

January 2026

*“Kindness is costless but also priceless”*

Warren Buffet

## Market Recap – Double-Digit Gains in 2025

2025 was a tumultuous year but ended up delivering strong gains in common stocks and solid returns on fixed income securities. Most equity market indices delivered double-digit returns to investors who preserved through the “Liberation Day” pullback in the Spring. Not only did the S&P 500 Index rise for the third year in a row, it was refreshing to see the international indices (finally!) reward patient investors as the primary indices for International Developed and Emerging Market stocks both returned over 30%.

Fixed Income investments delivered positive results also, with the Bloomberg Aggregate Bond Index rising over 7% and the Bloomberg Municipal Index up over 4%.

Asset Class	Benchmark	4th Quarter	2025
U.S. Large Cap Stocks	Benchmark 1: S&P 500 TR USD	2.7	17.9
U.S. Small & Micro Cap	Benchmark 2: Russell 2000 TR USD	2.2	12.8
International Developed Stocks	MSCI EAFE NR USD	4.9	31.2
Emerging Market Stocks	MSCI EM NR USD	4.7	33.6
Global Stocks	MSCI ACWI NR USD	3.3	22.3
U.S. Municipal Bonds	Bloomberg Municipal TR USD	1.6	4.2
U.S. Taxable Bonds	Bloomberg US Agg Bond TR USD	1.1	7.3
U.S. High Yield Bonds	Bloomberg US Corporate High Yield TR USD	1.3	8.6
International Developed Bonds	S&P International Sov Ex-US Bond TR USD	-1.6	8.3
U.S. REITs	MSCI US REIT NR USD	-2.0	1.7
Broad Commodity Futures	Bloomberg Commodity TR USD	5.8	15.8
Energy Partnerships	Alerian MLP TR USD	3.8	9.8
Gold	DJ Cmmddy Gold TR USD	12.2	62.5

## 2025 – Quite A Year

The year opened with change in the wind with then President-elect Trump poised to return to the White House with many campaign promises that he looked to fulfill. This left businesses and markets to figure out how the looming policy initiatives would alter the outlook for investments, growth, and inflation. Likewise, the Federal Reserve would need to navigate what the eventual set of policies passed by Congress and by executive order would mean for growth and inflation.

Investors, business leaders, and households spent the early part of the year digesting the scope and velocity of President Trump’s efforts to pressure U.S. trading partners into meeting the administration’s demands on

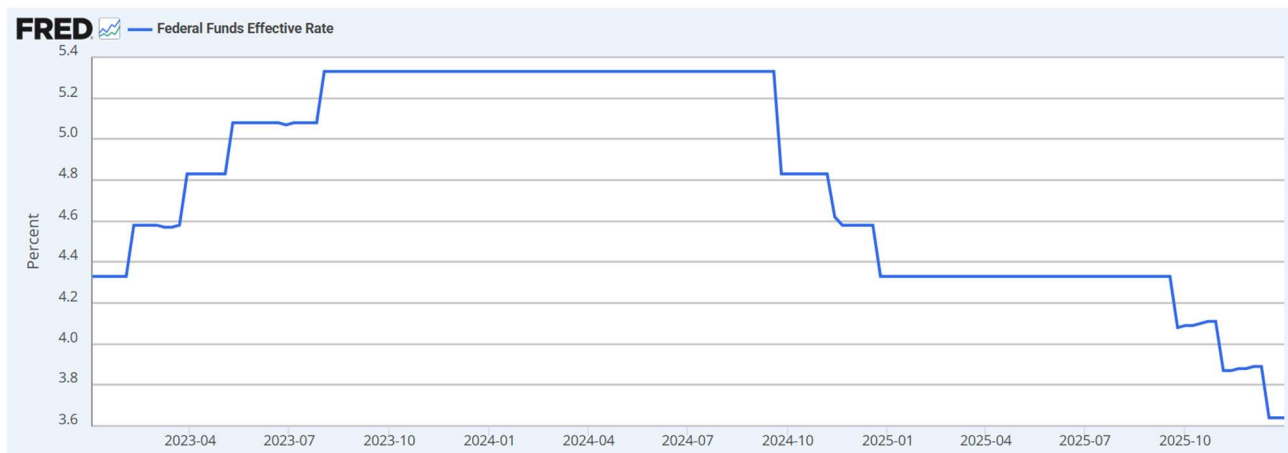
trade, national security issues, and immigration, shrinking the size of the federal government, and reorienting the trade norms of the global economy. The S&P 500 hit correction territory (a drop of at least -10% from previous high) in March as mounting concerns about the outlook for the economy, punctuated by threatening tariff headlines, led to an erosion of business, consumer and investor confidence.

The growing policy fears peaked in early April following President Trump stunning the markets by unveiling a suite of significantly higher tariffs on April 2 which amounted to a “worst case scenario” relative to expectations, causing recession fears to mount. From the record high on February 19, the S&P 500 declined more than -20% on an intraday basis to the low on April 8. Common stock prices skyrocketed on April 9, however, when President Trump dramatically reversed course by significantly walking back the aggressive tariffs and signaling a willingness to negotiate on trade.

