



OUR VIEW



Markets have been supported by the simultaneous alignment of pro-growth fiscal, monetary, and regulatory policies.

Third Quarter Review: From Fear to FOMO to...Exuberance?

In last quarter's commentary, we noted the S&P 500 had staged the 4th best advance off a major market bottom ever. The rally maintained that ranking at the end of the third quarter. The gain since April 8th has only been surpassed by the post-GFC and post-Covid rallies and the 1982 rally that launched an 18-year bull market.

S&P 500 Performance Off the Low Following a -15% Correction					
High	Low	Drawdown	+125 Days off Low	Next 65 Days	Next 125 Days
2/19/2020	3/23/2020	-34%	48%	11%	18%
10/9/2007	3/9/2009	-57%	48%	10%	14%
11/28/1980	8/12/1982	-27%	42%	13%	9%
2/19/2025	4/8/2025	-19%	33%	?	?
1/11/1973	10/3/1974	-48%	31%	15%	3%
4/29/2011	10/3/2011	-19%	29%	-4%	2%
7/17/1998	8/31/1998	-19%	28%	6%	10%
7/16/1990	10/11/1990	-20%	28%	1%	1%
9/20/2018	12/24/2018	-20%	24%	2%	10%
4/23/2010	7/2/2010	-16%	23%	6%	4%
2/9/1966	10/7/1966	-22%	21%	5%	10%
12/12/1961	6/26/1962	-28%	20%	6%	12%
11/29/1968	5/26/1970	-36%	20%	17%	22%
8/25/1987	12/4/1987	-34%	19%	0%	3%
1/3/2022	10/12/2022	-25%	16%	10%	6%
3/24/2000	10/9/2002	-49%	11%	16%	20%
8/2/1956	10/22/1957	-22%	10%	9%	20%
Average			27%	8%	10%
Median			24%	8%	10%

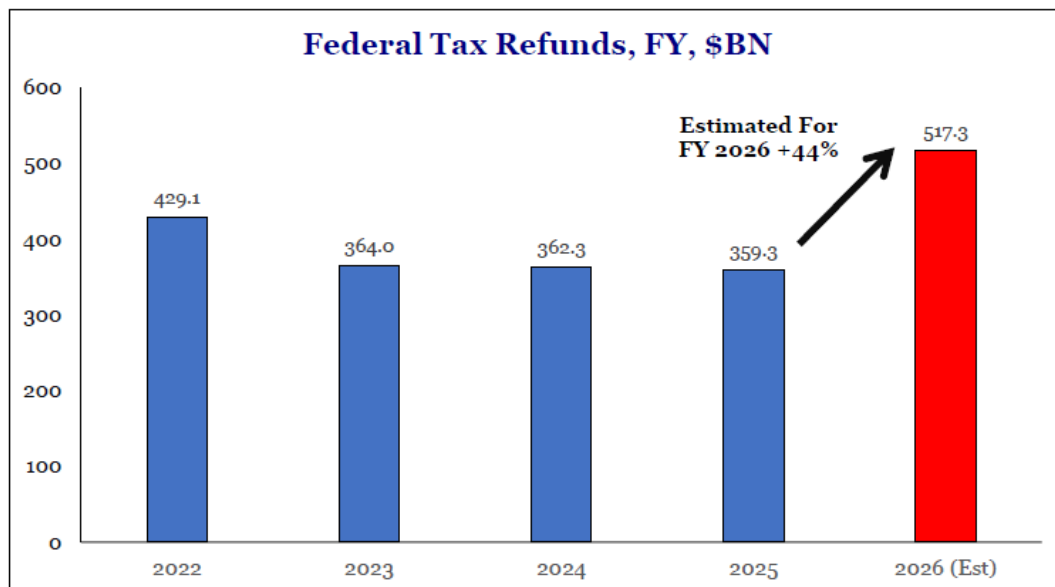
Source: Strategas

Markets have been supported by the simultaneous alignment of pro-growth fiscal, monetary, and regulatory policies.

Several OBBBA provisions (e.g. 100% expensing for capex, domestic R&D, and the building of production facilities) are retroactive to 1/1/2025 and are affecting companies' bottom lines now. September 2025 corporate tax payments are estimated to be 40% lower than the amount in September 2024 (and mostly offset by tariff revenues). Moreover, 328 companies mentioned the positive effects of OBBBA during the second quarter earnings reporting season with business tax cuts as the most cited benefit. The Act's stimulus for the consumer is significant but won't be felt until early 2026.



