

Market Update & Outlook 4Q 2025

Economic growth improved in the second half of the year, as consumer spending remained strong despite labor market weakness. Robust earnings propelled U.S. stocks to record highs during the quarter. International stocks were the top-performing asset class in 2025, with dollar weakness boosting returns for U.S. investors. Bonds finished the year with solid mid-single-digit returns.

Economic Growth Improves

While the third quarter economic growth report was delayed by two months due to the government shutdown, the results were worth the wait. The late-December release indicated the U.S. economy grew faster than expected at 4.3% in third quarter. The gains were powered by solid consumer spending, increased government outlays, and higher exports.

While overall consumer spending remains strong, it is concentrated in the top 10% of households by income level. According to Moody's Analytics, these households currently account for nearly half of total consumption. By contrast, lower- and middle-income families are feeling pinched by rising insurance premiums, higher food and utility costs, and the resumption of student loan payments. This disparity helps explain the decline in the University of Michigan consumer sentiment index, which fell to the lowest level since June 2022 despite a growing economy.

Inflation showed improvement toward year-end with CPI rising 2.7% for the 12 months ending in December, down from a peak of 3.0% in September. While this is encouraging, missed data collection periods in October and November during the government shutdown have distorted the readings for this period. A clearer inflation picture should emerge in January and February as normal data compilation resumes.

Source: Morningstar Inc, September 30, 2025.

Forvis Mazars Private Client

Services may include investment advisory services provided by Forvis Mazars Wealth Advisors, LLC, an SEC-registered investment adviser, and/or accounting, tax, and related solutions provided by Forvis Mazars, LLP.

Employment conditions softened in the fourth quarter. New job creation remains weak, with non-farm payrolls rising by only 50,000 in December. The unemployment rate for December was 4.4%, up from 4.0% at the start of the year. Developments in employment and inflation will be key factors determining Federal Reserve interest rate policy in 2026.

Stocks Rally to New Highs

The stock market continued to advance in the fourth quarter, albeit at a more gradual pace. After declining 15% year-to-date in early April, U.S. equities staged a remarkable comeback, finishing the year up more than 17%. Gains were fueled by strong sales and profit growth, with S&P 500 companies posting 8% revenue growth and 13% earnings growth in the third quarter. The U.S. market's forward price-to-earnings ratio ended the year at 22, consistent with its level at the start of 2025.

MARKET SCOREBOARD	4Q 2025	2025 YTD
S&P 500 (Large U.S. stocks)	2.65%	17.88%
MSCI EAFE (Developed international stocks)	4.86%	31.22%
Bloomberg Aggregate Bond (U.S. taxable bonds)	1.10%	7.30%
Bloomberg Municipal Bond (U.S. tax-free bonds)	1.56%	4.24%
Wilshire Liquid Alternative (Alternative investments)	.34%	6.04%

International stocks outperformed U.S. markets for the first time in several years. Both developed international and emerging markets gained more than 30% in 2025. This impressive performance was the result of strong local market returns combined with a weaker dollar, which boosted gains for U.S. investors.

U.S. stocks have now delivered three consecutive years of double-digit growth, powered by technology and AI-related stocks. The large-cap growth segment has significantly outperformed large-cap value during this period, but the return gap narrowed to just 3% in 2025. This indicates broadening participation in gains across sectors, which is a positive development from the standpoint of future return potential.

U.S. Economy Grows Despite Labor Market Weakness

Recent economic trends present an interesting paradox: economic growth and consumer spending are strong, even as labor market conditions weaken. The unemployment rate increased from 4% at the beginning of 2025 to 4.4% in December, and job creation slowed markedly through the summer and fall. Despite this, the economy expanded by a solid 4.3% in the third quarter. Consumer spending is expected to have grown 2.2% for the year, with a notable 3.5% increase in the third quarter alone.

The resilience in wages and spending, despite softer job growth, is attributable to rising productivity. Productivity is a measure of output produced per hour of labor. According to Goldman Sachs, annual productivity has been 0.4% higher over the past six years compared to pre-pandemic levels. For the trailing 12 months through September 2025, U.S. labor productivity rose 1.9%. As artificial intelligence becomes more integrated into the economy, productivity should continue to improve. Continued productivity gains should support healthy wage growth, bolster corporate profit margins, and help ease inflation pressures, creating a constructive economic backdrop as we enter 2026.

Source: Morningstar Inc, September 30, 2025.

Forvis Mazars Private Client

Services may include investment advisory services provided by Forvis Mazars Wealth Advisors, LLC, an SEC-registered investment adviser, and/or accounting, tax, and related solutions provided by Forvis Mazars, LLP.