A further de-escalation of trade tensions, the passage of the sprawling tax and spending bill in early July, combined with the Federal Reserve restarting rate cuts in September and very strong earnings growth in 2Q and 3Q 2025, sent stock prices to a series of all-time highs over the back half of the year. The S&P 500 hit a peak on December 24, representing a 17.9% gain on the year and a 39.1% advance off the reciprocal tariff low on April 8.

### **The Federal Reserve – A December Cut, Now Likely On Hold**

After discouraging hopes for a December rate cut at the October FOMC meeting, the Federal Reserve lowered the target range for the federal funds rate to 3.50% to 3.75% at the December 9-10 FOMC meeting despite having little fresh economic data to guide the decision due to the government shutdown. The Federal Reserve has now cut the federal funds rate 75 basis points over the past four months and by 175 basis points over the last 16 months.



Source: Board of Governors of the Federal Reserve System.

The third rate cut of the year was far from an easy decision, with Chair Powell saying the decision to lower rates was a “close call.” The twelve-person rate setting Committee delivered nine “yes” votes, two “no” votes from regional Federal Reserve Bank presidents, and recent President Trump appointee, Stephen Miran, again wanting a 50 basis point rate cut.

In addition to the two “no” votes on the rate cut, four other nonvoting meeting participants indicated that they did not support the decision to lower rates. The caution about additional rate cuts was evident in the rate projections, updated on a quarterly basis, which showed officials penciling in just one rate cut in 2026 and another in 2027.

Chair Powell emphasized again that there is no risk-free path for monetary policy currently as the central bank navigates the tensions between its employment and inflation mandates. Chair Powell justified the three

rate cuts since September as insurance against a weakening labor market, a position he first signaled in his Jackson Hole speech in August. Mr. Powell and several Committee members are clearly worried about the jobs market as the Federal Reserve research staff believes the payroll data could be overstating job creation by up to 60,000 jobs a month since April, implying monthly job losses of 20,000 rather than the moderate monthly job gains of 40,000 that have been reported.

The biggest surprise from the meeting was the announcement that the central bank will start buying Treasury securities again, \$40 billion of Treasury bills in December and likely similar amounts each month until at least April when income tax payments are due. Mr. Powell said the T-bill purchases are intended to maintain ample reserves in the banking system.

We view the dissents at the FOMC meeting as a reflection of a very uncertain outlook leading to healthy debate. The tariff policies of the Trump Administration have brought about a complicated outlook of tariff-related pricing pressures and softness in the labor market, which are impossible for the Federal Reserve to address simultaneously.

Given the lack of consensus on the FOMC Committee and the arrival of a new chair of the Federal Reserve in May, it is likely the Federal Reserve will remain on hold in early 2026 as Committee members weigh incoming data. We think it will take additional weak data on the labor market to spur the Committee to lower rates before the June 16-17 FOMC meeting with the newly appointed chair.

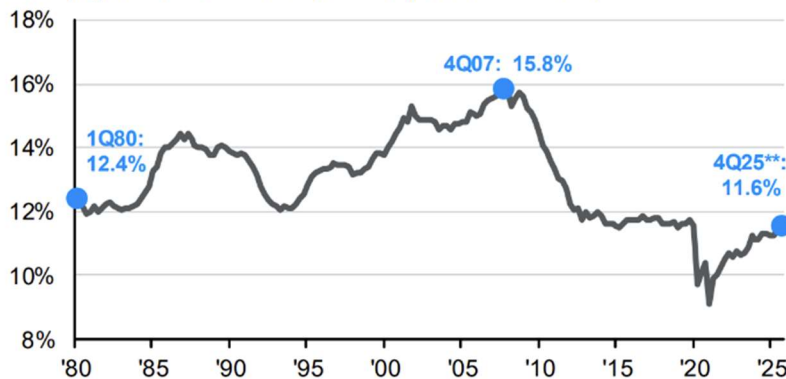
The market is expecting short-term interest rates to fall to just over 3.0% next year, which would be consistent with inflation falling toward 2.0% with a real, or inflation-adjusted, short-term interest rate at roughly 1.0%. The current rate expectations in the market are quite a ways away from President Trump’s recent comments that short-term interest rates should be near 1.0%, however.

## The Consumer – Doing Alright

Real GDP grew at a strong 4.3% annual rate in 3Q 2025 after growing at a 1.6% rate during the first half of the year and is higher by 2.3% year-over-year. The report, which was delayed nearly two months, showed that consumers continue to drive the economy, growing at a 3.5% pace, despite job gains which have been modest since April and weak consumer sentiment readings reflecting the high cost of necessities, along with everything from cars and homeownership to college tuition. Overall consumer spending remains solid and the household debt service ratio is within historical norms. AI-related spending also contributed to the strong quarter with both business capital spending on equipment and on intellectual property growing at 5.4% rates.

