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HUDSON VALLEY INVESTMENT ADVISORS, INC.

A subsidiary of Orange County Bancorp, Inc.

THE DELIBERATE INVESTOR

Gus Scacco

CEO and Chief Investment Officer

Hudson Valley Investment Advisors, Inc.

Gus brings over two decades of experience investing on behalf of individuals and institutions. If you watch Fox Business, you'll often see Gus as a regular guest talking about the markets. When he's not looking after portfolios, Gus is active with several not-for-profit organizations across the Hudson Valley.

For information on our latest client events and economic updates visit:
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Economy and Markets in Review

Q2.2025: Outlook & Market Commentary

Q2 2025 Dashboard

Markets: S&P 500 Index: 10.5% Q2 return, 5.5% YTD return thru 6/30/2025

Interest rates: FOMC held rates steady at all four meetings so far this year (currently 4.25-4.5% target range)

Economy: -0.5% annualized Gross Domestic Product (GDP) contraction in Q1 2025 (versus +2.4% growth in Q4 2024 and +3.1% growth in Q3 2024)

Inflation: 2.4% increase in Consumer Price Index (CPI) over 12 months through May

Q: Gus, what were the defining themes of the second quarter?

GS: I think there are three main themes that really shaped the quarter: inflation, tariffs and geopolitical developments.

Q: Ok, so let's talk about inflation first. We know that the pace of inflation has slowed over the past few months. What does the inflation picture look like now, and where are we still seeing hotspots?

GS: There are three main areas that affect inflation, and therefore three areas the Fed will be watching closely to determine whether to lower rates. Those are: labor, housing and goods.

On labor, we are seeing stable to declining costs. Job openings have declined, while hiring has been steady if not on a slight uptick over the past quarter.

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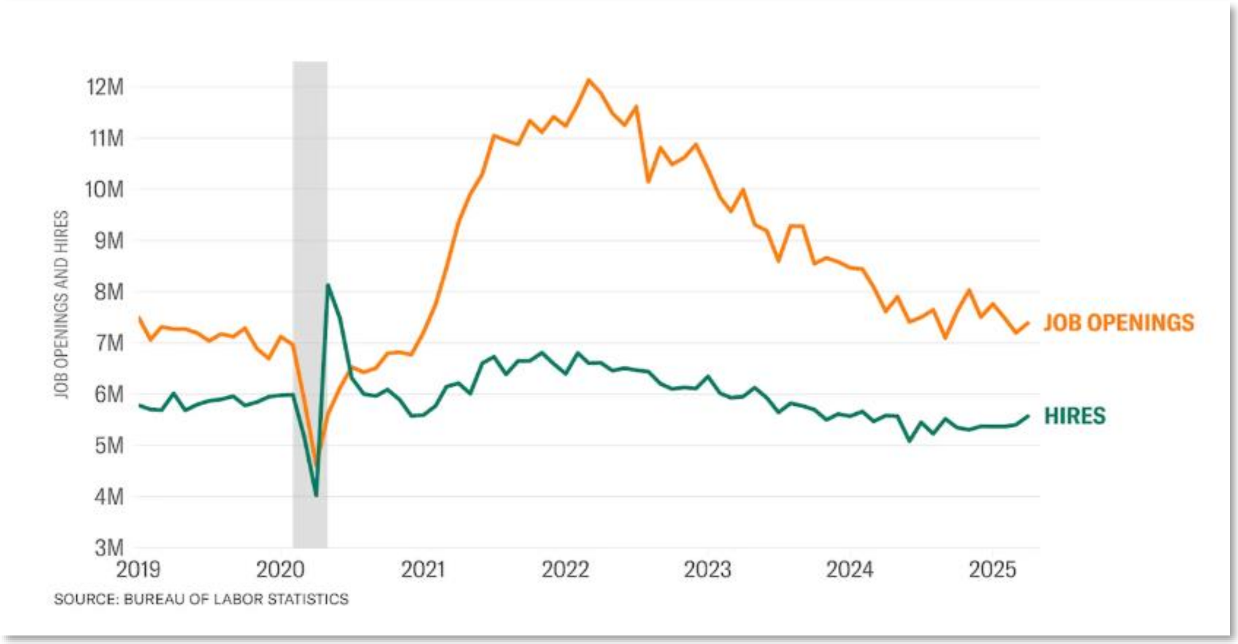
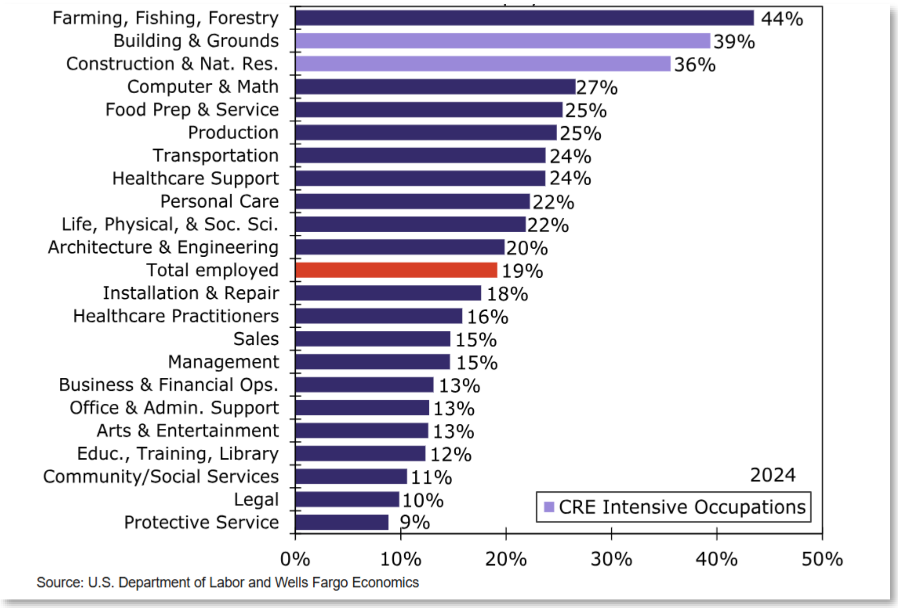
Economy and Markets in Review (continued)



