



Traphagen Q3 2025 Newsletter

The third quarter of 2025 was a continuation of the swift recovery of almost all financial markets from the volatility of March and April. Virtually all risk/stock assets, private/alternative investments, and even bonds had a good quarter with low volatility and solid returns. We will provide an in-depth review of market performance, portfolio adjustments, private investment updates, and our outlook for the remainder of the year in this newsletter.

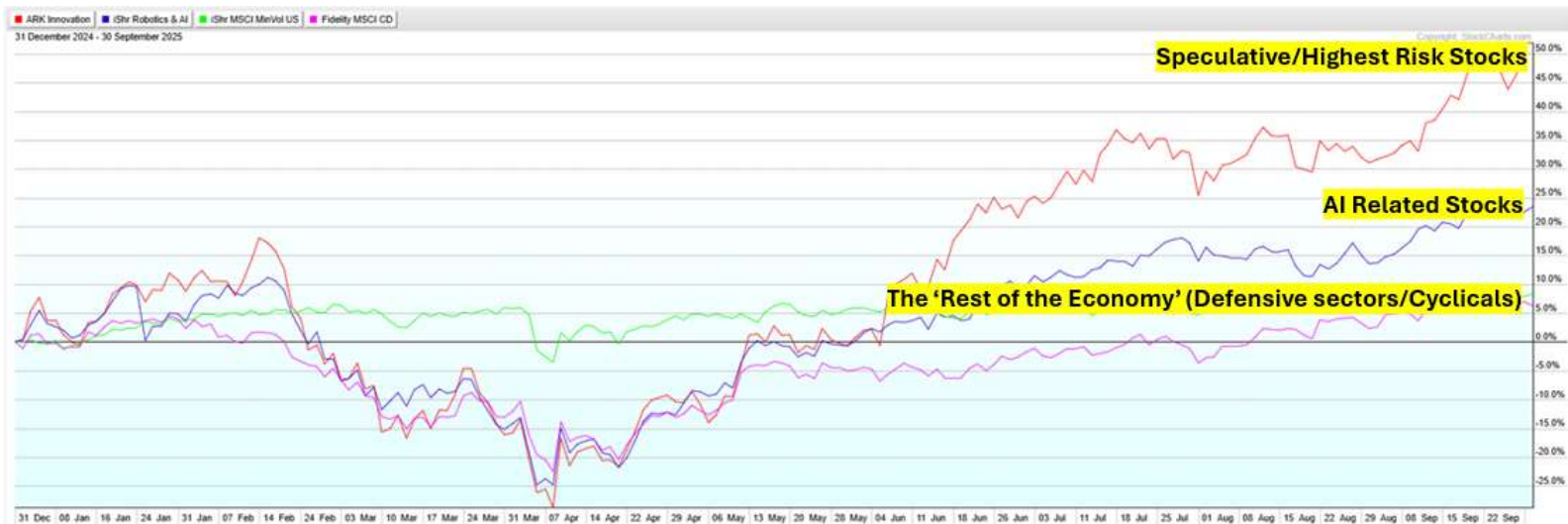
Economic & Market Update

The third quarter of 2025 continued the recovery we saw in the prior period with a steady climb for the SP500. Other assets, specifically, gold, bitcoin, and AI related stocks had more outsized moves to the upside. The **S&P 500** has now fully recovered from the April tariff announcement correction and then some...finishing up 14.8% for the first three quarters of the year and is now up more than 30% off the April 'liberation day panic' bottom. Small-cap US stocks, tracked by the **Russell 2000**, are lagging larger companies but still have had a good recovery, with a YTD return of 10.4%. International markets have worked well for the first time in many years with a declining dollar; the **MSCI EAFE** (developed foreign markets) surged 25% YTD, while **emerging markets** gained 29%. Traphagen has held little to no foreign stocks for more than 6 years. Over that time the US markets have outperformed foreign stocks by roughly 90% in absolute terms despite this year's trend reversal. We continue to be open to looking at an allocation to foreign stocks; however it remains a very high hurdle for us as the rule of law, international revenue diversification offered by US based companies, higher growth, better sector/technology/AI exposures, and superior economic dynamism/resilience all point to domestic stocks. **Our alternative/private suite (TRAPALTS)** continued playing both a stabilizing and offensive role, returning 7.5% to 8.5% through the first three quarters of the year. With this pace of nearly 10% annual net returns for our alternative suite along with almost no volatility or correlation with other markets it puts us in an enviable position to play offense and defense with the same portfolio allocation. This also has allowed us to earn stock-like returns, with the option of large reallocations when significant stock market drawdowns occur. **The US BOND Aggregate** returned 6% with mid-term rates coming down modestly during the year.

