

Market Commentary

Q3 2025



- U.S. equity markets continued to climb in Q3, with momentum driven by persistent inflows into AI-related themes across multiple sectors. The S&P 500 recorded 28 all-time highs through quarter-end.
- International equities outperformed, with the MSCI ACWI Ex USA NR USD (“ACWI ex USA”) beating the S&P 500 by the widest margin since 2009. Year-to-date, the ACWI ex USA returned 26.0%, versus 14.8% for the S&P 500.
- The Federal Reserve delivered its first rate cut since 2024 at the September meeting, citing a softening labor market and moderating inflation. Chair Powell emphasized a [“meeting-by-meeting”](#) approach, pushing back against expectations for a full easing cycle.

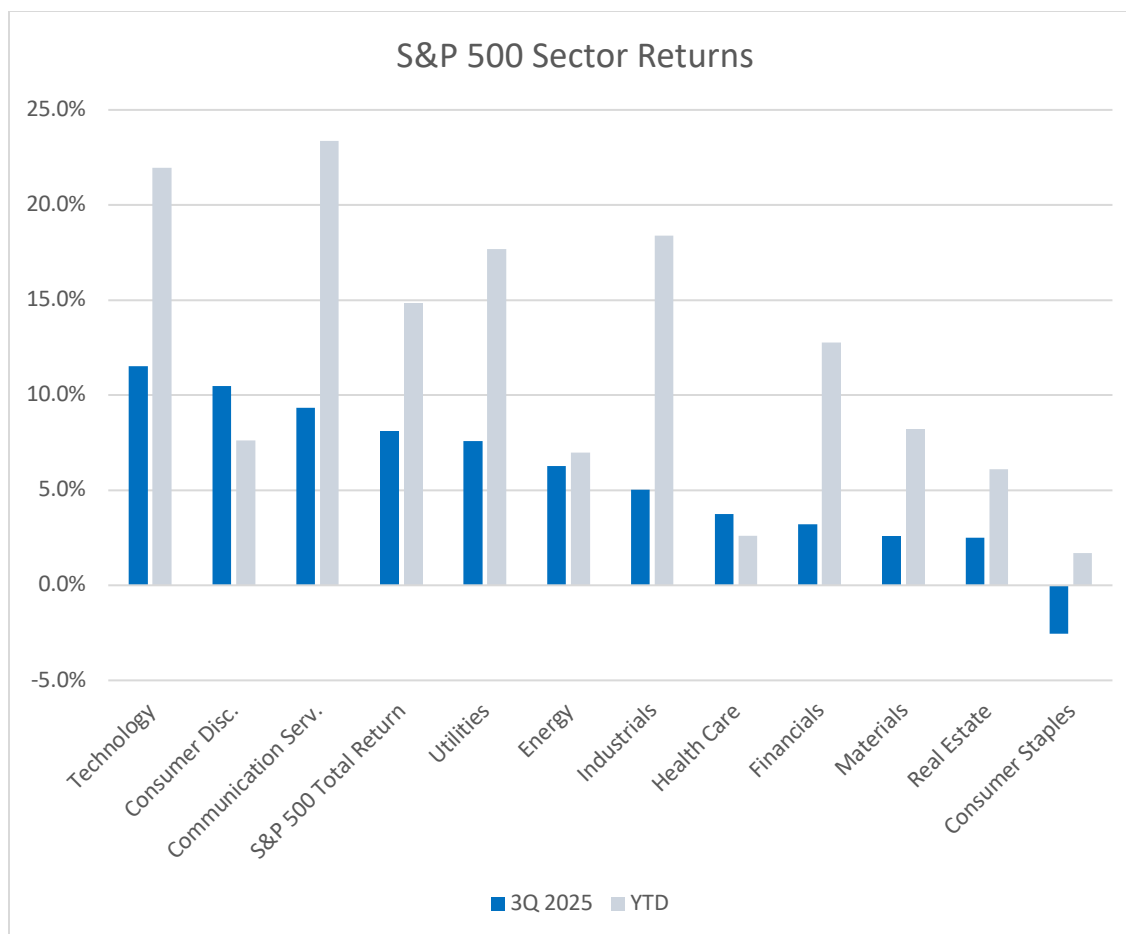
Market Total Returns

	Month %	QTD %	YTD %	1 Year %	3 Year %	5 Year %	10 Year %
S&P 500 TR USD	3.65	8.12	14.83	17.60	24.94	16.47	15.30
DJ Industrial Average TR USD	2.00	5.67	10.47	11.50	19.63	12.98	13.50
NASDAQ Composite TR USD	5.68	11.41	17.93	25.42	29.92	16.07	18.32
Russell 2000 TR USD	3.11	12.39	10.39	10.76	15.21	11.56	9.77
MSCI ACWI Ex USA NR USD	3.60	6.89	26.02	16.45	20.67	10.26	8.23
MSCI EAFE NR USD	1.91	4.77	25.14	14.99	21.70	11.15	8.17
MSCI EM NR USD	7.15	10.64	27.53	17.32	18.21	7.02	7.99
Bloomberg US Agg Bond TR USD	1.09	2.03	6.13	2.88	4.93	-0.45	1.84

Source: Morningstar Direct

U.S. Equities – Strength Broadens, but Leadership Remains Familiar

The rally in artificial intelligence and its related industries has helped the S&P 500 rebound over 30% from its April lows. Gains within the growth category have been notably concentrated, with NVIDIA (NVDA) alone contributing roughly [25% of the index’s Q3 return](#) and adding the combined impact of Tesla (TSLA), Broadcom (AVGO), and Microsoft (MSFT) accounting for over 55% of total gains during the quarter. At a sector level, technology drove 55% of growth index returns, and when combined with industrials and communication services, those three sectors made up [85% of the total contribution](#).



Source: Morningstar Direct

Despite ongoing concentration, U.S. equities extended their year-to-date rally in the third quarter. The S&P 500 Total Return Index is up 14.8% through September 30, notching [28 new all-time highs](#) during the period. Investor enthusiasm around AI-driven productivity, improving corporate earnings, and shifting expectations for Fed policy continued to support risk assets.

