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# Market Review & Outlook

Q4 2025 | As of December 31, 2025

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management llc

# Market Review

## Executive Summary

- Equity markets were mixed in the final month of the year with the dominant Large Cap Tech stocks showing fatigue after another strong year of gains. With that said, the S&P 500 finished the year near record highs with a Q4 return of 2.7% and 17.9% for all of 2025.
- The overall equity market saw bouts of rotation out of the market leading “Magnificent 7” Tech stocks and diversified into other sectors.
- By virtually all measures, and in fact general market consensus, much of the equity market is significantly over valued yet continued to march higher.
- The overall bond market returned 7.2% for 2025 driven by price gains in intermediate term maturities resulting from actual and expected Fed rate cuts, and a high level of income generation, particularly in Mortgage-Backed Securities.
- Fixed Income delivered a positive .9% in Q4 despite given back some return in December.
- The overall interest rate environment seems to have found fair value at current levels and could be largely rangebound in 2026.
- The Fed is likely to cut rates twice in 2026, which will only impact very short-term rates.



# Market Review

## Market Scoreboard

- Strong returns were again found across market sectors in 2025; however, previous market leaders began to show fatigue amid stretched valuations.

Market Summary - December 31st, 2025				
Bond Market	MTD	QTD	YTD	Yield
Total Bond Market	-0.3%	0.9%	7.2%	4.4%
US Treasuries	-0.5%	0.7%	6.2%	3.9%
US MBS Index	0.1%	1.6%	8.3%	4.7%
Corporate Bonds	-0.3%	0.8%	7.8%	4.8%
High Yield Corporates	0.7%	1.4%	8.5%	6.5%
US TIPS (Inflation Prot.)	-0.6%	0.0%	6.8%	1.7%
Merrill Muni Index	0.1%	1.4%	3.9%	3.5%
Floating Rate Corp	0.4%	1.2%	4.9%	4.8%
International Bonds	0.0%	-2.1%	6.6%	2.8%
Commodities/Other	MTD	QTD	YTD	End Value
Gold	1.9%	11.9%	64.6%	\$4,319
Dollar Index	-1.1%	0.6%	-9.4%	\$98
Oil (WTI)	-1.5%	-6.6%	-15.1%	\$57

Market Summary - December 31st, 2025				
Stock Market Indices	MTD	QTD	YTD	End Value
DOW Jones Avg.	0.9%	4.0%	14.9%	\$48,063
NASDAQ Composite	-0.5%	2.7%	21.2%	\$23,242
Large Cap Core (S&P 500)	0.1%	2.7%	17.9%	\$6,846
Equal Weight S&P 500	0.4%	1.4%	11.4%	\$7,764
Large Cap Growth	-0.2%	2.2%	22.1%	\$4,971
Large Cap Value	0.4%	3.2%	13.2%	\$2,093
Mid Cap Core	0.1%	1.6%	7.5%	\$3,305
Mid Cap Growth	-0.2%	1.3%	7.4%	\$1,572
Mid Cap Value	0.3%	2.1%	7.6%	\$1,055
Small Cap Core	-0.6%	2.2%	12.8%	\$2,482
Small Cap Growth	-1.3%	1.2%	13.0%	\$12,190
Small Cap Value	0.2%	3.3%	12.6%	\$19,782
Europe	3.7%	5.1%	41.9%	\$612
England	3.9%	6.8%	35.1%	\$9,931
Japan	0.2%	6.0%	29.3%	\$50,339
Shanghi 300	3.7%	2.1%	26.3%	\$4,630
International	3.0%	4.9%	31.9%	\$2,893
MSCI China	-1.2%	-7.4%	31.2%	\$666
Emerging Markets	2.2%	3.9%	34.0%	\$55

# Market Review

## S&P 500 Top 10

- AI heavyweights NVIDIA, Microsoft, Amazon and Meta showed vulnerability amid growing concerns of leveraging up and borrowing needs to support extraordinary investment, with uncertainty over the return on those investments.
- Furthermore, Google's (+28.8% in Q4) reveal of its AI chips and Gemini 3.0 model created a significant shift in sentiment as to the dominance of Nvidia and Open AI.
- The top 10 stocks, now at just under 40% of the S&P 500 market weight, showed very mixed results in Q4, including a negative December amid stretched valuations and rotation into cheaper sectors left behind.
- The varied performance of the top tech stocks suggest a topping out in valuation with a market transition to a "show me" sentiment in the market, beyond the physical buildout of data centers.
- Of the top 10, only NVDA, Broadcom, and Google outperformed the S&P 500 in 2025 showing the narrow leadership.

Top 10 Holdings Vs. Rest of S&P 500						
Company	Name	Price	Last 12M P/E Ratio	Next 12M P/E Ratio	Last 12M EPS Growth	Next 12M EPS Growth
NVDA	NVIDIA Corp	\$177.00	43.9	26.5	60.4%	67.4%
AAPL	Apple Inc	\$278.85	35.9	33.2	10.5%	10.4%
MSFT	Microsoft Corp	\$492.01	33.3	29.0	19.4%	15.5%
AMZN	Amazon.com Inc	\$233.22	32.3	30.0	51.3%	6.6%
AVGO	Broadcom Inc	\$402.96	48.7	32.7	40.0%	46.6%
GOOGL	Alphabet Inc Class A	\$320.18	30.4	29.3	34.5%	6.4%
META	Meta Platforms Inc	\$647.95	28.4	22.3	6.6%	28.9%
GOOG	Alphabet Inc Class C	\$320.12	30.4	29.3	34.5%	6.4%
TSLA	Tesla Inc	\$430.17	224.5	212.4	-20.8%	5.1%
BRK/B	Berkshire Hathaway Inc	\$513.81	22.3	24.1	17.8%	-6.2%

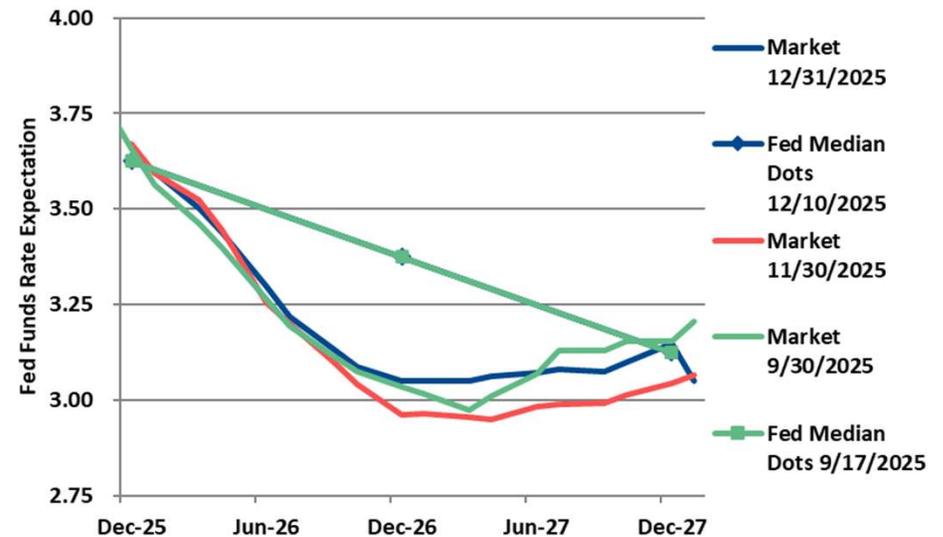
Top 10 Holdings Vs. Rest of S&P 500					
Company	Name	Dec-25 % Weight	MTD Return	QTD Return	YTD Return
NVDA	NVIDIA Corp	7.8%	5.4%	0.0%	38.9%
AAPL	Apple Inc	6.9%	-2.5%	6.9%	9.0%
MSFT	Microsoft Corp	6.1%	-1.7%	-6.5%	15.6%
AMZN	Amazon.com Inc	3.8%	-1.0%	5.1%	5.2%
AVGO	Broadcom Inc	2.8%	-13.9%	5.1%	50.6%
GOOGL	Alphabet Inc Class A	3.1%	-2.2%	28.8%	66.0%
META	Meta Platforms Inc	2.5%	2.0%	-10.0%	13.1%
GOOG	Alphabet Inc Class C	2.5%	-1.9%	28.9%	65.4%
TSLA	Tesla Inc	2.2%	4.5%	1.1%	11.4%
BRK/B	Berkshire Hathaway Inc	1.6%	-2.2%	0.0%	10.9%
Top 10 of SPX	Top 10 S&P 500	39.2%	-0.6%	3.6%	24.1%
Rest of SPX	Bottom 490 S&P 500	60.8%	0.5%	2.1%	14.1%
SPX Returns	Market Weight S&P 500	100.0%	0.1%	2.7%	17.9%
SPW Returns	Equal Weight S&P 500	100.0%	0.4%	1.4%	11.4%

# Market Review

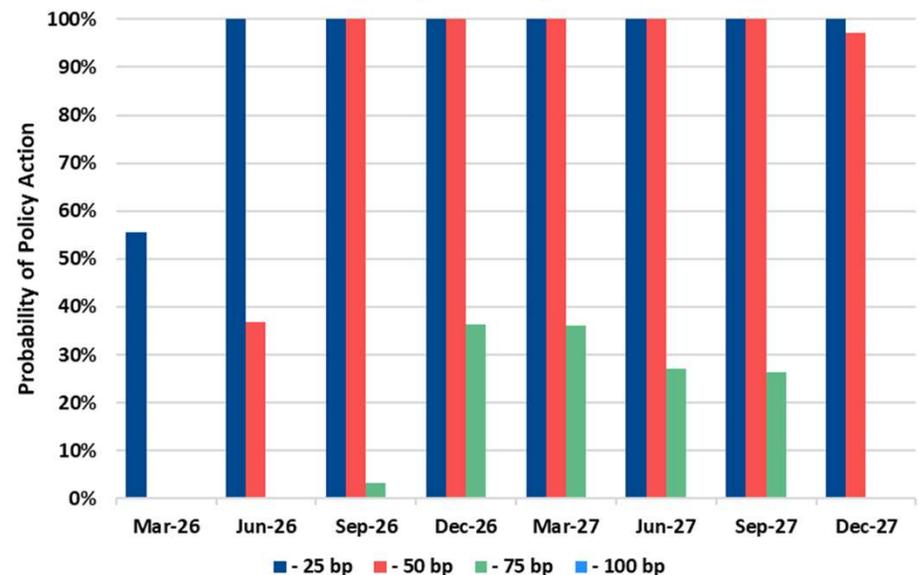
## Fed Policy

- The Fed cut interest rates three times in 2025 to 3.625% and comes into 2026 with only one more penciled in, while the market is expecting two more cuts by year end.
- Longer term market expectations remained relatively unchanged from the end of September with the Funds rate migrating toward 3% by the end of 2026. The Fed sees more gradual easing with their second ease coming in 2027.
- Fed Funds rate has come along way toward neutral, which we put at around 3%, and expect that the Fed will get there by year end, in agreement with the market.
- Inflation has continued to migrate toward the Fed's 2% objective, finishing the year at 2.7%. We expect continued progress as the year goes on driven by energy, housing, and consumer prices.
- Lower inflation combined with a continued static employment environment will allow the Fed to ease further.
- Tariffs did not pose the problems to inflation that the Fed and markets had previously determined would flow through to feed inflation. As noted in our reports earlier this year, we did not feel this would be an issue, and positioned for the Fed ease that occurred.
- The Fed impact on longer term interest rates will be diminished this year.