Equity Market Performance

US equity markets in Q3 have been characterized by several distinct themes/sectors. One is extremely speculative, and includes crypto-related equities, drones, nuclear, quantum, and other unprofitable technology. This area has seen extreme returns and, in our opinion, a good amount of froth. Second, we have larger and often profitable AI related companies in the energy, utility, industrial, and technology industries. This theme has also performed extremely well, but with more fundamental backing. Lastly, we have the 'Non-AI' economy which includes healthcare, consumer companies, materials, housing, and more cyclical companies. This section has underperformed with some sectors actually down in the period and others simply lagging.

The chart below illustrates prices of these themes year to date through September. **Red** = Speculative Technology (ARKK), **Blue** = AI related stocks (ARTY), **Green/Pink** = healthcare, defensive sectors and consumer stock



Sector	Q3 2025 Performance	Key Drivers
Technology	+ 15.6%	Highest correlation to AI, earnings growth
Healthcare	+ 3.4%	Weaknesses in large Pharma/lags as defensive
Consumer Staples	- 2.4%	Defensive sector that lags in large upswing
Utilities	+ 4.0%	Defensive sector that lags in large upswing
Energy	+ 11.1%	Favorable valuations, higher Q2/Q3 growth
Financials	+ 6.0%	Deregulation and market recovery/IPOs
Industrials	+ 7.8%	AI related trade & higher Q2/Q3 growth
Consumer Discretionary	+ 9.8%	Amazon, Tesla, and AI related trade
Materials	+ 7.3%	Higher GDP Q2/Q3 growth expected
Communication Services	+ 10.3%	META, GOOGL, NFLX, and AI trades

Bond Market Insights

The bond market, for the first time since 2020, is having a good (and above yield return) year to date. **Treasury bonds** (measured by the 7–10-year maturity index) is up 7% through September as the yield on the 10-year bond has gradually drifted down in 2025. The 10-year yield has come down from 4.5% on January 1st to the current rate of around 4%. This has provided a nice tailwind for bonds, and especially those between 5 years and 15 years in maturity. The range of returns for fixed income has municipal bonds lagging with +2% year to date performance, while investment grade and mid/long term Treasuries are the best returning assets with a + 7% to + 8% spread. It is a nice boost (especially for our more conservative clients) to have our traditional bond allocation working for us with solid yields and some modest price appreciation. Even including the 2025 positive performance, traditional bonds are now just breaking even from their October 2021 levels. Fortunately, during this four-year period of no returns and high volatility for the asset class, Traphagen has been largely absent this space or significantly underweight.