### Household debt service ratio

Debt payments as % of disposable personal income, SA



Source: J.P. Morgan Asset Management

Consumer spending is increasingly being driven by upper income households benefiting from large gains in asset values. Indications that low- and moderate-income households continue to struggle were evident in real, after-tax income being unchanged in 3Q 2025, with many households needing to dip into savings to maintain spending levels. Core consumer prices were higher by 2.9% on a year-over-year basis compared to a 2.6% reading in 2Q 2025. The combination of healthy growth and a little higher core inflation lowered the likelihood of a January rate cut even further to 13% compared to 20% prior to the release of the data. The key read-through from the third quarter data is that

the combination of strong growth in real GDP and a modest gain of only 154,000 jobs during the quarter points to a solid gain in productivity, which boosts profitability and leads to higher standards of living over time.

## Looking Ahead

Common stocks have been in a bull market since October 2022 following the reset in the market forced by the Federal Reserve tightening monetary policy and a significant rise in Treasury yields. The current bull market started with the typical price-to-earnings multiple expansion as stock prices almost always bottom before earnings. However, since mid-2024 earnings growth has taken over as the dominant driver of stock returns, which in our view is absolutely necessary for the bull market to continue.

Our expectation for higher stock prices in 2026 is largely based on our outlook for the economy's growth rate to accelerate this year on the continued AI buildout, the business capital spending incentives contained in the tax and spending bill signed into law last summer, along with larger than normal tax refunds from the tax cuts which were retroactive to the beginning of 2025.

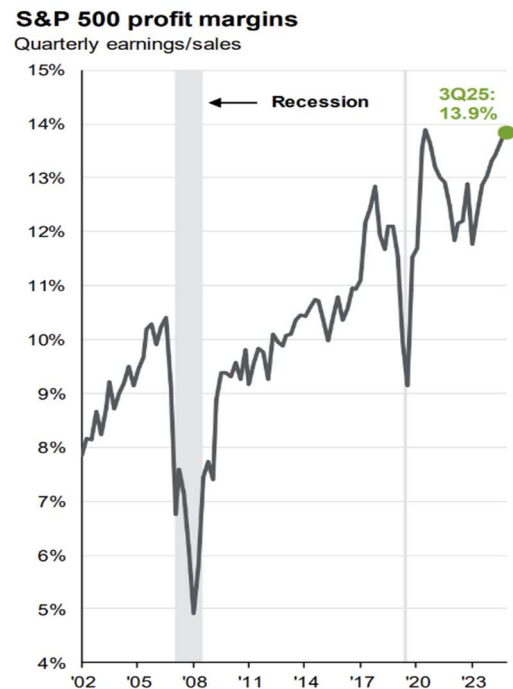
Add in an accommodative central bank, lower Treasury yields, generally healthy credit conditions, and a fading of policy uncertainty and a faster pace of economic activity should lead to a second consecutive year of above trend earnings growth. Supporting this perspective, the analysts at Standard and Poor's are looking for a roughly 17% gain in operating earnings over the four quarters of 2026, following a gain close to 13% for 2025.

The way we see it, the bull market in common stocks remains intact and appears poised to continue this year propelled by strong earnings momentum and a much better sentiment backdrop following the cleansing of some excessive optimism over the past couple months. We view the cautious sentiment regarding the somewhat open ended nature of the AI capital expenditure boom as a pretty clear indication that the stock market is not in bubble territory and still has room to run on the back of strong earnings growth driven by technology-led productivity gains and expanding profit margins.

Bubbles in stock prices that ultimately get burst in a serious bear market are not formed when investors question what companies are doing with their capital expenditures and critically analyze the expected return on those investments. We view the recent easing of monetary policy, with a little more likely to come this year, and core inflation trending toward the Federal Reserve's 2% target on the back of lower oil prices and moderating shelter costs and wage pressures as positives for common stocks.

While maintaining a positive outlook for common stocks this year, we expect a move higher in stock prices to be accompanied by a fairly healthy rise in volatility, particularly during the first half of the year. Consider that the deal which ended the government shutdown last year provided funding for most federal agencies only through January 30, 2026. Our Congressional leaders have not yet advanced spending proposals to provide funding beyond that date.

We think the lengthy list of positives for the economy and earnings will eventually carry the day this year, but we anticipate a bumpy ride higher for common stocks.



Source: J.P. Morgan Asset Management

## Happy New Year!

As we begin a new year, we want to say “Thank You” to our clients. We appreciate you, and the whole PCM Team is here for you – the Advisors, the Financial Planners, the operations and client service professionals. Please call us anytime. Finally, we thought you might enjoy a team photo (missing only Senior Client Service Associate Heather Johnson, Chief Compliance Officer Kara Marsh, and our newest addition, Senior Advisor Jason Romero!)



*Sincerely,*

*The Private Capital Management Team*

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