

GOLDBERG LARKIN

FINANCIAL EMPOWERMENT
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Fourth Quarter 2025 Outlook

Third Quarter Recap – Markets Continue to Grind Higher The Market

U.S. equity markets had another positive quarter, primarily led by surging technology stocks and the broad Nasdaq Composite Index, with market momentum showing little sign of abating. Continued political pressure and deteriorating jobs numbers, beginning with the July jobs report, increased the urgency for supportive action from the Federal Reserve (the “Fed”). The prospects for lower cost of money (i.e. lower borrowing costs) due to expected “Fed” interest rate cuts, tied with better-than-expected second quarter corporate profit growth boosted the rally. As anticipated, the September rate cut from the “Fed” provided further fuel for the market. Interest rates markets have priced in further rate cutting from the “Fed” in October and again in December. The Standard & Poor’s 500 rally tested, but failed to break, the 6,700 resistance level in the latter part of the quarter as geopolitical phenomena, like a potential government shutdown, made headlines. As it was, the shutdown did in fact occur starting October 1st.

Over the third quarter, the more value-oriented Dow Jones Industrial Average (DJIA) was up 5.8% on a total return basis. The S&P 500 advanced 8.1%, and the Tech-heavy NASDAQ composite climbed 11.4%, while the highly leveraged Small Cap Russell 2000 was up 12.4%¹.

On the sector front, Technology, Communication Services, and Consumer Discretionary were up the most, advancing 13.9%, 11.4%, and 10.6%, respectively. The laggards were Consumer Staples, down (2.7%), Materials up 2.0%, and Financials up 2.4% (Figure-1)².

In the bond market, interest rates moved lower across all maturities. Longer maturity bonds (more sensitive to interest rate movements) outperformed shorter ones. The Bloomberg U.S. Aggregate Bond Index, with moderate duration (6.1 years), was up 2.1%. Corporate bonds outperformed Treasuries as spreads continued to narrow. For example, the iShares 10-20 Year Treasury Bond ETF (ticker: TLH) was up 2.5%, while the similar duration corporate iShares 10+ Year Investment Grade Corporate Bond ETF (Ticker: IGLB) was up 4.0%³.

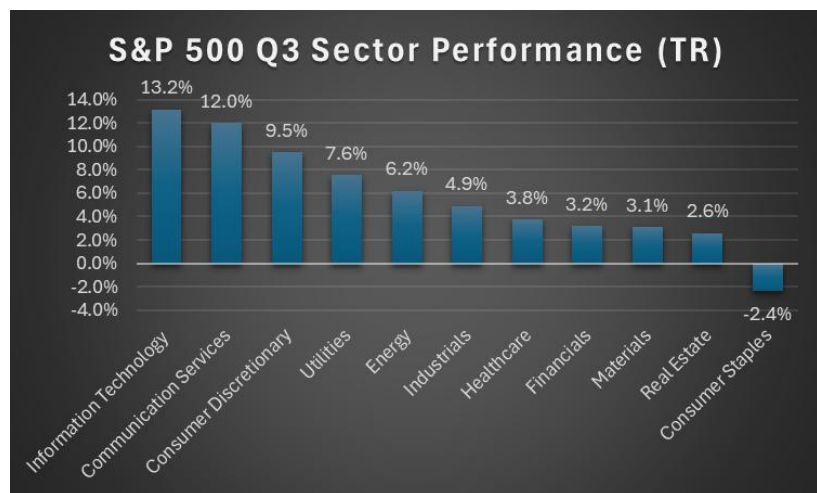


Figure 1 - S&P 500 Third Quarter Sector Performance (Total Return)

Corporate Center West • 433 South Main Street; Suite 305 • West Hartford, CT 06110

Ed Goldberg 860-706-1100 • Brenda Larkin 860-706-1101 • Fax 860-706-1110

egoldberg@westminsterfinancial.com • blarkin@westminsterfinancial.com

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Having a higher duration, or more interest rate-sensitive, bond portfolio added value compared to the AGG (iShares Core U.S. Aggregate Bond ETF) benchmark over the third quarter.

