HUDSON VALLEY INVESTMENT ADVISORS, INC.
A subsidiary of Orange County Bancorp, Inc.

First Quarter Outlook

As of April 2, 2020

Economy In Review

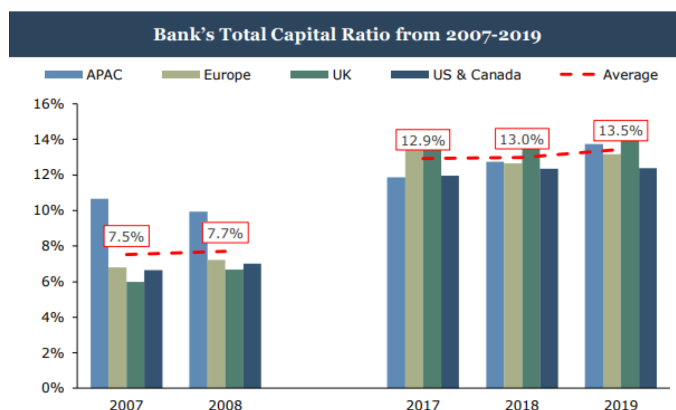
First quarter 2020 was the most volatile in stock market history. In addition to the equity markets, the public debt markets also saw a significant dislocation. Based on historical indicators we had potentially started the bottoming process in the equity markets thought high volatility still remains. However, it is lower than just a few weeks ago. Fixed income markets also partially returned to normalization. To review, the stock market started the year being near an all-time high. The economy was robust with the outlook showing continued strength; interest rates were low and expected to remain stable. The U.S. and China came to a trade agreement. The U.S. consumer was looking at record high confidence, strong job and housing market that looked to be taking another level of growth. The Coronavirus "COVID-19" came into focus in China during the middle part of January. This caused a supply shock as manufacturing in China was put on hold. Countries that maintain supply chains were impacted by limited supply of products and "work in process" interruptions. This was immediately followed by an energy shock as Russia and Saudi Arabia disagreed on oil production cuts. The ensuing supply disagreement pushed oil prices down over 65%. If that wasn't enough the COVID-19 virus then impacted the U.S., forcing the President and numerous State Governors to call for restrictions and the closing of businesses across the U.S. This combination of events placed the U.S. in a forced recession that should reverse once individuals and companies go back to work. The forced slowdown was put in place to slow the COVID-19 pandemic and lower the potential death rate.

To alleviate the negative impact from the Government-induced recession Congress put through a stimulus package of close to $2.0 trillion. We believe that this program will be extremely helpful to "bridge" the recession which is reducing demand for consumers and businesses. To provide some perspective, the U.S. Economy is approximately $20 trillion in GDP per year. Each quarter generates U.S. GDP of $5 Trillion. If we lose 50% of quarterly GDP we would see a $2.5 trillion decline of the normal $5 trillion quarter. The Government stimulus program, if started as fast as claimed, should allow some of the demand to stabilize and allow the economy to come back on line and allow for stabilization and a return to potential growth. We now stand at a point in time that the waiting for businesses to get back on line, revenues, earnings and risk are able to normalize.

The credit markets, in turn, became a major concern. The financial "plumbing" for the U.S. financial system saw a significant increase in risk. Spreads, the difference between government "risk free" securities and high yield bonds, saw the largest difference in a number of years. Commercial paper (short term financing), and repurchase agreements (Repo's), which is a main tool for financial trade, all saw their rates rise. This rapid increase in rates indicates stress in these markets and the potential of credit markets freezing up, which would halt commerce. This building stress worried government officials as capital flows had the potential to stop on a worldwide basis. To their credit, the U.S. Federal Reserve was proactive in lowering rates and adding liquidity into the financial system. Other measures were taken to limit the potential of the U.S. financial system from freezing up.

In spite of the negatives listed above, one has to remember that this is not the 2008 financial crisis. The center of the '08 crisis was the banking sector. It is now the most secure it's been since World War II. Most banks today have strong balance sheets holding the least amount of debt in a few generations. Housing is well positioned with only 3 months of inventory vs. over 13 months of housing inventory in '08. Both interest rates

and gas prices being lower, should help consumers over the shorter term. In addition, we are expecting individuals and businesses to be back at work. This should help to get the economy back on track in a more normalized level. A large number of unemployment is expected to be brought back once the virus subsides. Individuals are sitting on strong balance sheets and have been increasing their savings while limiting borrowing having learned from previous downturns.



We realize at this point in time fear has taken over versus potential. We focus on earnings as a guidepost for market direction. We believe that markets are discounting a continued negative demand for an extended period of time. Our thoughts are that the rebound is being built. As this "spring of pent up demand" is growing, companies will resume their business practices. Consumers' pent up demand should help propel markets to a higher level of growth than what is currently being expected.

Finally, the race for the 2020 Presidential election is still on and we believe that some of the populous ideas that were present and creating risk may be dampened during this warlike period that bands individuals together. We believe that we have potentially reached a generational buying opportunity in the equity markets and that in retrospect have benefited from maintaining equity positions during this period.

Present

During the quarter, the S&P 500 saw both the largest historical point drop and also the largest point gain all within a few days. The volatility was due to the shocks to both U.S. demand and supply sides of the economy, coupled with the dislocation of credit markets. The expectations for both revenues and earnings are discounting a worst case scenario. This is due to the U.S. Government has taken the unprecedented steps to making the economy close down and move the U.S. into a recession. This is one of the reasons we believe things will come back strongly as the normal "imbalances", such as inventories, credit, etc.…, were not the reason for the slowdown. Demand was strong and the expectation for future growth was ongoing. We are now in a position in which estimates are non-existent. The current environment does not have a similar scenario to use as a framework. We believe that the closest 2020 can be related is to 1987, where the market saw a 37% drop and rebounded to see positive results by year end. We believe that the economy drives financial markets. There is a dislocation between the economic environment and stock market returns. The longer this continues the bigger the impact to future earnings results. As long as interest rates remain accommodative we believe we will remain in a trading range until markets gain revenue and earnings clarity from the current COVID-19

quarantine.

