Morgan Stanley

WEALTH MANAGEMENT

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The recent performance of small cap stocks was much like the Cleveland Guardians incredible run during the final months of the regular season. Having lagged the broad markets for much of the year, and having periods of painful losing streaks, small caps came on with a vengeance during the third quarter, climbing into contention with the rest of the market by quarter end. The third quarter brought positive total returns of 8.1% for the S&P 500, while 10 of its 11 sectors posted gains quarter-over-quarter. Energy stocks get the Tiger award, being the only sector losing ground for the quarter. The Russell 2000 Index, the small-cap benchmark, rose 12.4%, beating out other stalwart equities including the S&P 500, Nasdaq, Dow, and EAFE index, of which all did reach new all-time highs amid strong quarterly earnings and renewed expectations for easing monetary policy. Over the same time frame, while the Bloomberg US Aggregate Index, a broad measure of the US bond market, increased by 2.0%, bringing the year-to-date return to a competitive 6.13%. The yield on the 10-year US Treasury note closed the third quarter at 4.15%, while the three-month US Treasury bill yield ended at 3.93%. Gold prices increased about 16.8%, and are now up about 47% year to date. [1]

The Federal Reserve opted to keep its policy rate unchanged at both its July and August FOMC meetings but reduced its federal funds target range by 25bps in September. The market is pricing in 100 basis points of additional cuts in the coming year, bringing the neutral rate to 2.75% to 3.00% by the end of 2026.

With the current economic backdrop, the Global Investment Committee is market-weight equities. In equities, we recommend the equal-weighted index to cap-weighted and recommend quality cash-flow stories in both growth and value universes. The GIC maintains overweight positioning in fixed income assets and recommends modestly underweight-duration positioning, as the trajectory of US debt and deficits may crimp potential declines in longer-term US Treasury yields.

Although the market continues to advance, breadth has improved, and technical remain strong, there are several reasons to be cautious, including complacency, high levels of margin debt, reduced retail cash, and near record high valuations based upon every metric which can be measured, including the Buffett indicator, all of which are illustrated in your quarterly report commentary.[2]

As always, please reach out to anyone on our team if you have any questions, and we wish you a wonderful fall and upcoming holiday season!

Best Regards,

Porter Vergon
Executive Director
Financial Advisor
Portfolio Management Director
Alternative Investment Director
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Sources:
[1] Morgan Stanley Q3 2025 client market commentary letter
[2] Morgan Stanley Wealthbook slides, October 2025
[3] Capital Market Indices, October 1, 2025

Please contact your Financial Advisor for a complete listing of all transactions that occurred during the last twelve months.

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