In sum, it was another strong quarter for stocks and bonds, with resilient earnings and the surge in capital investment on artificial intelligence (“AI”) supporting stocks. Weaker jobs numbers contributed to the prospect for lower interest rates (i.e. further rate cuts) helping bond prices rally.

Q4 Outlook

The Economy

The Labor Market – In a Low-Hiring and Low-Firing Mode

In our third quarter outlook written on July 8th, 2025, we wrote “*A major tailwind for stocks and economic activity is the probability that the “Fed” cuts interest rates in the next six months. Tariff-induced inflation has not yet shown up in the data, though the consensus expects an uptick in prices later this year. However, the “Fed” may cut rates anyhow as economists have, so far, been wrong on tariffs and inflation, and the economy has been gradually slowing. This will certainly be the case if the labor market shows any weakness.*”

Indeed, the labor market has weakened over the past few months, but the economy has remained strong due to robust consumer spending and technology companies’ massive investments in AI, leading to a boost in worker productivity. In sum, the U.S. economy is growing above trend but with less job creation.

With revisions to initial estimates for monthly job numbers, the labor market has downshifted since May, from adding over 158,000 jobs in April to only 19,000 in May and shedding jobs in June (a loss of 13,000)⁴. Using three-month moving averages to smooth the data and identify a trend, one can see that monthly jobs added have slowed considerably to a rate around 29,000 per month over the last 90 days (Figure-2)⁵. Economists cite a lower labor supply due to the enforcement of policies on illegal immigration as well as an increase in youth unemployment due to the anticipated efficiency gains of artificial intelligence and a subsequent reduction in hiring.

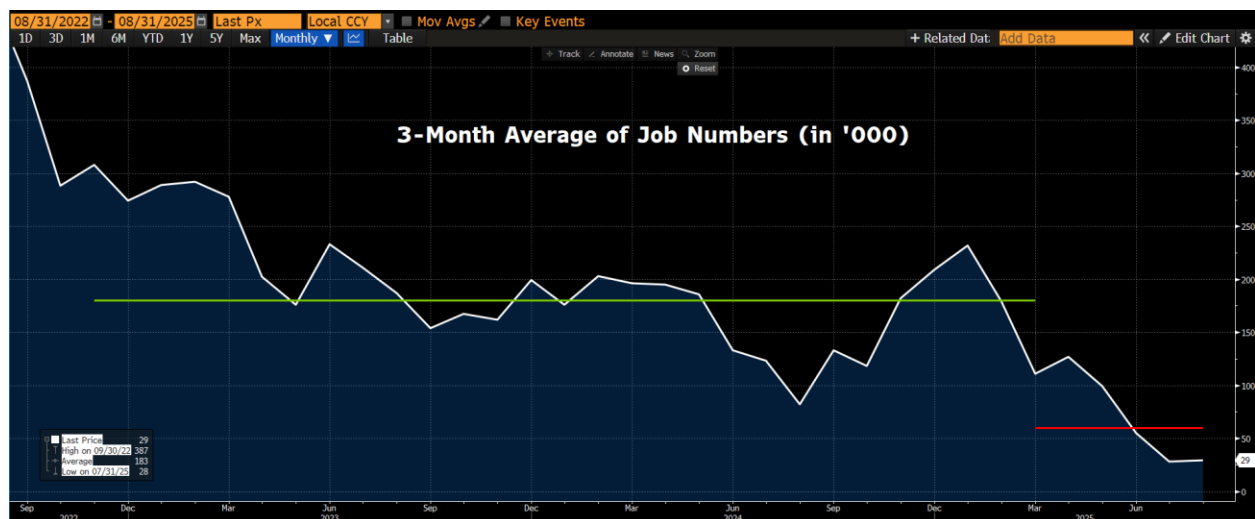


Figure 2 - Three-Month Average of Non-Farm Payrolls

Even though the labor market has slowed, it is also in a “low-firing” mode as seen from the 4-week moving average of weekly initial jobless claims in Figure-3⁶. This economic series has historically been, in past economic cycles, a leading indicator of what to expect in the monthly jobs report. Chart readings sustainably above 260,000 weekly jobless claims are when economists start to worry about major economic weakness ahead. The current data is averaging around 221,000 per week, hence no sign of massive layoffs as of yet.