Market Expectations of Fed Funds  
Fed Meeting Date vs Month End



Probability of Policy Action



# Market Review

## Fed Policy

- The Fed continues to get whipsawed by their short-term focus in economic projections and rate moves.
- Fed forecasts this year have underestimated growth while overestimated inflation and employment, leaving their expectations of Fed Funds too high, and having to adjust regularly.
- The Fed raised Real GDP Growth forecasts again in December for 2025 and 2026, while lowering their inflation targets back down after raising them the previous quarter.
- After easing in December, the Fed has a dramatic difference in opinion within the committee as to where monetary policy should be.
- We feel the Fed will cut twice in 2026 and hold near 3% for an extended period of time.

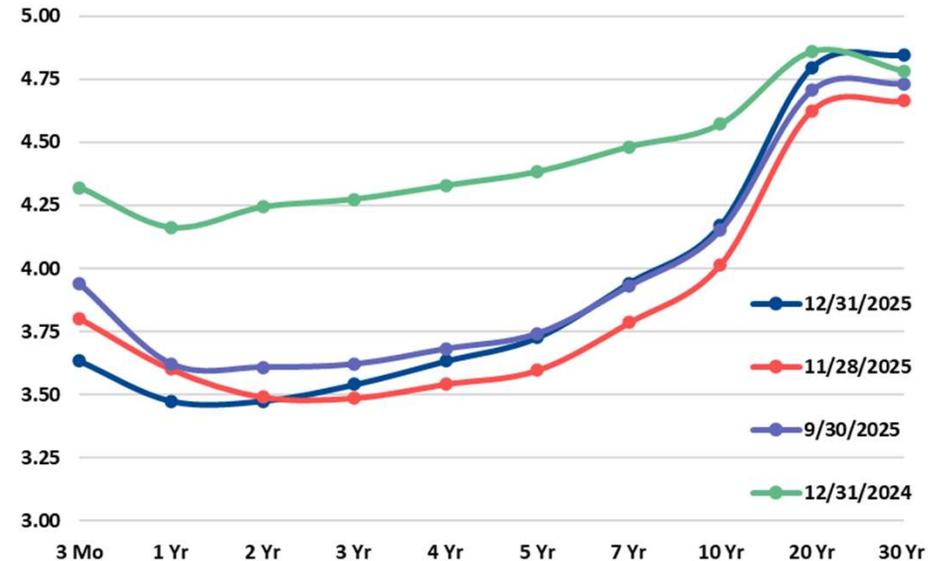
Federal Reserve Median Economic Projections						
As of 12/10/2025						
	Actual	2025	2026	2027	2028	Longer Run
<b>Change in GDP</b>						
December 2025 Projection		1.7	2.3	2.0	1.9	1.8
September 2025 Projection		1.6	1.8	1.9	1.8	1.8
June 2025 Projection		1.4	1.6	1.8		1.8
Actual Q3 2025	<b>4.3%</b>					
<b>Unemployment Rate</b>						
December 2025 Projection		4.5	4.4	4.2	4.2	4.2
September 2025 Projection		4.5	4.4	4.3	4.2	4.2
June 2025 Projection		4.5	4.5	4.4		4.2
Actual December 2025	<b>4.4%</b>					
<b>PCE Inflation</b>						
December 2025 Projection		2.9	2.4	2.1	2.0	2.0
September 2025 Projection		3.0	2.6	2.1	2.0	2.0
June 2025 Projection		3.0	2.4	2.1		2.0
Actual September 2025	<b>2.8%</b>					
<b>Core PCE Inflation</b>						
December 2025 Projection		3.0	2.5	2.1	2.0	
September 2025 Projection		3.1	2.6	2.1	2.0	
June 2025 Projection		3.1	2.4	2.1		
Actual September 2025	<b>2.8%</b>					
<b>Projected Policy Path- Fed Funds</b>						
December 2025 Projection		3.6	3.4	3.1	3.1	3.0
September 2025 Projection		3.6	3.4	3.1	3.1	3.0
June 2025 Projection		3.9	3.6	3.4		3.0
Actual December 2025	<b>3.6%</b>					

# Market Review

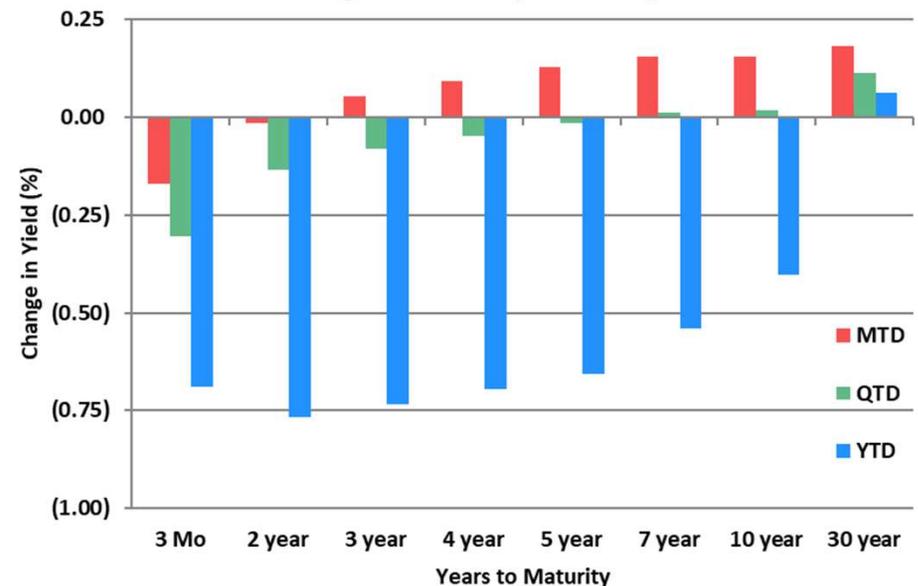
## Yield Curve

- Rates fell across yield curve maturities, except the 30 year.
- The drop in rates was led by intermediate rates reflecting actual and expected Fed rate cuts.
- The 30-year yield rose in recognition of still higher current and potentially future debt issuance.
- The yield curve has steepened to a more normal positive slope. Just the short end inside 1 year is inverted, which should also normalize as the Fed cuts again, bringing down money market rates.
- The overall interest rate environment has normalized with the relationship across maturities near long term averages since 1984.
- The absolute level of interest rates is about .50% - .75% below long-term averages since 1984, which seems justified given current level of moderate inflation and economic growth; however, continued debt issuance is a risk.
- The overall level of interest rates seems to be in equilibrium with the economy and may likely remain in a relatively narrow range for 2026.

Historical Yield Curve



Change in Yield by Maturity

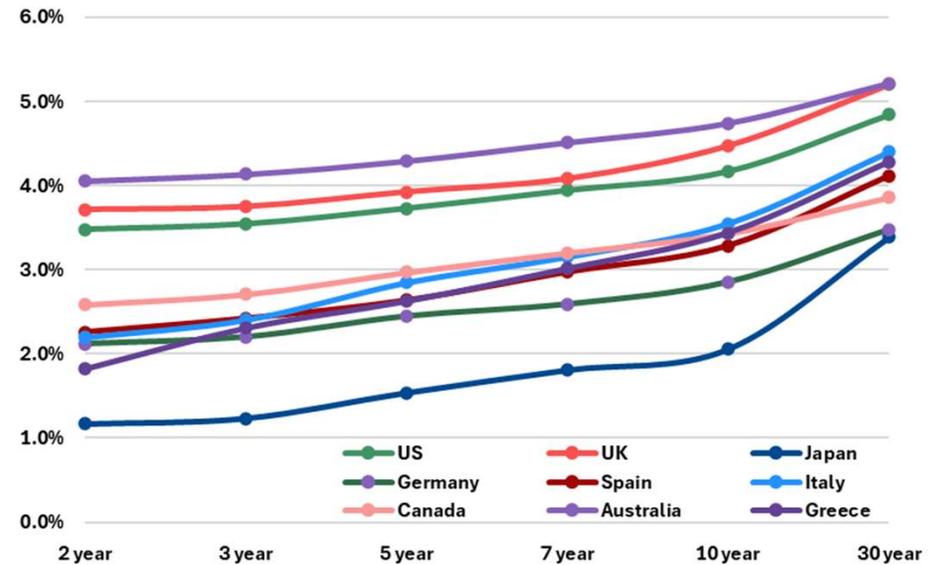


# Market Review

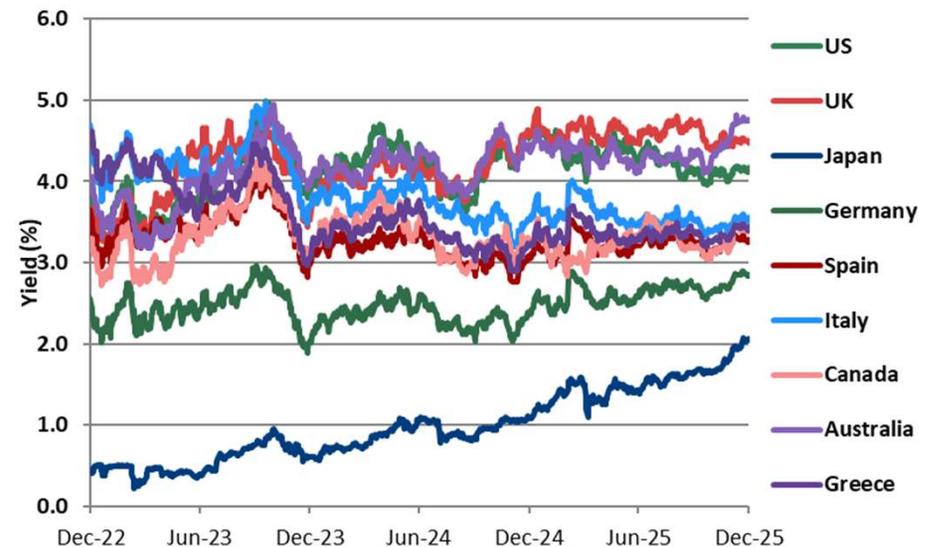
## International Yield Curve

- International central banks have been more aggressive at easing interest rates, ahead of the US, except for Japan who has been tightening, but have recently paused.
- International economies have shown slower growth, including recession in Germany, with lower inflation than their 2% targets.
- Longer term interest rates are rising around the world in response to significantly expanding government deficits, interest expenses, and debt issuance.

