

October 2025

Once again, it was an excellent quarter to be an investor. Global returns in Q3 were strong, led by double-digit three-month returns from U.S. Small Caps. This is despite a daily backdrop of chaos and uncertainty. In fact, what we wrote several months ago to describe the returns from the previous quarter can apply seamlessly to Q3 just as well as it did for Q2:

These strong returns may come as a surprise to anyone following the daily onslaught of economic and non-economic news coming out of the White House along with the recently escalated conflict in the Middle East. Indeed, it has been a tumultuous start to the year compared to normal.

It is important to recognize that our personal sentiments on the market, economy, or world at large may not always align with how markets actually perform. We tend to overweight our personal attitudes toward the world around us and often project that optimism or pessimism onto how we expect investments to behave.

Interest Rates

Without a doubt, the hottest topic in the investment and financial planning world over the past month has been interest rates. In September, the Federal Reserve cut rates by 0.25% with strong guidance indicating further rate cuts in 2025 and 2026. So, what does this mean for investments?

Mathematically, declining interest rates are *good* for bond returns. As interest rates fall, the 'value' of existing bonds generally rises. While seemingly counter-intuitive, it's clear if we break down what is happening:

Imagine you have a US government bond that you purchased for \$10,000 that pays 5% interest per year and returns your \$10,000 after five years. A year later, the Federal Reserve has lowered interest rates by 1% and the government is issuing new bonds that carry a 4% rate. You could now go out and purchase a new bond for \$10,000 that would provide 4% interest and return your \$10,000 after four years. Which bond is better, the one providing 5% interest or the one providing 4% interest?

Obviously, the bond paying 5% interest is superior. As a result, market participants would pay a premium for your bond with the higher rate, thus increasing the trading price and

investment gain of your 5% bond. So, the trading value of existing bonds will likely rise in a falling rate environment.

On the other hand, the effect that falling interest rates may have on stocks is a bit murkier. Broadly, companies are likely to benefit from lower borrowing costs which could allow them to deploy capital and make expenditures with less of a cashflow drag from interest. But, the capital structure and position in the market cycle unique to each company will do more to dictate whether falling rates will actually be advantageous on a case-by-case basis. There is no simple mathematical binary we can look at with stocks the way we can with bonds.

Research from Avantis identifies that the U.S. stock market has performed better in periods where rates have fallen by more than 1% compared to other interest rate environments.

Average Monthly Return for the U.S. Stock Market

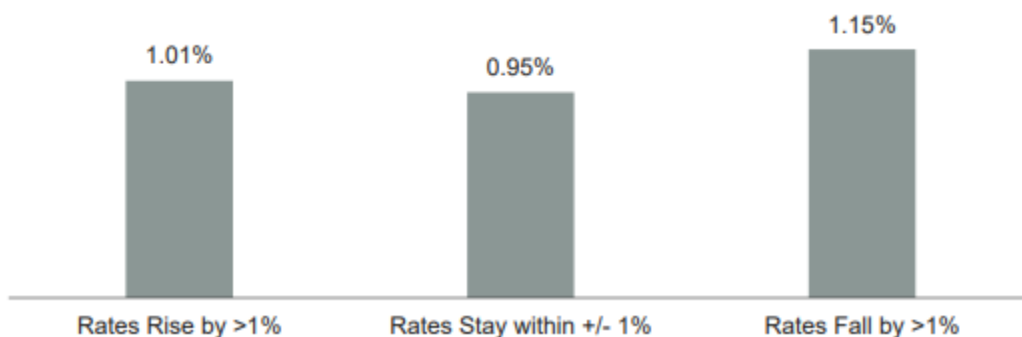


Chart source: Avantis Investors. Data from 1973 - 2024. U.S. stocks the Market Portfolio from Ken French's Data Library. The total rolling one-year periods in the analysis are 613. Total rolling 1-year periods when rates rise by >1% are 93, periods when rates fall by >1% are 93, and periods when rates stay within +/- 1% are 410.

Now, how much interest rates may fall and how quickly that decline occurs is basically a game of guesswork. In these very market commentaries from a couple years ago we highlighted the folly of predicting interest rate moves. Market expectation, and even guidance from the Federal Reserve itself, is often unreliable in charting the path of rates. The trajectory we are on today is based upon the Federal Reserve's expectations for the economy, inflation, and unemployment. If any of those factors differ from what the Fed forecasts them to be, interest rate forecasts may adjust, as well.

The Federal Reserve operates on a "dual mandate" to target maximum employment and price stability (low inflation). While official backward-looking numbers today are at reasonable levels on both metrics, forward-looking estimates project increases in both inflation and unemployment. Historically, lower interest rates have helped the American economy in periods of high unemployment. But, there is concern that falling rates could

yield way to rising inflation. As these indicators shift, the Fed can always change its plan for future interest rate moves.

New Features for Clients

Over the summer, our team dedicated time to evaluating new portfolio management platforms to enhance our ability to serve our clients' investment needs. After extensive research and testing, we will start to roll out our new system in the coming months. What this means for you, as a client, is two fold:

- 1) Your quarterly reports will look a little different in the new year. Our goal is to keep all of the relevant information you have come to expect from our quarterly reports. But, things may be laid out a bit differently.
- 2) We will have a new, proper client portal that we will use to transmit and store documents electronically. This Autumn, please look out for communication from our team to establish a login when we are ready to go live with the platform.

SEC Disclosures

We have made adjustments to the way we are compensated for clients who work with us for limited-engagement, hourly financial planning. As a result, we are required to furnish our revised Form ADV Part 3 to all existing clients of FJWM. Please find included with your quarterly report this disclosure. If you are an on-going investment management client, this does not have any effect on you, the services we provide, or the fees you pay.

If you have any questions about this information or anything else discussed in this quarterly commentary, please don't hesitate to reach out to Derek or Jon and we will be happy to talk through anything you have questions about.

Past performance is no guarantee of future results.

This newsletter contains general information that may not be suitable for everyone. The information contained herein should not be construed as personalized investment advice. Past performance is no guarantee of future results. There is no guarantee that the views and opinions expressed in this newsletter will come to pass. Investing in the stock market involves gains and losses and may not be suitable for all investors. Information presented herein is subject to change without notice and should not be considered as a solicitation to buy or sell any security. Investment advisory services offered through Ferguson-Johnson Wealth Management, a registered investment adviser.