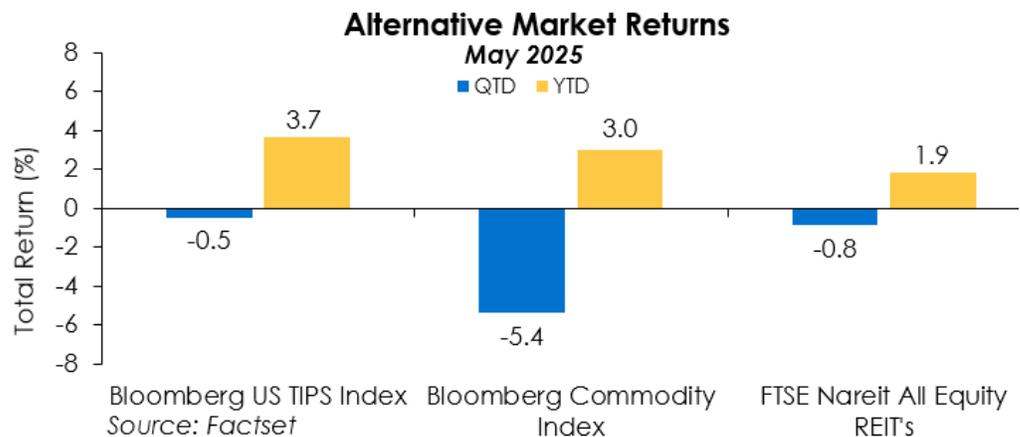
growth and higher inflation by this year's end. Despite the implied "stagflationary-lite" backdrop, Bond returns have generally held up better than US Stocks year-to-date despite this reversing materially in the month of May amid trade war de-escalation. International (Bloomberg Global Agg ex US) has been the standout for the year due to dollar weakness while long duration Treasuries have lagged.



Alternatives

Commodities have been weak in the second quarter on cooler inflation reports and as OPEC increased oil production. Meanwhile, publicly traded Real Estate (REITs) posted marginally positive

returns for the year comparable with US Large Cap Stocks. Finally, year-to-date returns on Treasury inflation protected securities (TIPs) have performed slightly better than nominal Treasuries amid volatile (first rising, then falling) inflation expectations.



Market Outlook

**“It’s Tricky to rock a rhyme, to rock a rhyme that’s right on time.
 It’s Tricky.”**

– Run DMC, *It’s Tricky* (1986)

As the page turns further into 2025, we remain focused on the ever evolving Tricky “Tri-Cycle” – the “three cycle” framework we’re using to assess the landscape. A stagnating (and late) Economic Cycle, quickly maturing Profit Cycle and wildly reversing Policy Cycle – makes for the continuation of a Tricky backdrop that

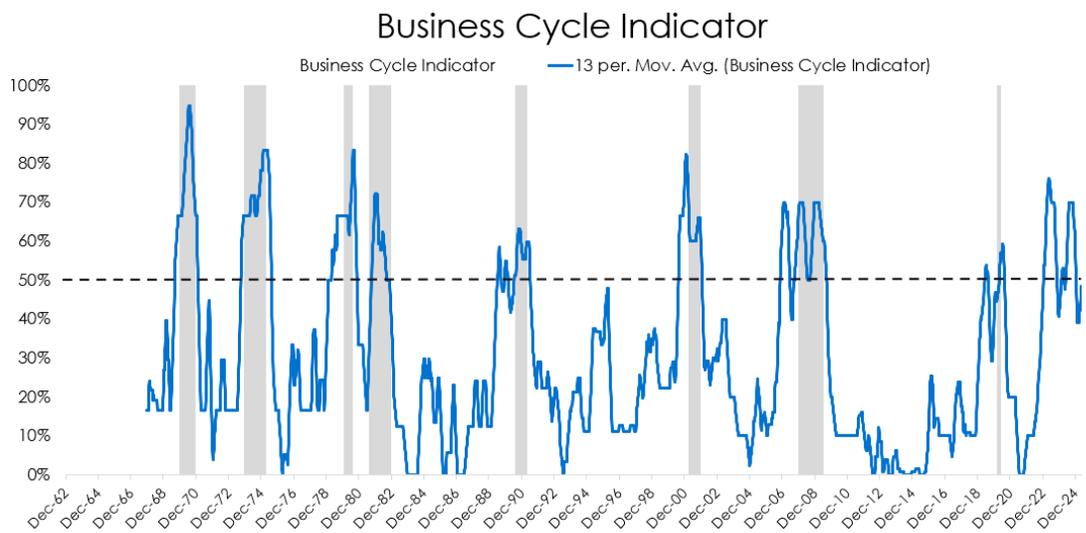
requires investors to keep their proverbial eyes up and “Head on a Swivel”. Let’s explain.