International Yield Curves



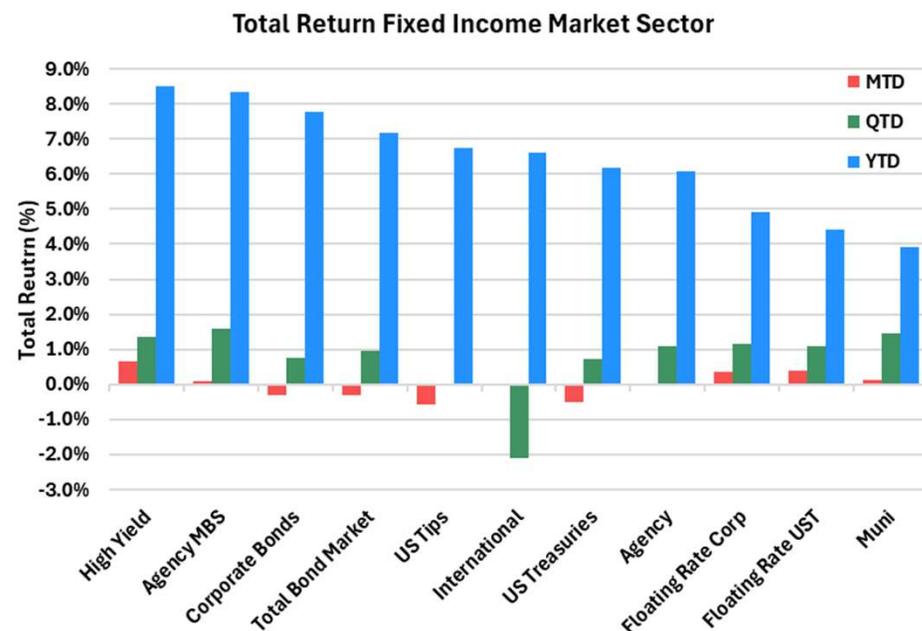
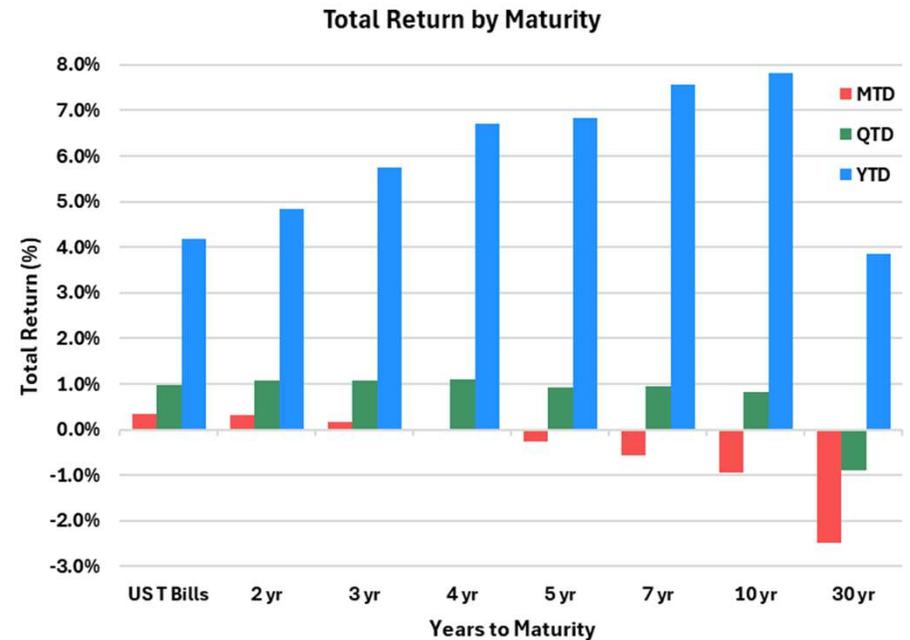
Historical International 10 Year Yields



# Market Review

## Fixed Income Returns

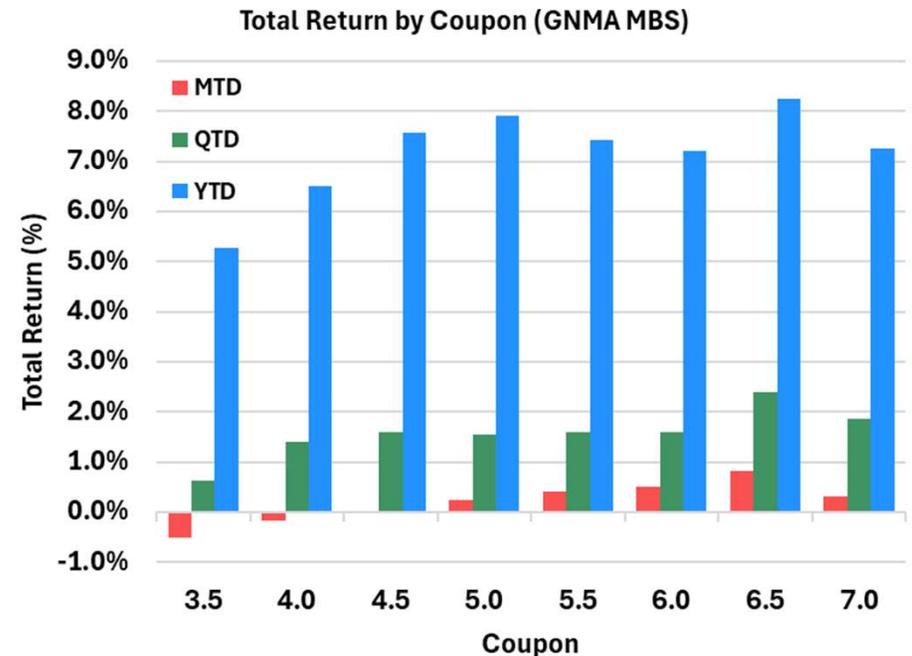
- The drop in rates with a steepening yield curve has benefitted intermediate maturities in Q4 and Year to date showing strong total returns.
- Year to Date, the total bond market has generated a 7.2% total return including income and price appreciation. Gains have been led by the 4-to-10-year maturities. 30-year maturities gained in total return (despite negative price move) due to generating higher income in a positively sloped yield curve environment.
- Agency Mortgage-Backed Securities led returns in Q4 and for the year and have been the best performing sector with High Yield in 2025 at over 8% due to higher income and spread tightening. Corporate bonds have also performed well for the same reasons but have begun to see some stress.
- Municipal bonds were the worst performer of the year, underperforming even on an after-tax basis.
- Vectors strategy has continued to focus on high quality Mortgages and intermediate maturities but have continued to reinvest into longer term maturities opportunistically out a steeper yield curve.



# Market Review

## Fixed Income Returns

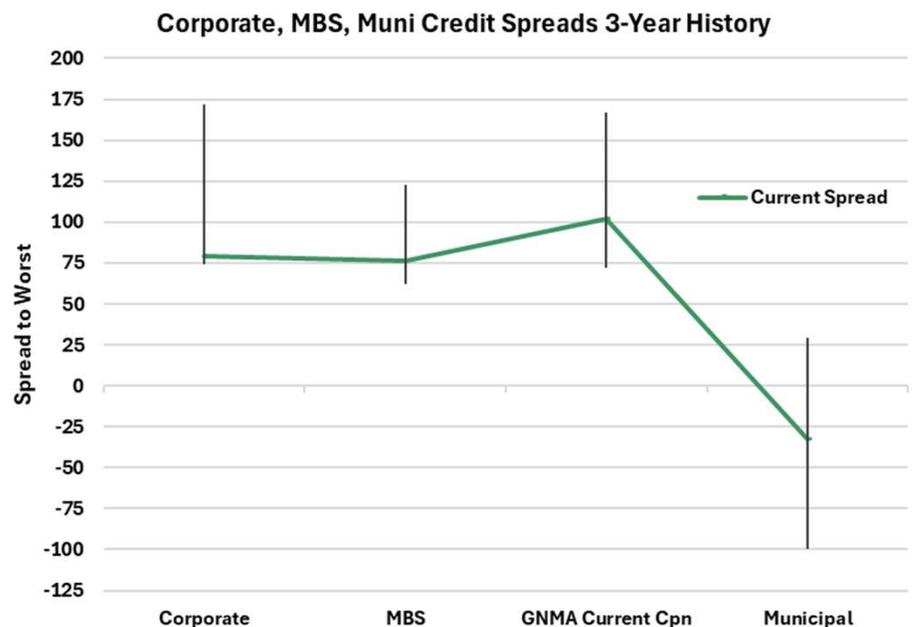
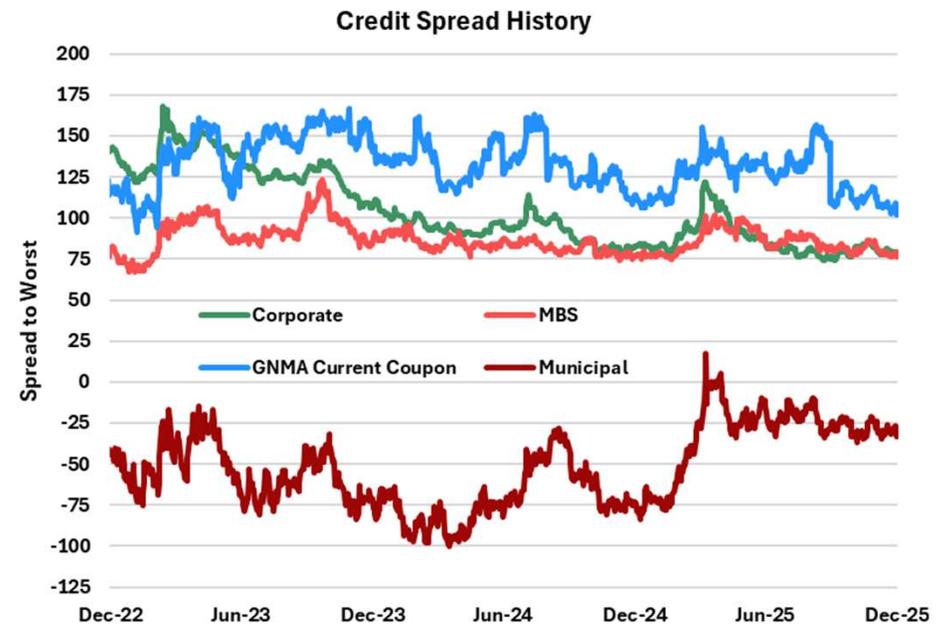
- Mortgages continue to perform well, with “current” coupons (4.5% - 5.5%) seeing the best returns.
- Year-to-date 4.5% - 5.5% coupon mortgages have performed the best due to higher income and price appreciation as rates have fallen and spreads have tightened.
- Vectors has shifted our MBS strategy down in coupon from 5, 5.5 and 6 coupons to 4.5, 5, and 5.5 coupons as further drop-in rates will increase prepayments on high coupons.
- Housing affordability has been an issue stifling the housing market with rates stuck above 6%. Part of the issue is that mortgage spreads in the market remain wide, which makes for good investment that generates high income.
- As spreads narrow and rates dip below 6% amid low rate volatility, prepayment and housing turnover will incrementally increase prepayment activity on higher coupons.
- 5.5% to 6% mortgage rates are historically “normal”, 3% is not. We do not expect mortgage rates to dip below 5.5%.