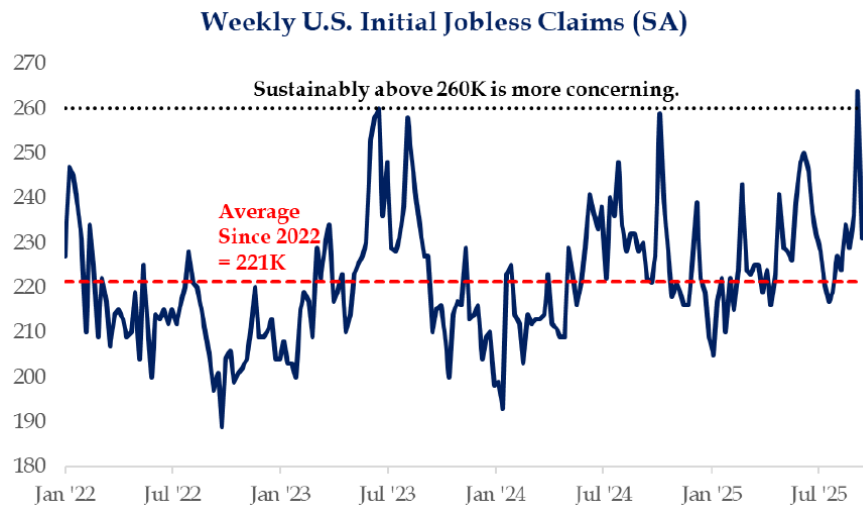


Figure 3 - How Many People Are Filling, Weekly, for Unemployment Benefits for the First Time?

U.S. GDP Growth – The Weak Job Market Is Not Translating to a Weaker Economy

The final reading for U.S. economic growth for the second quarter came in at a 3.9% real growth rate, surprisingly higher than many economists expected. Reasons for this positive economic surprise are three-fold. First, consumer spending continues to be resilient, thanks to upper income consumers’ robust spending as well as that on the part of the retiring baby boomers generation. It is worth noting, upper-income households account for the bulk of consumer spending (Figure-4)⁷. Even though conditions are not as upbeat for lower-income households, their spending is supported by robust wage growth that is exceeding inflation and the strong gig-economy, which serves as a financial bridge, helping them make ends meet. Another positive is continued growth in household net worth. Expanding net worth is being powered by the relentless equity rally in the markets and higher shares of home equity across the economy.

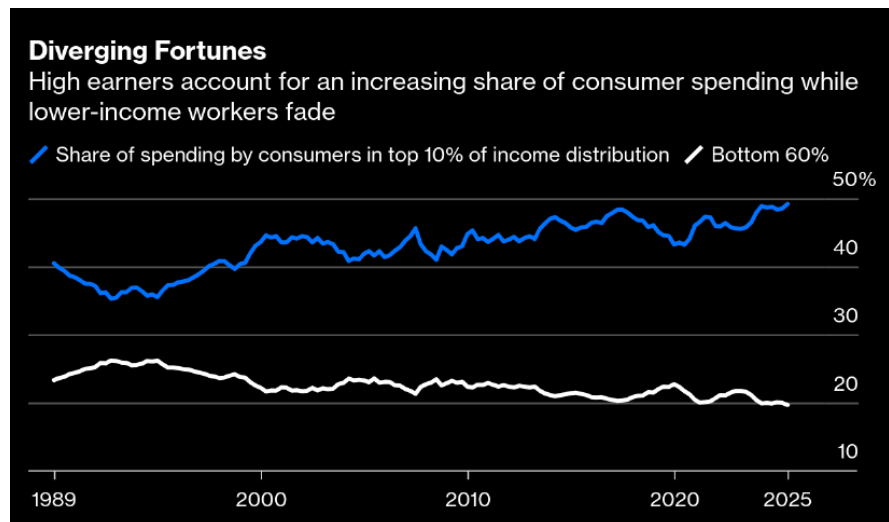


Figure 4 - Share of Consumer Spending by the Top 10%, and the Bottom 60% by Income