Tricky "Tri-Cycle"	
Cycle	Stage
Economic Cycle	Stagnating
Profit Cycle	Maturing
Policy Cycle	Reversing

Economic growth remains choppy with a stagnating impulse, in part, due to elevated uncertainty from trade and fiscal policy. Such uncertainty comes from the combination of global trade negotiations and a US budget negotiation that

appear to have become attached at the hip. That’s because it would seem that revenue from tariffs have been identified as a way to pay for a good portion of the tax cut extensions that would be required in attempting to keep the budget deficit neutral (on top of material spending cuts). This not only adds uncertainty among consumers and business owners but to the Fed as well. Consumption spending weakened in the 1Q GDP report ahead of what might be a level up in prices on many imported goods. While a recent court ruling stated the tariffs violated the rules under which they were enacted (IEEPA guidelines), the Administration has a couple

more paths to pursue that look potentially viable (section 338 and 122). What’s more, we believe there’s fundamental evidence – including the yield curve, leading economic indicator composites,



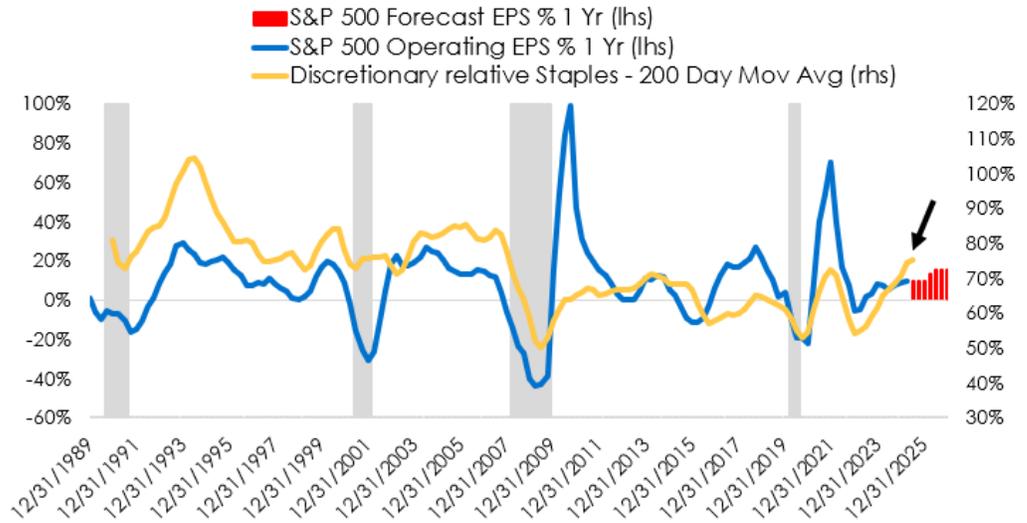
Source: Factset and Yellow Cardinal Research; the Business Cycle Indicator is a proprietary dashboard of financial conditions that historically have provided some context of business cycle duration and lead time on recessionary events. When more than half of the weighted average signals were triggered, this often preceded a recession. The Business Cycle Indicator is a weekly signal with the 13 week moving average smoothing the volatility.



certain survey relationships and especially labor market measures – that point to being on the later side of the economic cycle. As can be seen in our business cycle indicator on the prior page, an increased percentage of measures being triggered is a good illustration that we remain at comparable late cycle levels in the economy (with recessions designated by shaded regions).

At this point, the profit cycle doesn't look as late as the economic cycle but changes in the policy setup suggest the risk of a maturing backdrop. As can be seen in the chart at right – the good news is that profit growth (blue line) continues to ramp off of the earnings recession trough in 2022 with the consensus forecast (red bars) suggesting acceleration into 2026. Also note, that when

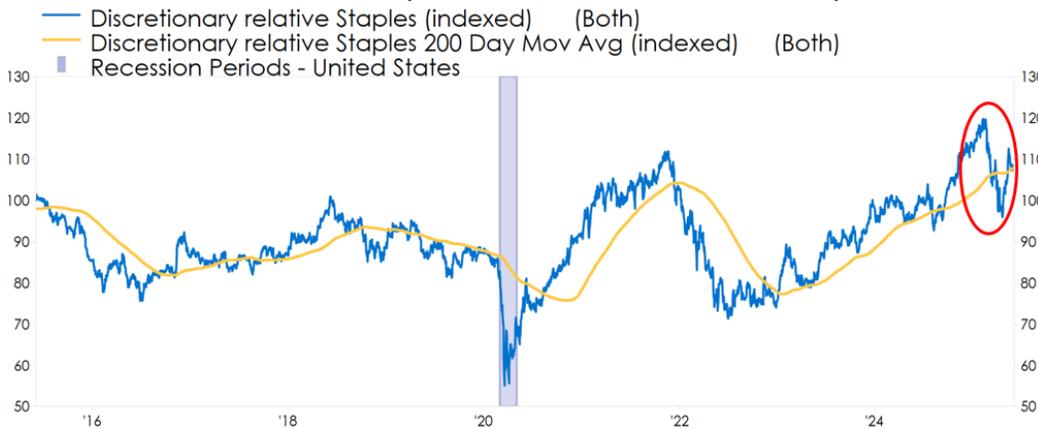
Cyclicals Confirming Earnings Acceleration