# Market Review

## Credit Spreads

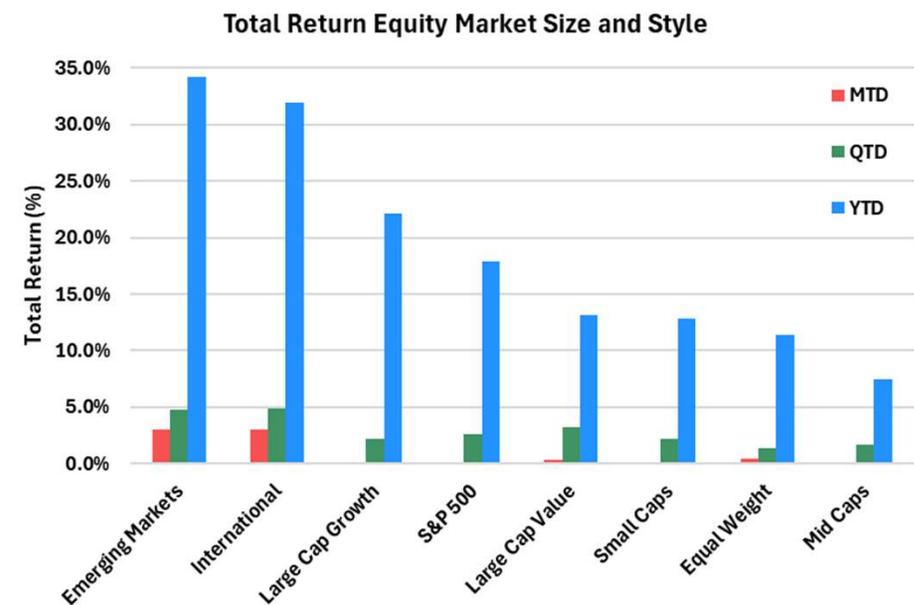
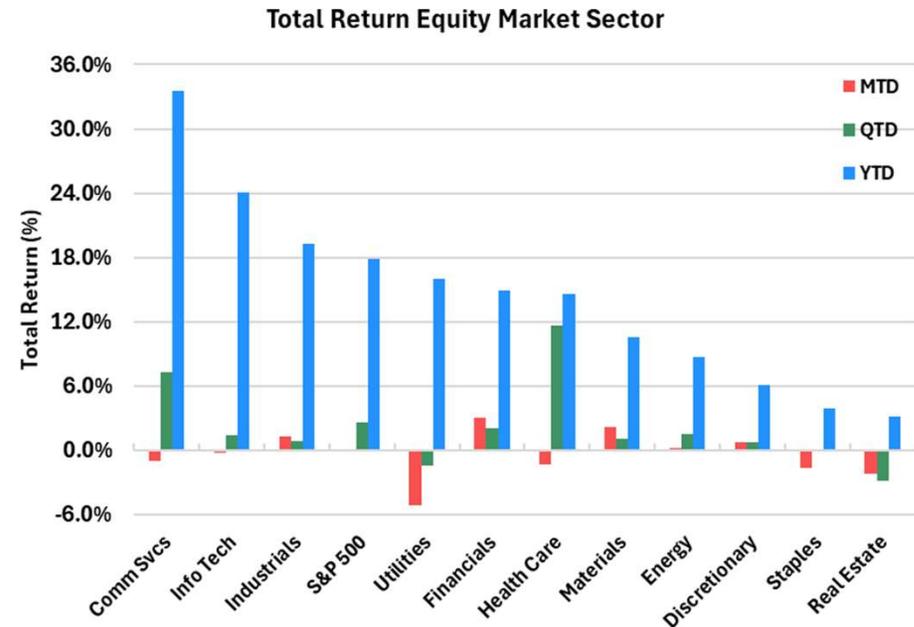
- Yield spreads in corporate bonds settled in near historically tight levels after some mid year volatility.
- Corporate fundamentals came into the year on solid footing; however, the ever-growing private credit markets began to see some stress.
- Interest costs are increasing after a number of years of cheap financing from artificially depressed levels.
- Corporate issuance grew significantly. The environment was marked by the significant widening of Oracle bonds amid a large issuance to fund data center build out.
- Current Coupon MBS remain better relative value than corporates despite recent tightening.
- Overall interest rate volatility should continue to decline, bringing further tightening to Mortgage spreads, pulling absolute level of mortgage rates lower, and helping the housing market.
- Municipals begin to offer relative value for higher tax brackets but in lower quality.



# Market Review

## Equity Returns

- The communications sector was the clear sector winner for the year, led by Google (+29%/66% Q4/YTD, and growing to 5.6% of the S&P 500).
- Info Tech led markets for much of the year but staggered into year end amid stretched valuations and divergence among the “Magnificent 7”.
- The AI momentum was interrupted by growing concerns over excess spending with doubts growing on the return on those investments and how to pay for them.
- Market rotation began to pull up lagging sectors including Health Care, materials and Industrials.
- The S&P 500 equal weighted index regained some ground on the market weighted index at year end due to the drop in Info Tech and its extraordinary weighting while there was an uptick in Value stocks.
- Amid the rotation and quest for diversification, International, Small and Mid cap stocks posted gains, also assisted by the now lower rate environment and chances of further Fed rate cuts.



# Market Review

## Equity Relative Valuation

- The Market Weight S&P 500 trades at a significant premium to other indices currently. With a 22.9 next-twelve-month P/E ratio assuming 11.3% earnings growth.
- Historically, these elevated relative valuations have lasted for some amount of time, but eventually the valuation reverts to the long-term average.
- The Equal Weight S&P 500 is much closer to fair value, trading near its long-term average P/E ratio and has lower growth assumptions suggesting better value for “the rest” of the membership beyond the largest cap members.
- While lower growth assumptions may seem initially negative, it is essentially a lower bar for companies to beat, while the expectations for the market weight S&P 500 is for continued double digit growth for a number of years.
- If the market weighted index fails to hit these earnings growth targets, we could see a quick correction in the valuation of those large stocks.

SPX Index	Act. Growth		Est. Growth			
	Last 12M	12.5%	Next 12M	11.3%	5.6%	0.0%
Headline EPS						
S&P 500	Act. EPS	\$269.3	Est. EPS	\$299.6	\$284.4	\$269.3
Market Weight						
Scenario	Last 12M P/E		Next 12M P/E		Price	
<b>12/31/2025</b>	<b>25.4</b>	<b>\$6,845</b>	<b>22.9</b>	<b>\$6,847</b>	\$6,500	\$6,153
(+1 Std Dev)	23.4	\$6,294	20.3	\$6,077	\$5,769	\$5,461
LT Average	19.3	\$5,208	17.0	\$5,097	\$4,838	\$4,580
LT Median	18.5	\$4,983	16.2	\$4,861	\$4,614	\$4,368
(-1 Std Dev)	15.3	\$4,122	13.7	\$4,117	\$3,908	\$3,699

SPW Index	Act. Growth		Est. Growth			
	Last 12M	9.0%	Next 12M	6.5%	3.2%	0.0%
Headline EPS						
S&P 500	Act. EPS	\$418.8	Est. EPS	\$446.0	\$432.4	\$418.8
Equal Weight						
Scenario	Last 12M P/E		Next 12M P/E		Price	
(+1 Std Dev)	20.4	\$8,563	18.7	\$8,320	\$8,066	\$7,813
<b>12/31/2025</b>	<b>18.5</b>	<b>\$7,764</b>	<b>17.4</b>	<b>\$7,765</b>	\$7,528	\$7,292
LT Average	17.7	\$7,407	16.4	\$7,331	\$7,108	\$6,885
LT Median	17.5	\$7,324	16.5	\$7,338	\$7,114	\$6,891
(-1 Std Dev)	14.9	\$6,251	14.2	\$6,343	\$6,150	\$5,956

# Market Review

## Equity Relative Valuation

- The S&P 400 Mid Cap index offers even better relative value than the Equal Weight S&P 500 Index. Earnings growth expectations are higher, but this is usually the case for smaller companies that are earlier into their business cycle.
- If the earnings expectations aren't met by these smaller companies, we may see a correction below the long-term average valuation, but the downside is much less risky than the market weight S&P 500.
- The S&P 600 Small Cap index shows a similar story to mid caps, at an even more attractive valuation, but slightly lower expected earnings growth.
- The lower rate environment is also beneficial to small and mid cap stocks due to their degree of floating rate debt financing.

MID Index	Act. Growth		Est. Growth		6.0%	0.0%
	Last 12M	1.1%	Next 12M	12.1%		
Headline EPS						
S&P 400						
Mid Cap	Act. EPS	<b>\$180.2</b>	Est. EPS	<b>\$202.0</b>	\$191.1	\$180.2
	Last		Next			
Scenario	12M P/E	Price	12M P/E	Price		
(+1 Std Dev)	22.9	\$4,136	18.4	\$3,725	\$3,524	\$3,323
LT Median	19.5	\$3,508	16.5	\$3,333	\$3,153	\$2,973
<b>12/31/2025</b>	<b>18.4</b>	<b>\$3,313</b>	<b>16.4</b>	<b>\$3,308</b>	\$3,129	\$2,951
LT Average	19.5	\$3,512	16.4	\$3,312	\$3,133	\$2,955
(-1 Std Dev)	16.0	\$2,888	14.4	\$2,900	\$2,743	\$2,587

SML Index	Act. Growth		Est. Growth		5.0%	0.0%
	Last 12M	8.0%	Next 12M	10.0%		
Headline EPS						
S&P 600						
Small Cap	Act. EPS	<b>\$86.9</b>	Est. EPS	<b>\$95.7</b>	\$91.3	\$86.9
	Last		Next			
Scenario	12M P/E	Price	12M P/E	Price		
(+1 Std Dev)	29.5	\$2,567	19.1	\$1,826	\$1,742	\$1,659
LT Average	21.5	\$1,871	16.6	\$1,591	\$1,518	\$1,445
LT Median	20.7	\$1,796	16.5	\$1,580	\$1,508	\$1,436
<b>12/31/2025</b>	<b>16.9</b>	<b>\$1,466</b>	<b>15.4</b>	<b>\$1,469</b>	\$1,402	\$1,335
(-1 Std Dev)	13.5	\$1,176	14.2	\$1,356	\$1,294	\$1,232