Consumers are expected to receive an additional \$150bn in refunds during the 2026 tax season.



Source: Strategas

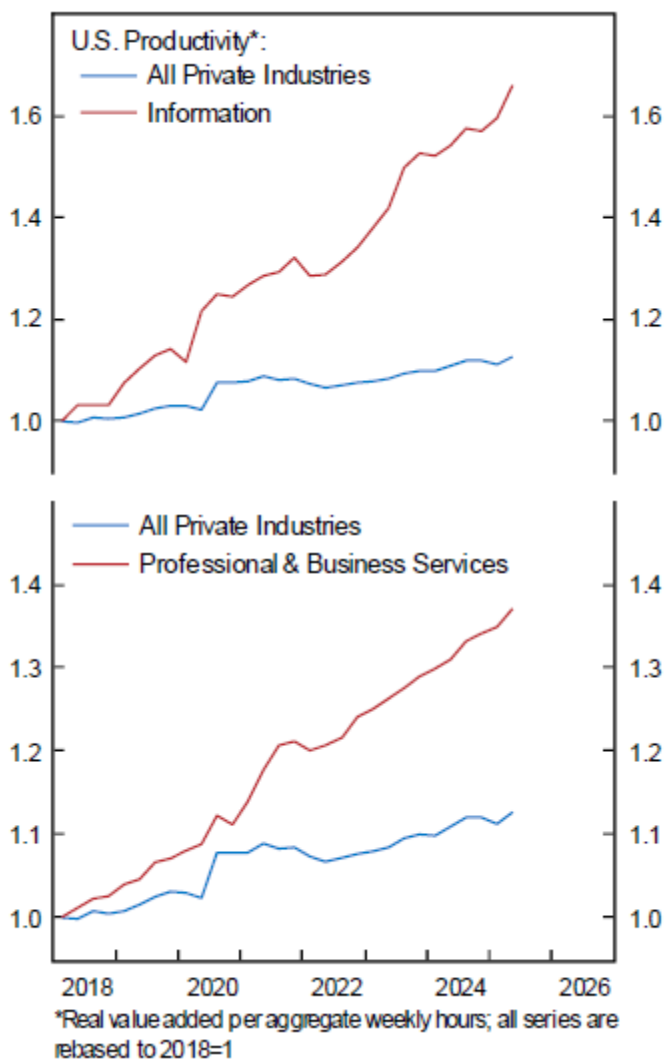
The Federal Open Market Committee (FOMC) lowered the fed funds rate by 0.25%. The FOMC is expected to lower rates by an additional 0.50% before the end of the year.

While we wouldn't call monetary policy easy, it's at least becoming easier. The Federal Reserve Open Market Committee (FOMC) responded to a weakening labor market by lowering the fed funds rate by 0.25% at its September meeting. The FOMC is expected to lower rates by an additional 0.50% before the end of the year. The Fed's actions will affect the economy with a lag, but they may have more immediate effects on smaller businesses which often finance with floating rate debt. Additionally, easier monetary policy may indirectly help to lower mortgage rates and revive the persistently sluggish housing market.

Deregulation in the financial sector could increase M&A and enable banks to allocate excess capital toward loan growth and share buybacks and dividends. The energy and healthcare sectors may also benefit from ongoing deregulation.



U.S. companies delivered another quarter of strong earnings growth that exceeded expectations.



Source: Alpine Macro

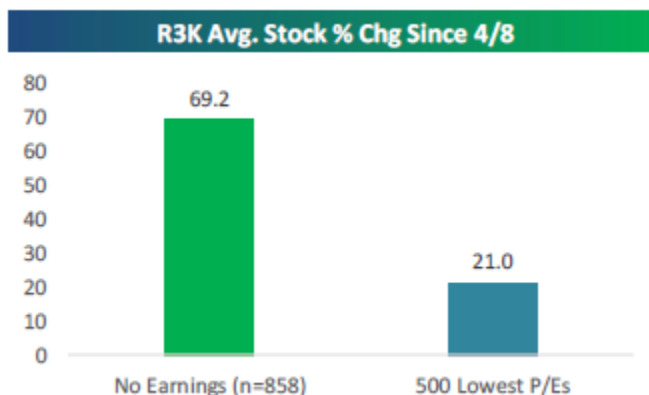
Additionally, U.S. companies delivered another quarter of strong earnings growth that exceeded expectations. As the earnings reporting season began, estimates called for 6% year-over-year earnings growth. Actual earnings rose 13%. Recall that first quarter earnings followed a similar pattern with initial estimates for 8% profit growth coming in at 14%. Profit margins are nearing record levels. A resilient economy has supported top-line growth while companies continue to manage costs effectively. Productivity growth may also explain the impressive gains in corporate profits. Since the pandemic, productivity growth has been driven by several factors. The work-from-home transition and rebalancing of workers from low to higher productivity sectors have been two factors. Recently, the sectors most exposed to A.I. have seen sizable productivity gains.