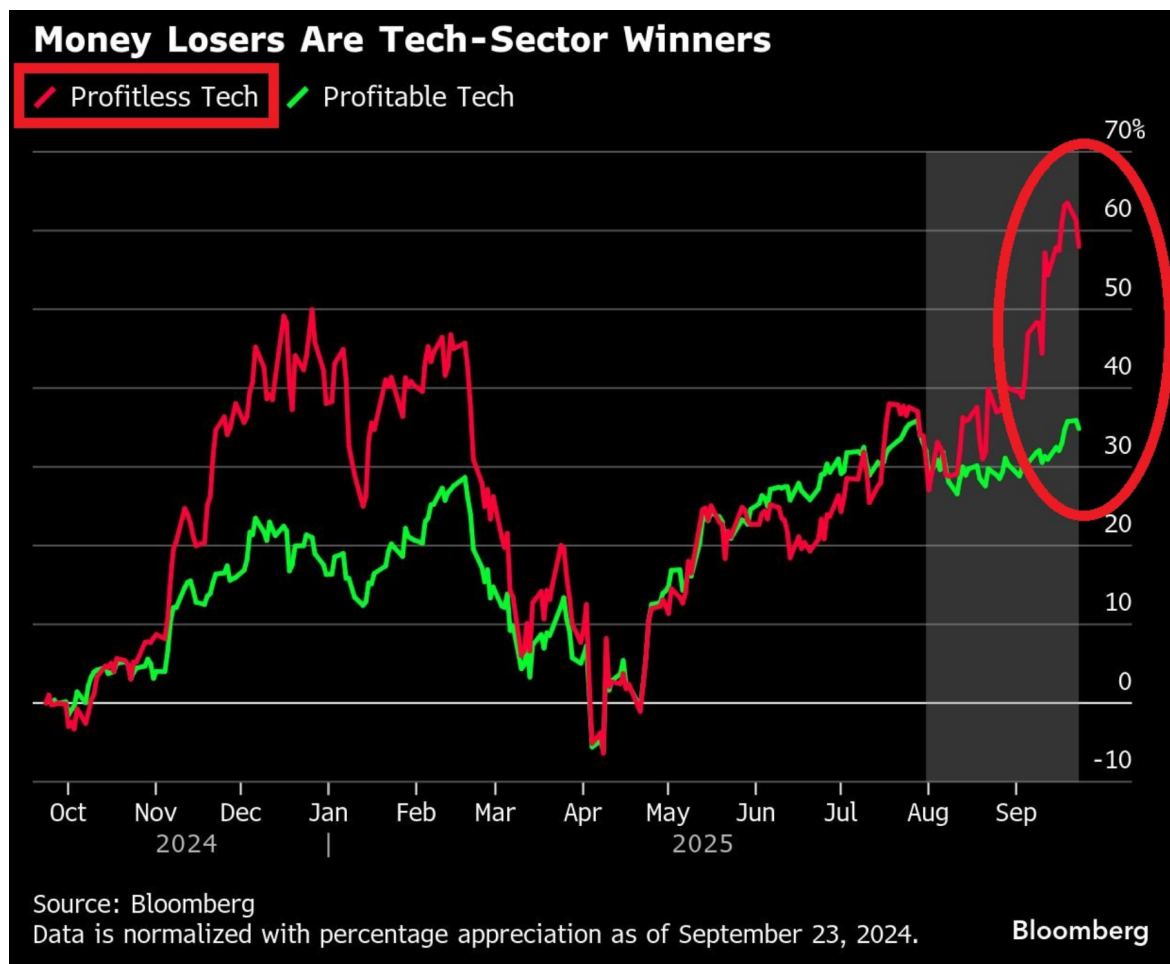
Importantly, market breadth improved modestly in Q3. Small-cap equities outperformed large caps for the first time this year, with small-cap value, core, and growth all outperforming their mid- and large-cap counterparts.

	3Q 2025			YTD		
Large Cap	5.3%	8.0%	10.5%	11.7%	14.6%	17.2%
Mid Cap	6.2%	5.3%	2.8%	9.5%	10.4%	12.8%
Small Cap	12.6%	12.4%	12.2%	9.0%	10.4%	11.7%
	Value	Core	Growth	Value	Core	Growth

*Index returns are reflective of the Russell 1000, Russell 2000, and Russell Mid Cap

Source: Morningstar Direct

One notable theme within this broader participation was a sharp rebound in unprofitable or early-stage tech companies, often viewed as proxies for speculative sentiment. With markets increasingly pricing in potential Fed rate cuts in Q4 and into 2026, retail traders and risk-on investors rotated into more volatile corners of the equity market. UBS's [“profitless tech”](#) basket has outperformed profitable tech stocks by a wide margin — up 21% versus 2.1% since the end of July, and rallying nearly 60% from the April lows.



This rotation into unprofitable AI, quantum computing, and nuclear-related names underscores rising speculative activity and reinforces how rate expectations and liquidity shifts continue to influence risk appetite.

Retail traders, who have largely outperformed institutional investors in 2025, began pulling back from some of the market's more speculative corners in September. While the "profitless tech" trade remained active, risk appetite showed signs of cooling, with notable outflows from cryptocurrencies and popular leveraged ETFs tied to the semiconductor sector and Tesla. Day traders — recently dubbed the "Casino Crowd" by Bloomberg — were early buyers of leveraged funds in January and added heavily during April's lows, positioning them well for the year's rally. However, recent retreat from riskier positions may reflect growing caution amid rising volatility, a looming government shutdown, and the lack of economic data releases due to federal agency disruptions.