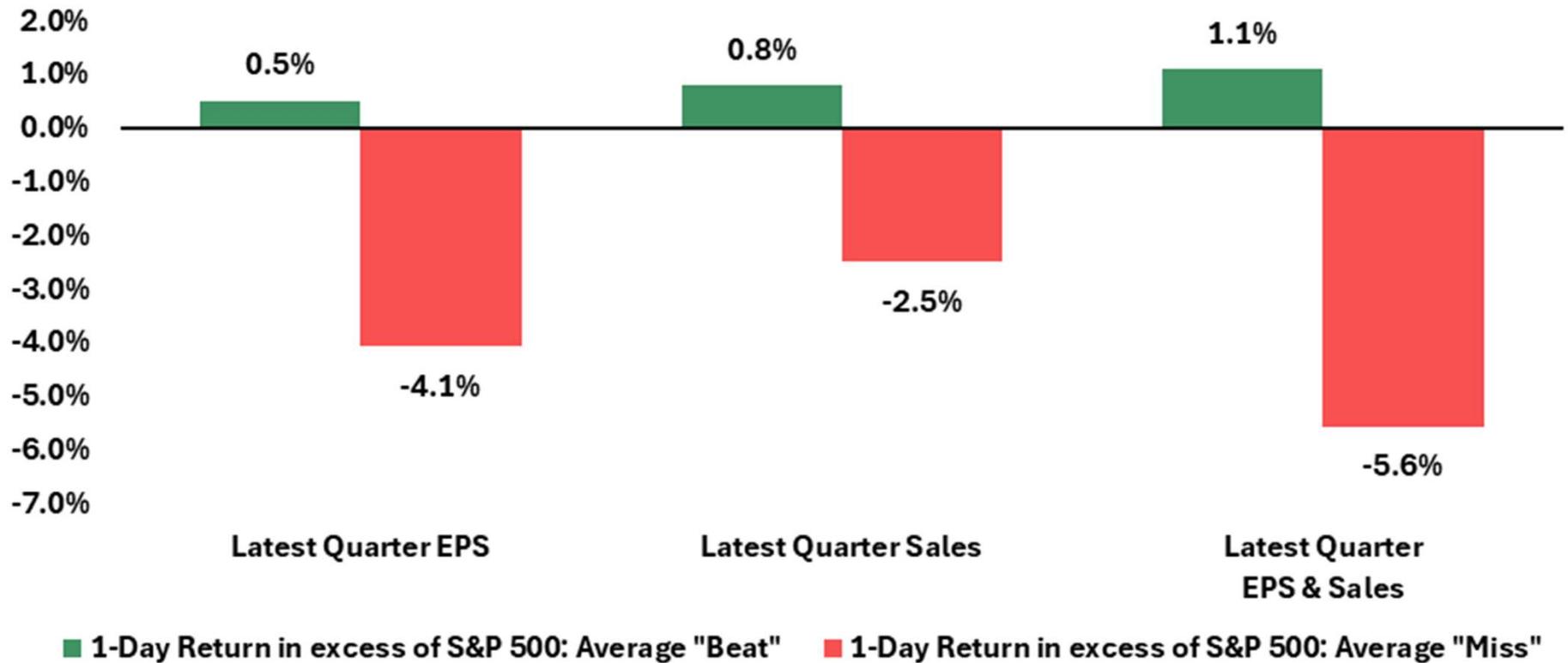
# S&P 500 Sector Scorecard

- Technology, Financials, Industrials, and Communications had the highest earnings growth Y/Y for Q3 2025.
- These sectors are expected to continue to have strong earnings growth over the next several quarters, while a number of sectors are expected to see a dip over the next two quarters.
- The expectation in technology earnings growth is reliant on continued high capital expenditures from the hyperscalers. This would also affect other sectors but affects technology the most.

Sector	AQ3 2025 Y/Y Growth	EQ4 2025 Y/Y Growth	EQ1 2026 Y/Y Growth	EQ2 2026 Y/Y Growth	EQ3 2026 Y/Y Growth	EQ4 2026 Y/Y Growth
Communications	15.7%	7.3%	-2.1%	9.7%	5.7%	14.9%
Discretionary	6.8%	-3.1%	-8.6%	10.3%	8.4%	20.3%
Staples	0.7%	-0.4%	5.2%	7.0%	6.2%	8.9%
Energy	-2.0%	2.4%	3.1%	12.7%	7.8%	12.4%
Financials	21.6%	5.0%	14.9%	7.5%	2.7%	12.3%
Real Estate	2.0%	0.3%	2.4%	1.4%	3.4%	7.4%
Health Care	4.8%	-0.4%	3.8%	7.8%	9.0%	14.0%
Industrials	20.3%	6.4%	5.0%	10.8%	16.9%	20.1%
Technology	27.5%	22.4%	26.2%	29.7%	23.9%	23.6%
Materials	13.0%	3.7%	22.4%	19.2%	17.4%	25.3%
Utilities	9.6%	4.2%	5.6%	12.4%	6.0%	13.1%

# S&P 500 3Q25 Price Reaction

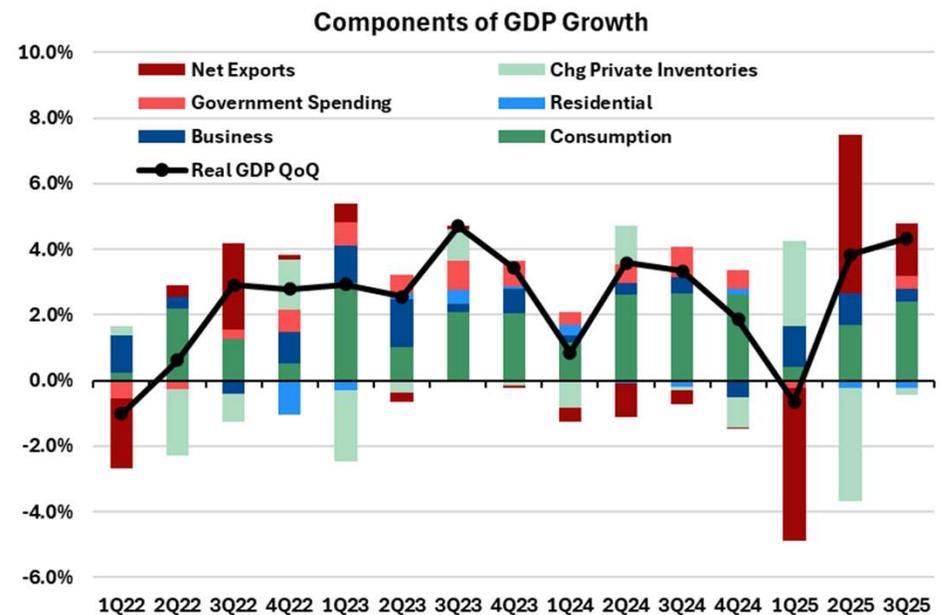
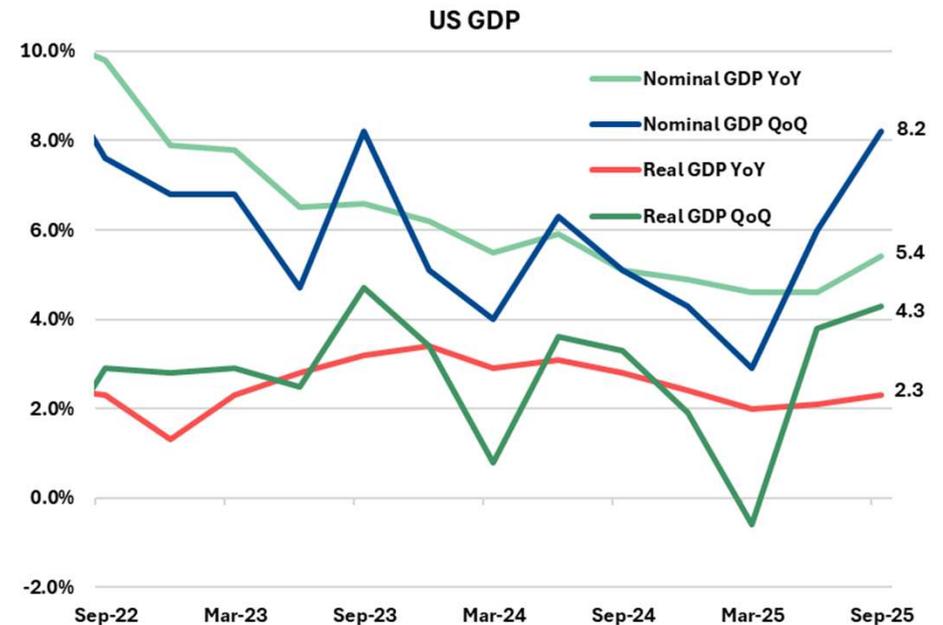
## S&P 500 EPS, Sales Surprise vs. Average Price Change



# Economic Outlook

## Economic Activity

- Measured GDP has been strong the past two quarters in part due to significant changes in Net Exports, reversing the Q1 tariff induced drop. With that said, the trade gap declined significantly in 2025.
- The overall economy is bifurcated, or K shaped, if not trifurcated along upper, middle- and lower-income consumers, with higher income continuing to spend, lower income cutting back, and middle income migrating to bargains.
- Demographic groups are also showing differentiating economic behavior.
- Consumption has been a strong contributor to overall GDP in the recent two quarters.
- Business investment (AI and Data Center related) has been strong but has begun to decline after a surge that has powered stock returns.
- Residential investment has been nonexistent amid affordability issues in the housing market.
- There has been virtually zero growth in Government spending YTD.



# Economic Outlook

## International Economic Activity

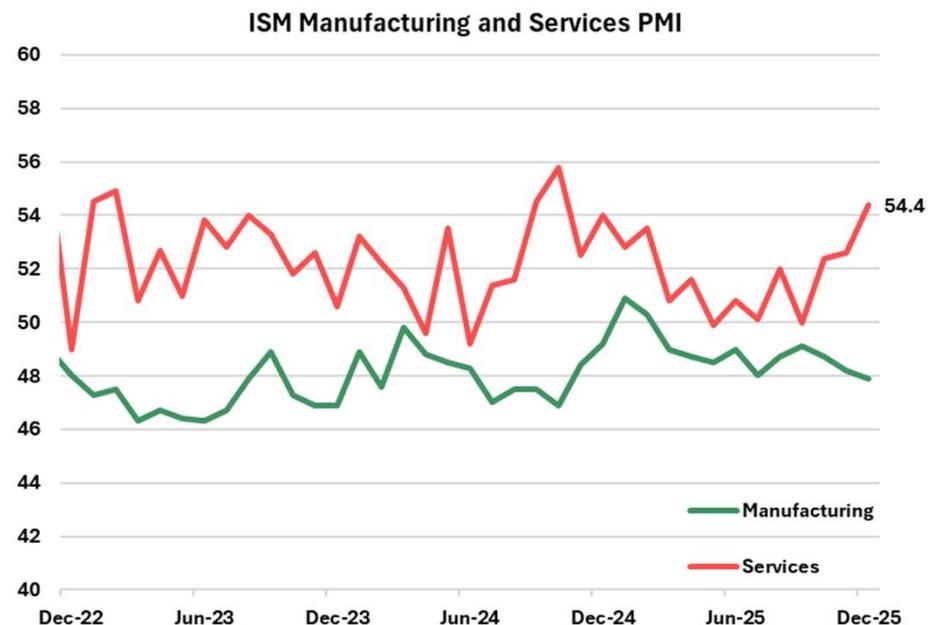
- Central bank rates have fallen around the world over the past year, except in Japan, which raised rates.
- Global GDP seems to have stabilized at a low rate, while improvement in year over year inflation seems to have stalled, and even upticked, but still at levels closer to Central bank targets.
- Global trade has been upended with considerable impacts to regional GDP measures, and will likely continue to do so for the balance of the year.

