Summit Trail Advisors

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October 2025

Summary

- **Market returns remained positive** in October despite heightened volatility around tariff escalation, high profile defaults, and concerns around a bubble in artificial intelligence spending. Strong earnings reports from large US Banks and Technology leaders like Microsoft, Google, Apple, and Amazon drove the S&P 500 to new highs. The Federal Reserve delivered an additional 25 basis point cut to the Fed Funds rate as expected but threw cold water on the certainty of future rate cut expectations given lack of data due to the government shutdown.

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Market Overview

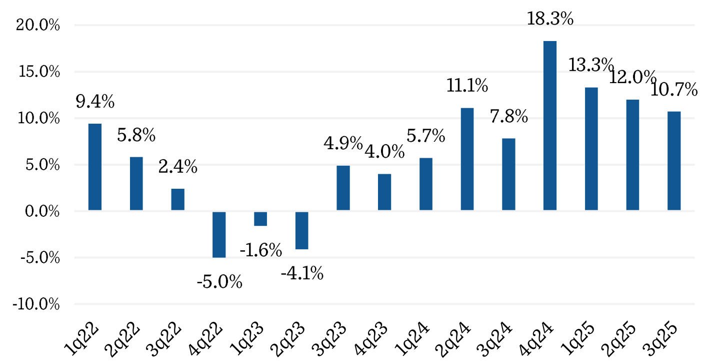
- **Equity markets** saw modest gains across the board as 3rd quarter earnings season delivered additional growth to expectations entering the quarter. The Financial and Technology sectors led earnings growth and 9 of 11 GICS sectors saw earnings growth rates increase from the start of the month. Emerging Market stocks delivered leadership globally, buoyed by South Korea, which returned over 20% in October on strength from companies like Samsung and SK Hynix.
  - US Large Cap stocks (S&P 500) rose 2.3%, led by Technology and Health Care. Earnings momentum continued for Microsoft while Apple delivered surprisingly strong results on demand for iPhone 17. Nvidia, Google, and Amazon were key contributors with the latter two companies also exceeding analyst expectations for earnings. Year to date, the S&P 500 is up 17.5%.
  - US Small Cap stocks (Russell 2000) gained 1.8% in October, again being overshadowed by Large Cap earnings growth. Biotech stocks saw double-digit monthly gains as well as smaller Technology names, but the overall index was dragged down by Financials on market credit quality concerns. Year to date gains stand at 12.4%.
  - Non-US stocks (MSCI EAFE Net) rose 1.2% for the month as foreign Technology companies also saw investor interest, but the index weighting to Financials that declined slightly is almost 3x the Technology weighting. Year to date gains are 26.6%.
  - Emerging Markets (MSCI Emerging Markets Net) led performance with a 4.2% return in October. South Korea returned 22.7% and is up over 92% in 2025. South Korea's index is dominated by Samsung and SK Hynix which represent 40% of the country's market capitalization. Year to date returns are up 32.9%.
- **Interest rates** declined slightly in October, dropping from 4.15% on the 10-Year Treasury to 4.10% at month-end. The absence of jobs data has forced markets to focus on private ADP payroll data. The September CPI release was delayed but delivered inflation numbers in-line with expectations.
  - High Grade Taxable bonds (Bloomberg US Aggregate) were up 0.6% for October as interest rates declined slightly and mortgage spreads remain intact. Year to date gains are 6.8%.
  - Municipal bonds (Bloomberg 1-10 Year Muni Bond) added 0.5% in October as longer duration municipals continued to reverse out-performance of 4-6 year municipal bonds from earlier in 2025. Municipal bonds are now up 4.6% for 2025.

- Investment Grade and High Yield bonds saw subdued performance given a modest increase in credit spreads after a couple of high-profile defaults in October. Investment Grade bonds (Bloomberg US Corporate Investment Grade) were up 0.4% for the month, bringing gains for 2025 to 7.3%. High Yield bonds (Bloomberg US Corporate High Yield) rose just 0.2% for October, bringing gains for 2025 to 7.4%,

◆ **Commodities** (Bloomberg Commodity Index) rose 2.9% in October marking a second month in a row of positive returns in the face of a stable or increasing US Dollar. Gold added to 2025 gains, increasing 3.7% despite retreating from an all-time high mid-month. Natural gas rocketed 25% higher as the US continues to increase production and exports.