A second driver for the economy is the incredible amount of capital spending on AI boosting business investment. In fact, data center construction has boosted sales for industries as diverse as construction to semiconductor & chip equipment makers and everything in between. Since the launch of ChatGPT in November 2022, construction spending on data centers has increased 199%. This underpins many areas of the economy (Figure-5)⁸.

The third driver of the economic strength is technical: many companies, expecting new tariffs, increased imports substantially in the first quarter. Subsequently, imports have shrunk in the second quarter and potentially the third quarter as well. Imports subtract from Gross Domestic Product (“GDP”) growth, so a slowdown in imports is additive.

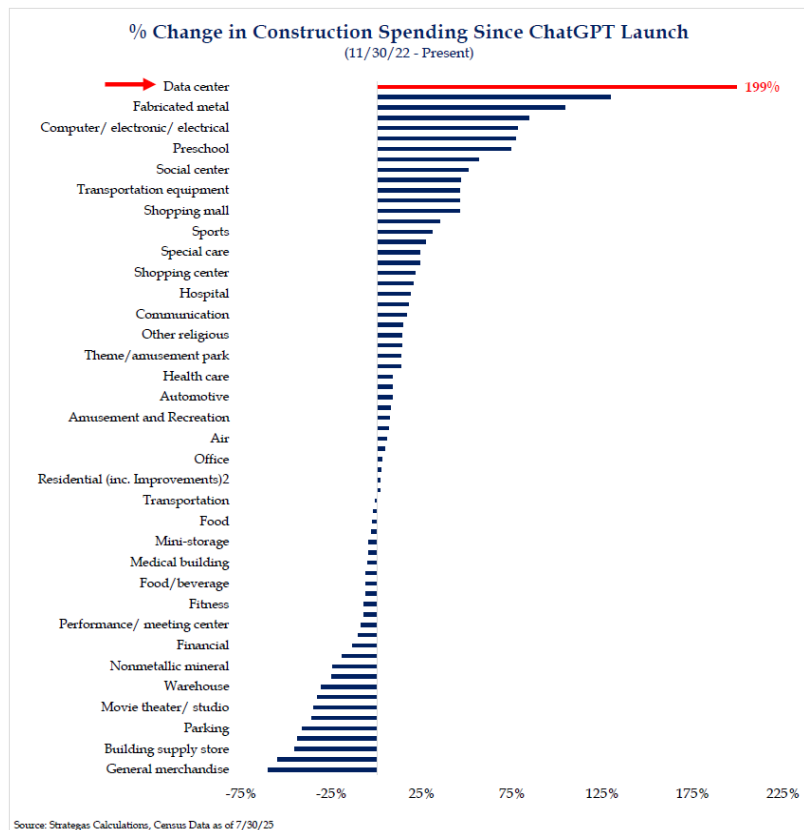


Figure 5 - Data Center Construction Growth Is Off the Chart

Looking ahead, live estimates for real economic growth, such as the Atlanta “Fed” GDPNow “Nowcast”, stand at 3.8% for third quarter (Figure-6)⁹, with consumer spending and fixed business investment, powered by AI capital spending, continuing their ongoing strength. Additionally, further “Fed” rate cuts could help the struggling residential (housing) market and the manufacturing/industrial sector.

The official initial reading of third quarter GDP will come out on October 30th and is likely to show another strong quarter, as productivity gains are more than offsetting a weakening labor market.

