Post Oak Private Wealth Advisors

ADVISORY, CONSULTING & INVESTMENT MANAGEMENT

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Monthly Market Commentary

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Throughout October, stock investors had plenty of reasons call time on the current market rally, which had carried the S&P 500 to a record high by the end of the third quarter. The first came at midnight on October 1 with the ongoing federal government shutdown, although markets largely looked past this latest episode of partisan theatrics and continue to do so. Then there were worries about AI spending, with valuations for the big tech firms looking frothy. Talk of an "AI bubble" began to percolate.

We also got a "Liberation Day" rerun on October 10; stocks suffered their worst one-day decline since April after President Trump threatened to raise tariffs on Chinese imports to 100%. That announcement was a response to new restrictions by the Chinese government on the export of rare-earth minerals that are critical to many modern conveniences such as smartphones and electric vehicles. The flare-up in trade tensions was mostly posturing by both nations as they positioned for talks between Trump and Chinese president Xi Jinping later in the month. The market volatility was sharp, but fortunately brief as the rhetoric cooled down.

Stocks rallied over the rest of the month to return the major market indices to record territory, with stellar revenues and news of investment deals among the AI heavyweights giving investors a shot of confidence. The S&P gained 2.3% for October while optimism around the tech sector boosted the Nasdaq Composite to a 4.7% monthly return. Despite the positive results and buoyant sentiment, tech stocks remain frothy and fears of an AI bubble continue to simmer. A tricky situation for stock investors.

Is there an AI bubble?

Several clients have asked me this over the last few weeks, so I would like to take time in this month's letter to address this question. To start, it's fair to ask if AI stocks are in a bubble, given how much they have impacted stock market returns and inflated valuations over the last three years. But AI's reach extends beyond the financial sphere; some of the biggest tech companies (Alphabet, Amazon, Meta Platforms, Microsoft and Oracle) are investing heavily in the AI buildout, combining for as much as $342 billion in estimated capital expenditures this year, according to J.P. Morgan Asset Management. That's a 62% increase in capex over last year, on top of a 67% capex increase in 2024 from the year before.

This investment surge is contributing mightily to U.S. economic growth, even outpacing the contribution from consumer spending. Harvard economist Jason Furman calculated that investment in computer hardware and software was responsible for 92% of GDP growth in the first half of 2025. Taking out this investment would reduce GDP growth to an annual rate of just 0.1% for the first six month of this year.

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Also inflating this bubble is the impression that some of this investment involves deals that are circular. For example, Nvidia invested up to $100 billion in OpenAI, which in turn is buying millions of Nvidia's chips. These interconnected relationships have raised concerns about whether the AI ecosystem can sustain itself if enthusiasm wanes. But they also reflect the reality that AI requires infrastructure that few companies can afford alone.

The question really boils down to whether AI will ultimately generate enough value to justify all of this spending. The companies making the biggest capital expenditures are also very profitable, which is a key difference with the dot-com bubble of the late 1990s when a lot of firms had zero profitability. When the dot-com bubble burst in March 2000, the S&P 500 had a price/earnings ratio of nearly 30-times trailing earnings, compared to around 25-times as of the most recent month-end. Today's P/E is well above average and shows markets are pricing in significant future growth, but it's important to remember gains from innovative technologies don't happen overnight. It takes time for new technologies to achieve widespread adoption, particularly among businesses that must re-organize their operations to see benefits to their bottom lines.

AI represents a genuine technological revolution that will likely transform the economy over time. However, the path from here to there may be more volatile and take longer than current market enthusiasm may suggest. Rather than trying to predict whether this is a bubble, we encourage you to focus on maintaining a long-term view to benefit from innovation while managing risks. One way to do that is by owning some of the large, well-managed and profitable companies that are at the center of this revolution and investing in their core capabilities. Another is to own the "picks and shovels"—companies that are on the receiving end of the investment in data centers, such as industrials and utilities. Our portfolios include a variety of firms in both categories, along with a diversified mix of non-AI companies that stand to benefit from the efficiencies AI promises to deliver.

A lot to like in Q3 earnings

Eventually, stock investors set any bubble concerns aside (at least in the present moment) and focused on earnings and economic reports. There was a lot to like in third-quarter earnings; with nearly two-thirds of S&P 500 companies reporting as of October 31, earnings-per-share growth is estimated to come in at a 10.7% year-over-year rate. If that rate holds through the rest of this earnings season, it will be the fourth-straight quarter of double-digit earnings growth—impressive given the pressures companies have had to deal with in the current economic climate.

And as a counter to the AI-bubble talk, the technology sector has led the way in posting the top earnings growth for Q3. The firms contributing the most to Q3 earnings growth have all been tech giants—Alphabet, Amazon, Apple and Microsoft—although it should be noted that Meta Platforms' big earnings miss made the Facebook/Instagram parent the leading detractor to Q3 earnings growth.

Tech was the top performing S&P 500 sector for October and contributed nearly all of the index's 2.3% return for the month. But the earnings story was not all about technology; as an overall sector, financials have contributed the most to earnings growth for Q3 (although these great results didn't translate into good performance for October.) And the utilities sector, which is participating in the AI boom as data centers increase the demand for power, delivered strong earnings growth as well.

