

Monthly Download

August 2025

Summary

- ◆ **Markets were modestly higher** in August with momentum for stocks continuing to the upside. Expectations for Fed rate cuts, consumer resilience, solid earnings growth, and narrowing trade uncertainties were all factors in supporting performance. Fed Chair Powell's speech at the annual Jackson Hole conference was more dovish than expected, emphasizing softness in the labor market and limited inflation pressures. US equities were led by strong performance from more rate-sensitive small companies like homebuilders, while non-US stocks continued their strong leadership for the year. Treasury yields declined on weaker jobs data and Powell's speech despite concerns about tariff impact starting to show up in inflation data.

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Market Overview

- ◆ **Equity markets** finished August with modest gains, though sector leadership reflected the month's economic themes of companies benefiting from more accommodative monetary policy. Rate-sensitive areas more represented in small cap indexes like regional banks, biotech, and homebuilders led performance, while AI sentiment was tested by Nvidia's in-line earnings at month-end.
 - US Large Cap stocks (S&P 500) rose 2.0%, led by Materials and Healthcare. Big tech was mixed, as Nvidia's earnings "just" delivering on expectations rather than a substantial beat like past quarters kept broader technology and AI enthusiasm in check. Market breadth improved with the equal-weight index slightly outperforming the traditional cap-weighted index, up 2.7%. Year to date, the S&P 500 is up 10.8%.
 - US Small Cap stocks (Russell 2000) gained 7.1% in August, outperforming US large cap counterparts. Strength was broad-based, with housing-related and rate-sensitive names rallying into expectations of Fed easing. Year to date gains are now 7.1%.
 - Non-US stocks (MSCI EAFE Net) rose 4.3% in August on currency tailwinds and steadier macro data. Year to date gains are 22.8%, extending their strong relative performance versus US equities.
 - Emerging Markets (MSCI Emerging Markets Net) added 1.3%, led by strength in India and Brazil, though China remained under pressure from property-sector stress. Year to date returns are up 19.0%.
- ◆ **Interest rates** drifted lower in the aftermath of the weak July jobs report while Powell's Jackson Hole remarks reinforced expectations for a September rate cut. The 10-year US Treasury yield ended at 4.23%, down from 4.36% at the beginning of August.
 - High Grade Taxable bonds (Bloomberg US Aggregate) were up 1.2% in August, supported by lower Treasury yields and steady corporate fundamentals. The backdrop of declining rates provided price appreciation, while credit spreads held firm. Year to date gains are 5.0%.
 - Municipal bonds (Bloomberg 1-10 Year Muni Bond) added 0.8% in August, helped by lower yields and strong seasonal demand following summer issuance. Year to date, municipals are up 3.1%. Underperformance to taxable bonds reflects heavier-than-usual municipal supply earlier in the year and investor caution around potential tax-policy changes, which pressured municipal valuations despite the broader bond rally.
 - Investment Grade and High Yield bonds experienced similar performance in August. Investment Grade bonds (Bloomberg US Corporate Investment Grade) added 1.0% for the month, bringing gains for 2025 to 5.3%, as

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lower rates supported spreads but left the sector sensitive to volatility. High Yield bonds (Bloomberg US Corporate High Yield) rose 1.3%, bringing gains for 2025 to 6.4%, as risk-on sentiment and improved earnings outlooks drove demand for lower-rated credit.

- ◆ **Commodities** (Bloomberg Commodity Index) rose 1.9% in August, driven primarily by the strong rally in precious metals, which more than offset the decline in energy. Gold was up 5.0% as precious metals benefitted broadly from safe haven demand and accommodative monetary policy expectations post-Jackson Hole. Oil fell 7.6% on a series of Russia-Ukraine headlines and rising OPEC output. Commodities are now up 7.1% in 2025.

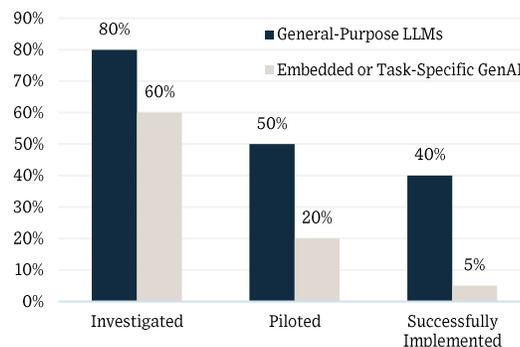
Economic Commentary

Jerome Powell's Jackson Hole remarks were the focal point for markets in August. He acknowledged that inflation has moved decisively lower from its 2022–2023 peak and noted softening signs in the labor market. Still, Powell emphasized the Fed's independence and cautioned against prematurely declaring victory against inflation. His comments came against a backdrop of political pressure on the Fed to accelerate rate cuts ahead of the 2026 election cycle. The firing of Fed Governor Lisa Cook on allegations of mortgage fraud added to the sense of political interference, though markets treated the event as a non-issue. Investors seem to be implying the real risk would come if Powell himself were directly targeted or replaced. Markets to date appear content to look past pressure campaigns and personnel changes that do not affect the Fed's central decision-making apparatus. The lack of reaction to Trump's efforts with the Fed is part a general market appetite for lower rates and part investor confidence in US courts to provide a check on the President's actions. Markets also appear to trust Powell's credibility, viewing an eventual rate cut in September as justified by disinflationary trends and early signs of weakness in the labor market rather than purely political motivations. Investors agree with the perspective that acting before unemployment rises sharply is a prudent course of action. Investors are also choosing to pay more attention to underlying fundamentals that remain supportive of risk assets than politics. Strong corporate earnings growth, the prospect of lower interest rates, and ongoing capital expenditures in artificial intelligence have combined to keep risk assets buoyant. Inflation risk from lowering interest rates too early is different from the inflationary surge of 2022–2023, which was driven by supply shocks, surging demand from the post-pandemic reopening, and unprecedented fiscal and monetary stimulus. Current monetary policy remains restrictive (the Fed Funds rate is well above annual inflation), fiscal deficits are smaller, and technological advances could prove disinflationary if productivity accelerates. Market critics can argue that investors have a habit of ignoring clear warning signs until it is too late, pointing to past episodes like the Financial Crisis (2008), European debt crisis (2010–11), China devaluation and oil collapse (2015–16), and inflation spike followed by Fed rate hikes (2022–2023). Yet history shows that betting on resilience has been the winning strategy. Markets have repeatedly rebounded from these events and until the primary drivers of current market performance—earnings, interest rates, capital investment, and innovation—begin to break down, investors see little reason to preemptively price in political concerns, except at the very fringes of the bond and currency markets. Powell closed Jackson Hole by reiterating that the Fed will cut rates when conditions warrant, not when politics demand it, and markets seem comfortable with that balance.