Q: Speaking of labor, one of the things we've spoken about in the past is how integral immigrant workers are to our labor force. Give us a sense of where those immigrants work. Are most day-laborers?

GS: There are certainly a significant number of immigrants who work in manual labor jobs, but when you look at the statistics it's spread across quite a few different sectors of the economy. As you'll see from the chart below, it's quite a diversity of job types including many professional services roles. As I've said before, we need immigrants to make our economy go.

Foreign-Born Share by Occupation : Percent of Total Employed



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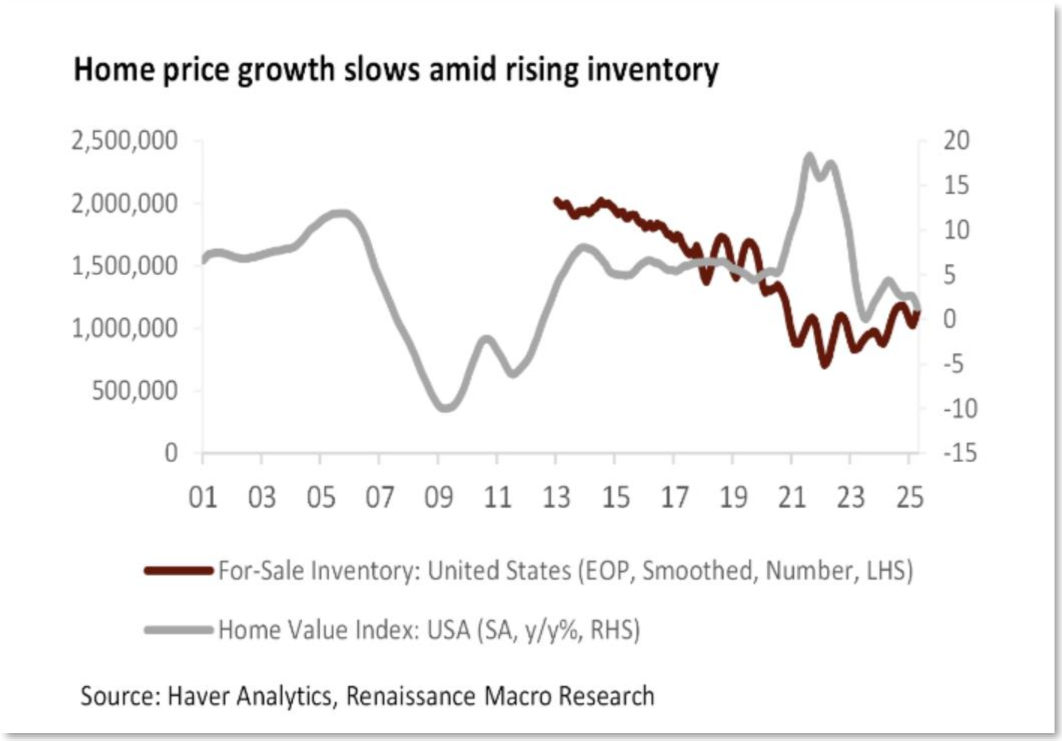
Economy and Markets in Review (continued)

