



## 4<sup>th</sup> Quarter 2025 Review & Outlook

Dear Client,

The turn of the year offers a unique vantage point to reflect on the prior year's precedents while facing the "clean slate" of the future. This transition often evokes a duality of excitement and trepidation; no crystal ball can discern whether the coming months will be calm, cruel, or chaotic. In truth, most years contain elements of all three, and 2025 was certainly no exception to that.

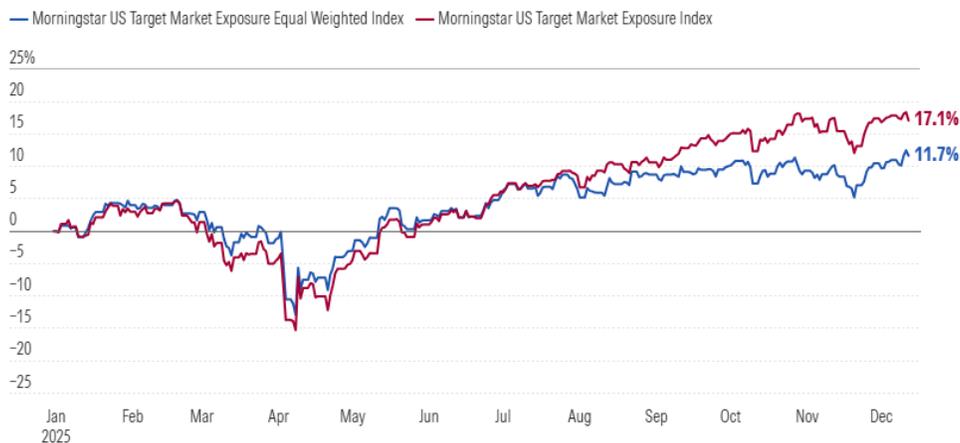
The year began with deceptive tranquility, with the S&P 500 gaining +4.5% through mid-February. However, a quiet storm was brewing as rhetoric regarding global tariffs intensified. This culminated in the "Liberation Day" volatility of April 2nd, when the administration introduced reciprocal tariff rates that were far broader than the market had anticipated. The reaction was visceral: a 21% decline by April 7th marked the second-fastest descent into a bear market in history. Recession surveys spiked to 70%, the VIX surged above 50, and investor sentiment plummeted to levels not seen since 2009. By early April, many feared the year was already lost.

Yet, markets are rarely linear. Just one week later—likely influenced by the severe dislocations in the equity and credit markets—the administration pivoted. Reciprocal rates were largely paused as nations returned to the negotiating table. While trade headlines dominated the spring, the secular tailwinds of Artificial Intelligence (AI) continued to provide a

fundamental floor for the economy. Performance was driven by semiconductor leaders like Nvidia and AMD, and we maintain our conviction in **Applied Materials (AMAT)** to capture essential equipment demand. Furthermore, we integrated **Eaton (ETN)** into portfolios last April to participate in the critical infrastructure theme, as the aging electric grid faces unprecedented demand from AI data centers.

As we enter 2026, the stage is set with a complex backdrop: expectations for robust double-

### Market-Cap-Weighted vs. Equal-Weighted Returns



Source: Morningstar. Data as of Dec. 12, 2025. [Download CSV](#)

digit earnings growth (approx. 15%) are colliding with valuations that sit near historical highs. We anticipate the Federal Reserve will continue to ease interest rates, applying downward pressure on the short end of the yield curve. While employment growth has moderated, we have yet to see the systemic job losses indicative of a true recession.

The bar for growth in 2026 is high, but we must remember that markets have historically finished higher in three out of every four years. Equity volatility remains the "price of admission" for the world's most effective wealth-creation engine. We remain committed to using our advanced planning software to tailor asset allocations to your specific needs, ensuring sufficient liquidity for the next 12 months of cash flow. As we cross into the latter half of the 2020s, we welcome the opportunity to review your financial plan and portfolio with you.

