October 2025

Market Update

The third quarter of 2025 saw markets behaving very much like they have been since 2023 – with US large growth stocks pulling ahead under the promise of AI productivity and profitability. Even so, the rest of the market also performed well and now every broad asset class is positive for the year. There continues to be concerns about the level of inflation as well as slowing growth now that the Federal Reserve has begun cutting interest rates.

YTD, Bonds are up 6.1% with TIPS (Treasury Inflation-Protected Securities) bonds up more at 6.9% showing investors are looking for ways to hedge future inflation. With interest rates moving somewhat lower, shorter term bonds (+4.0%) and floating rate notes (+3.7%) are up less. The S&P 500 is up 14.8% with growth stocks up more (+17.2%) than value (+11.7%). US small caps are now positive, up 10.4%. However international and emerging market stocks are the best performing equity asset class, up 25.1% and 27.5% respectively. In those markets value stocks are outperforming growth stocks. These returns are about 10% better than the US because the dollar is down -10%. The dollar weakness and inflation concerns have also led to gold being the best YTD performer up 44.8%. US REITs are up 4.5%, MLPs are up 5.8%, and commodities are up 2.8%.

The Federal Reserve began cutting interest rates in the 3rd quarter and the market prices indicate there are expectations for two more. The rate cuts are occurring as economic numbers have slowly gotten weaker over the last few years. Jobs numbers and consumer defaults have both been weakening and there is a rising, but not probable, chance of a recession. These cuts could help with growth but also could reignite inflation.

Our primary concern for equity markets remains the valuation US large caps. Fueled by huge returns in a handful of AI and tech stocks, the S&P 500 has generated 15% annualized returns over the last 1, 5, 10, and 15 years. This is well above its 10% long term average and the valuation of the US large cap space is at a level we have rarely seen in history. High prices often mean lower future returns, so while we recommend maintaining exposure to US large caps we also recommend diversification within equity portfolios, and that means having exposures to value stocks, mid and small cap stocks, and international stocks.

Our base case for 2025 is that GDP will slow from current levels. Higher interest rates and higher debt pressure on US households will have a slowing effect on spending and growth. Household net worth is likely to remain bolstered by home values and investment accounts which have remained high. Inflation may have become entrenched above the Fed's 2% target. Markets and interest rates generally appear to be at appropriate levels with the exception of the largest and growthiest US companies which are trading 2-3 standard deviations above their typical valuations.

Fixed Income Strategy

Fixed income markets posted another solid positive return in the third quarter, although more muted than Q1 and Q2 returns. It was a tale of two curves during the quarter as Treasury yields 3 years and longer parallel shifted lower between 7 to 11 basis points, while very short rates out to 1 year moved lower by 20 to 40 basis points. Short maturity yields declined more as the Federal Reserve's FOMC initiated its first rate cut of the year in September by 25 basis points (bps), bringing the Fed Funds rate down to 4.25%. The market anticipates additional FOMC rate cuts, which is reflected in a 2 year Treasury yield that is lower than the current Fed Funds rate. The 2 year Treasury yield moved lower by 11bps in the quarter, ending at at 3.61%, while the 10 year benchmark Treasury moved lower by 8bps, closing the quarter at 4.15%.

Reading the economic tea leaves in the third quarter was quite a challenging exercise for the market and the Federal Reserve. GDP printed higher than expected growth, trade policy and tariff impacts remained an ongoing focal point and consternation, labor market weakness was confirmed by a significant negative BLS adjustment to prior job growth as immigration policy is anecdotally reducing labor supply, while inflation remained elevated and meaningfully above the Fed's 2% target. Firms are processing the administration's trade policy and are in a 'not hiring, not firing' stasis. AI's impact to the labor market is unknown but is likely not additive to hiring. The Federal Reserve's dual mandate of maximum employment and stable prices are in tension with a weakening labor market and elevated inflation. The FOMC's cut in September prioritized weakening labor market dynamics over inflation. Chair Powell acknowledged the challenging economic environment and reiterated there is no predetermined path forward. He characterized the cut as a 'risk management' move, which can be interpreted as an insurance cut.

