ACM QUARTERLY MARKET COMMENTARY – THIRD QUARTER 2025

Capital Markets

Global stocks began the quarter with a sharp 12% drop over just four days on the announcement of the Trump administration's initial tariff policy and its highly punitive rates. Trump took note of the market's displeasure and was quick to announce a ninety-day pause on the afternoon of April 9th to allow for tariff negotiations with each of our trading partners. The market celebrated this announcement with a massive one-day rally. The S&P 500 jumped 10.5% on that day, which was its third-largest one-day gain since 1950. However, this rally occurred over less than three hours! Stocks were up and down for about a week thereafter, but then resumed their recovery. By the end of the quarter, global stocks had reached new all-time highs and have trended even higher since. The bond market was also volatile as it digested the tariff turmoil, with interest rates falling as low as 4.0% in early April, but rising to a high of 4.6% about six weeks later. Rates then trended back toward 4.2% by the end of the quarter, enabling U.S. aggregate bonds to return 1.3% in the quarter and bringing their year-to-date return to a respectable 4.0%. Municipal bonds, however, were flat in the second quarter to remain down slightly on the year. Finally, commodities more or less mirrored the volatility in stocks and interest rates. Prices collapsed in response to the initial tariff plans, but then rallied sharply thereafter. Nevertheless, the Bloomberg Commodity Index was still down 3% in the quarter.

The Economy

The global economy continues to be strong with the Global PMI climbing 0.5% to 51.7% in June and another 0.7% in July to 52.4. These readings indicate that a global slowdown is not imminent, despite any tariff concerns. The U.S. economy remains one of the world's strongest, with real GDP growth of 3.0% in the second quarter. Most economists continue to argue that even the more moderate tariff agreements that the U.S has negotiated will still decrease GDP growth meaningfully over the next year or so. We expressed our concerns regarding tariffs and their effect on growth and inflation last quarter. However, the stock market seems less concerned, so for the time being, we are inclined to follow the market's lead rather than theoretical economic models.

Portfolio Management

As we highlighted in our last letter, we were not caught off guard by the market volatility in April. The market had been rising more or less continuously for almost two years, with valuations and bullish sentiment stretched thin. Had it not been the tariffs, it likely would have been something else for a market that was overdue for a reset of expectations. Our portfolios were defensively positioned heading into the second quarter with less than target allocations to stocks. As a result, we were able to moderate our losses during the correction. More importantly, we made a decisive move to reposition our portfolios to a more aggressive posture on April 8th. This decision was based on some of our favorite indicators that were flashing contrarian buy signals for a market that was deeply oversold in the short-term and sentiment indicators that had reached high levels of fear. Of course, our timing could not have been more perfect as the massive rally occurred the very next day.

By the end of April, the market had enjoyed a 15% rally and more than retraced its tariff price collapse. We felt it prudent at that point to rebalance our portfolio back down to target allocations, believing that the market was likely to retest its April lows at least once based on the still existing lack of clarity around the administration's tariff policies. The market did trade down for a few days thereafter. But we were proven wrong in short order as the market was able to shrug off overbought conditions and bullish sentiment to rally into quarter-end. In deference to our trend indicators, we have let our market profits ride since, and our portfolios have gradually risen back to above target allocations. Overall, we are pleased by the performance of our portfolios this year and how we have navigated a very volatile and uncertain time.

Looking Forward

Last quarter, we ended our letter by proclaiming that "Trump's tariff policies just need to get out of the way of this bull market." While they have not entirely gotten out of the way, they have moderated enough for this powerful bull market to resume its advance. That this rally has sustained itself despite some continued tariff concerns is evidence enough of its health. For the time being, we view this market as being in a goldilocks environment in which the economy is strong enough to drive corporate earnings higher, while inflation remains mostly subdued. As a result, investors are in a mindset where, more or less, both good and bad economic news are received positively, with the latter simply raising expectations for a resumption of Fed rate cuts.

In the U.S., market breadth continues to impress with 10 of the 11 S&P sectors closing above their 200-day moving averages at the end of July. Going back to 1950, the market has cycled from a zero reading to this level on nineteen previous occasions. In all of these cases, the market was higher six months later with a median gain of 10.1%, and in all but one case, the market was higher twelve months later with a median gain of 16.3%. Global breadth also remains strong as the percentage of countries with a positive one year rate of change has recently risen back above 80%. Going back to 1970, in this mode, global stocks have risen at an average clip of 16.9%. Finally, the percentage of central banks that are cutting interest rates has risen above 90%, which is also consistent with a market that should trend higher.

Though we would not be surprised to see at least one more decent correction in the coming months, ultimately, we are confident that we will end the year at even higher prices. As such, unless we see bullish sentiment reach max levels, for the time being, we are inclined to ride this market with our portfolios running modest above-target allocations to stocks.

This market continues to remind us of the late 1990s. We see this market as one that has entered “casino mode.” Margin debt as a percentage of GDP is surging steeply higher. The pace of new ETF launches has accelerated to an almost frenzied pace, with many of them tied to individual stocks. Take for example NVIDA (NVDA). Investors can choose from multiple ETFs that provide 2x or 3x long or short exposure, as well as ETFs that pursue NVDA covered-call strategies. They trade like hotcakes, and this extends to almost every popular stock you could name. In a sign of the escalation of this ETF “arms race”, approval for a 2x Bullish (BLSH) ETF was filed last week before the stock had even gone public! Just as it occurred in the dot-com bubble, an increasing number of companies that go public are not profitable, well oversubscribed, and jumping 100% or more on day one. However, in the late 1990s, that was only a stepping stone to a final blow-off where many IPOs coming to market were “pre-revenue” (a nice way of describing a cash-burning company with a dream and no sales). We would not be surprised to see this bull market end with a similar crescendo of greed and optimism, perhaps around a peak in AI excitement. For now, though, this is “casino mode” and investors can make plenty of money during this phase, just as they did in the final years of the dot-com bubble. We are well-suited for this type of environment, having deftly navigated that period and calling that epic market top with precision. Additionally, the trend component of our asset allocation models is designed to keep us invested in the later stages of a bull market even in the face of lofty valuations, and to guide us to a defensive posture when price momentum eventually wanes.