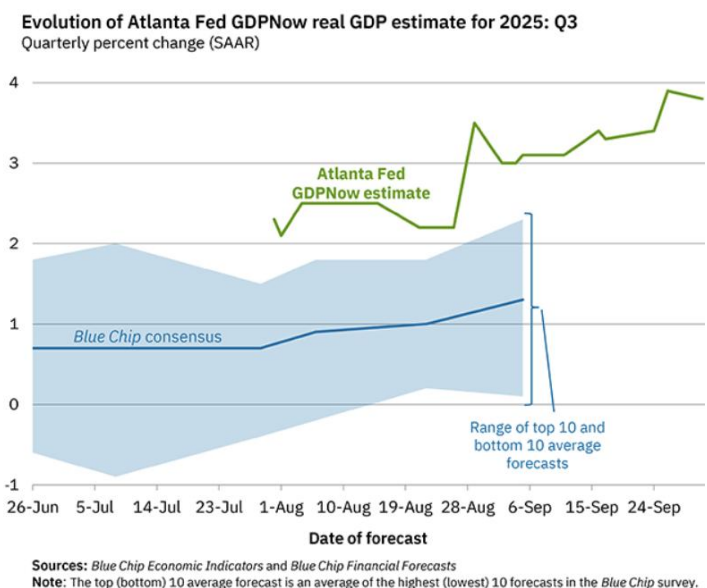


Figure 6 - Third Quarter 2025 Real GDP Growth Is Estimated at Above 3%

The Equity Market – A Young Bull

The stock market's considerable rally from the April low is one for the record books. The S&P 500 is up 35% from its April 8th low through September's close, while the NASDAQ Composite is up 49% and the "Magnificent-7" stocks are up 61%¹⁰. Market technicians are calling for a consolidation phase (sideways market) before moving higher as the year comes to a close. Fundamentals strongly support this outlook as earnings growth is expected to continue higher in each of the next four quarters.

However, it is worth taking a step back and looking at a longer time horizon to compare how this the current bull market, started in October 2022, compares to prior bull markets. Is the current market rally long in the tooth? Figure 7¹¹ shows all of the bull markets since 1928. The x-axis shows the duration of a bull market, and the y-axis shows the total return for that particular bull market. The two

Bull Market Not All That Extended on x or y Axes...

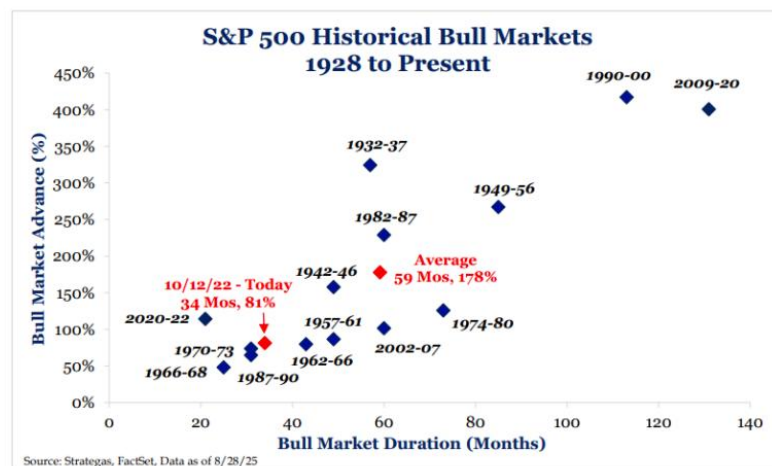


Figure 7 - The Current Bull Market Is Younger in Duration and Less Extended Than Average Bull Market Since 1928

red dots show the current market and the historical average bull market. You can see that the current bull market is young and not extended compared to the average. It is up 81% in 34 months - the average bull market typically advances 178% and lasts 59 months. Note though that this is the average and there are outliers on both sides. Even so, history suggests further gains ahead, especially given the acceleration in earnings estimates for next few quarters.

There has been a lot of concern about market bubbles in the media in recent weeks and comparisons to the Dot-Com bubble of the late 1990s are widespread. While we acknowledge there are some parts of the market that look frothy and show exuberance, such as cryptocurrencies and non-profitable technology companies, the overall market rally is still profits-driven, rather than speculative and valuation driven.