Adding to the uncertainty, at the end of the quarter, Congress was unable to pass a budget and therefore nearing another government shutdown. A shutdown does not allow for government economic data to be calculated and distributed, which increases the challenge for a data dependent Fed. Additionally, Fed independence was directly challenged as the President attempted to fire Fed Governor Cook for cause, regarding alleged personal mortgage fraud. The Supreme Court recently blocked the administration from immediately firing Governor Cook and will hear oral arguments in January 2026.

Investment Grade spreads continued their path to lower and historically tight spreads, which narrowed by 9 bps and ended the quarter at 74bps. A similar theme occurred in High Yield as spreads narrowed 23bps to 267bps at quarter end. Investment grade corporate issuance remained robust during the quarter as solid credit fundamentals and demand supported the corporate markets. Even as spreads are historically tight, the attractiveness to corporate bonds has been their all-in yield: corporate spread + Treasury yield.

Due to what we feel are a wide range of policy and economic outcomes, along with tighter corporate spreads, we are maintaining balance in our core strategy. There was one incremental change we made during the quarter to help defend against the potential for longer rates to rise in a setting where inflation remains elevated. We added an overweight in the 5 year maturity, while the remaining maturities remained somewhat evenly distributed. Overall, we are targeting a roughly 70% corporate bond / 30% Treasury allocation, which includes exposure to TIPS as a hedge against higher inflation.

Equity Income Strategy

The Equity Income strategy's primary goal is to provide reasonable income while also offering the potential for capital appreciation.

Capital preservation strategies underperformed the broader market in the third quarter. The "risk-on" sentiment, which continued into the third quarter, favored more speculative, low-profitability companies instead of equities with steady, reliable cash flows. These strategies, which focus on minimizing volatility and prioritizing stable assets, couldn't capture outsized returns as the overall U.S. market and growth stocks outperformed, particularly the Information Technology and Communication Services sectors. Overall, traditionally defensive sectors like Health Care and Energy (which make up a large percentage of the portfolio) have outperformed year-to-date due to specific equity holdings. Relative to the benchmark, the Equity Income strategy delivered a return of about +3.8% in the third quarter, outperforming the underlying benchmark, which rose about +2.5%.

In the quarter, we had no trades to report.

As always, we continue to look for opportunities to upgrade the quality of the portfolio while staying true to our disciplined valuation process.

Defensive Equity Strategy

The Defensive Equity strategy remains focused on identifying companies with stable operating results and reduced stock price volatility in the broader market.

In the third quarter, we saw the market's strong preference for Growth. While Defensive Equity is underweight the Information Technology and Communication Services sectors and overweight cash, we saw outperformance against the benchmark as stock-specific holdings like Oracle, Alphabet, and Apple outperformed due to AI tailwinds. As a result, the Defensive Equity strategy returned about +3.9%, while the benchmark returned about +1.3% in the third quarter.

In terms of portfolio allocation, our strategy maintains an overweight position in high-quality stocks while deliberately underweighting sectors that are sensitive to economic cycles, such as Financials and Materials. This approach aims to mitigate risk and emphasize stability in uncertain market conditions.

Additionally, we continue to hold cash and have a small position in gold.

From a portfolio perspective, we added Synopsys.

Core Equity Strategy

The third quarter of 2025 represented a significant period of market resilience, as a rebound in U.S. equities pushed major indices to new record highs. Despite worries over rapidly accelerating tariffs, rising geopolitical tensions, persistent inflation, and domestic policy uncertainty, the S&P 500 Index delivered a total return of approximately +8.2%. The advance was fundamentally underpinned by a rotation toward cyclical and high-beta stocks, supported by the Federal Reserve cutting interest rates and strong corporate earnings. In the third quarter, investor focus shifted from recessionary fears, which dominated the first half of 2025, toward capitalizing on recent megatrends. Primarily, overwhelming investment and optimism surrounding Artificial Intelligence (AI) not only propelled the Information Technology and Communication Services sectors but also the Utilities sector, which is traditionally a defensive sector.