Country	Central Bank Rate		2023	2024	Real GDP YoY	Real GDP YoY	1 Year GDP	Inflation	Inflation	Inflation
	1 Year Ago	Central Bank Rate	Debt to GDP %	Debt to GDP %	1 Year Ago	% Change	Trend	1 Year Ago	Inflation	Trend
US	4.50%	3.75%	119.0%	120.8%	2.8%	2.3%	-0.5%	2.9%	2.7%	-0.2%
Eurozone	3.15%	2.15%			1.0%	1.4%	0.4%	2.4%	1.9%	-0.5%
Germany			62.9%	63.9%	-0.6%	0.3%	0.9%	2.6%	1.8%	-0.8%
France			109.8%	113.1%	1.1%	0.9%	-0.2%	1.3%	0.8%	-0.5%
Italy			134.6%	135.3%	0.5%	0.6%	0.1%	1.3%	1.2%	-0.1%
UK	4.75%	3.75%	100.4%	101.3%	1.3%	1.3%	0.0%	2.5%	3.4%	0.9%
Canada	3.25%	2.25%	107.7%	110.8%	2.5%	0.4%	-2.1%	1.8%	2.4%	0.6%
Mexico	10.00%	7.00%		45.1%	1.4%	-0.1%	-1.5%	4.2%	3.7%	-0.5%
Australia	4.35%	3.60%	49.0%	49.8%	0.8%	2.1%	1.3%	0.8%	2.1%	1.3%
Japan	0.25%	0.75%	240.0%	236.7%	0.8%	0.6%	-0.2%	2.9%	2.9%	0.0%
China	3.10%	3.00%	82.0%	88.3%	4.6%	4.5%	-0.1%	0.1%	0.8%	0.7%
Russia	21.00%	16.50%	19.5%	20.3%	3.3%	0.6%	-2.7%	9.5%	5.6%	-3.9%
Brazil	12.25%	15.00%	84.0%	87.3%	4.1%	1.8%	-2.3%	4.8%	4.3%	-0.6%

# Economic Outlook

## Economic Activity

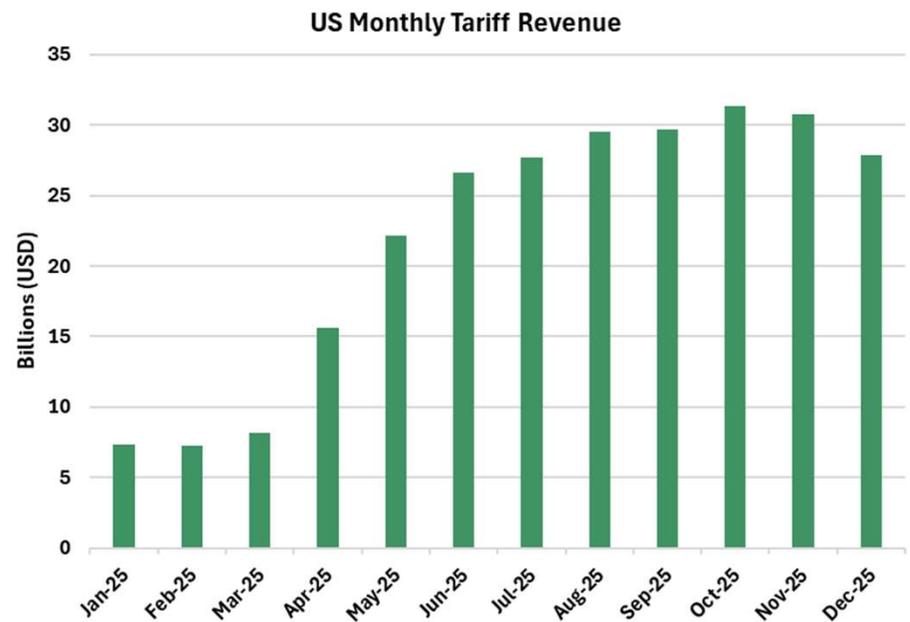
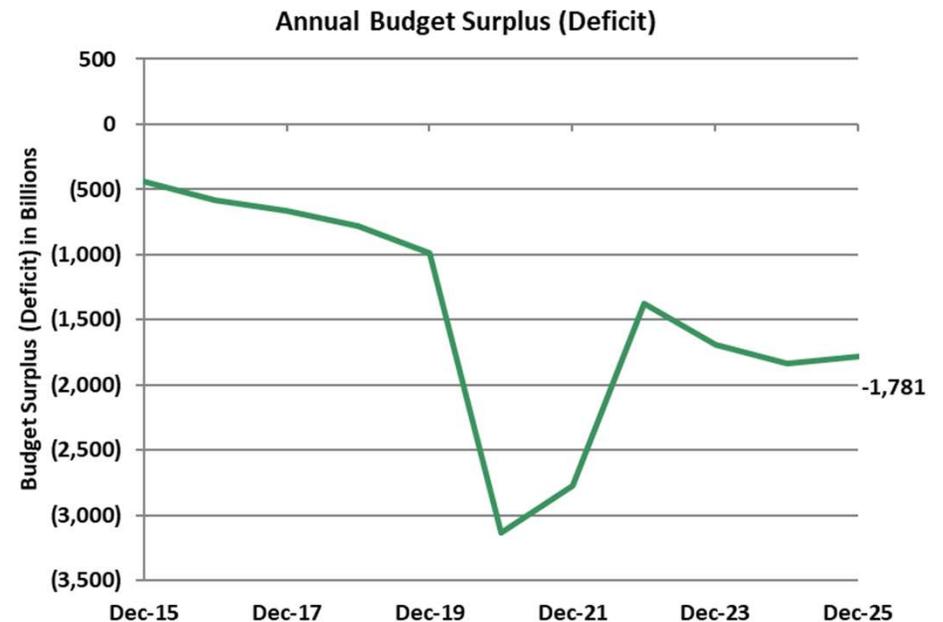
- The Citi surprise index is slightly positive and a bit more stable, however there has been a lack of data due to the US Government shutdown.
- The service sector continues to dominate consumer activity, driven by higher income earners, baby boomers, and those benefitting from the market wealth effect.
- Better than expected inflation also supports the Surprise index while the overall employment environment has weighed on it, but overall moderation has kept expectations close to reality.
- ISM Services is resurging stronger than expected and helping to drive economic activity.
- Manufacturing continues to struggle to get above 50, and remains in contractionary territory, moderating economic activity and surprising to the downside.
- Expectations are that reshoring and buildout of manufacturing through trade deals, and the build out of data centers and required energy infrastructure will boost the manufacturing and production components of the economy.



# Economic Outlook

## Fiscal Policy

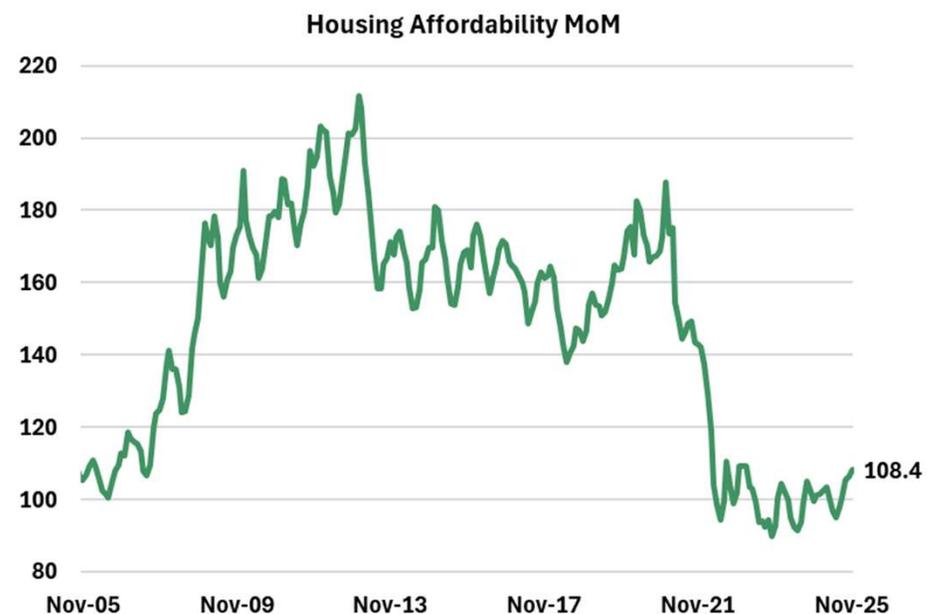
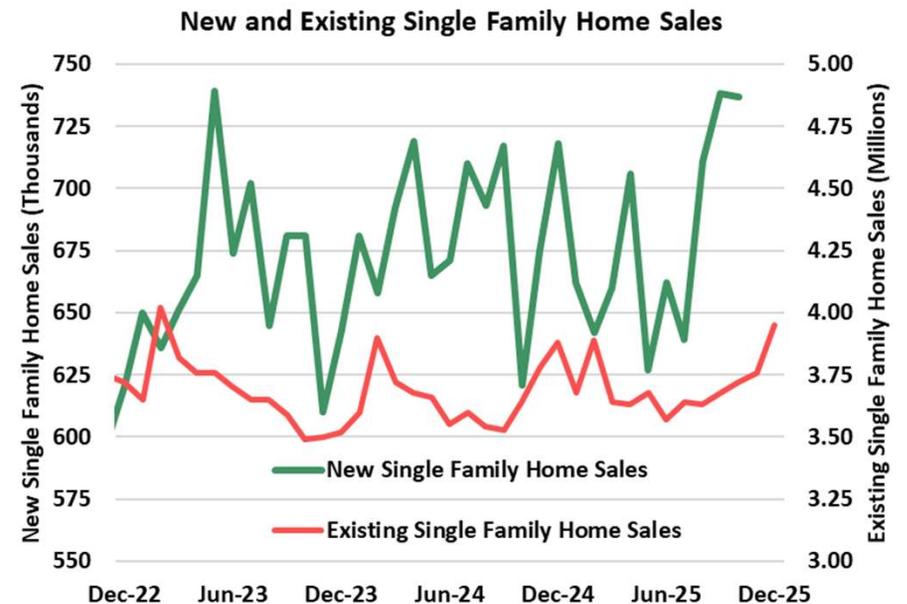
- The US budget deficit has stabilized and continued to work itself lower after a period of massive and excessive borrowing.
- The One Big Beautiful Bill curbed spending growth, which was helpful to the budget in 2025, but will also bring in tax cuts that will reduce tax revenue.
- Trade policy has generated a significant increase in Tariff revenue, up to \$30 Billion monthly, that has helped the budget deficit.
- The Supreme Court has yet to weigh in on the legality of current tariffs, while the administration prepares alternative support for current tariffs if they are ruled against. It is unlikely that collected tariffs with need to be returned.
- Tariff income will be volatile as trade deals continue to be worked out, and global flows continue to shift, and all will have a significant impact on overall economic activity.
- The overall budget deficit is still a problem as interest income continues to be a significant component of government spending at more than \$1 Trillion per year.



