Market Commentary

Market Movements

Despite some signs of a cooling labor market and continued uncertainty over inflationary pressure, the third quarter delivered another solid period of sustained market optimism and economic resilience. On a surprising note, quarterly GDP expanded at an annualized rate of +3.9%, outpacing most expectations. This was on the back of strong consumer spending and easing trade headwinds. Meanwhile, core inflation remained relatively stable hovering at around 3.1%. However as was indicated by Jay Powell in his September FOMC post meeting address, the noticeable softening of the labor market encouraged the Committee to shift its focus, at least temporarily, from concern over its inflation mandate to its second mission: keeping unemployment low. On this shift, the FED announced its first 25bps interest rate cut of 2025 and as we head into the FED's next meeting coming up on October 28th, it appears we'll likely see another quarter point cut, bringing the overnight borrowing range to 3.75%-4.00%. On top it all, at least at this writing, the markets are pricing in a 71% chance of a third cut following the FED's final meeting in December. We're not quite sure that will materialize but it would be even more tasty for continued market strength!

Between the economic and financial market resilience we've witnessed through the third stanza, US equities led the global markets higher with the S&P posting a +8.1% gain over the period and +14.8% on the YTD. This on the back of AI productivity, which fed into corporate earnings strength along with the prospect of monetary easing. In fact, it was the S&P 500's best third quarter performance since 2020! Not to be outdone, the Nasdaq technology driven index delivered +11% for the quarter, while the Russell 2000 small cap index outpaced both, generating some +12%. For small caps which have seen more than a year's long relative rut, the index reached its first record high since November 2021. We suspect their upward move has everything to do with rate cuts and the prospect of easing debt on their balance sheets. And clearly across all the equity asset class indices, the stock market remains biased to growth over value investing. Notwithstanding all of the forementioned, this period's returns are remarkable particularly given that summer returns are typically flat and, at least historically speaking, often followed by September markets that can be mercilessly volatile.

As to the global equity markets, after an impressive 2Q upward move, the International developed markets as measured by the MSCI (Europe, Australian and Far East) index, rebounded up +4.8% in 3Q, while the emerging markets surprisingly delivered just over +10.3% for the quarter.

Turning to the bond markets, early quarter job and growth data gave the FED reason to hold rates steady through the first half year. But as indicated earlier, weaker jobs reports commencing in July shifted the FED's focus to the prospect of easing and signaling to the market that a cut or cuts were likely coming. As yields began easing, bond returns materially improved. The Bloomberg 10-Year Municipal Bond index delivered +3.03% on the quarter and +4.1% on the YTD. The Investment Grade Aggregate Index (taxable governments and corporates) generated +2.03% on the quarter and +6.13% on the YTD, and the Bloomberg High-Yield index delivered +2.54% on the quarter and +7.22% on the YTD.

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As to our currency movement, which is something we don't often comment on, the US dollar had taken an early year beating following the administration's trade policy announcements that began on Trump's so coined "Liberation Day". From that point forward the US dollar index fell by as much as 10-11% through mid-year, making its fall one of the steepest declines since the 1970's. However, since successful trade negotiations with some of our largest trading partners have been announced, dollar volatility has retraced a good portion of its weakness through this date. It's not surprising to note that at the same time the dollar was depreciating, its alter ego gold was having one of its best years in over four decades reaching an apex price of $4,359 per ounce; a +63% upside move before moderating to a 52% return through this date.

Finally, energy and the oil markets are navigating a period of transition characterized by slowing demand, increasing supply, and structural shifts toward cleaner sources. Interestingly, the US reclaimed its position as the world's top oil producer with output exceeding some 13.5 mil barrels per day, an all-time high! Similarly natural gas production remains one of America's core energy strengths as the current administration continues to focus on deregulation. All that said the long-term global energy mix is still gradually shifting toward decarbonization and electrification.

Looking Forward

As we look ahead to the near term and the close of 2025, as is usual, there's always a handful of concerns that can crop up anytime to challenge the current market run, not the least of which is the current government shutdown now in its third week and the second longest in US history! While it's clear the markets have so far been agnostic to the current political impasse, the continued lack of government sponsored data may eventually catch up with us should this outage be prolonged. That said, history does suggest that while shutdowns do have a nominal negative effect on economic growth, financial markets tend to remain immune which is precisely what we've seen over the last few weeks.

In closing and on a larger more important note, it is an excellent time for all of us as investors to carve out time to review our portfolios as we near year end, simply to re-assess where they stand relative our investment objectives and risk tolerance. The equity markets have been very generous again so far this year, which for many may translate into portfolio imbalances that need to be addressed. Whether they do or not, it's always reassuring to know that a quality control check was accomplished. To that end, we look forward to and stand ready to convene with you for our year end investment review at your convenience. Until then all best wishes!

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