The S&P 500 Index's robust Q3 performance was highly concentrated in Information Technology, Communication Services, Consumer Discretionary, and Utilities, which returned about +14.5%, +13.4%, +9.4%, and +7.2% this quarter. The Information Technology and Communication Services sectors were partly driven by strong earnings growth and new announcements like OpenAI's Stargate AI infrastructure project partnerships, which provided a positive sentiment boost. Furthermore, the Utilities sector outperformed in Q3, driven by the accelerating demand for data center power. Expectations for above-average earnings growth are driven by the uptrend in U.S. electricity consumption, fueled by AI data centers and manufacturing reshoring.

While the S&P 500 Index achieved record highs, the market performance was far from uniform. Sectors like Consumer Staples, Materials, and Real Estate lagged due to exposure to the stressed U.S. consumer, the inflationary effects of tariffs, and high borrowing costs, returning approximately −3.1%, +0.7%, and +1.9% in the third quarter. The weakness in the Consumer Staples sector was due to the erosion of the U.S. consumer's financial strength, as real disposable income growth slowed to a cycle low. In addition, households faced multiple financial stressors, including the renewed burden of student loan repayments, sustained high borrowing costs, and fears over rising unemployment. The Real Estate sector continued to underperform due to elevated and volatile interest rates, exacerbated by long-term fiscal deficit concerns driving bond yields higher. The combination of high costs of capital and elevated building materials constrained new construction activity.

The Federal Reserve executed a pivotal monetary shift, implementing a 25-basis point rate cut at its September meeting, signaling the formal resumption of the easing cycle. This action was primarily driven by mounting concerns regarding the stability of the labor market, specifically a decline in job growth to below the rate required to maintain employment stability. Corporate earnings remain strong while the economy contends with stubborn inflation. Stagnant economic growth and high inflation create the risk of stagflation.

From a portfolio standpoint, we added a few new names: Chipotle and Eli Lilly. We exited positions in Micron Technology, Hershey, and Arista Networks in the quarter.

International Equity Strategy

International markets' strength continued in the third quarter of 2025 with gains of around +4.8%. The

Financials, Industrials, and Consumer Discretionary sectors led the way, rising approximately +8.9%, +6.8%, and +6.7%, respectively. Year-to-date, international equities continue to outperform U.S. equities.

The Industrials sector's strong performance was supported by the continued strength of capital expenditures related to AI and countries ramping up spending toward defense and infrastructure. Meanwhile, industrial segments like construction and housing remained soft. In the third quarter, Financials outperformed due to the interest rate policies of Europe and Japan. The ECB's decision to pause the rate-cutting cycle provided European banks with a period of Net Interest Margin (NIM) stability. This rationale was rooted in the persistence of underlying inflation pressures. Financial companies from Japan gained on the anticipation of more rate hikes. The possibility of the Bank of Japan raising rates establishes a high probability of future Net Interest Margin expansion, which would lead to higher profitability if the zero-rate environment concludes.

Our goal is to have a portfolio of high-quality businesses with competitive advantages that can withstand changes in economic conditions and thrive throughout a business cycle. Companies with established moats often expand market share and strengthen their business during a downturn. These are the types of companies that we continue to look for in the International Equity strategy.

While we cannot predict near-term risk factors, we can control the companies we invest in. Our disciplined approach of owning high-quality, financially viable, and intrinsically cheap companies forms the International Equity portfolio.

From a portfolio standpoint, we added Lululemon. We exited positions in Celestica, NXP Semiconductors, and Anheuser-Busch InBev in the quarter.

Value Strategy

The Russell 1000 Value benchmark recorded a total return of approximately +4.4% in the third quarter, while the Value strategy returned approximately +2.4%. Outperformance in the third quarter was concentrated in the Communication Services, Utilities, Energy, and Information Technology sectors, which returned approximately +11.8%, +7.7%, +5.4%, and +5.2%, respectively. This performance was driven by either direct exposure to the AI infrastructure buildout or operational strength in the Energy market. Conversely, traditional defensive sectors such as Health Care and Consumer Staples lagged significantly, returning about −2.8% and +3.5%, respectively, due to the market's enthusiasm for riskier assets. The Materials sector, which underperformed in the third quarter, returned about +3.5% while grappling with a squeeze from rising input costs and soft global demand.

