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Doll's Deliberations®

Weekly Investment Commentary

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Summary

Stocks were mixed last week (S&P 500 0.37%). August non-farm payrolls delivered another weak print with unemployment edging higher. The report caused a big rally in Treasurys as Fed cut expectations increased. Best sectors were communication services (5.08%) and consumer discretionary (1.68%); worst sectors were energy (-3.48%), financials (-1.67%), and utilities (-1.01%).

Equity markets (Index total return %)	Last week	Year-to-date
DJIA	-0.26	8.03
S&P 500	0.37	11.20
NASDAQ	1.16	12.89
Russell 1000	0.66	11.49
Russell 1000 Growth	0.83	12.25
Russell 1000 Value	0.01	10.02
Russell 2000	0.57	7.67

S&P equity sectors (Index total return %)	Last week	Year-to-date
Communication services	5.08	23.89
Consumer discretionary	1.68	3.73
Consumer staples	0.43	6.00
Energy	-3.48	3.75
Financials	-1.67	10.71
Heathcare	0.36	1.17
Industrials	-0.71	15.30
Information technology	0.20	14.27
Materials	-0.22	11.39
Real estate	-0.30	5.35
Utilities	-1.01	11.85

Key takeaways

1. The August jobs report came in at +22,000 vs. +75,000 consensus estimates. This sets up a dovish September FOMC, but sticky inflation makes it premature to commit to a series of rate cuts.
2. August ISM Manufacturing was mixed, with stronger orders offset by weak production and employment.
3. Income and spending data confirm resilient consumption and sticky inflation; however, slowing labor momentum makes us cautious.
4. Because immigration has slowed very significantly, a slowdown in job growth may not cause a rise in the unemployment rate.
5. A U.S. appeals court ruled that most of President Trump's tariffs are illegal. The court allowed the tariffs to remain in place through Oct. 14, giving the Trump administration a chance to file an appeal with the U.S. Supreme Court.
6. Consensus inflation forecasts are roughly 0.3% per month (which of course annualizes at around 3.5%), up from many months of 0.2% per month (which of course annualizes at around 2.5%).
7. The S&P 500 is selling at a forward P/E ratio of 22.4 times, 1.6 standard deviations above its 30-year average and almost its highest since the tech bubble.
8. Looking at the earnings growth rates for the Magnificent 7 and the remaining 493, they show the second quarter of 2026 is expected to be an inflection point when the 493 begin to grow faster than the Magnificent 7.
9. Notably, upward earnings revisions in small cap space have accelerated in recent months.
10. Congress returned to D.C. facing a staggering agenda, which includes a potential government shutdown (the odds of a government shutdown have risen above 50% in Poly-Markets), a legal fight over tariffs, a controversy with the Fed, and several simmering foreign crises.

Earnings are supportive, but rich valuations limit potential

Investors are in an exuberant mood (aside from some occasional indigestion), with the S&P 500 up markedly since early April on the back of a sharp rebound in Mag 7 stocks from this year's lows, the AI theme, plentiful global liquidity and expansionary G7 fiscal policy. The current macro backdrop for risk assets is favorable, with the global economy proving resilient, the Fed biased to ease, and corporate profits expected to keep rising. U.S. economic growth and hiring have downshifted from a rapid pace, but there is no catalyst for a recession on the horizon.

At the same time, a lot of good news is already discounted. The U.S. equity market trades at an expensive 12-month forward P/E ratio of 23, when profit margins are already historically high, corporate credit spreads are very tight, and markets are discounting 150+ basis points (bps) of Fed rate cuts in the next year. Meanwhile, President Trump is pushing for the Fed to cut interest rates by 300 bps, despite sticky core inflation, a U.S. economy still operating well above estimated potential, and elevated asset prices. Pouring any more gasoline on the fire adds to the upside risks for inflation even as the flow-through from the tariffs into consumer prices is set to increase. Were Trump to get his way, inflation pressures could intensify markedly.

As we have stated in many weekly Doll's Deliberations, the current risk-on environment will last until the bond market revolts or the global economic expansion falters. While G7 10-year government bond yields are well-behaved, 30-year yields are at or near multi-decade highs and represent a warning sign that bond market vigilantes are awakening.

International equity markets (Index total return %)	**Last week**	**Year-to-date**
MSCI ACWI	0.29	14.63
MSCI ACWI EX U.S.	-0.36	21.20
MSCI EAFE	-0.78	21.83
MSCI EM	0.27	19.34

Fixed income markets (Index total return %)	**Last week**	**Year-to-date**
Bloomberg U.S. Aggregate Bond	0.45	5.46
Bloomberg U.S. Corp High Yield	0.10	6.46
Bloomberg U.S. Gov/Credit	0.44	5.27
Bloomberg U.S. T-Bill 1-3 Month	0.04	2.93

Alternatives (Index total return %)	**Last week**	**Year-to-date**
Real estate (FTSE NAREIT)	-0.82	3.53
Commodities (DJ)	-0.27	6.78
Global listed private equity (Red Rocks)	-1.35	8.68
Currencies (DB Currency Future Harvest)	0.52	0.24

Global economic expansion and supportive monetary and fiscal policies point to the outperformance of stocks versus bonds on a six- to 12-month horizon. However, U.S. policy uncertainty remains elevated and stretched equity valuations imply a less pro-growth portfolio tilt than macro fundamentals suggest. The technical backdrop also remains favorable.

The Fed is set to resume easing, which historically has only occurred during meaningful growth slowdowns, looming recessions or crises, and should help underpin the underlying global earnings uptrend. Investor sentiment is also positive, although indicating increasing complacency. U.S. Treasury implied volatility has declined sharply in recent months and is at the lowest level since before the Fed began its hiking cycle in 2022, with markets surprisingly confident about the outlook for inflation and Fed policy. The VIX index of U.S. equity volatility is well below its long-term average and consistent with little investor concern about the earnings outlook. Both the forward P/E ratio and credit spreads reflect highly optimistic investor sentiment and are a significant offset to the positive macro climate and thus a reason to temper a pro-growth appetite.

Conclusion

We expect stocks to remain positive (albeit bumpy), but the risk-reward is less favorable than the supportive macro and policy outlook suggest. Stocks are expensive and bond yields could move higher given sticky inflation.

Source: Bloomberg as of Sept. 5, 2025