Housing is one of the stickiest areas of inflation—and one of the last components to come down after a period of high inflation. As rising home prices have fallen off and the supply of available homes climbs, we expect a leveling off of rents.

With respect to goods, we're seeing a supply shock as China has been flooding the market with inexpensive products. One example is a Chinese car assembled in Mexico that sells for US$19,000, which would be the equivalent of a $30,000 U.S.-made car. This advantage of having car factories in Mexico (to get around tariffs) has given the company a 20% share of the Mexican car market; they had zero market share five years ago.



Q: We've spoken of a 'two-consumer' economy in past issues of The Deliberate Investor. Is that still the case?

GS: Absolutely. The first group of consumers tends to be older with higher income. They're generally retired Baby Boomers, they're sitting on $45 trillion in stocks, bonds and mutual fund assets. They have a house paid off and are often sharing it with their kids. Why is their income higher? With interest rates where they are, they're getting a 4½% to 5% yield on their assets—and they're spending it.

For that second consumer type, they tend to be younger, still working, still saving for retirement and still have a mortgage. And they may have children, elderly parents or both at the same time.

That first group is part of what's fueling the continued strength of the U.S. economy.

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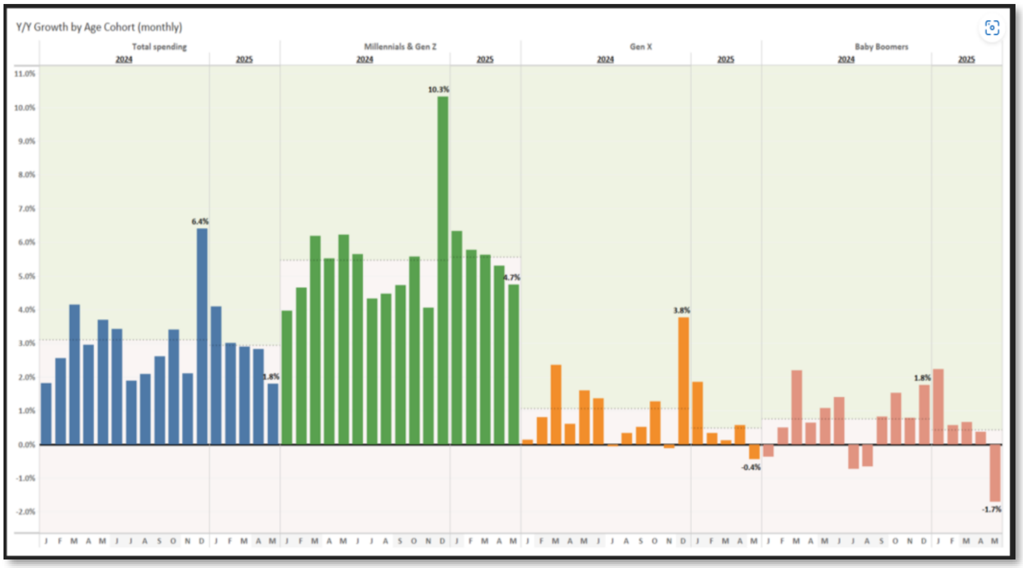
Economy and Markets in Review (continued)

Q: What if we look at consumer spending more strictly by generation or age cohort? Any interesting trends there?