The Russell 1000 Value benchmark's lagging performance relative to the S&P 500 Index and the Russell 1000 Growth Index over the past year highlights the persistent divergence between value and growth investing styles in the current market cycle. This confirms that the majority of market momentum remains concentrated in the largest, fastest-growing technology companies.

The Energy sector's strong performance was partially driven by resilient demand for oil and gas, record U.S. Liquified Natural Gas (LNG) exports, and robust downstream (refining and petrochemical) margins, all of which were identified as leaders in the third quarter. This was true despite softer crude prices. Utilities directly benefited from the Federal Reserve's pivot toward easing, as the sector's high capital expenditures and heavy debt loads benefit from lower interest rates. Also, the increasing demand stemming from the AI boom serves as a significant growth driver. The underlying reason for the Materials sector's underperformance was a margin squeeze, as the sector was constrained by soft global demand and oversupply. This prevents companies from passing through spiking input costs for steel, natural gas, and copper, for example.

As always, valuation continues to guide sector positioning. At present, we see compelling opportunities in Health Care and Consumer Staples, where relative value remains attractive.

From a portfolio standpoint, we added a few new names: Adobe, Gartner, Restoration Hardware, Constellation Brands, Deckers Outdoor, Accenture, Marvell Technologies, and Waters Corp. We exited positions in Celestica, Micron Technology, Microchip Technology, Estee Lauder, and Baxter in the quarter.

Thematic Equity Strategy

Thematic is by far our most aggressive growth strategy with over 40% in Technology and 10% in Biotech –to this extent Thematic outperformed this quarter due to its exposure to Technology and investors increasing their risk spectrum.

As ever, we remain vigilant in our efforts to identify new themes of secular growth that would benefit the strategy.

Sources & Disclosures

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All earnings data comes from Standard and Poors' S&P 500 Earnings and Estimates Report as of 9/30/2025

All economic data comes from Federal Reserve Economic Data (FRED) as of 9/30/2025

Asset class performance numbers come from Morningstar as of 9/30/2025

The S&P 500® is widely regarded as the best single gauge of large-cap US equities. There is over USD 9.9 trillion indexed or benchmarked to the index, with indexed assets comprising approximately USD 3.4 trillion of this total. The index includes 500 leading companies and covers approximately 80% of available market capitalization.

Treasury yields are yields on debt obligations issued by the US Government. US Treasuries can be purchased individually.

The Russell 2000 Index® measures the performance of the 2,000 smallest companies in the Russell 3000 Index.

The iShares Russell 2000 ETF (the IWM ETF) seeks to track the investment results of an index composed of small-capitalization US equities.

The Russell 1000 Value Index measures the performance of the large-cap value segment of the US equity securities. It includes the Russell 1000 index companies with lower price-to-book ratios and lower expected growth values. It is market-capitalization weighted.

Standard deviation is a statistical measurement that shows how spread out a set of data is. It is used to assess risks of investments.

A "Moat" is a term that refers to a business's ability to maintain a competitive edge over its competitors.

The Magnificent Seven is a group of high-performing US stocks and includes Alphabet, Amazon, Apple, Meta Platforms, Microsoft, NVIDIA, and Tesla.

Treasury Inflation-Protected Securities (TIPS) are US Treasury bonds indexed to inflation to protect investors from decline in the purchasing power of their money. The principal value of TIPS increases with inflation and decreases with deflation.

Investors should be aware that there are risks associated with options. Additionally, options transactions produce tax consequences when closed. Market related actions, political issues, and economic issues can adversely affect the option market. These factors could restrict, halt, suspend, or terminate option positions written (sold) or purchased, which would prevent us from an ability to act or react to any of these conditions. Note: Options involve risk and are not suitable for everyone. Prior to buying or selling options, you should read the option disclosure document, Characteristics and Risks of Standardized Options, which can be obtained on the Options Clearing Corporation website at https://www.theocc.com/about/publications/character-risks.jsp, or by contacting your custodian.

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