Future Path of Fed Policy is Uncertain

The Federal Reserve ended 2025 with a third consecutive 0.25% rate cut. As the Fed funds rate approaches levels consistent with economic balance, disagreements have emerged within the Federal Reserve Open Market Committee (FOMC) regarding the future path of rates. The decision to cut rates in December was not unanimous, with three dissenting votes—one favoring a larger cut and two preferring no reduction at all.

FOMC forecasts for 2026 reflect a split between members expecting additional cuts and those anticipating no further action. This division highlights growing tension in the economy. Certain Fed members are most concerned about persistent inflation amid robust economic growth, and as a result are in favor of holding rates steady. Others worry more about the weak labor market and rising unemployment, arguing for more rate cuts.

Compounding the uncertainty, Jerome Powell's term as Fed Chair ends in May. The Administration has been very vocal about wanting lower rates, so the nomination of a successor who supports further cuts seems likely. Given the stability of the December employment report, the Fed is expected to hold rates steady in the near term. Barring significant deterioration in employment or inflation data, the next rate cut will likely be deferred until the new Fed Chair is appointed.

2026 Market Outlook

2025 proved to be a fantastic investment year. U.S. stocks posted a third consecutive year of double-digit gains, and diversified portfolio returns were well above average. However, the path to a successful investment year was treacherous at times. Market volatility surged in April due to tariff-related disruptions, spiking to levels last seen during the Great Financial Crisis of 2008–2009 and the Covid-19 pandemic in 2020. During

this period, U.S. markets declined nearly 20%. Despite turbulence, portfolio discipline was rewarded as markets stabilized and began a steady upward trek to new highs in the second half of the year.

Diversification played a meaningful role throughout the year, helping to limit losses during the April downturn while also propelling gains later on. All four major asset classes delivered positive results, led by international stocks. Bond performance returned to typical mid-single-digit levels and helped stabilize portfolios during the stock market turmoil.

Looking ahead to 2026, the investment outlook remains generally positive, based on the following factors:

- **Accommodative Federal Reserve Policy** – The Fed has reduced the Fed funds rate by 1.75% over the past two years and is likely to cut rates further in 2026.
- **Favorable Tax Policy** – The 2025 *One Big Beautiful Bill Act* (OBBBA) budget bill preserved historically low tax rates for individuals and businesses and introduced new provisions that should enhance corporate profitability.
- **Rising Productivity** – Technological advancements continue to improve efficiency and productivity across industries, supporting strong earnings trends.
- **Diminishing Tariff Effects** – As last year's tariffs are "lapped" in 2026, inflation should resume its downward drift toward the Fed's target of 2%.

That said, there are risks that warrant attention in the new year. While economic growth has improved the last two quarters, gains have been "K-shaped." Higher-income households are benefitting from rising asset prices and strong income growth (top portion of the "K") while lower- and middle-income households (bottom portion of the "K") are strained by

higher living costs and limited wage growth. This imbalance could increase the vulnerability of the economy to a downturn.

Meanwhile, U.S. stock valuations are at the upper end of the historical range. While higher profit margins and lower tax rates offer some justification for current market prices, forward returns tend to be lower when starting from higher valuation levels. Because of this, we expect more moderate returns from U.S. stocks in 2026.

Portfolio diversification should continue to benefit investors in the new year. International valuations remain attractive compared to U.S. markets, and bonds continue to offer appealing risk-adjusted returns at current yield levels. We expect a more balanced return contribution across asset classes, which should support positive investment outcomes in the year ahead.

On behalf of the Forvis Mazars Private Client team, we hope you had a wonderful holiday season, and we look forward to making more progress together in 2026!

Jeff Layman & Andrew Douglas

Forvis Mazars Private Client services may include investment advisory services provided by Forvis Mazars Wealth Advisors, LLC, an SEC-registered investment adviser, and/or accounting, tax, and related solutions provided by Forvis Mazars, LLP. The information in this commentary should not be considered investment advice to you, nor an offer to buy or sell any securities or financial instruments. The services, or investment strategies mentioned in this commentary may not be available to, or suitable, for you. Consult a financial advisor or tax professional before implementing any investment, tax or other strategy mentioned herein. The information herein is believed to be accurate as of the time it is presented and it may become inaccurate or outdated with the passage of time. Past performance does not guarantee future performance. All investments may lose money.

Source: Morningstar Inc, September 30, 2025.

Forvis Mazars Private Client

Services may include investment advisory services provided by Forvis Mazars Wealth Advisors, LLC, an SEC-registered investment adviser, and/or accounting, tax, and related solutions provided by Forvis Mazars, LLP.