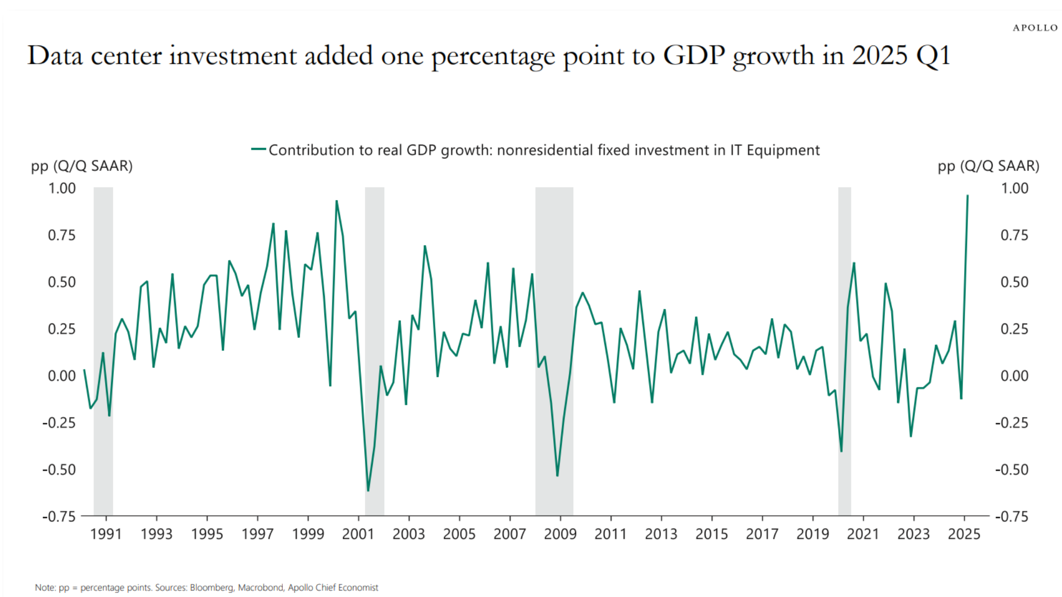
GS: Well, as you'll see in the chart below, Millennials and Gen Z spending is growing much faster than that of Gen X and Baby Boomers over the past 12 months.



Source: McKinsey

Q: Speaking of the strength of the economy, what other factors are giving it that staying power?

GS: The economy is also benefiting from buildout of data centers that will support artificial intelligence-related business. As you'll see from the chart below, that accounts for one full percentage point of GDP growth.



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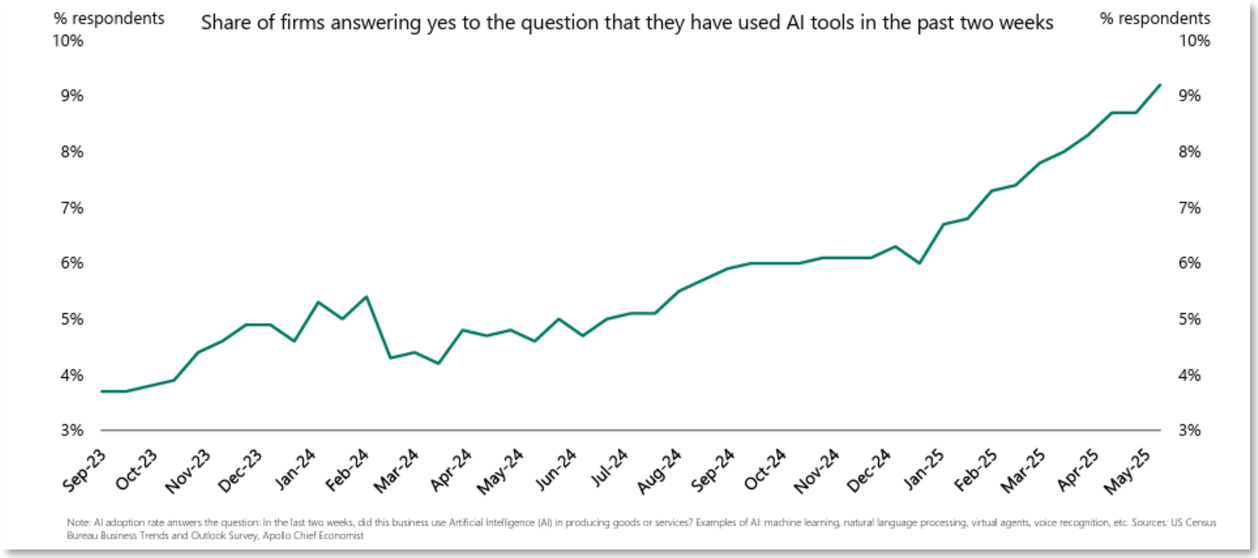
Economy and Markets in Review (continued)

Q: Wow, so this seems to provide support for the "AI trade"? Is it fair to say that AI continues to broaden out to non-tech areas of the economy?