To illustrate this point, let's look at the change in S&P 500 *earnings* weight of the Technology sector compared to the change in its *market cap* weight three years prior to the Dot-Com bubble burst and in the current last three years. Please see Figure 8¹². By this comparison, Tech stock prices collectively have not gone up as much as they did in the Dot-Com bubble. Based on this analysis, any bubble calls may be premature.

Furthermore, sales growth for the S&P 500 has been outpacing cost growth (Figure-9)¹³. That is, the strong global economy is leading to superior S&P 500 sales growth that is more than exceeding tariff-related and other cost increases. This has resulted in record high margins for many S&P 500 corporations, giving companies a buffer to offset unexpected future shocks. Historically, estimated profit margins are a leading indicator for stock prices. Estimates see profit margins expanding further, another bullish signal for stocks.

TECH SECTOR MULTIPLE EXPANSION APPEARS TAME WHEN COMPARED TO “DOT-COM” MANIA

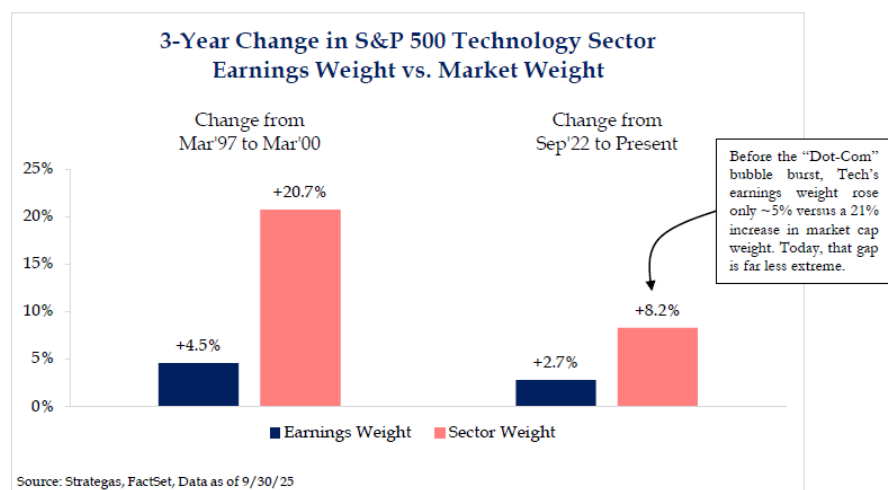


Figure 9 - Change in Technology Earnings vs. Change in Market Cap Weights (Now vs. Dot-Com)

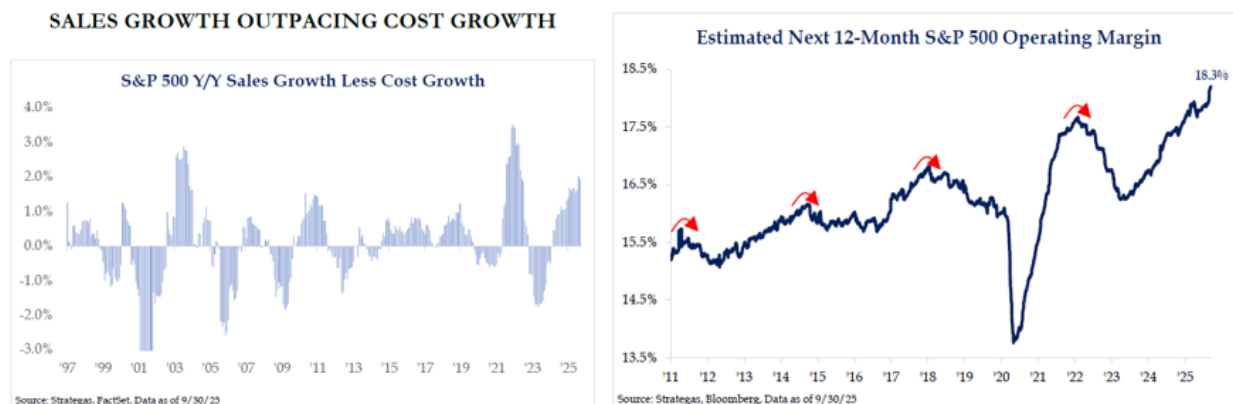


Figure 8 - S&P 500 Sales Growth Is Outpacing Cost Growth, Boosting Profit Margins

Conclusion

The U.S. economy is surprising even the most optimistic economists out there. Consumer resiliency, corporate AI investment, productivity gains, and the upcoming 2026 tax bill stimulus are major drivers of the current above-trend economic growth. To be sure, there are some spots of weakness and risks including a labor market hanging in the balance, sluggish manufacturing, and a frozen housing market.

