

Private Client Letter

by John E. Chapman

The Good Times Roll On

U.S. stocks performed strongly in October 2025, led by the technology sector and a surge in AI-related stocks. The S&P 500 rose approximately 2.3% to 2.6%; the Nasdaq jumped 4.7%, and the Dow Jones Industrial Average gained 2.5%, marking multi-month winning streaks across all major indices. The rally occurred despite an ongoing U.S. government shutdown, volatile Treasury yields, and persistent inflation concerns.

The S&P 500 extended its run to six consecutive positive months, its longest since 2018, while the Nasdaq notched its seventh straight monthly gain and hit new year-to-date highs. Tech and AI-linked companies, especially Amazon (which surged 9.6% after blockbuster earnings), were instrumental in these gains. Broader average returns masked wide sector dispersion, however. Even with about 60% of stocks in the S&P indices finishing the month lower, tech outperformance drove the indices higher.

All of this is especially notable given October's longstanding reputation as the most volatile month for U.S. equities, driven by a history of dramatic stock market swings and several prominent crashes. Statistical evidence confirms this reputation: since 1950, October has had more trading days where the S&P 500 moved by 1% or more than any other month, and its standard deviation of monthly returns is about 33% higher than the average for other months (Investopedia).

Supported by the Fed's dual announcement of a 25 basis points (bps) cut in the Fed Funds rate and the official end of quantitative tightening on December 1st; investors appear to be encouraged by continued strength in corporate earnings and optimism involving artificial intelligence. Indeed, investors seem undeterred by stretched valuations, growing internal market weakness, and rising speculative activity.

One sign of speculative activity can be found in the use of leverage by investors. New York Stock Exchange (NYSE) margin debt has surged more than 32% since the end of April. The acceleration in the use of leverage exceeds what was seen during the major market run-ups in the late 1990s, the mid-2000s, and the post-COVID period.

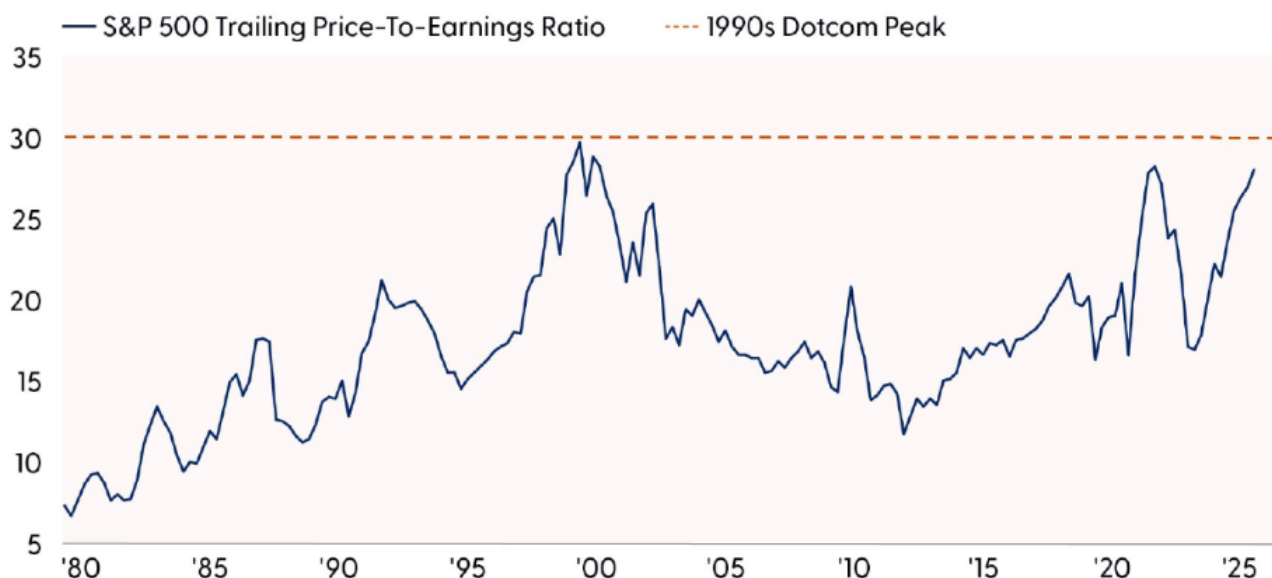
The actual level of speculative leverage in the market is likely far higher than margin debt figures alone would suggest due to the embedded leverage within investments such as zero-day options (ODTE) and leveraged exchange-traded funds (ETFs); both of which have gained in popularity. Historically, such dramatic increases in the use of leverage have tended to mark poor entry points for equity investors, as they often preceded periods of drawdown and heightened volatility.

While many market participants see higher prices as the path of least resistance, this complacency can raise the prospects for a correction in the market.

Compounding the challenges for investors today comes from the government shutdown. With the exception of a single inflation report, there has been no economic data from the federal government in over a month. Reports from September, before the government shut down, appeared to be showing some cracks in the economy. Employment data showed a decline, while manufacturing numbers were signaling contraction. Even the services data fell to its second lowest level this year.

High levels of global liquidity, low interest rates, and a reasonable profits outlook push asset valuations higher by reducing discount rates and encouraging risk-taking. As more investors participate, the market's equilibrium valuation level shifts upwards, so what was previously considered "expensive" may be perceived as a new normal in a world with persistent liquidity growth. There's been a lot of bubble talk recently, given the expansion and concentration of the technology sector which is now at an all-time high of roughly 35% weighting in the S&P 500. Coupled with rallies in momentum stocks and unprofitable companies, many have drawn comparisons between this market environment and the dotcom boom of the late 1990s.

Using a basic valuation approach with the price-to-earnings ratio (P/E) for the S&P 500 on a trailing four-quarter basis, we find that the index currently trades at a P/E of 28, very close to the 1990s dotcom peak around 30 and well above the respective 10-, 20-, and 40-year averages of 21.1, 18.4, and 18.3 (LPL Financial).



Note: Series represents operating earnings excluding non-recurring and non-operating items.

Source: LPL Research, FactSet, 10/23/25

Disclosures: Indexes are unmanaged and cannot be invested in directly. Past performance is no guarantee of future results.

True bubbles and reversals tend to become obvious only in hindsight, as participants are lulled into a "this time is different" mindset, sometimes rationalized by apparent structural changes in the economy or markets. In this case, the AI boom currently dominates the market narrative. There is too much capital chasing the space for the narrative to downshift near-term. However, the boom can't last forever, and it's anyone's guess when trillion-dollar capex spending, rapid increases in leverage, and massive changes to the energy system finally run out of steam.

While many dangers lurk below exuberant markets, the bullish momentum in today's market is likely to persist until some exogenous event rattles investor confidence. Bull markets for stocks can last longer than many people expect due to a combination of structural, technical, and behavioral factors that support continued price increases and delay corrections.

So, for now the good times roll on.

Thank you for your continued confidence in our abilities to help you navigate the many challenges associated with growing and protecting your wealth.

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