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## Looking Ahead: Navigating the Bull and Bear Case

As is often the case in the markets, there are compelling reasons to be bullish and bearish at the same time. To help you navigate the year ahead, we have synthesized the primary arguments from both the bulls and the bears:

### The Bull Case: Momentum & Fiscal Tailwinds

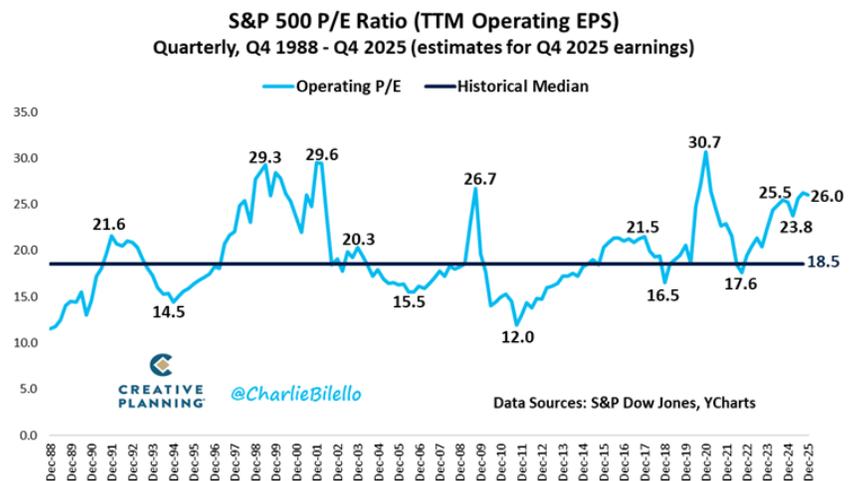
Optimists point to a resilient economy that refuses to quit, bolstered by fresh policy support.

- **Robust Earnings & Rate Relief:** The S&P 500 is entering the year with earnings growth expectations in the mid-double digits (approx. 12-15%). As the Federal Reserve continues to lower the fed funds rate—likely toward a neutral target of 3.0%–3.5%—we expect to see "sidelined cash" migrate out of money market funds and back into risk assets in search of greater returns.
- **The "Big Beautiful Bill" Stimulus:** This spring, many households will feel the tangible effects of the newly signed tax legislation. With a permanent extension of the 2017 tax cuts, a significantly higher standard deduction, and new deductions for overtime and tips, we expect a mid-year boost to consumer discretionary spending.
- **Technical Momentum:** Momentum remains a powerful force. Without a major external shock, the status quo suggests a path of least resistance that leads higher, particularly as AI adoption moves from "hype" to "harvesting" real corporate productivity.

### The Bear Case: Valuation & Social Friction

Conversely, the "bears" find plenty of reason for caution, even if their warnings have been ignored during the recent rally.

- **Historic Overvaluation:** The bear case begins and ends with price. The S&P 500 is currently trading at roughly 22.5x forward earnings and 26x trailing earnings—nearly 40% above the historical median since 1989. This leaves a razor-thin margin for error; any earnings disappointment could trigger a sharp re-pricing.
- **A "Tale of Two Economies":** While the wealthy benefit from a "wealth effect" driven by record stock and real estate prices, the bottom two-thirds of the country is feeling the "K-shaped" divide. Lackluster job growth in non-tech sectors and the cumulative weight of post-COVID inflation continue to suppress broader consumer sentiment.
- **Midterm & Geopolitical Volatility:** 2026 is a midterm election year, which historically introduces higher-than-average volatility and marginally weaker returns as political uncertainty peaks. When you layer in rising government debt and the "wild card" nature of current global geopolitics, the risk of a sudden market "de-risking" event remains elevated.



### **Our Stance: Transitioning to the "Back Half"**

So, where do we fall? We believe the "easy money" phase of this bull market is behind us. While our top-down view edges toward the cautious side given these valuations, we remain confident that 2026 will offer numerous pockets of investing opportunities. The winners of 2026 may not be the "hottest" AI names of the last two years, but rather the high-quality, cash-flow-positive companies where we focus our portfolios that can thrive in a more nuanced economic environment.

*“Never get too high in a bull market, or too low in a bear market. You’re not smarter when the market goes up, and you’re not dumber when it goes down either.” - Howard Marks*