# Economic Outlook

## Housing

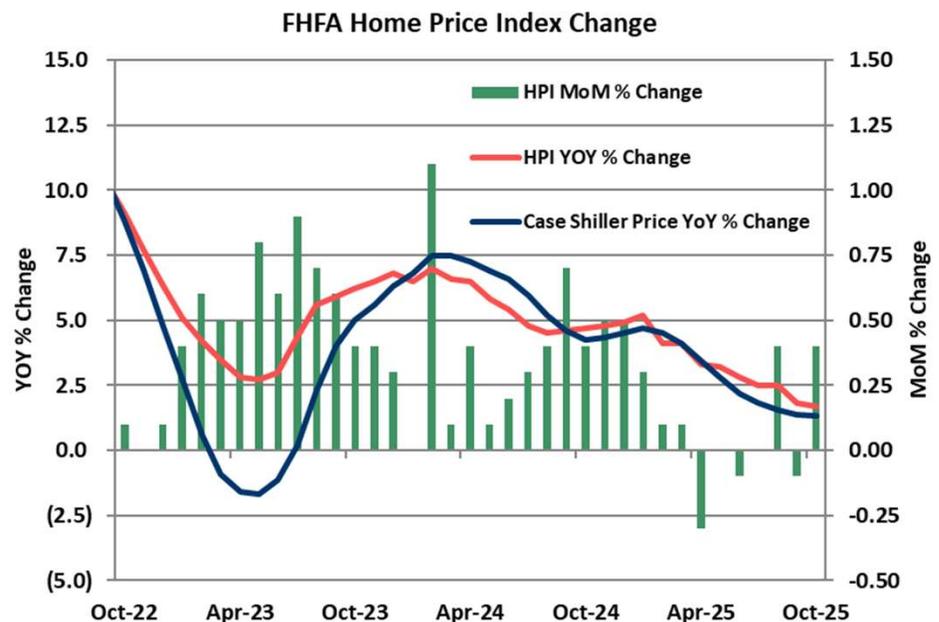
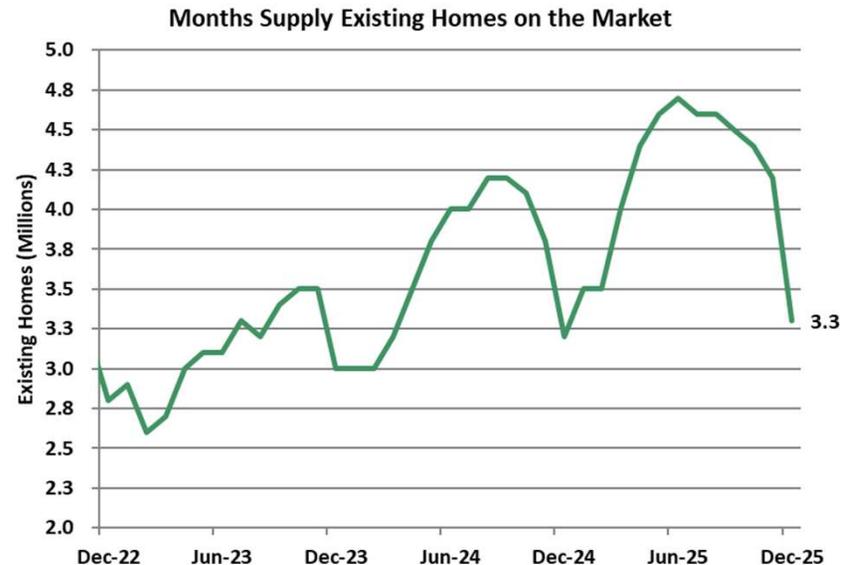
- The housing affordability index has recently ticked up after a few years at depressed levels due to recent decline in rates and prices, leading to increased home sales.
- Mortgage rates continue lower, aided by lower overall market interest rates, and tightening mortgage spreads in the bond market.
- New single family home sales have risen recently as the mortgage rate has continued to drift lower, and home prices have moderated and in fact fallen in some parts of the country.
- Builder discounts and rate buydowns have also boosted sales of new homes. 41% of builders have cut prices recently.
- Existing home sales did not see the same degree of rise, as new homes are cheaper with incentives and many existing homeowners do not want to give up their lower-than-market rate to move.
- Pent up demand and acclimation to current market conditions have contributed to activity.



# Economic Outlook

## Housing

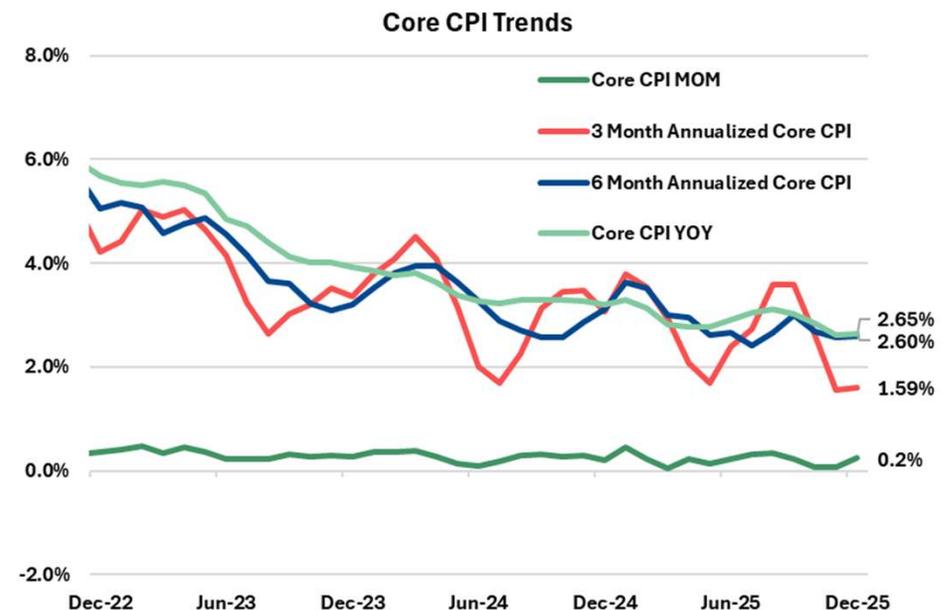
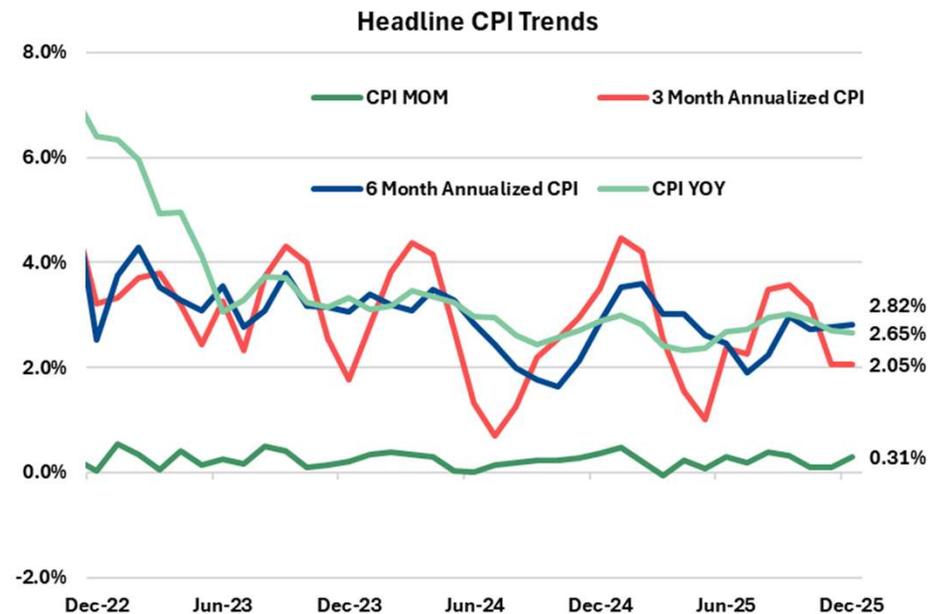
- The housing market is trying to find equilibrium amid price changes, interest rates, and available housing inventory.
- The increase in affordability and sales has taken some inventory off the market.
- Home prices have also been volatile as an overall declining/stabilizing level and have been increasingly divergent across the country.
- This continued fall in Mortgage rates and housing turnover has generated increased refinance activity.
- If 30-Year Mortgage rates continue to fall, it is very likely that refinances will continue, raising prepayments on higher interest rate mortgages.
- It is to be seen if lower rates can further spur increasing home sales without a further fall in prices.



# Economic Outlook

## Inflation

- Headline CPI inflation finished 2025 at 2.7%, while Core finished at 2.6%, incrementally moving toward the Fed's 2% target.
- Recent readings are a bit murky due to the Government shut down that eliminated the report for November.
- After ticking up a bit, recent readings have dipped back down, continuing the decelerating trend as can be seen in the rolling 6 month and 3-month basis.
- The annualized 3-month Core CPI has dipped below the 2% level.
- We expect energy, housing, and consumer prices to continue to flow through to allow inflation indicators to continue their downward trend.