The durability of the AI investment cycle faced renewed questions in August. Technology leadership has powered markets since the release of ChatGPT in late 2022, but valuations and capital spending in the sector have reached levels that invite scrutiny. The central question is whether the extraordinary sums being spent to build out AI infrastructure will translate into a sustainable return on investment and when. A widely circulated MIT study¹ titled "GenAI Divide" sharpened these concerns during the month and brought attention to the chasm between experimentation and measurable outcomes. Despite tens of billions in enterprise spending, the report found that

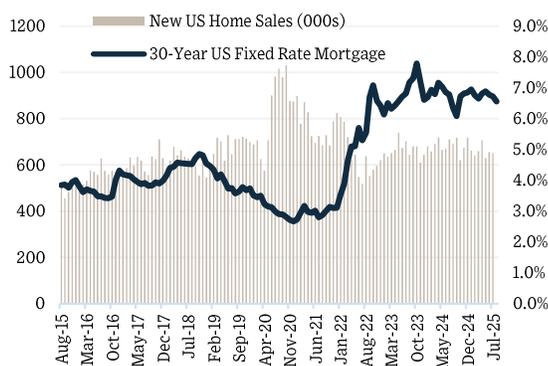
¹MIT NANDA Initiative. *The GenAI Divide: State of AI in Business 2025*.

roughly 95% of organizations experimenting with generative AI have seen little to no measurable business impact. Adoption is high as most companies have piloted tools like ChatGPT or Copilot, but transformation is rare. Only a handful of organizations have successfully crossed from pilot to production, and those that have done so are typically using systems that learn, adapt, and integrate into existing workflows. The findings highlight a mismatch between the hype surrounding AI and the reality of stalled deployments, brittle workflows, and misplaced investment in visible but low-ROI use cases like marketing over more transformative back-office automation. Market expectations were tested at the end of the month when Nvidia, the poster child of AI-driven growth, reported second-quarter results. The company reported incredibly strong results by any standard, except maybe Nvidia's recent results. The 2nd quarter numbers were "only" in-line or barely above analysts' expectations and certain segments came in just below projections. For most companies, such growth would be celebrated, but for Nvidia it marked the slowest revenue growth since early 2024. Data center revenue, its largest segment, fell short of forecasts due in part to reduced chip sales to China. The market reaction was subdued with shares initially trading lower and ending flat the day after the report. After such a massive run-up in the stock, investors' expectations appear to be catching up or even surpassing actual results. They want evidence that the AI spending wave will remain both durable and broad-based. Together, the MIT findings and Nvidia's earnings illustrate the current state of AI sentiment. The positive outlook remains enthusiastic about the possibility of transformative productivity and the capital spending required to deliver that vision. But increasingly, questions are mounting over whether the extraordinary capital investment is translating into meaningful productivity gains and therefore return on the capital investment. For now, AI remains a critical pillar of market performance, but its long-term impact will depend on whether enterprises can cross the "GenAI Divide".



MIT Study on Corporate Adoption of Task-Specific GenAI Tools
Source: MIT NANDA, Data from January – June 2025

August housing data highlighted the ongoing tension between affordability pressures and early signs of stabilization. The average 30-year fixed mortgage rate held near 6.7%, continuing to weigh on buyers and leaving affordability stretched. Higher borrowing costs remain one of the key drivers behind the Trump administration's calls for lower interest rates, even as fixed income investors have benefited from higher yields on mortgage-backed securities. Against this backdrop, new home sales came in at an annualized pace of 652,000 in July, essentially in line with expectations but slightly weaker than June's upward revision and well below levels one year ago. Inventory slipped modestly to just under 500,000 units, representing about 9.2 months of supply. Prices remain under pressure with the median sales price down nearly 6% from last year to \$403,800, the lowest level in eight months. Builders have responded with a combination of price cuts and incentives, a sign that they are still struggling to clear supply in a higher-rate environment. New home sales serve as a leading economic indicator since they generate downstream activity in construction, materials, and labor demand. Despite the current weakness, homebuilder stocks have outperformed the S&P 500 index over the past 3 years including a double-digit rally in August on the



New Home Sales vs. 30-Year Fixed Rate Mortgage
Source: Federal Reserve Economic Data, Federal Reserve Bank of St. Louis, Data from January – June 2025

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expectation that Fed easing is coming in September. Mortgage rates tend to track the 10-year Treasury yield more closely than the Fed Funds rate, and while the 10-year has fallen modestly, longer maturity interest rates remain elevated given concerns regarding inflation expectations and US deficit financing. Unless interest rates fall more decisively across the yield curve, the housing market is likely to remain in this uneasy balance, caught between price stabilization from a healthy consumer and persistent headwinds from mortgage rates.

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