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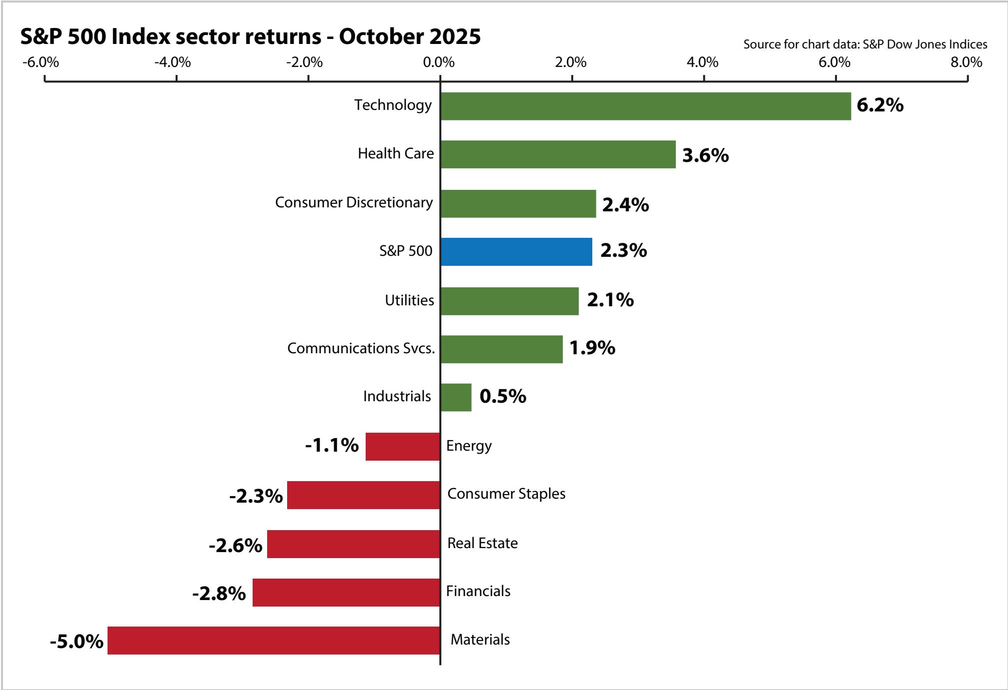

As for economic reports, there was less to like—only because the government shutdown meant fewer data releases for investors and Federal Reserve officials to consider. Even with the dearth of data, markets expected and the Fed delivered a quarter-point rate cut at its October 29 meeting. Probably the biggest hole in the economic data was nonfarm payrolls, but announcements of widespread layoffs among large employers—notably Amazon, General Motors and UPS—and anecdotal reports of hiring slowdowns continued to confirm overall weakness in the jobs market and supported the Fed's decision to continue monetary easing.

One report that did come out in October was the Consumer Price Index for September; both the headline and core rates rose to 3.0% year-over-year—well above the Fed's inflation target level—but these increases were just modestly higher than the previous month and lower than economists' expectations. Gas prices were down year-over-year and shelter costs eased a bit. Some of the biggest price gains were found in basic commodities such as coffee (up nearly 19% YoY), beef (up 14% YoY) and candy (up nearly 10% YoY as Halloween beckoned.)

While the Fed' s October rate cut was widely expected, Fed Chair Jerome Powell gave investors something to think about for future monetary easing, calling a December rate cut far from a foregone conclusion. The lack of solid data on the economy, specifically the monthly jobs numbers, is clouding the outlook for future rate cuts, with the possibility of the Fed's erring on the cautious side and holding rates steady. There also seems to be widening split among members of the Fed's rate-setting committee, with rate hawks warning against too much easing and others wanting to enact bigger cuts.

As of this writing, a quarter-point cut looks likely for December, but the picture gets murky as we look ahead to 2026. Much will depend on the resumption of official employment data, but that's dependent on Senate Republicans and Democrats making a deal to end the shutdown that

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can also get Trump's signature. No deal appears to be on the horizon, but as funding pressures mount—from paychecks for air traffic controllers, to SNAP benefits for needy families—that could be the catalyst to get lawmakers back to the negotiating table.

From a position of strength

As we head into the final two months of 2025, it's hard to not marvel at the resilience that the US economy have demonstrated this year. The ability of our best companies to drive toward innovation and be agile in the face of geopolitical turbulence, inflation uncertainty and a rapidly changing tech landscape is truly remarkable. On top of that, these firms combined have consistently delivered double-digit earnings growth over the last 12 months. That is the hallmark of capitalism.

Looking ahead, these challenges will continue to evolve in the coming months. Last month's US-China trade spat showed that the financial markets may continue to react to tariffs but will likely take any news in stride. Recent corporate bankruptcies have revealed stress in the credit markets. An extensive federal government shutdown could leave the Federal Reserve in the dark as it tries to navigate monetary policy in a tricky economic climate. As wealth advisors, we are here to monitor all of these developments for you as we seek to keep your portfolio on track for your financial goals.

Please do not hesitate to contact us if you would like to discuss your investment plan or have questions about the market outlook. As always, we thank you for your continued trust in our services.