# Economic Outlook

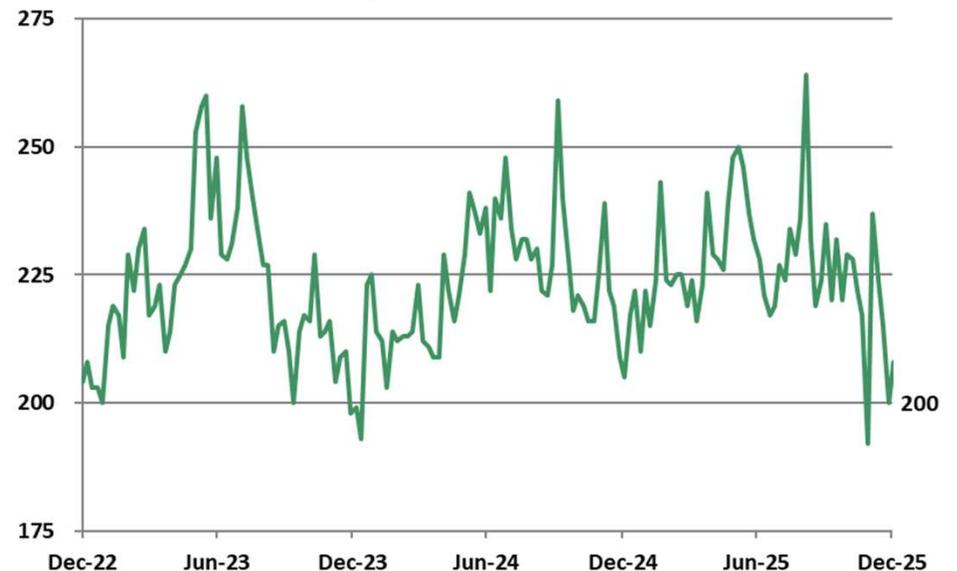
## Labor Market

- Job openings continue to trend lower as companies adopt a no-hire, some-fire policy with the growing economic uncertainty.
- There have been a significant number of corporate layoff announcements recently.
- Weekly unemployment claims remain in a range just above 200k showing limited layoffs. The holiday period and government shut down have created volatility in the numbers.
- The US Government shutdown has paused BLS labor market data. It has begun to catch up and is being reported with moderate numbers. We expect continued moderation with significant revisions over the first quarter.

US Job Openings Total (JOLTS)



Weekly US Initial Jobless Claims

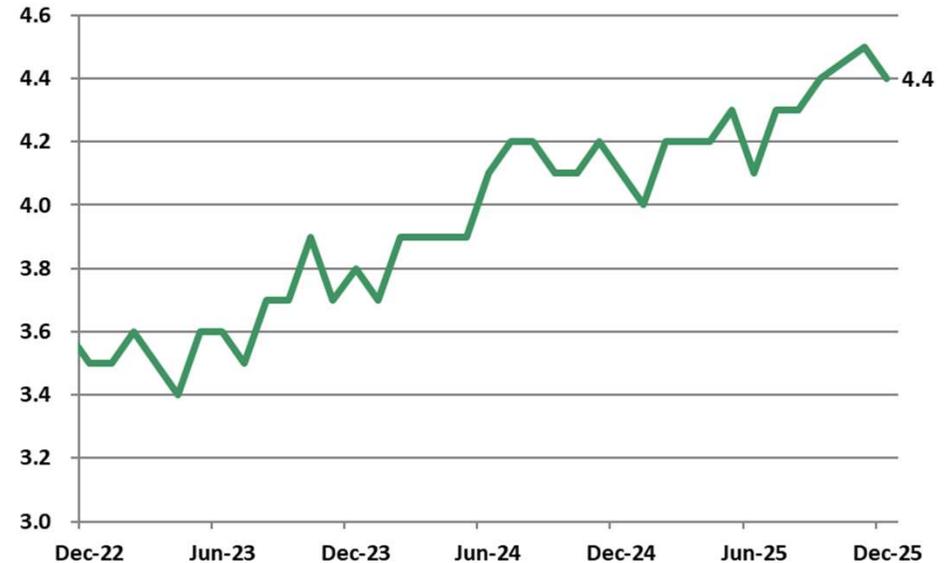


# Economic Outlook

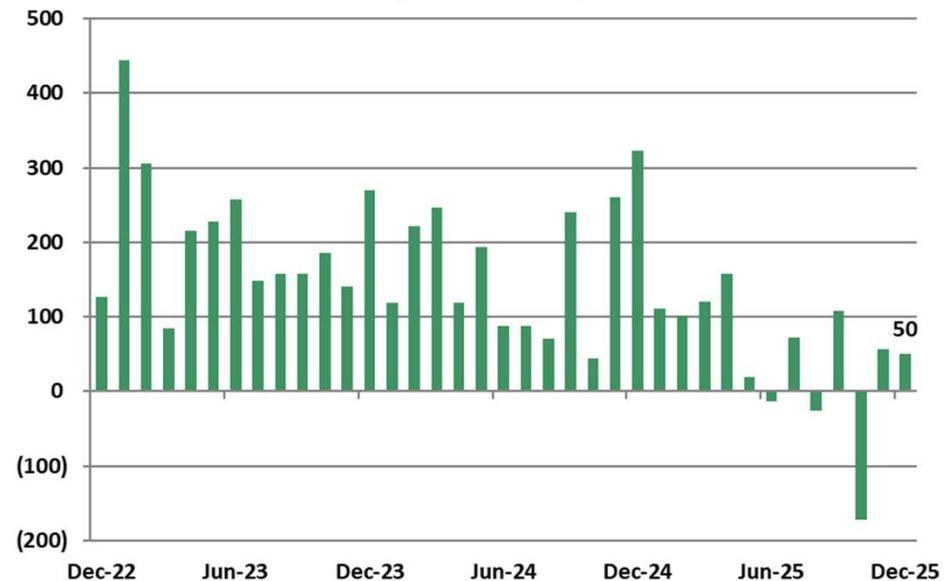
## Labor Market

- The unemployment rate has risen to 4.4% due to a lack of new jobs, which averaged less than 50k in 2025, and averaged -15k in the second half of the year as hiring stopped and layoffs picked up.
- Monthly Payroll additions have seen significant downward revisions and continue to dwindle as few new jobs are being created outside the Health Care and Social Services sectors, while Government employment is being reduced..
- Layoffs continue in technology, and have spread to some other cyclical economic sectors, while new jobs are getting harder to find.
- Government and corporate layoff announcements have begun to flow through the data.
- We expect that the employment picture will improve in the second half of the year as job openings and hiring will increase with the next stage of data center, manufacturing reshoring, and growth in energy production start to take place.

Historical Unemployment Rate



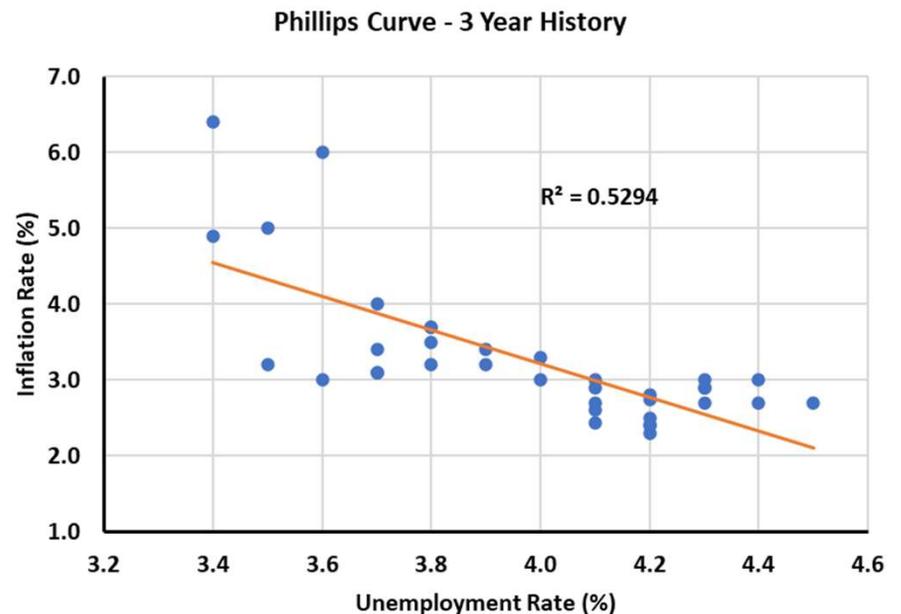
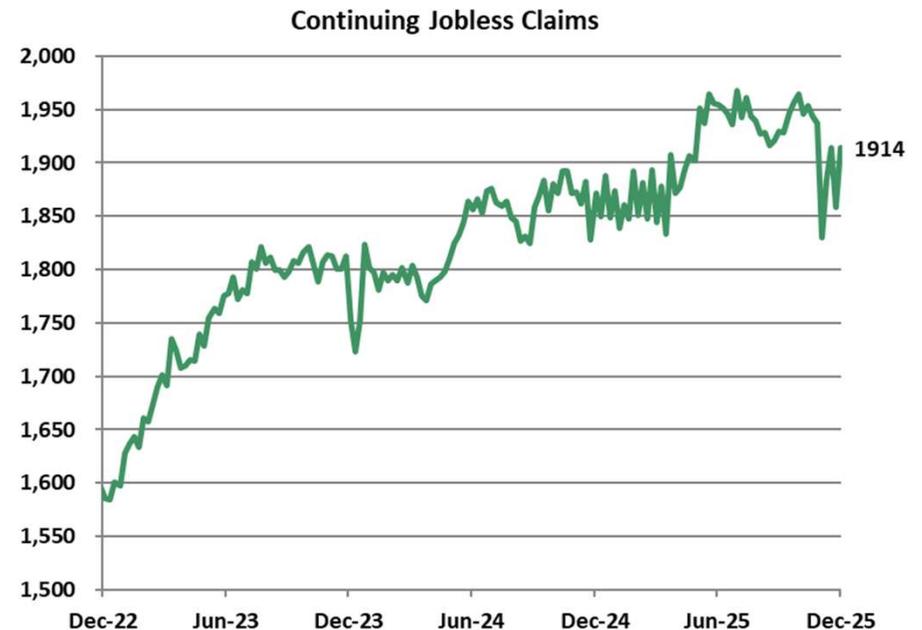
Monthly Non-Farm Payrolls



# Economic Outlook

## Labor Market

- The increase in continuing claims shows that it is getting harder to find work after layoffs.
- The increased unemployment rate will continue to weight on consumer demand, putting additional downward pressure on inflation.
- The Phillips Curve seems to be intact over the recent few years as we move on from the high demand for labor period.
- Average Hourly earnings rose 3.4% in the past year, down from the previous years growth, but still above inflation, which would be net stimulative to the economy.
- Again, we expect that the employment picture will improve in the second half of the year as job openings and hiring will increase with the next stage of data center, manufacturing reshoring, and growth in energy production start to take place, which may incrementally increase inflationary pressures again.



# Economic Outlook

## Oil Prices & The Dollar

- Oil prices have been volatile due to geopolitical conflicts in the Middle East and Venezuela but remain in a downtrend due to increased production and we expect this to continue through 2026. Prices may decline below \$50.
- Natural Gas will take on a greater role in energy going forward including production, use, and exporting of liquified natural gas. Natural Gas prices have increased.
- The dollar remains at weaker levels but has reversed from the lows. It will remain volatile amid monetary and fiscal policy, uncertainty around trade policy, and growing geopolitical risks.
- The USD on the chart is the trade weighted dollar, which remains volatile.
- Turmoil in trade and volatility in currency markets has boosted the price of Gold.

