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Dear MFC Clients,

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“The obscure we see eventually. The completely obvious, it seems, takes longer.” Ed Murrow
Economic forecasting has been challenging since Covid because we are truly in “uncharted waters”. I have seen those very words on too many nautical charts to count over my years of navigation, and, in said areas, trepidation is wise. The breadth and depth of our lack of knowledge, aided by willful ignorance, is gravely concerning. Existential risks appear to be everywhere: AI, nuclear war, natural disasters, floods and pandemics, to name only a few. The result is a cacophony of conflicting opinions that feed a crisis of purpose and a loss of trust. These pressures are rising and to paraphrase Rudyard Kipling – ‘if we can keep our wits, when others are losing theirs, then we must not be understanding what is happening!’ I remain optimistic because while we can be irrational individually, collectively, we will develop solutions. Despair is often the harbinger of enlightenment! Our problems are man-made; no new physics is needed, the solutions simply require a respect for others (aka the Golden Rule) and a commitment to the Rule of Law.

The first half of 2025 has been a mass of contradictions with alternating bouts of elation and depression, but it is hard to discern any real trends or new results. It has been “much of a muchness” in the economic data and most markets are either even or above where they began the year. Hard to believe given all the ‘Sturm und Drang’ over immigration, tariffs, & wars. Here is our short list of the key 1st half data points:

- GDP fell in the 1st Q due to ‘front running’ of the tariffs. All forecasters have been dialing back their annual GDP estimates due to the many uncertainties, which promote inertia.
- The Leading Economic Indicators have been contracting for months, but so far are not indicating a recession.
- Unemployment rates are stable, job growth has been mixed, JOLTS data is cooling but not collapsing.
- Inflation is trending down but remains above the Fed’s target of 2%. Housing costs are the main ‘upward-driver’ while labor, energy, and food costs are flat to down.
- Housing, despite a rise in listings, is forming a bottom with flattening monthly sales (the lowest May monthly sale number since 2009) due largely to the combination of high rates and high prices.
- In sum, the consumer is still spending, and there is evidence of resilience in the face of headwinds, but the year is far from over and many warning signs are flashing!

The markets have been equally resistant showing a small rise in the broad indices up to Liberation Day, then a rapid 20% decline and slow rise back to mid-single digits. The sector performances showed a slightly greater return disparity with Utilities, Industrials, Communication Service, & Financials up by 9-12%, Tech, Materials, & Cons. Staples up by 6-8%, and the remaining sectors are reporting flat to modest declines.

Globally, for the first time in years, we are seeing market returns that dwarf the USA results. The top stock market returns in dollar terms year to date are Hong Kong +20%, the German DAX +18%, Italy +15% and the rest of the major world indices recorded mid to high single digit returns. After more than a decade in the parched performance wilderness, international investors finally have smiles on their faces. Ditto for value investors for this style is finally even-pacing the growth sectors across the capitalization spectrum. The greatest disparity of returns is between the US small cap growth at -12-15% and international small cap growth at +17-20%! As of 6/30/25, the S&P 500 showed a total return of 6.2%.

Fixed income investing has likewise been a tale of two worlds: short and long. Movement in the short-duration bonds up to 10 years has been modest, with a variance of under 1%. Au contraire, long rates have been “whipsawed”, causing indigestion in the pension and insurance businesses. Long known as the ‘boring’ side of the business, it has been anything but. Due to the global geo-political uncertainties, the growth vs. recession forecasts vary widely week to week, resulting in wide swings in long rates. This translated to similar swings in short-term profits/ losses, which upset the bond markets where consistency and stability are valued. While there was weakness in May in both the US and Japan 20-year Bond sales, the subsequent auctions, which average \$50bn a month, have done well. A real danger to watch for is a declining attendance and/or bids at said Treasury auctions forcing rates to rise, thus precipitating a crisis. Add one more to our lengthening list of Existential Crises! Ultimately, it is a confidence game, and President Trump’s actions, like them or not, are inspiring more uncertainty than confidence amongst the rest of the world. It is time to dial back the inflammatory rhetoric.

Turning closer to home, your portfolios have more than enough cash and bonds to cover all near-term expenses. We are finally earning real yields (after adjusting for inflation) of between 1-4%, starkly different than several years ago. Investment grade debt trades around the 5%+ mark, which is excellent given their balance sheets and state of the economy. High yield can reap near-equity returns of 7%+. Even humble cash earns 3.5-4% over the past 12 months. These rates will fall, but they are still comfortably above the flat to declining inflation figures, thus providing a ‘real’ yield!

Growth stock funds have predictably suffered ytd, yet value funds have provided both ballast, balance and returns. Our small-cap allocation witnessed double-digit declines, and these were only partially offset by our international funds, as the latter is usually a smaller percentage allocation due to years of underperformance. Overall, this is how we hope a diversified portfolio works: the ‘strong’ shelter the ‘weak’; unfortunately, these roles change with great unpredictability!

Our voyage through uncharted waters will require courage, adaptability, and a willingness to embrace the unknown. New technologies and innovative approaches will be crucial to navigating these waters. The risks are well known: on the one side is the high interest rate ‘Rock of Scylla’, and on the other side are the ‘Charybdis Whirlpools’ of declining demographic/GDP growth. Both are perilous, so to keep life simple, my advice is to check that the 10-year T-Note rate lies between 4-5% and then go about your day. For those that would like to see a practical plan to address our fiscal incontinence, Google ‘Ray Dalio’s 3% solution’, which he is pitching to Congress.

It is always a good time to count our blessings, and we need to focus more on the things we agree on, which are many, and practice ‘selective deafness’ to the issues that divide us. Never forget to find some amazement in every day. Please do call or email us if you have any questions or concerns about your investments.

Best, Lanny, Teri, Kurt, and Liz