Fixed Income — Yield Moves, Policy Signals, and Global Ripples

U.S. & GLOBAL BOND MARKETS

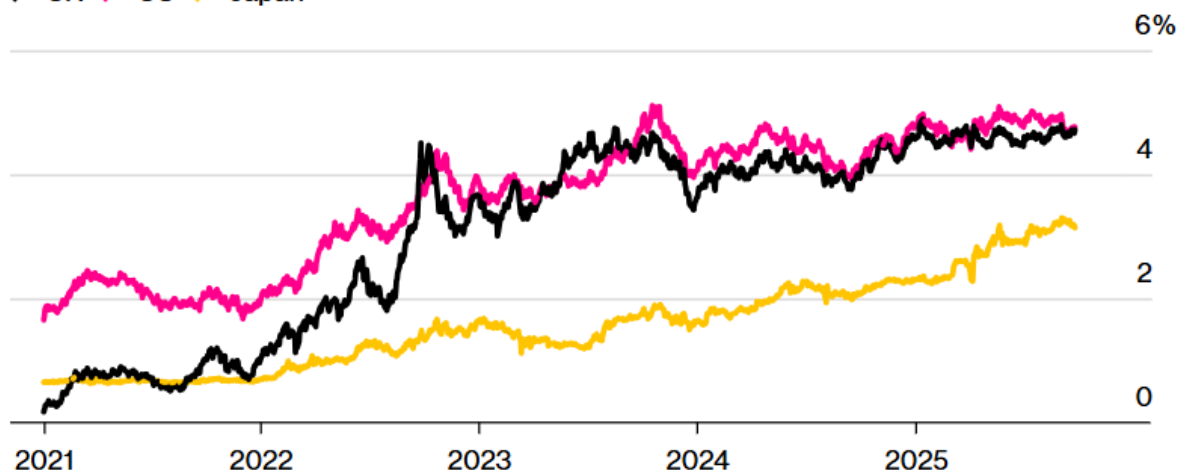
Long-dated bonds saw notable yield compression in Q3. U.S. and Japanese 30-year yields fell by roughly 20 basis points, while U.K. 30-year gilts dropped about 10 bps. The rally reflected renewed demand as investors hunted for value in high-quality duration amid softening economic signals.

One of the key drivers behind the rally in long-duration bonds has been the shift in sovereign debt issuance strategies. Several major central banks are reducing their planned sales of ultra-long debt, easing supply pressures in markets already hungry for duration. Japan is scaling back its upcoming auctions of 30-year and 40-year bonds, while the Bank of England is lowering the proportion of long-term securities in its quantitative easing program starting next month. In Australia, officials have indicated that they are considering a reduction in ultra-long bond issuance due to rising borrowing costs and concerns about market volatility. These adjustments are helping to support prices across the long end of global yield curves.