Asset Class Performance Review

In the U.S. the Russell 2000 index of small companies rose 12%. Lower quality stocks were the best performers.

Each asset class in your portfolio delivered positive returns during the quarter. Despite its history as the weakest quarter of the year, Q3 turned out to be quite strong for stocks. In the U.S., the Russell 2000 index of small companies rose 12%. Small companies may be the most direct beneficiaries of the fiscal, monetary, and regulatory tailwinds discussed earlier. Technology and communications services were the best performing sectors. Additionally, the lowest quality stocks gained the most. Retail investors have been major contributors to the “junk” stock rally. Since the market low on April 8th, stocks in the Russell 3000 with negative earnings have risen by an average of 69% while the 500 stocks with the lowest price-to-earnings ratios have risen 21%. There were 19 stocks up more than 400% during that time, and only four of them have positive earnings.



Source: Bespoke Premium

Outside the U.S., China led a strong rally in emerging market stocks. Beijing is beginning to target domestic consumption with policy easing, a necessary antidote given extremely high savings rates and a dis-engaged consumer. For example, the government has announced subsidies for families with young children and may introduce tuition-free pre-school education. Despite sluggish economic data, Chinese 10-year bond yields have been rising, suggesting economic growth will improve and deflation will subside.

China led a strong rally in emerging market stocks.

Developed international equities were led by Japan. The Nikkei 225 rose 11% during the quarter buoyed by a rise in business confidence, strong corporate earnings results, and positive domestic political developments. After a strong rally in the first half of the year, European equities delivered modest gains.



Municipal bonds rebounded as investors took advantage of historically attractive muni-to-treasury yield ratios.