GS: Yes, and in fact the number of companies that are using AI continues to grow. It's the anticipated productivity gains that explains the market's enthusiasm for AI-related businesses.

More companies are using AI: Productivity gains are coming

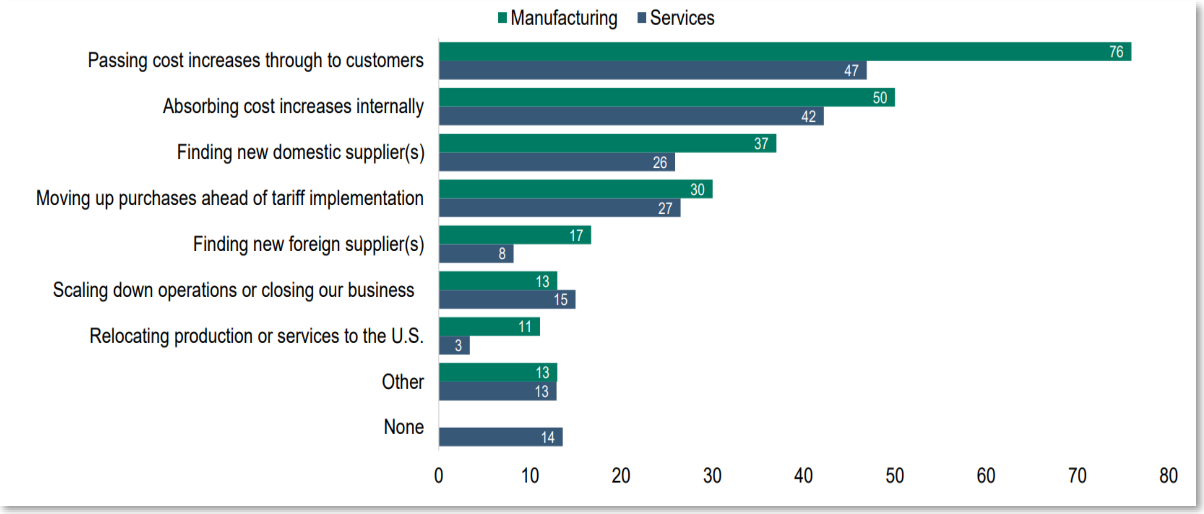


Source: Apollo

Q: That leads nicely into U.S. trade policy. Where are we with the tariff situation?

GS: Overall, we think the tariff situation will level the playing field over the medium to long term, despite some short-term cost increases and market volatility as we move through this period of trade negotiations.

Actions firms are taking in response to higher tariffs



Source: Federal Reserve Bank of Dallas, Apollo Chief Economist

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Economy and Markets in Review (continued)

The U.S. is the world's largest supermarket, and the administration is using tariffs as a way to reset our trading relationships with countries around the world. Over the quarter, we saw fresh agreements with China, Canada and Mexico, and more in the works with other countries.

And of course, we'll see if the end of the 90-day tariff pause goes into effect as planned on July 9… the administration has indicated there may be some flexibility there. And markets have certainly rallied in anticipation that some deals will come out of that.

Q: So, what's happening with the onshoring trend?

GS: Our view is shaped by the manufacturing and municipal worker organizations we speak to in New York State, for example, and they comment about how they are looking to regain manufacturing here. What we're seeing is more exports of U.S. goods.

Starting back in the '70s and '80s, Japanese companies set up car assembly plants in the U.S. as a way of escaping tariffs. Over time, foreign-owned auto factories popped up in places like Marysville, Ohio and Chattanooga, Tennessee; Spartanburg, South Carolina and Marietta, Georgia. We're going to see more of that. The U.S. has the lowest percentage of exports that are not commodities.

The U.S. is the largest supermarket in the world for other countries.

Q: Let's wrap up our review of the economy and markets with the geopolitical situation.

