

MARKET COMMENTARY

Q3 2025

MARKET REVIEW

The third quarter of 2025 delivered broad gains across global markets. Equities benefited from easing trade tensions, ongoing enthusiasm around artificial intelligence, and rising confidence that the Federal Reserve will begin lowering interest rates in the months ahead. These forces combined to lift investor sentiment and extend the market rally.

Growth stocks led global markets as excitement around AI spending remained strong. The U.S. equity market advanced on solid second-quarter earnings and a resilient economy, even as labor data revealed cooling job growth. International stocks also performed well, with Asian markets leading the way after an extension of the U.S.–China trade truce and renewed support for domestic chipmakers. Emerging markets broadly outpaced developed peers, helped by a softer U.S. dollar and improving global demand.

Bond markets were volatile but ultimately positive. Government bonds rallied as investors shifted focus from inflation to slower growth. The Federal Reserve lowered its policy rate by a quarter point in September, its first cut of the year, and signaled that further easing may follow if inflation continues to moderate. Credit spreads tightened and high-quality corporate bonds delivered steady returns, supported by solid earnings and manageable default risk.

Commodities ended the quarter higher, led by strength in precious metals. Oil prices slipped slightly as expectations of a supply surplus outweighed geopolitical risks. Gold continued to attract buyers seeking stability amid policy uncertainty and lingering inflation concerns.

Economic data reinforced a picture of gradual cooling rather than sharp contraction. Consumer spending remained resilient, but hiring slowed and unemployment edged higher, suggesting that the economy is moving closer to balance. Inflation drifted upward to just under 3 percent year over year, yet the impact of tariffs has so far been less severe than many feared.

Despite the mixed signals, the overall market tone remains constructive. Corporate balance sheets are generally healthy, consumer confidence is holding up, and financial conditions have eased slightly as rate expectations shift lower. The combination of durable spending, slowing inflation, and strong cash flow generation has provided a supportive backdrop for risk assets. Still, with growth moderating and valuations elevated, investors appear increasingly selective, favoring companies with consistent earnings, strong pricing power, and exposure to structural growth themes such as artificial intelligence and infrastructure investment.

LOOKING FORWARD

GOVERNMENT SHUTDOWN, EPISODE 21

While volatility often rises when economic data is delayed, markets have historically viewed government shutdowns as political theater rather than a lasting economic threat, with equities typically steady or higher once operations resume. This shutdown, however, may pose greater risk. Threats of permanent cuts to the federal workforce and the possibility that furloughed employees will not receive back pay could weigh on both employment and consumer spending.

DUDE, WHERE'S MY DATA?

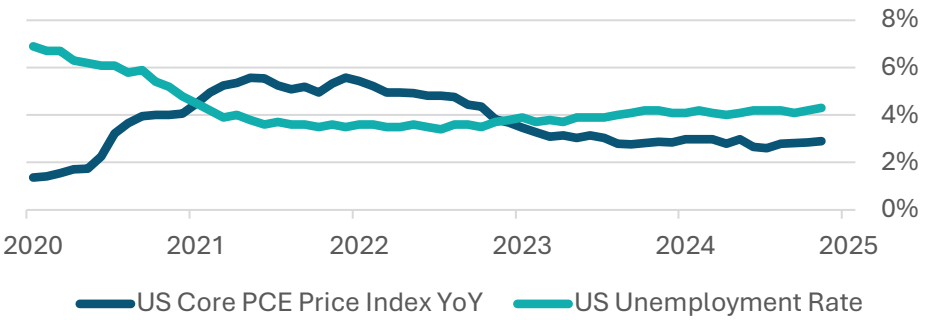
The absence of timely economic data leaves the Federal Reserve navigating a difficult policy crossroads. Core inflation remains stubbornly above target while unemployment edges higher, forcing policymakers to weigh whether to cut rates to support the labor market or hold them steady to ensure inflation remains in check. The situation is further complicated by uncertainty over how new tariff policies might stoke inflation and by mounting political pressure on the Fed to begin lowering rates.

ARTIFICIAL OPTIMISM?

Many investors are concerned that the market's enthusiasm for artificial intelligence resembles the euphoria that preceded the dot-com bubble. This concern is understandable, as major technological revolutions often go through a period of exuberance when optimism runs ahead of near-term fundamentals. However, the environment today has some notable differences. Today's leading AI companies have very deep pockets and are supported by well-established business models rather than speculative concepts. While valuations have risen, the recent five-year rally has been far more measured than the surge that led up to the 2000 collapse, suggesting a more grounded, though still speculative, phase of innovation.