However, although inflation is above the “Fed’s” target rate, it is still within their preferred range, allowing it to continue to cut rates in the next couple of quarters. Easing the cost of debt should help these weaker sectors of the economy. Moreover, upper-income consumers are a sustainable

driver for robust consumer spending given the increase in asset prices, while lower-income consumers seem to be making do and bridging the gap through the gig-economy. These dynamics call for consumer spending to continue to be healthy over the next 12 months.

The U.S. equity market should continue to rally in the fourth quarter with occasional profit-taking episodes, but overall, the quarter should be positive for the market on better seasonals (Figure-10)¹⁴, end-of-year fear of missing out (FOMO) by the short-term traders, and another strong earnings season starting mid-October. Valuations are historically expensive, but record profit margins and rising profit estimates should go a long way toward justifying them for now.

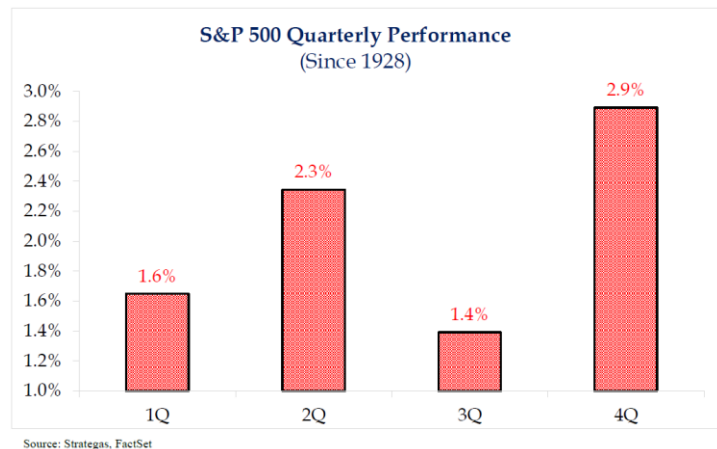


Figure 10 - S&P 500 Quarterly Seasonality Since 1928

The bond market should also do well. “Fed” rate cuts and the weakening labor market will likely continue to be catalysts for lower interest rates in the 3–10-year maturity range (the belly of the yield curve) and thus higher bond prices. Hence, allocating away from short-term maturities and to the belly of the curve could add value to balanced portfolios by offering a hedge to stocks as interest rates come down.

We continue to recommend investing in stocks and taking advantage of any pullbacks, if the opportunity arises, to deploy new capital.

We are here to support you, so if you have any questions, please do not hesitate to contact us.

Respectfully,

Edward M. Goldberg, CFP®, ChFC, CDFA®

Brenda L. Larkin, CDFA®

The Westminster Financial Investment Policy Committee

Resources

- ¹ Figures are total return. Source: Bloomberg
- ² WFA Charting through Bloomberg
- ³ U.S. Treasury and Bloomberg
- ⁴ U.S. Bureau of Labor Statistics
- ⁵ U.S. Bureau of Labor Statistics, and Bloomberg
- ⁶ U.S. Department of Labor, and Bloomberg
- ⁷ Moody's Analytics and Bloomberg
- ⁸ Strategas, and Census Data
- ⁹ Federal Reserve Bank of Atlanta
- ¹⁰ Figures are total return. Source: Bloomberg
- ¹¹ Strategas, and FactSet
- ¹² Strategas, and FactSet
- ¹³ Strategas, Bloomberg, and FactSet
- ¹⁴ Strategas, and FactSet

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