RESEARCH CAPITAL CORPORATION

SPECIAL NOTE

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A SLIGHT CHANGE IN GEAR

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The first few months of 2025 have been anything but boring. My notes below summarize my overall thoughts on what I believe could be happening in the current economic/market environment. I've tried to use bullet points so as to keep from getting bogged down in too many details as there is a lot to cover.

The market has seen extreme volatility over the past few months – down and back up again. To be back up close to the index peaks given weak consumer and corporate sentiment indicators, is in my mind, a gift opportunity to shift gears and prepare for the fairly reasonable possibility of a recession and further market dislocation and volatility. It was likely we were headed toward a recession coming into 2025, even without trade disputes. Investment sentiment appears complacent in light of the extreme economic uncertainty and erratic nature of recent trade related events/ announcements/ executive orders/ deferrals/ walkbacks/ threats, etc. It is changing daily and nobody knows exactly where this will end up.

Consumer spending slowed considerably over the past year. The economic tailwinds of excess savings from Covid lockdowns appear to have been mostly spent. In 2025, consumer facing companies have been adjusting their growth and earnings forecasts down (Walmart, Target, Lowes, Home Depot, to name a few). Airlines have been lowering forecasts. Domestic North American airline leisure travel is down significantly. These are signals of a weakening end consumer.

Corporations are lowering their spending plans and/or stalling until they receive further trade/tariff clarity.

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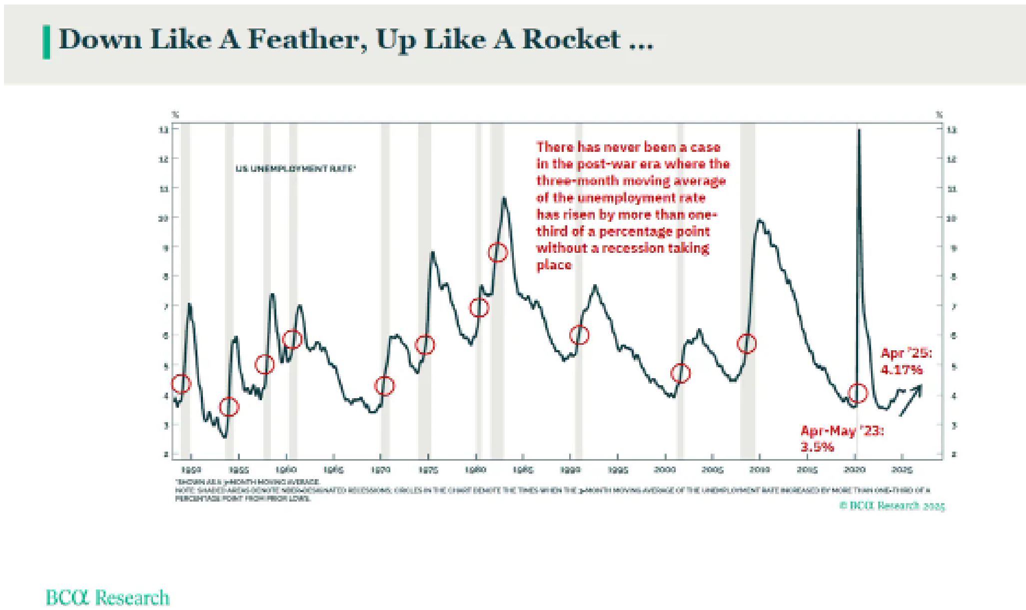
The labour market has started to slow. It might not seem like much right now, but the chart below shows what tends to happen as unemployment rates begin to rise. It could accelerate quickly from here.



Public companies are pricey now. An economic slowdown/recession is not currently priced in. That's irrespective of trade issues. If a slowdown is starting, corporate guidance will continue to guide lower or be pulled all together. In addition to this, companies that cannot pass all tariffs onto consumers will have to absorb them, causing a margin squeeze and a re-rating of equities.

Bringing production back to the US is not an easy task after decades of globalization.

I think it is reasonable to expect impulsive, maximum shock value, and erratic behaviour from the US government for the next 3 years. As a result, equity risk premium should rise.

I think an examination of high valuation companies that are more susceptible to an economic slowdown or trade shocks is warranted. My overall recommendation is to reduce or trim exposure to high-growth companies and skew more to defensives, add quality fixed income and cash alternatives, and increase European exposure. Within North America, tilt to companies that are more immune to tariffs with stable revenue streams. It's not an all-or-nothing situation. Please view this as an overall perspective or lens through which we can craft our portfolios to prepare for the next few years.