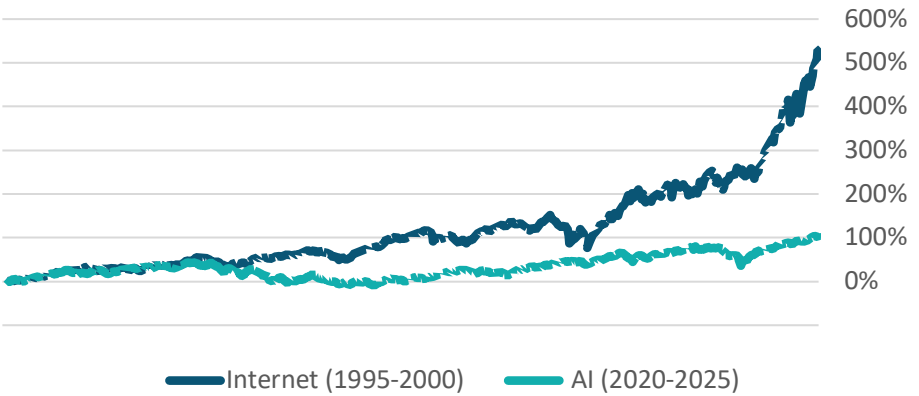
U.S. Government Shutdowns	
Number of Government Shutdowns (1976–2019)	21
Average Length (Days)	8.2
Average S&P 500 Return During Shutdowns	+0.3%
Average S&P 500 Return 12 Months After Shutdowns	+12.7%

Policy Crossroads



Nasdaq Performance

Internet vs Artificial Intelligence



OUR TAKE

Despite steady headline numbers, the underlying story of the economy is becoming more complex. Growth remains positive and inflation has moderated, but both trends mask a widening divide beneath the surface. Consumer strength has become increasingly uneven, corporate earnings are relying more on cost controls than true revenue growth, and markets are being lifted more by optimism surrounding rate cuts and artificial intelligence than by broad-based economic momentum. With so much of today's market performance driven by these narratives, investors should recognize the risks and be prepared for volatility if reality fails to meet expectations.

Will the Federal Reserve deliver on rate cuts? Currently, the Fed's projections and market pricing are broadly aligned, suggesting two additional quarter-point cuts by the end of 2025. Yet with the Fed positioned squarely between stubborn inflation and a softening labor market, expectations could shift quickly as new data emerges. Historically, when forced to choose, the Fed has tended to side with preserving price stability. That priority reflects the need to protect the central bank's credibility and preserve confidence in the U.S. dollar as the world's reserve currency. While higher unemployment is painful in the short term, it is far easier to repair than a loss of confidence in the central bank.

Left to its own judgment, we believe the Fed will likely move more cautiously in cutting rates than either markets or the Trump administration would prefer. But will the institution yield to political pressure or change direction once the Fed Chair's term ends in May 2026? For now, we believe that risk appears limited. The Fed has weathered political interference before, and its structure is designed to protect it from short-term political cycles. Recent Supreme Court commentary reaffirmed the independence of its leadership, and the 14-year terms of Fed Governors help insulate the institution from abrupt shifts in policy.

Fiscal policy will also be a source of risk in the quarter ahead. While the government shutdown is unlikely to disrupt markets immediately, it does not inspire confidence in the U.S. financial system, which is already strained by unsustainable debt levels and unpredictable trade policy.

These challenges have encouraged many countries to look for ways to store value outside the reach of U.S. regulation, a trend that has contributed to the nearly 10 percent decline in the dollar year to date and supported alternative stores of value such as gold and bitcoin. Unless the U.S. restores fiscal discipline soon, we expect this gradual erosion of confidence to continue. Considering these risks, we continue to limit exposure to long-term Treasuries, which remain sensitive to inflation expectations and concerns about government solvency. Instead, we favor assets that tend to hold or gain value as the dollar weakens, including gold, international equities, and inflation-protected Treasuries.

Investor enthusiasm for artificial intelligence remains another defining feature of today's market landscape. By most measures, large-cap technology valuations are elevated relative to history, and every major technological revolution, from railroads to the internet, has produced periods of excessive optimism. Yet today's AI leaders differ meaningfully from the speculative startups of the dot-com era. They are highly profitable, well diversified, and deeply embedded in the modern economy.

Even so, volatility should be expected as lofty expectations meet operational realities. While we are optimistic about long term AI applications, the current level of market concentration and valuation leaves us cautious. We are defending against these risks by maintaining global diversification, modestly underweighting AI-linked companies within U.S. equities, and overweighting defensive sectors. We are also deploying more active management to focus on fundamental strength and avoid speculative hype.

It is also worth remembering that many of the risks discussed here have been present for well over a decade. Investors who allowed these concerns to drive their decisions missed out on substantial gains. Even someone who invested in the S&P 500 at the peak of the dot-com bubble has seen their investment grow more than sixfold. History shows that technological innovation, while volatile in the short run, has consistently been a powerful driver of long-term wealth creation. Staying invested through periods of uncertainty remains the most reliable path to capturing those advances.