GS: Right now, there are multiple hotpots around the world. Between Israel-Hamas, Russia-Ukraine and Israel-Iran conflicts (not to mention Syria), we think the maximum geopolitical upheaval has been dialed back at this point.

The U.S. attack on key nuclear enrichment facilities in Iran has set the country back months if not years. Even though early reports are that the underground facilities themselves were not destroyed, the damage done on the surface entrances to these facilities make them very difficult to reconstitute any time soon. This is changing the Middle East calculus, and time will tell if a ceasefire will eventually lead to a broader peace in the region.

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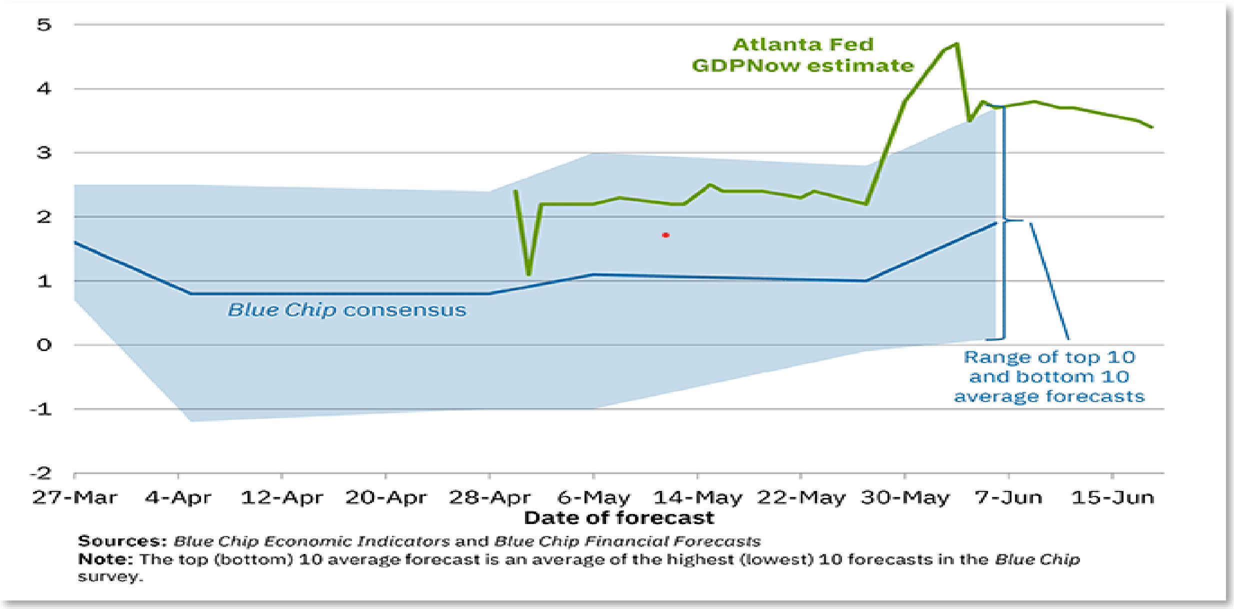
Outlook

Q: Where does the economy go from here?

GS: GDP is one of those lagging indicators, and we think GDP may bounce back in the second quarter from its first quarter contraction. The Atlanta Federal Reserve's GDPNow estimate for Q2 as shown in the chart below estimates Q2 real GDP to be around 3.4% near quarter end.

Evolution of Atlanta Fed GDPNow real GDP estimate for 2025: Q2
Quarterly percent change (SAAR)



Q: Do we expect interest rate cuts?

GS: We do expect two cuts from the Federal Reserve this year, but it doesn't matter much even if they do decide to cut rates. Much of it hinges on the broader impacts that tariffs will have on the economy and what happens with the labor market.

Q: Given that consumer spending represents roughly two thirds of US GDP, how do you expect that to evolve over the next quarter or two?

GS: We think the consumer is holding up well through all the turmoil. That first group of consumers who are retired continue to eat out at restaurants and spend. And millennial/Gen Z spending is up significantly year over year. Expect that to continue.

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What this Means for Your Portfolio

Q: Have there been any changes in client portfolios over the quarter, either in response to market conditions or for other reasons?

GS: We added eight names to the portfolio to reduce the risk of the overall portfolio by reducing position sizes. We typically have 40-some stocks in the portfolio, now we hold over 50.

Q: So, has that impacted sector exposure?