Pressure on Long-Dated Bonds Has Slightly Eased

Yields on global 30-year bonds have dipped this month

— UK — US — Japan



Source: Bloomberg

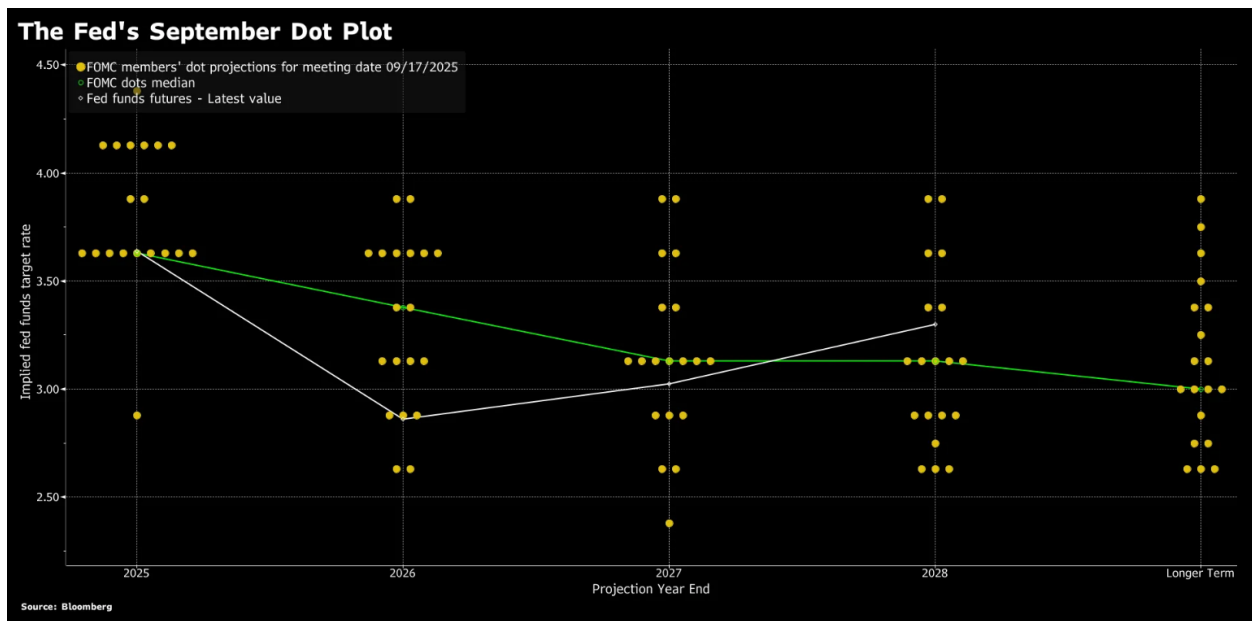
Earlier in the year, weak demand from pension funds and insurers had weighed on bond markets. TS Lombard economist [Davide Oneglia](#) noted that these institutional investors were phased out of the long end due to tighter quantitative policy, but shifting supply dynamics have helped revive interest. Oneglia added that “more forceful action from authorities to reduce long bond issuance should present investors with decent opportunities”.

U.S. FED & MONETARY POLICY

The September FOMC meeting marked the first rate cut since 2024. The dovish move was underpinned by weakening labor metrics and inflation trends aligning more closely with the Fed's 2% target. However, [Chair Powell emphasized a “meeting-by-meeting” approach](#), indicating cuts would not follow a predetermined path.

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Source: Bloomberg

Inflation remains a key variable. [The Dallas Fed's trimmed-mean PCE measure](#), which excludes outlier price moves, is now at its highest for the year and nearing the upper end of the Fed's comfort zone. If inflation remains stickier than expected, the Fed may act more cautiously than markets hope.

Fixed Income - Returns

The third quarter delivered broad-based strength across fixed income markets. In the U.S., convertibles led with a 10.35% gain, while core sectors like the Bloomberg U.S. Aggregate Bond Index rose 2.03%. Long-dated Treasuries added 2.45%, supported by cooling inflation and shifting Fed expectations. High yield also participated, though gains moderated toward the end of the quarter as risk sentiment pulled back.

Select Fixed Income Returns	3Q 25	YTD
Bloomberg US Convertible Comp TR USD	10.35	17.75
Bloomberg Municipal TR USD	3.00	2.64
ICE BofA US Corporate TR USD	2.65	6.96
Bloomberg US Corporate High Yield TR USD	2.54	7.22
Bloomberg US Treasury 20+ Yr TR USD	2.45	5.10
Bloomberg Treasury 7-20 Yr TR USD	2.16	6.79
Bloomberg Treasury 5-7 Yr TR USD	1.43	6.78
Bloomberg 1-5 Yr Treasury TR USD	1.14	4.64
Bloomberg US Treasury Bill 1-3 M TR USD	1.10	3.25
Bloomberg US Agg Bond TR USD	2.03	6.13

Source: Morningstar Direct

Looking ahead, policy uncertainty poses a key risk. A prolonged U.S. government shutdown or renewed fiscal standoffs could erode investor confidence and delay critical economic data. While short-term disruptions may be absorbed, a drawn-out impasse could inject volatility into rate markets and credit spreads as the fourth quarter unfolds.