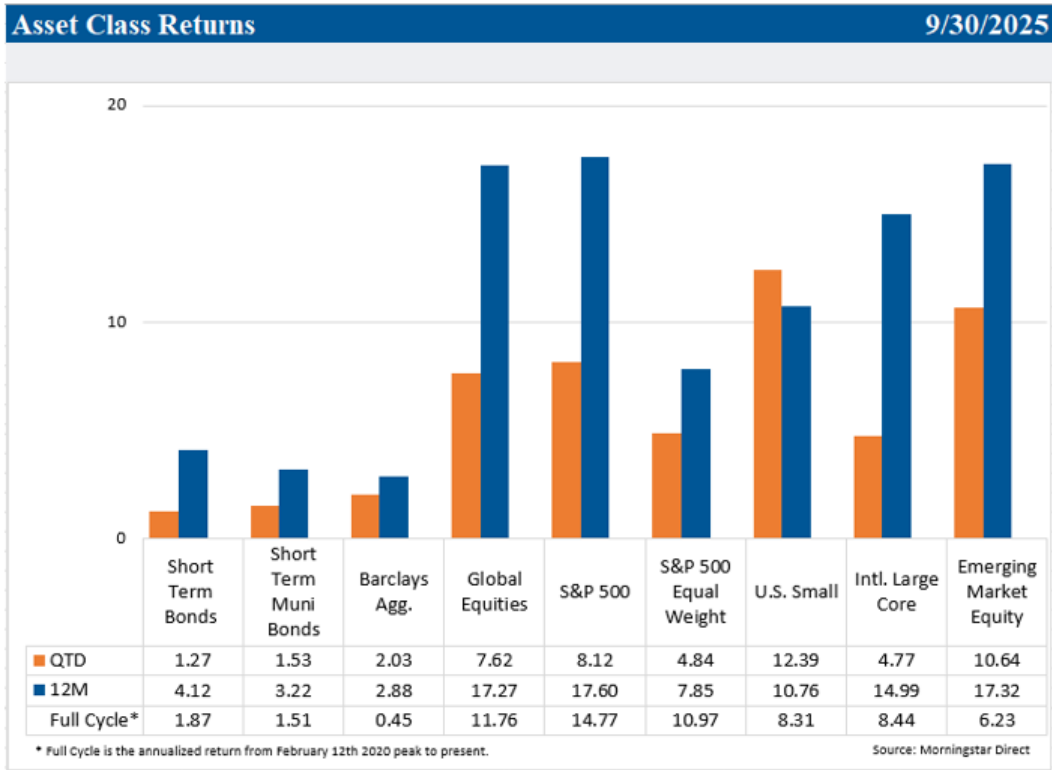
Source: Strategas

Furthermore, similar to the U.S. market, emerging markets benefitted from increased fervor over A.I. with several large semiconductor stocks posting significant gains.

All major fixed income categories delivered positive returns. Yields declined across the curve especially for shorter maturities as investors anticipated the resumption of Fed easing. Multi-sector fund returns were fueled by continued spread tightening. In fact, credit spreads for both investment grade and high-yield bonds ended the quarter at or near their tightest levels ever. Municipal bonds were the best performing sector as investors took advantage of historically attractive muni-to-treasury yield ratios.



High premium income and a benign hurricane season were tailwinds for reinsurance.



As a group, Diversifying Assets provided returns that exceeded fixed income. Reinsurance and multi-strategy were the best performing strategies. The reinsurance fund continues to accrue a high level of premium income while insured claims are low due to a remarkably benign hurricane season.

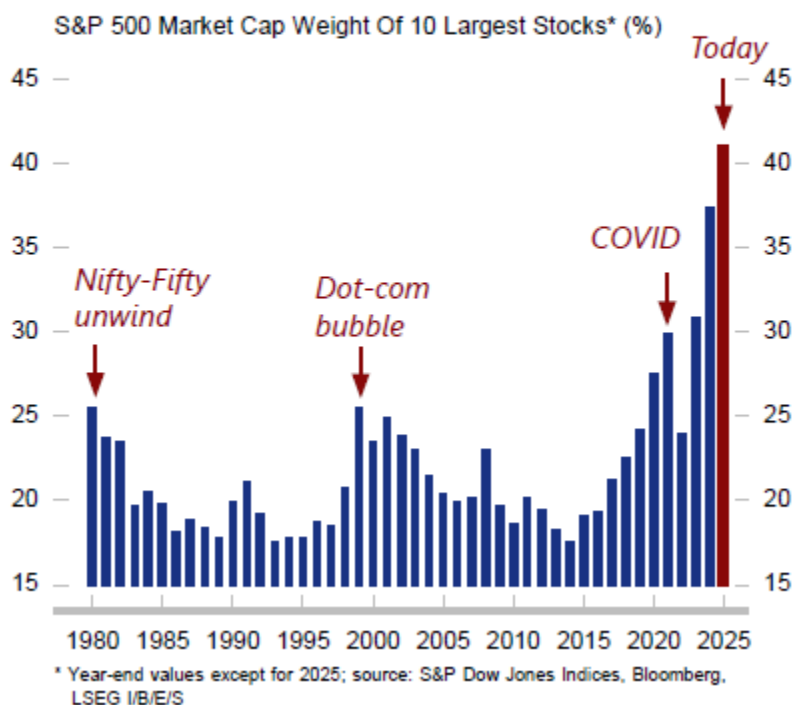
The 10 largest stocks in the S&P 500 comprise over 40% of the index's market capitalization. This percentage vastly exceeds the prior levels of the Dot-com bubble in the late 1990s and the Nifty Fifty era in the 1970s.

Portfolio Strategy and Outlook: Revisiting Market Concentration (and the late 1990s)

Currently, the 10 largest stocks in the S&P 500 comprise over 40% of the index's market capitalization. That percentage has doubled over the last decade and now vastly exceeds the prior levels of the Dot-com bubble in the late 1990s and the Nifty Fifty in the 1970s. This concentration hasn't spooked investors. Every dip in this group of stocks has been bought, and every correction has been embraced as an opportunity to reload before eventual all-time highs. That strategy has worked well, and perhaps there are justifiable reasons for it. Earnings growth for this cohort has significantly outpaced the rest of the market.



Chart 1 The Concentration Of The U.S. Equity Market Is High Relative To History



Source: MRB Partners

We see differences, but also increasing similarities, between the present environment and the late 1990s.