Economic Commentary

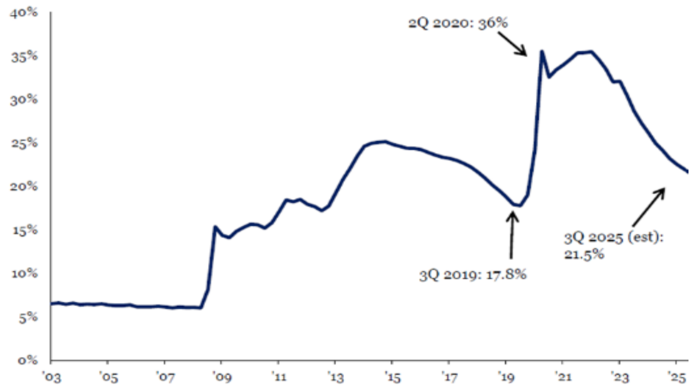
3rd Quarter S&P 500 Earnings continued momentum from the 2nd quarter with reported earnings through October outpacing analyst expectations. Analysts entered the reporting season expecting 8% earnings growth after a surprisingly strong 2nd quarter reporting season that delivered 12% year/year earnings growth. As of October 31st, earnings growth for the 3rd quarter increased to almost 11% driven by strong reports from Financial and Technology companies. While those sectors led earnings performance there was also broad improvement with 9 of the 11 S&P 500 GICS sectors seeing increases in earnings growth from where expectations stood on September 30th. Microsoft, Apple, Amazon, and Google all delivered strong earnings reports that propelled their stock prices higher. Large banks also delivered excellent earnings despite concerns on credit losses given a handful of high-profile defaults as well as some select weakness in smaller regional bank earnings. Large companies are seeing operating margin improvement despite the uncertainty created by trade policy. Major cost inputs for S&P 500 companies like wages and energy have seen slower growth despite stubborn inflation data for consumers that is more focused on shelter and services. Capital spending on AI development has cooled off free cash flow growth from Mag7 companies but has not put pressure on overall S&P 500 profit margins to date. Mag7 companies (ex Amazon and Tesla) had been operating margin leaders prior to the recent AI capex cycle but remain well above averages in the S&P 500 that include much more capital-intensive sectors like Energy, Industrials, and Materials. Corporate defaults like First Brands, rising concerns on lower-income consumers, and weak job growth have created questions for investors on whether the positive economic and market cycle can continue. Yet, the AtlantaFed GDPNow forecast for the 3rd quarter is at 4.0% percent and S&P 500 earnings growth is forecast to remain close to 10% for the coming quarters through 2026. The key risks to the positive forecasts would be a slowdown of AI capex if investors or companies rethink investments that have not shown much of a return to date or the job market shifting from no growth to job losses. We do not think that is the likely scenario for the remainder of 2025 and next year, but the labor data especially should be watched closely.



Year/Year S&P 500 Earnings Growth
Source: FactSet Earnings Insight as of 10/31/25

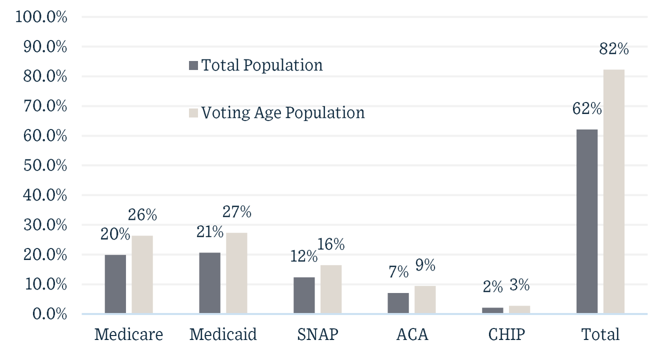
The Federal Reserve cut the Fed Funds Rate by a quarter point on October 29th to a range of 3.75% to 4.00%. The rate cut was in-line with expectations but the voting showed less unanimity than prior meetings with one vote for holding rates steady, and another vote for a half point cut. Fed Chair Powell followed the FOMC release at his press

