Huff Wealth Management

Despite concerns over tariffs and firm inflation reports, the stock market hit record highs during the quarter. Strong economic growth (+3.9%), solid corporate earnings, and hopes of interest rate cuts were the key drivers. Though Tech/AI related sectors dominated the headlines, Small Cap stocks actually outpaced Large Cap stocks, a performance typically only seen when coming out of a recession - indicating a broadening participation of the rally. Another surprise was a shift in drivers of economic growth. For the first time ever, Capital Expenditures, particularly for AI Infrastructure, outpaced the growth of Consumer Spending. This change will have lasting implications on the course and design of the future economy. Meanwhile, the Bond market also saw gains as the Federal Reserve cut short term rates by 25 bps, citing weakness in the labor market. Separately, Foreign markets continued to perform very well this year as they have benefited from more accommodating monetary policies and a weaker US dollar. In sum, investor confidence remains quite high, fueled by aggressive AI spending and falling interest rates.

Index Returns:	QTD	YTD		QTD	YTD		QTD	YTD
S&P 500 (SPY)	8.15%	14.66%	U.S. Growth (SCHG)	10.44%	14.84%	U.S. Short Bond (BSV)	1.38%	4.74%
S&P 500 Equal Weight (RSP)	3.62%	9.68%	U.S. Value (SCHV)	4.68%	13.43%	Intermediate Aggregate Bond (AGG)	2.15%	6.19%
Foreign Developed (MAIIX)	4.96%	26.16%	Small Blend (IWM)	11.30%	10.36%	High Yield Bond (HYG)	2.27%	7.28%

Market Outlook: Unstoppable freight train. The pace of change in AI and its adaptation in business continues to accelerate, transforming almost every facet of the US and global economy. The positive side is that it is providing a new engine of growth, prompting new innovations, greater efficiencies and productivity. The potential negative is that it has also increased the risks taken by both businesses and investors. Large tech companies, startups and related industries are unabashedly issuing massive amounts of debt (in the billions) to support the insatiable demand for data centers and power sources. If there is any falter in their ability to pay, it could have huge negative implications in the Bond market and ripple into the entire economy. At the same time, investors are increasingly becoming more speculative, as seen by very elevated stock valuations, and new highs in Gold and Crypto currencies. <u>It could be argued the markets are perhaps in the beginning stages of a bubble but no one is willing to 'miss riding the train'</u>. While many parts of the economy are benefiting from AI, other parts are stalling, in particular the labor market. AI will likely replace many jobs, and if so, what will be the condition of the consumer to support the economy? This is the conundrum the Fed is facing and it will become an increasing factor as AI becomes more embedded in the economy.