

Doll's Deliberations®

Weekly Investment Commentary



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Summary

Stocks rose again last week (S&P 500 +1.60%). All major averages were higher, but breadth was significantly negative as the equal-weighted S&P 500 underperformed the cap-weighted index by 130 basis points (bps). All eyes are on the Fed with an expectation of a 25-bp cut at this week's meeting. Outperforming sectors were technology (+3.09%) and utilities (+2.44%); laggards were consumer staples (-0.15%), materials (+0.03%), and healthcare (+0.16%).

Key takeaways

1. Core CPI inflation rose 0.35% in August, and over the last three months, core CPI rose 3.65%, the fastest three-month pace since January.
2. Initial jobless claims came in much firmer than estimates, rising to 263,000. The four-week moving average rose to 240,500, the highest since the end of June.
3. While a lot will depend on the data, we think we are set up for a Fed cut of 25 bps this week, and a similar cut in December.
4. Labor-market disappointments have provided a window for Fed rate cuts. Momentum could push yields a bit lower in the near run, but the bond market is now priced for a persistently dovish Fed and limited inflation risks.
5. With more accommodative monetary policy in the quarters ahead and the likelihood of a lesser deflationary impulse from energy in 2026, the path of least resistance seems higher for inflation next year.
6. By any measure, the markets are celebrating, with stocks hitting records and corporate credit spreads at quarter-century lows, plus many signs of speculative fervor. Those include margin debt topping \$1 trillion for the first time, the revival of initial public offerings (most of which have experienced big opening-day price pops), record options activity, and even the revival of special purpose acquisition companies, or SPACs. Those are hardly circumstances suggesting the need for easier money.
7. Shares surged over 30% on Wednesday after Oracle reported that multi-cloud database revenue from Amazon, Google, and Microsoft grew at the rate of 1,529% in its last quarter. The AI trade is alive and well.
8. Despite the large beat to Q225 EPS due to the easing of tariffs throughout the quarter, and consensus slashing estimates rather quickly around so-called liberation day, Q3 estimates have seen very little upward movement.
9. The top 100 companies generate nearly 20% free cash-flow margins, more than twice that of their smaller counterparts.
10. The U.S. budget deficit fell in August, marking the fifth time in the past six months that the deficit came in lower compared to the same month one year ago. Tariff revenue made the difference for the deficit to go down.

Equity markets (Index total return %)	Last week	Year-to-date
DJIA	0.97	9.07
S&P 500	1.60	12.98
NASDAQ	2.05	15.20
Russell 1000	1.65	13.07
Russell 1000 Growth	2.48	15.03
Russell 1000 Value	0.51	10.58
Russell 2000	1.29	9.60

S&P equity sectors (Index total return %)	Last week	Year-to-date
Communication services	0.87	24.97
Consumer discretionary	1.29	5.07
Consumer staples	-0.15	5.84
Energy	1.58	5.39
Financials	1.34	12.19
Healthcare	0.16	1.34
Industrials	0.45	15.81
Information technology	3.10	17.81
Materials	0.03	11.43
Real estate	0.39	5.76
Utilities	2.44	14.58

The Fed's focus on the labor market (at the expense of inflation) paves the way for a cut

The U.S. economy is drifting toward a slow growth, sticky inflation environment. Growth has cooled from the past two year's strong pace, and employment growth in particular has markedly slowed. Yet underlying inflation has proven sticky this year and, if anything, has slightly firmed recently. Some of the U.S. economic downshifting and price pressures (primarily goods prices) are related to higher tariffs, but the backdrop was already headed toward a whiff of stagflation even if tariffs had been left unchanged. The dearth of economic slack and deceleration in new hiring (mostly reflecting the sharp drop in immigration) were already in process before the tariff war.

The good news for the economic outlook is that the U.S. and global corporate profit cycle is still intact, and developed-market central banks are dovishly biased (even though the ECB looks to have completed its easing phase). The 10-year yields remain in a trading range, as inflation complacency is very much intact. Higher corporate earnings and a benign bond market backdrop equals risk-on, and indeed, equity and credit markets continue to grind higher.

The main cyclical risk is the likelihood that inflation will not follow the bond market's expectations of drifting back to 2%. The inflation backdrop is far from the brutal levels of the 1970s, but it is notable that inflation rates are still holding above the levels of the 2010s. Any improvement in economic growth will likely sustain the mildly inflationary environment. This plus the historically worrisome fiscal policies (including high and still rising debt/GDP levels), will eventually push up bond yields and trigger some de-rating in risk asset market valuations, many of which are already stretched.

Economic pessimism has noticeably increased, albeit not due to final demand growth, but rather because of weaker employment growth. Although new hiring has slowed considerably from recent years, it has coincided with the increase in tariffs and related uncertainty. Recessionary conditions do not exist, and the labor market is expected to remain tight. The low hiring/low firing environment reflect both solid profit levels (therefore, low firing) yet decreased confidence in the future (therefore, low hiring), courtesy of increased policy uncertainty (especially regarding tariffs and trade).

The Fed is keen to lower the policy rate and will act on its dovishness this week. Lower policy rates will not stimulate greater hiring per se, rather it will take clarity on the source of what has caused businesses to sit on their hands in order for employment growth to firm. Here we only envision modest improvement ahead, given the sharp drop in immigrant employment. One silver lining from this year's economic/employment bump likely will be that the U.S. administration will likely not again pursue potentially economic-damaging policy initiatives, such as occurred in the first half of this year.

In the end, as go corporate profits, so goes the economic cycle. Here the picture remains fairly upbeat, although investor expectations appear too optimistic.

Conclusion

The Fed is set to resume lowering its policy rate this week even though U.S. inflation has stalled well above the Fed's target and has firmed slightly in recent months. U.S. monetary and fiscal stimulus will persist. This, plus the ongoing rise in U.S. and global corporate earnings, bode well for further risk-asset price inflation, at least for now, and despite valuation concerns.

Source: Bloomberg as of Sept. 12, 2025

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International equity markets (Index total return %)	Last week	Year-to-date
MSCI ACWI	1.66	16.74
MSCI ACWI EX U.S.	1.61	24.41
MSCI EAFE	1.13	24.50
MSCI EM	2.73	24.01

Fixed income markets (Index total return %)	Last week	Year-to-date
Bloomberg U.S. Aggregate Bond	0.55	6.54
Bloomberg U.S. Corp High Yield	0.30	7.02
Bloomberg U.S. Gov/Credit	0.54	6.35
Bloomberg U.S. T-Bill 1-3 Month	0.05	3.03

Alternatives (Index total return %)	Last week	Year-to-date
Real estate (FTSE NAREIT)	0.69	5.28
Commodities (DJ)	1.41	8.29
Global listed private equity (Red Rocks)	2.53	11.57
Currencies (DB Currency Future Harvest)	0.77	0.63