International Markets – Resilient Gains Abroad Amid Diverging Macro Backdrops

International equities continued to show resilience in Q3, with the MSCI ACWI ex USA Index returning 6.89%, again outperforming the S&P 500. Several markets posted double-digit gains, supported by improved risk sentiment and easing dollar strength.

In Europe, performance was mixed. Greece led developed markets with a 12.0% gain, followed by Spain (11.8%) and Luxembourg (11.3%), while Germany declined by 1.0%, dragged down by recession concerns and poor manufacturing data. France posted a modest 3.2% return amid political uncertainty and rising long-term yields. In the UK, equities rose 5.1%, aided by stabilizing inflation and expectations for Bank of England rate cuts.

Japan continued its equity rally with the S&P Japan BMI up 8.6%, supported by a weaker yen and robust export activity. Meanwhile, Korea (10.3%) and Mexico (12.2%) benefited from improving growth expectations and strong trade links to the U.S.

China stood out with the MSCI China A Index rallying 19.8%, one of the strongest country-level performances globally, as they were [helped by new capital market reforms](#), tech sector momentum, and perceived policy support.

In Latin America, Mexico rose 12.2%, supported by strong U.S. trade flows and nearshoring tailwinds, while Brazil gained 7.4%. However, Argentina declined sharply (-31.9%) amid political and economic instability ahead of its presidential election.

Select Developed and EM Country Returns	3Q 25	YTD
MSCI China A NR USD	19.8	23.7
S&P Mexico BMI NR USD	12.2	44.2
S&P Greece BMI NR USD	12.0	66.7
S&P Spain BMI NR USD	11.8	58.8
S&P Luxembourg BMI NR USD	11.3	59.4
S&P Canada BMI NR USD	10.8	28.1
S&P Korea BMI NR USD	10.3	54.4
S&P Japan BMI NR USD	8.6	22.1
S&P Italy BMI NR USD	7.7	45.1
S&P Brazil BMI NR USD	7.4	41.3
S&P United Kingdom BMI NR USD	5.1	25.7
S&P France BMI NR USD	3.2	24.7
S&P Germany BMI NR USD	-1.0	32.8
S&P Argentina ADR NR USD	-31.9	-46.6
Benchmark: MSCI ACWI NR USD	7.6	18.4

Source: Morningstar Direct

Watching the Crosswinds: Sentiment, Rates, and Currency Trends

With the fourth quarter underway and 2026 on the horizon, the global market backdrop remains uneven. The U.S. economy remains surprisingly resilient, but weaker consumer sentiment and growing concerns about the distribution of spending pose potential cracks under the surface. In September, [the University of Michigan index fell to a four-month low](#), and inflation expectations among households rose to 4.7%, a level that could sap consumption if sustained.

Meanwhile, the U.S. dollar continues to soften, down around 10% year-to-date. This has been a tailwind for corporate earnings and global assets. However, the pace and magnitude of capital flows into the U.S. are increasingly hedged. [Over 80% of equity inflows and about 50% of bond inflows into U.S. markets are now currency-hedged](#). This signals that global investors remain bullish on U.S. risk assets but are becoming more cautious about currency exposure.

- Key themes heading into year-end include the Fed’s rate path, consumer resilience, and dollar weakness. Risks such as a prolonged U.S. government shutdown, tariff escalation, or Fed missteps could sharply shift sentiment and add volatility.
- Unprofitable tech stocks surged in Q3, with [UBS’s “profitless tech”](#) basket up ~22% since late July—far outpacing ~2.5% gains for profitable peers. The sharp divergence may reflect elevated investor appetite for risk in a low-yield environment, but it also raises questions about sustainability if macro or earnings conditions deteriorate.



FOOTNOTES:

Past performance is no guarantee of future returns.

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Data from Morningstar. Returns over one year are annualized.

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