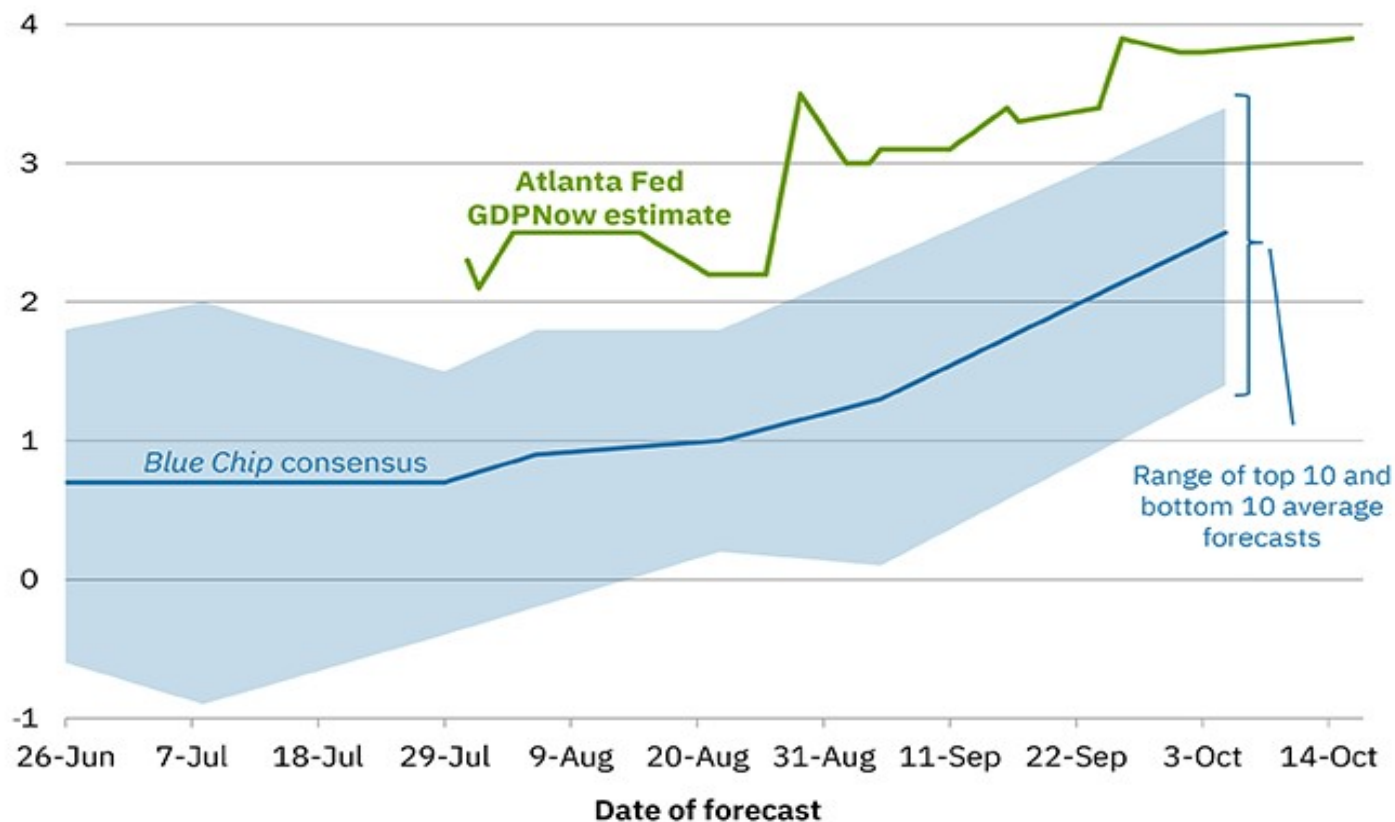
One of our tax-free municipal bond funds we have held since 2019 (TSIFX) has been liquidating its holdings for the past year and returning all proceeds (interest and capital) back to shareholders in the form of large cash distributions. The fund has now completed its sale of all bond holdings, and over the next 1-2 months the fund will be completely exited. All cash received will be returned to shareholders and then reinvested in other investments. The return on TSIFX has been disappointing (roughly -5% since original purchase) amid rising rates, COVID impacts, and bond sales.

Economic Indicators

Broad economic data provides additional reasons for this positive market movement. **GDP growth** accelerated to an annualized rate of 3.0% in Q2, up from **-0.5%** in Q1, reflecting solid economic momentum. Not only has growth accelerated in the 1st half of the year, recent estimates for Q3 and Q4 continue to increase as well.

Economist estimates for Q3 2025 GDP (US economic growth) have quickly and meaningfully increased from less than 1% in July to somewhere around 3% as of the most recent survey. Other indicators (like Atlanta Fed GDP Now estimate) have figures closer to 4%.

Below: Chart of analyst estimates for Q3 GDP growth in the US economy; (blue shaded area), along with Atlanta FED estimate; (green line.)



If the US economy can sustain economic growth in the 2%-3% range (or higher) it would be tough to get a sustained stock market correction of more than 10% - 15%.



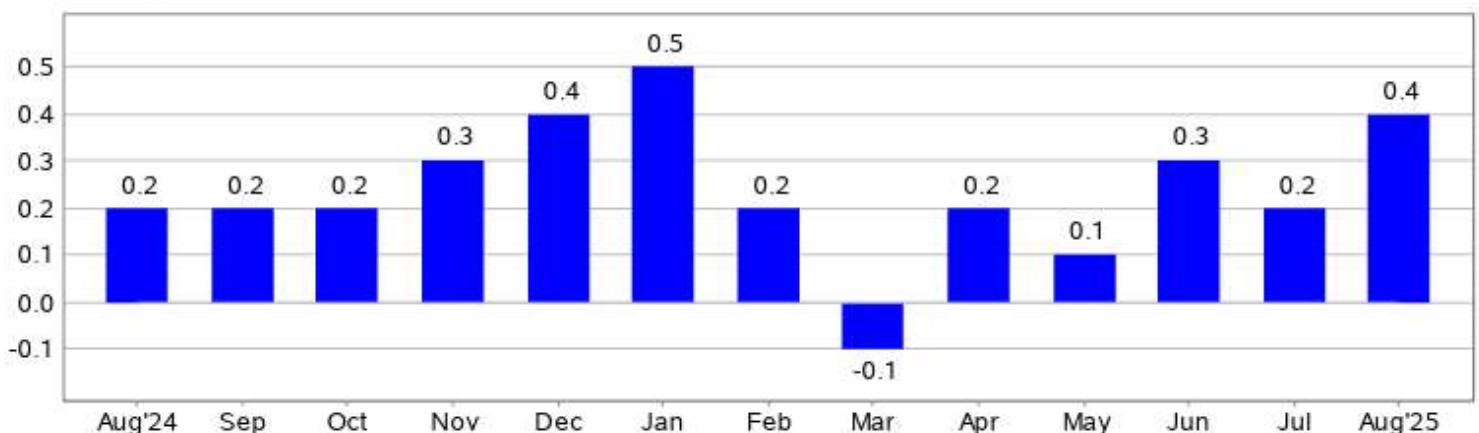
Above: US Unemployment rate over the past 5 years. After reaching the low 4% level in late 2021 (post pandemic) this metric has been mostly rangebound between 3.8% and 4.3%

