INVESTMENT STRATEGY AND OUTLOOK

The third quarter of 2025 marked a continuation of the strong rebound in US equities since April's trough, reflecting the market's willingness to shrug off macroeconomic tumult. The S&P 500 advanced approximately 7.0% over the quarter, recovering from first half volatility and reflecting investor confidence in the durability of the US economy. The tech-heavy Nasdaq-100 surged by approximately 9% in the same period, on the back of optimism in the artificial intelligence space, and the Dow Jones Industrial Average climbed almost 6% as cyclical industrials, financials, and consumer-related names began to participate in the strong domestic market.

However, the market continues to be led by its largest constituents leaving those hoping for a broadening of participation wanting. The equal-weight S&P 500 managed to advance by nearly 5% in Q3 – a very strong result but still about 2.3% lower than its market-cap weighted sibling. This persistent lagging has frustrated investors as the rally is still mostly driven by seven or eight companies. The exuberance extended beyond domestic shores as the MSCI EAFE index also delivered positive mid-single digit returns, aided by a dollar that remained soft relative to the first half. On the fixed income side, intermediate US investment-grade bonds also posted gains, mostly from coupon income supported returns.

Several forces combined to drive these outcomes, notably the interaction between the Federal Reserve, fiscal policy, and global demand dynamics. Investor sentiment improved after the Federal Reserve signaled its readiness to ease policy, with the first rate cut of the year arriving in September. This move reassured markets that policymakers were attentive to slowing growth risks, and it helped compress discount rates applied to equities, boosting valuations. At the same time, inflation remained contained, though some in the pundit class still expressed trepidation that the potential inflationary impacts of tariffs are still not fully being realized. Gold's banner 2025 continued to be fueled not only by lower real yields but also as a source of diversification stemming from elevated geopolitical risks, namely continued and heightened tensions in the Middle East and Europe, as well as ongoing debates over US fiscal sustainability. Taken together, these dynamics painted a picture of a financial market environment that was both supported by policy and liquidity and seemingly impervious to macro and geopolitical crosswinds.

Looking ahead to the fourth quarter, the key question for investors is whether the momentum in US equities can be sustained, or renewed volatility might emerge as monetary policy and politics collide. Headlines pertaining to government shutdowns, escalated Middle East conflicts, etc. used to negatively impact the markets. Since the market resiliency displayed during COVID, participants are increasingly tuning out those variables. Whether that is a positive or negative development can be debated, but as our attention remains on individual companies, an environment focused on business execution and fundamentals is welcomed.

Technology will likely remain the engine of US stock indices, though investors may increasingly rotate into more cyclical portions of the market if the economic soft-landing narrative holds. Stocks in that portion of the market are well situated for strong business characteristics and attractive current valuations. Bonds are positioned for steady income with modest price appreciation if yields edge lower, and gold will likely continue to attract flows given central bank demand and some participants hedging against a return to equity markets' trepidation around geopolitics. The US dollar is expected to weaken modestly further as additional Fed cuts materialize, providing support to non-US risk assets and commodities. The outlook is not without risks. Should inflation surprise to the upside from the passed-through tariff impact or political uncertainty intensifies in Washington, markets could quickly reprice. For now, the balance of evidence suggests that Q4 2025 will likely carry forward the themes of Q3—US equities as the central pillar of global market strength, anchored by a more accommodative Federal Reserve, solid earnings reports, and persistent investor appetite for risk assets.

October 1, 2025