Source: Factset; S&P Global Indices with operating EPS defined on a trailing twelve month basis. Discretionary relative Staples is defined as the relative 200 day moving average using the S&P 500 equal weighted sectors indexed back to inception through 6/2/25.

comparing the price action of the Consumer Discretionary sector against the Consumer Staples sector (both on an equal weighted basis using the relative 200 day moving average – yellow line), this relationship tends to coincide with the ebbs and flows of earnings growth – so far confirming the earnings acceleration.

Consumer Discretionary relative to Consumer Staples



Source: Factset as of 6/2/25.

However, the bottom chart suggests some uncertainty brewing. This chart shows the daily price change against that 200 day moving average measure. The recent choppiness of Discretionary stocks relative to Staples stocks (blue line) is



material enough to suggest that we may be nearing the peak in the forward earnings growth rate faster than the consensus expects. Such a change would suggest a downshifting in the profit cycle that has historically come with some rotational leadership changes. The bottom line is that the equity market is grappling with an environment that might lead to a faster maturing profit cycle.

Add to that, the third leg of the stool – a policy cycle that’s abruptly reversing from looser fiscal and (relatively) tighter monetary to one that suggests the opposite. An unhealthy deficit setup is leading to reductions in government spending (tighter fiscal) and higher than anticipated tariff rates are likely to cause the Fed to react in lowering rates (looser monetary) – though this might be delayed due to the inflationary nature they initially cause. This abrupt change in policy is causing investors, consumers and companies to re-think the backdrop. The good news is that the rally in risk assets in the back half of April and into May was a constructive move that flipped the technical script from bearish to bullish. This suggests that the market hasn't deemed anything a foregone conclusion and, as we noted in the opening, the hard data thus far has held up. With what seems like an increasingly large number of potential scenarios still on the table, it’s no wonder that the only certainty might be a high degree of uncertainty.

The Certainty of Uncertainty

Past Policy	Future Policy
Looser Fiscal	Tighter Fiscal
Tighter Monetary	Looser Monetary

So what are the implications and key takeaways for portfolios?

From a portfolio positioning perspective, we continue to emphasize the importance of diversification and balance as a way to mitigate the high uncertainty as referenced above. While diversification has previously been an uncontroversial concept, the concentration present in passive indices today – by virtue of the price action over the last couple of years – suggests this notion remains a relic of the past. We respectfully disagree and earlier this year took the opportunity to rebalance portfolios to maintain that degree of balance. In so doing, we took some profits in US Large Caps and added to our overweight (OW) in US Core Fixed Income. As a result, we’ve remained UW the most expensive and concentrated areas where we’ve viewed the long-term risk reward less favorably.

Within equities, our positioning incorporates balance geographically (tilt toward International) and within our US Large Cap exposure especially. Our bias has generally been to have more exposure to less expensive areas (down market cap vs top). As such, we’ve maintained a larger OW in Cyclical Value and Defensive sectors combined with a smaller sized cap bias. We remain UW the most concentrated and expensive Cyclical Growth areas.



Within fixed income, we remain biased toward the higher quality US Core Fixed Income segment – where we're slightly longer in duration. This exposure remains among our larger OW's in portfolios for diversification purposes though we've also added to International Fixed Income (EW), where the end of negative interest rate conditions has led to more attractive opportunities. Maintaining a higher quality bias means that we still remain UW the most expensive part of the bond market (High Yield) where tight spreads have made this unattractive in our view.

Within alternatives, we remain fairly balanced across the board with neutral positions in Diversified Alternatives, Real Estate and Commodities. Most recently, we adjusted our mix of Diversified Alternative managers in order to provide greater insurance against market volatility by emphasizing income and short exposure – areas that can benefit from choppy market conditions, thus, enhancing diversification.

Above all else, we find investors should keep in mind the following:

- Stay focused on the things you can control like ensuring you have adequate 6-12 month liquidity needs which should allow your long-term investment monies to stay invested.
- Has the structural integrity of your plan changed (purpose of money, time horizon, liquidity needs, risk tolerance)? If the answer is no, then recognize that the economy and the market run in cycles that diversified portfolios are there to help mitigate.
- Short term volatility is often the price one pays for the benefit of higher long-term returns.

Thanks for giving this a read.

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