However, today's market is not only highly concentrated in terms of market value, but it has also become increasingly and highly leveraged to a single theme. Of course, we are referring to the boom in artificial intelligence. The hyperscale cloud providers (Microsoft, Meta, Alphabet, and Amazon) make up about 20% of the index. Two semiconductor companies, NVIDIA and Broadcom, comprise another 10%. Collectively, these six stocks have a market value of more than 50% of U.S. GDP. It is estimated the hyperscale cloud providers account for 30% of all capital expenditures made by companies in the S&P 500.

Even the historically defensive utilities sector has participated in the AI narrative as several large utilities exposed to data center growth have risen significantly this year.

Many investors have compared the current environment to the late 1990s. We see some differences, although the similarities are becoming more apparent. Unlike the 1990s, investors aren't piling capital into cash-burning companies with no earnings or customers. The six companies mentioned earlier have entrenched business models, generate significant free cash flow, and are hugely profitable.



We believe the bull market may have entered a more exuberant and hence more unpredictable phase.

However, investor and corporate behavior is becoming more reminiscent. The A.I. capex spending binge is beginning to resemble the telecom buildout of the internet era. A series of large related and interconnected transactions has created a circular ecosystem that is heavily concentrated in just a handful of companies. "Nvidia plans to invest in OpenAI, which is buying cloud computing from Oracle, which is buying chips from Nvidia, which has a stake in CoreWeave, which is providing artificial intelligence infrastructure to Open A.I.¹ Nvidia is receiving equity in OpenAI in return for delivering chips while Advanced Micro Devices is giving away equity to OpenAI in exchange for revenue. Several of these transactions are reminiscent of vendor financing in the late 1990s in which telecom equipment makers loaned large sums of money to both new and established carriers to enable them to purchase equipment.

Table 1 S&P 500 Top-10 Holdings: Today Vs The Dot-Com Bubble Peak

September 26, 2025			March 24, 2000		
	Market Cap (US\$ bn)	Weight (%)		Market Cap (US\$ bn)	Weight (%)
NVIDIA	4,330.6	7.64	Microsoft	560.7	4.34
Microsoft	3,801.8	6.71	Cisco Systems	546.9	4.23
Apple	3,791.1	6.69	General Electric	522.5	4.04
Alphabet	2,985.4	5.27	Intel	463.6	3.59
Amazon	2,343.9	4.14	Walmart	247.2	1.91
Meta Platforms	1,868.4	3.30	Oracle	245.5	1.90
Broadcom	1,579.8	2.79	Pfizer	219.9	1.70
Tesla	1,464.4	2.58	IBM	215.2	1.66
Berkshire Hathaway	1,078.6	1.90	Nokia	205.0	1.59
JP Morgan	869.1	1.53	Citigroup	203.9	1.58
Top 10	24,113.1	42.55	Top 10	3,430.4	26.53
S&P 500	56,663.8		S&P 500	12,931.0	

Source: Bloomberg

No one can forecast with precision how long this trend will continue. Alan Greenspan's infamous "irrational exuberance" speech in December 1996 led to an initial (and brief) swoon in stocks before they doubled over the next three years. We are reminded of the oft cited quote from John Maynard Keynes, "The market can remain irrational longer than you can remain solvent." Regardless, we believe that the bull market has entered a more exuberant and hence more unpredictable phase. The market's leverage to the A.I. theme leaves it more vulnerable to any perceived threat to the sustainability of the investment boom in A.I.

¹ "The AI boom's reliance on circular deals is raising fears of a bubble," Rob Wile, Nbcnews.com



Our equity portfolios have direct exposure to A.I. but not overconcentrated in the largest A.I.-associated companies.

Our equity portfolios have direct exposure to A.I. but are not overconcentrated in the largest A.I.-associated companies (such as Nvidia, Microsoft, Alphabet, etc.). We complement that exposure with broad diversification across other sectors, market caps, geographies, etc. Balancing portfolios with fixed income and non-correlated asset classes coupled with disciplined rebalancing are designed to provide resilience in most market and economic environments ahead.

Please join us for our upcoming webinar, “One Year Since the Election: A look back and a look forward.” The event will be held on November 6 from 11:00am-Noon. Invitations to follow!

Please contact your TFC Advisor or us directly if you have any questions or would like to discuss your portfolio further. Thank you.

Sincerely,

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