Summit Trail Advisors LLC ("STA") is a SEC registered investment advisor headquartered in New York, NY. Please see the Important Information section for additional disclosures conference by throwing cold water on the certainty of a December rate cut pointing to the lack of data the Fed is receiving during the government shutdown. Markets wobbled, but remained positive in October and expectations for a December rate cut remain at about 70%. More important than the rate cut for markets was the announcement of an end to the Fed's policy of Quantitative Tightening (QT). QT is the oppositive of Quantitative Easing (QE), a process of reducing rather than expanding the Fed's balance sheet, primarily by not repurchasing fixed income securities that mature. QT or QE have impact on liquidity in markets. If the Fed is actively purchasing securities like they do in QE there is a robust buyer for assets that are typically found on bank and corporate balance sheets, which was the Fed's playbook after the Financial Crisis and during Covid. QT then means as securities mature, or are sold, the Fed is not an active buyer and there can be less liquidity in markets. Bank reserves and money market funds are often the areas where impact from QT can show up. Bank reserves have been falling in-line with the reduction in the Fed's balance sheet, although much of that reduction happened early on in 2022. Bank reserves at $3 trillion remain well above any historical period other than immediately following Covid. The Fed announced that QT would be ending on December 1st, a bit further out than expectations. One measure of liquidity stress, comparing the Secured Overnight Financing Rate (SOFR) rate that measures the cost of borrowing overnight among banks with Treasuries as collateral to the benchmark Fed Funds effective rate, had shown intermittent stress in funding markets over the course of October. Easing that stress to support liquidity makes the Fed's announcement look reasonable. The Fed's balance sheet has also generally returned to levels prior to the pre-Covid explosion, which may have marked a range the Fed was comfortable returning to before ending the decline. However other measures of market liquidity and speculation remain rampant: Bitcoin had touched an all-time high in October prior to pulling back, as had gold which typically is a measure of monetary policy. Markets are close to all-time highs and speculation is rampant across levered ETFs and meme stocks. The end of QT does not mean the beginning of QE, but moving to a more accommodative monetary policy with current market conditions and inflation well above target raises the question of what tools the Fed would use in an actual market or economic downturn.



Federal Reserve Balance Sheet as a % of US GDP
Source: Strategas, Federal Reserve

The US Federal Government shutdown became the longest on record on November 5th, surpassing a 34-day shutdown during the 1st Trump administration in 2018. The dispute driving the shutdown is primarily over Affordable Care Act (ACA) subsidies that were created in 2021 under the Biden administration. Democrats had created an expiration at the end of 2025 for the ACA subsidies in the American Rescue Plan and Inflation Reduction Act primarily because of how expensive the subsidies would be in terms of the Congressional Budget Office "scoring" of those bills. Both parties use expiries with various policy measures to make the cost more palatable in the bill approval process. The ACA subsidies were credited with dramatically increasing enrollment in the public government-backed health care plans, but then of course the success of enrollment creates an even larger problem when the subsidies are set to expire. Without the subsidy in place, consumers using the public health plans are estimated to see 20 to 30 percent increases in premiums at the end of 2025. Democrats were looking to avoid this issue by extending the subsidy and Republicans want the pandemic-era subsidy to expire given the pandemic is over and the state of US fiscal deficits. Government shutdowns have historically not lasted very long on average because during the shutdown federal workers and the military are left unpaid as well as many other services either being cut back or closed. Each payroll cycle ramps up pressure on both parties and historically has brought the parties together to compromise. For the current shutdown, the Trump administration has funded military payrolls through private donations allowing them to dilute pressure on Republicans not paying our troops. Federal workers remain unpaid and on November 1st the Supplemental Nutrition Assistance Program (SNAP) lapsed despite back and forth in courts on whether the President has authority to not pay SNAP benefits. The administration has also announced cutbacks to Federal Aviation Administration (FAA) employees that are causing havoc for consumers using air travel. Historically, government shutdowns have had limited economic and market impact because they have been short-lived and typically have not spilled over into consumer sentiment or spending. Markets have continued to move higher during the current shutdown on AI capex spending and strong S&P 500 3rd quarter earnings. However, missing or late data on employment and inflation is increasing challenges for the Fed in guiding monetary policy. The current shutdown exemplifies the politics of trying to reconcile US government spending with the size of many government spending programs. Between Medicare, Medicaid, SNAP, and the ACA marketplaces, more citizens (and voters) than ever are tied to the government's willingness to spend. Each of these programs has grown substantially, doubling on average in terms of population due to expansionist government policy and the economic hardship brought on by the Financial Crisis and pandemic. There is overlap among participants in the programs which overstates the number, but a simple measure of the number of participants in each program versus our total population and total voting age population shows 62% and 82% total respectively in just 5 programs (Medicare, Medicaid, SNAP, ACA, and CHIP). That voting bloc combined with a shifting adoption in both traditionally Republican and Democratic states makes the likelihood of longer and more impactful government shutdowns a rising risk to markets and the economy. We expect the current shutdown will be resolved in advance of the holidays, but we would expect consumer spending data for October and November to show the increasing impact of government spending on consumption in the US economy.



Percentage of US Population in Various Government Programs
Source: US Census Bureau, USDA Food and Nutrition Service

Important information