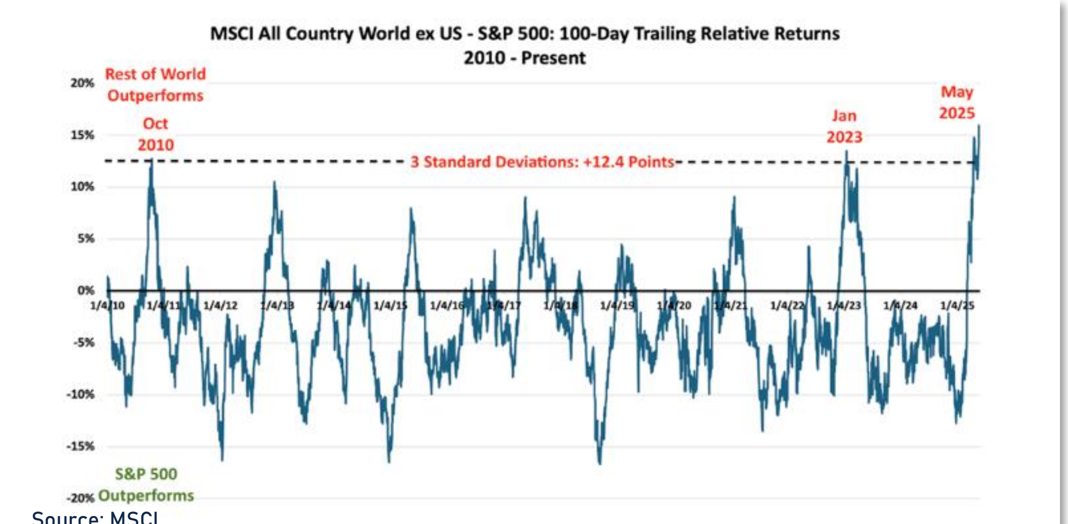
GS: Not really. We still have our overweights to industrials and tech, for example. We've just dialed down the stock-specific risk while keeping sector allocations largely the same.

Q: What other opportunities have surfaced for the HVIA investment strategy?

GS: Our patient, deliberate approach has enabled us to buy undervalued stocks that would normally be too expensive for us to buy on a valuation basis.

Q: International stocks have been doing quite well this year. How does that square with HVIA's philosophy of buying US-based multinational companies?

GS: If you look back over the past 15 years, the U.S. has performed better than non-US stocks (see chart below). Why is that? If you look at the 10 largest firms in the world, nine of them are US-based. If I'm looking at the leading technology companies, they're almost all US-based. Our software helps us with more productivity gains than anywhere else. That's where the difference is.



Source: MSCI

But it's also the fact that we have deep liquid pools of capital that are utilized here and not overseas. So, you have more companies getting funded here if you have a good idea.

Another point is that our strategy gets non-US exposure through multinational companies, which means we are still participating in the performance of overseas businesses but with the benefit of a stable U.S. regulatory framework.

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Q: So, final question: "Recession" was on the tip of everyone's tongue not that long ago. Where does the economy stand?

GS: The economy has exemplified significant resiliency, and it seems likely that we will stay out of a recession, barring any outside events that could have an impact on employment. As a result, continued growth may very well be the outcome throughout the remainder of the year.

You might be familiar with the acronym RMD?

RMD, or Required Minimum Distribution, is the minimum amount of money you are required to withdraw annually from most retirement accounts, like traditional IRAs and 401(k)s, once you reach a certain age (currently 73). It's essentially the IRS's way of ensuring that you eventually pay taxes on the money you've deferred in these accounts. Even at age 70, now is a great time to talk to your tax professional to determine where you stand with your RMD situation and start preparing for the coming year end requirement. IRS penalties for not taking your RMD can be quite substantial, so plan accordingly.

Hold the Date: Annual Client Event

People say that time flies when you are having fun. 2025 marks the 30th anniversary of Hudson Valley Investment Advisors, Inc.! We have historically held this event later in the fall, but this year we are changing things up a bit and we will be holding our Annual Client event on Wednesday, September 24, 2025.

West Hills Country Club will, once again, be the location for this event with an anticipated start time of 5:30 p.m. In the coming weeks, please be on the lookout for both an email correspondence and a formal mailed invitation with the details and RSVP information.

We'd love to see you there!

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