

**The Novelli Group
At Morgan Stanley
Private Wealth Management**

October 2025 Perspectives

What Inning is it?

As fall settles over Houston, we welcome milder temperatures and longer evenings, with the clock change on November 2nd reminding us that the holidays are just ahead. Late-October also means post-season baseball - the 2025 World Series kicks off this weekend, with the 2024 champion LA Dodgers defending their title against the resurgent Toronto Blue Jays, in what promises to be an electric matchup.



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It's a fitting backdrop for reflection: Much like baseball, markets have their cycles. After a three-years of outstanding returns, a key question is what stage we're in for the current bull market. The US stock market has been in a bull phase since its October 2022 low, marking three years of upward momentum as of this month. Using the baseball analogy, it feels like we could be entering the late innings—perhaps the seventh or eighth—of this economic expansion and market rally, as the post-pandemic recovery shows signs of maturation.

Some indicators suggest we could be in the later stages of the cycle, though not yet at the point of imminent reversal. The bull market's duration aligns with historical patterns where rallies often extend beyond three years, but momentum can wane as excesses build. Sentiment is a key gauge: The AAI Investor Sentiment Survey shows bullish readings at 33.7% as of mid-October, down from recent highs around 46%, with bearish sentiment rising to 46.1%¹—levels that are elevated but not at euphoric extremes that typically signal a top. Similarly, Bank of America's October Global Fund Manager Survey indicates that 60% of investors view stocks as overvalued, reflecting caution rather than overconfidence². This tempered optimism suggests the rally could persist for another year or more, provided sentiment doesn't fully overheat and trigger a pullback. Markets often climb a wall of worry, and we're not yet seeing the widespread exuberance that marked peaks like 2000 or 2021.

That said, the macro backdrop offers reasons for continued optimism, including monetary and fiscal policy tailwinds. Last month the Federal Reserve resumed monetary policy easing, cutting the Fed Funds rate by 0.25%, with two additional 0.25% cuts projected before year-end and more into 2026³. Easing cycles have historically supported stock performance and lower rates could bolster economic growth amid stable inflation. On the fiscal side, ongoing deficits and stimulus measures provide support, amplified by the One Big Beautiful Bill Act (OBBBA), signed into law in July, which introduces tax deductions for tips, overtime pay, and car loans, increases the small business deduction to 23%, makes the adoption tax credit partially refundable, and revives 100% bonus depreciation⁴—measures expected to boost consumer spending and entrepreneurial activity next year.

However, investors should remain cognizant of risks: S&P 500 valuations feel stretched, with the forward 12-month P/E ratio at 22.4, well above the 5-year average of 19.9 and signaling limited margin for error⁵. The ongoing government shutdown, now in its 21st day since October 1, adds uncertainty, disrupting services and potentially weighing on confidence if prolonged. Additionally, job market growth is slowing, with only 50,000 jobs added in September⁵—below expectations and a deceleration from prior months—raising questions about labor market resilience. The absence of current data from the sidelined Bureau of Labor Statistics increases the risk of data surprises.

Corporate Earnings provide a solid but moderated foundation. FactSet data projects S&P 500 earnings growth of 7.5% for Q4 2025, with revenue up 6.4%, building on a full-year 2025 estimate of around 9% earnings expansion⁷. Into 2026, expectations accelerate, with Q1 growth at 11.9% and Q2 at 12.8%, driven by sectors like technology and financials amid lower rates and potential productivity gains. However, this outlook assumes no major disruptions; if economic softening persists or trade tensions re-escalate, revisions could trend lower. Earnings have been a key driver of the bull market, and their trajectory will be crucial in determining whether the rally can extend.

Notably, Mike Wilson, Morgan Stanley's Chief Investment Officer, has been making an out-of-consensus case for a new bull market starting in April 2025⁸. His research posits a 3-year rolling recession began in 2022, when the Fed began to hike rates aggressively to reign in the post-pandemic inflation, and bottomed in April 2025. During this period, most individual sectors of the economy experienced recession at different times. The April 2025 Liberation Day tariff announcements were the negative surprise that sparked a final capitulation. In this new cycle, the Fed may allow inflation to run above target, which is supportive of corporate earnings growth. Therefore, quality stocks could be a cheaper inflation hedge, especially vs. precious metals which have already made a big run. Mike cautions that a significant correction is possible in the near term, which would be normal for this stage of the cycle and present a buying opportunity. Potential catalysts could be escalating US/China trade tensions, funding markets stress, and negative earnings revisions breadth. In other words, despite a possible near-term correction, Mike's research suggests it's *early* innings.

Is that plausible? Perhaps, but other risks warrant monitoring, such as those emerging in the private credit market. With the sector ballooning to \$1.5 - \$3T globally⁹, concerns include potential defaults among highly indebted companies, especially if interest rates don't fall as expected or economic slowdowns intensify. Indirect bank exposures, opacity in lending practices, and vulnerabilities from private equity ties could amplify stresses, though lower rates may mitigate some pressures in the near term. Geopolitical uncertainties and policy shifts add to the watch list, underscoring the need for vigilance.

In our view, the environment calls for prudence. Positioning should emphasize liquidity for coming expenses and diversification across asset classes, sectors, and geographies to mitigate high valuations and macro risks. We continue to favor tilting portfolios toward quality business with strong balance sheets, value stocks, investment grade fixed income for income stability, and alternative investments, when suitable, such as real assets and hedged strategies. But it's not time to head for the exits just yet – this year's regime change may set the stage for extra innings.

Fall reminds us that change is inevitable, but with thoughtful strategy, we can weather the seasons ahead. Whether you're rooting for the Dodgers, the Blue Jays, or just hoping, like me, that your team gets another shot next year, enjoy the series, and remember: in baseball and markets alike, patience and perspective go a long way!

Sources:

¹ The AAI Investor Sentiment Survey, 10/16/2025, www.aaii.com/sentimentsurvey

² Bank of America's October Global Fund Manager Survey, 10/13/2025

³ Reuters, 'US Fed to trim rates twice more this year; 2026 rate path very unclear', 10/21/2025

⁴ Key Tax Law Changes Under the OBBBA: A Comprehensive Overview, Jackson Walker, 8/1/2025

⁵ FactSet, Earnings Insight, 10/17/2025

⁶ KPMG, 'September payrolls likely to pick up', 8/29/2025

⁷ FactSet, Earnings Insight, 10/17/2025

⁸ Morgan Stanley, 'Time for a Bull Market Correction?', Mike Wilson, 10/20/2025

⁹ Morgan Stanley, 'Understanding Private Credit's Rapid Growth', Ashwin Krishnan, 10/3/2025

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