



NEWPORT CAPITAL GROUP

Market Commentary and Outlook

Q3 2025

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Capital Markets Performance

U.S. equity markets ended the third quarter near record highs, as strong corporate earnings and the anticipation of the Federal Reserve resuming its rate-cutting campaign drove returns. Global capital markets remained resilient despite mixed economic data and continued trade and political headlines. The S&P 500 ended the third quarter up 8.1% and 14.8%, year to date. Growth stocks outperformed value stocks for large caps, while value led growth in the mid and small cap segments of the market, with Small Cap Value the best relative performer for the quarter, up 12.6%. Ten of the eleven S&P 500 sectors were positive for the quarter, led by the Technology and Communication Services sectors. The Consumer Staples sector was the only negative-performing sector in the third quarter.

International stocks produced solid returns in the third quarter with mixed performance versus the U.S. as the MSCI All Country World Index ex USA gained 6.9%, while the MSCI Emerging Markets Index was up 10.6%. International stock returns year to date have benefited from a weaker U.S. dollar as well as fiscal and monetary stimulus.

Interest rate volatility continued during the third quarter as the market digested U.S. policy uncertainty and global inflation concerns. The U.S. yield curve steepened as short-end Treasury yields fell in anticipation of the Fed resuming its rate-cutting campaign. Credit spreads continued to tighten from historically low levels as investors grew more comfortable owning corporate debt amid strong corporate earnings reports. The U.S. Aggregate Index was up 2.0% in the third quarter, with all six sectors recording gains led by Corporate Bonds and Mortgage-Backed Securities. Lower-rated bonds and longer-duration bonds were relative outperformers for the quarter.

U.S. Economy and the Federal Reserve

The U.S. economy expanded by 3.8% on an annual basis in the second quarter following a 0.6% contraction in the first quarter. The rebound in Real U.S. GDP primarily reflected a decrease in imports, which declined following the early April tariff announcement. While we still anticipate slower economic growth into year-end, the economy should be able to grow and avoid a recession this year, in our view. However, the ongoing U.S. government shutdown adds a level of uncertainty. Importantly, tax cuts should be a tailwind for consumer spending and economic growth in the first half of 2026.

The U.S. job market weakened in the third quarter as monthly job gains slowed, with the August unemployment rate at 4.3% and wages up 3.7% year-over-year. The unemployment rate had been in a narrow range of 4.0% to 4.2% since May 2024, and we believe it could work its way towards 4.5% in a softer economic environment.

Inflation continued to move higher in the third quarter and remained above the Fed's 2.0% annual target. Tariffs represent a one-time step up in prices and would boost inflation in the short term, pushing inflation back up above 3.0% and further away from the Fed's desired rate. Consumers have yet to feel the full effect of the tariffs as pre-tariff inventories continued to be depleted. We anticipate the tariff rate on U.S. imports may approach 20.0% as compared with a 2.4% rate last year. In early April, the markets were digesting the potential for a tariff rate on U.S. imports at or above 30.0%.

The U.S. Federal Reserve reduced its target federal funds rate at its September meeting to a range of 4.0% to 4.25%, citing softness in the job market. This was the first interest rate cut since December 2024. The Fed updated its forecast for two additional 25 basis point cuts this year, with one 25 basis point cut next year. The Fed appears willing to allow inflation to remain above its target with a focus on its maximum employment mandate. Current market expectations are consistent with the Fed's forecast for two 25 basis point rate cuts by the end of the year, with the market forecasting two to three additional 25 basis point cuts next year. We expect the Federal Reserve's terminal rate to be in the range of 3.0% to 3.25% by the middle of next year.

Outlook and Portfolio Positioning

We believe a cooling but still growing U.S. economy, along with additional Fed interest rate cuts and solid corporate earnings, should be supportive for markets as we head into year-end. The odds of a recession or potential stagflation appear unlikely in the short term, in our view. Policy uncertainty, geopolitical tensions, and stretched market valuations for certain areas of the market remain potential risks.

Market performance year to date in 2025 reiterates the importance of being diversified across asset classes and geographies. In our view, the best way to navigate the current market environment is with a disciplined and well-diversified approach. That is why we remain balanced in our equity across growth and value styles, different market capitalizations, and global regions. Market rotation has been significant year to date, with international markets outperforming the U.S. markets by over ten percent and small caps outperforming recently. A continued weaker U.S. dollar, fiscal and monetary stimulus and still attractive relative valuations remain catalysts for international equities. In the U.S., value and small-cap stocks remain relatively attractive versus growth and larger capitalization stocks.

Our fixed income portfolio remains positioned toward intermediate duration and a tilt toward quality, consistent with our expectations for economic data to soften into year-end. Interest rates have moved lower this year, which has boosted fixed income returns and provided ballast for our portfolios. Higher coupon rates also help insulate fixed income holdings from any potential movement higher in interest rates.

Despite market uncertainty, it remains critical to stay diversified and committed to long-term investing. Market history shows that time in the markets produces better outcomes than attempting to time the markets.

As always, we thank you for your continued support and trust in Newport Capital Group.

Disclosures

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