In addition to the COVID-19 ramifications, we still are in the midst of a Presidential election and period in which we will have policy disagreements due to the recent $2 Trillion dollar fiscal stimulus bill. We believe that divisions may appear regarding the amount of continued stimulus needed to support the economy and the large budget deficits being created. Another area that has taken a backseat is that of overseas relations. At the time of this letter, China appears to be getting back to normal with workers returning to work and industrial production restarting. A number of U.S. companies have indicated that they need to reexamine the location of their supply chains and if China locations make sense. Several experts put the U.S. situation one month behind China. President Trump is being proactive in trying to get workers back to work in a faster than anticipated manner. Expectations are for workers to return to work at the end of April.

In spite of the dire scenarios this is also a time a stress and change. Often this changes investment landscapes and individual investments. We feel that digital payments, online transactions and technology that aids on line learning are areas that may see greater demand as we move forward. We also expect the U.S. to remain the best economy positioned for continued growth. Domestic investments and will be better situated compared to their overseas counterparts.

Since our founding in 1995, our returns have been driven by a formulated investment process that starts with our top down analysis of economic inputs. Our equity investment focus is Growth at a Reasonable Price (GARP) while concentrating our fixed income on quality income producing investments. Of the S&P 500 groups, all eleven groups reported negative returns for the quarter. Returns by sector were as follows: Technology (-12.22%), Healthcare (-13.07%), Consumer Staples (-13.39%), Utilities (-14.19%), Communications Services (-17.23%), Consumer Discretionary (-19.59%), REITs (-19.84%), Materials (-26.6%), Industrials (-27.41%), Financials (-32.34%), and Energy (-51.06%). At quarter end we expect the economy to start the healing process as companies return to work and the economic process of a market economy moves forward and tries to retain the momentum seen prior to the slowdown.

Outlook

U.S. GDP growth is anticipated to see a historically sharp decline followed by a second half that could provide a potential record advance. Recent reading of economic statistics is no longer relevant in the short term as the focus is more directed to the healthcare crisis. Financial markets will move before the improvement will be seen in COVID-19, investors are looking at the rate of change in virus cases. The improvement in the economy should come in the back half of the year as normalcy comes into focus. We are confidence that we will see a "normality" in markets as we pass the height of the virus and consumer get back to work. Expectations are for pent up demand to spike as the virus fades. Europe and other parts of the world try to overcome prior "non-virus" issues that were never addressed after the '08 financial crisis and are now impacting their economies.

We expect revenues to come back off of depressed levels and that investors will focus in a greater way on 2021 expectations. The damage done to the financial markets will require continued government intervention. Based on past market shocks we should expect a sideways movement in markets until a clearer picture emerges for demand, revenues and earnings potential.

After considering the economic positives and the noted risks, the S&P 500 is discounting a poor environment, with earnings expectations low, risk high and outlook murky at best. We are expecting normalization in business activity as the year progresses, interest rates to remain low and the effect of a record amount of financial stimulus to work its way through the economy. It's difficult to estimate what comes next but we are bullish on the U.S. versus the rest of the world as we have the most adaptive economy in the world, an innovative workforce and an economic system that rewards hard work, adaptability and innovation. We are keeping an eye on the way the economy comes back, what other effort that the government pushes forward to support the economy and the way consumers return to their everyday routines.

Summary

Hudson Valley Investment Advisors, Inc. continues, over the longer term, to favor equities over fixed income. Over the past few quarters the higher level of volatility has allowed HVIA and our clients an opportunity. We have taken this opportunity, where appropriate, to rebalance portfolios to take advantage of the market pullback. This allows for better positioning into the future. In many circumstances we have adjusted sector weightings, removed companies, as well as, added companies that have previously held valuations too high to be considered for our strategy and clients.

The economy was shut down by government efforts to stem the COVID – 19. Economic imbalances (inventories, debt, etc...) were limited prior to the recession and monies have been put in place to bridge the U.S. economy to get us past the time when economic activity was held back. We anticipate that the COVID-19 will end and the economy will get back to working in a more traditional manner. The differentiation among investments has begun and the passive investing may no longer be as beneficial as we move forward. The Federal Reserve is extremely accommodating and will provide economic support for an extended period as we come out of this unprecedented time. One last thought is that we are in this for the long term, our firm has helped investors for 25 years. We are here for our clients, we are here to speak with you to relieve your fears and provide insight. You can also hear and see our thoughts on our website. There you will find videos and audio content that provides some of our insights. Again, overall, even though growth in the U.S. has slowed in the short term, we feel that equities for the long term will be the best place to invest, in fact we believe we've potentially made a generational low recently, and will be in a better position compared to fixed income over the short to intermediate term.

Hudson Valley Investment Advisors, Inc. continually strives to meet your investment goals in the forever changing market environment. We will continue to apply our process to allow your portfolio to benefit from our insight and investment strategy.

We welcome you to take a look at our website http://www.hviaonline.com which now has educational videos, market updates, thought pieces and recent TV appearances. In addition, our Facebook page, Hudson Valley Investment Advisors, Inc., provides insight that investors should find useful. We welcome your feedback and thank you for your support as clients.

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