In terms of unemployment, we remain in a long-term range of 3.7% to 4.3%. Since late 2021 we have remained in this range and since June of 2024 unemployment has been abnormally steady between 4.1% and 4.3%. We do continue to monitor any weakening here with increased AI usage and tariff drags, but to this point there is no meaningful trend, and we remain near historically low levels.

Corporate earnings have been robust through 2025, despite the April ‘liberation day’ and tariff day selloff and related uncertainty/volatility. Interest rates decreasing modestly, a lower US dollar, increased certainty on tariffs and tax legislation, and especially one of the biggest infrastructure/technology buildouts in history (AI) have bolstered SP500 aggregate earnings. The latest estimate for full year 2025 earnings is 11% growth over 2024 levels, and profit margins look to be near or at all-time highs of around 13%.

As somewhat of a counterbalance, recent revisions in job creation over the past 1.5 years have come out significantly more modest than originally thought. In addition, we are at the higher end of the recent unemployment range. Given these cross currents, Traphagen continues to monitor unemployment and if we see a sustained move above 4.5% and other forward-looking metrics look weak, we could take action within portfolios.

Inflation, as measured by the Consumer Price Index (CPI), continues to be roughly steady between 2.5% and 3.0% over the past year, with no clear trend in place. The most recent readings of + 0.4% in August 2025 and + 2.9% year over year were at the upper end of this range. **Below is a chart of month-over-month inflation for the past year.** Over this period there appears to be no definitive trend, although as of late summer we were at the upper end of this range and still well above the FED’s 2% target. We think the market would be very sensitive to any further movement higher. The relationship between inflation, anticipated interest rate cuts, and the financial markets is extremely important.



Real Estate and Alternatives

Non-Single-family home real estate continues to be the poorest performing asset class over the past 2-3 years with the NCREIF real estate index down close to 15% from top to bottom. This lackluster performance has been almost purely a result of higher interest rates and leverage costs. The actual fundamentals of most real estate (outside of legacy office) have remained strong with very high occupancy rates and solid rent growth. This is especially true in parts of the multi-family, data center, and shopping center/non-mall retail areas. The specific real estate holdings we are invested have fared better than the index, although still are the most modest portfolio performers with year-to-date returns ranging from down 1% to up 5%.

Traphagen's Private/Alternative investment suite (**TRAPALTS**) continues it's well above target performance trend for 2025. In addition to stock-like returns, our suite has exhibited almost no volatility or correlation to traditional financial markets, with a cash yield over 5%. **TRAPALTS** was up roughly 8% through the first three quarters of 2025, and as we write this update our estimate for full year returns are in the 10% - 11% range.

Over the past 5 years, the **TRAPALTS** has averaged + 8.4% per year net of fees with almost no volatility. We continue to use this part of the portfolio as an extremely valuable tool as both offense and defense. It is important to note that through time we are constantly reviewing and changing (if needed) the exact make up of the suite between the component parts (private real estate, several types of private credit, private equity, insurance linked securities, and infrastructure).

Major Factors Impacting Markets in Q3 2025

Three primary factors have shaped the market landscape this quarter, each with significant implications for investors:

1. **Increasing Importance of the Artificial Intelligence (AI) Buildout**

AI is now by far the most talked about (and arguably the most fundamentally important) factor within the financial market landscape. AI is not just Nvidia anymore; this infrastructure and AI spend/build out is now impacting many industrial, utility, financial, legacy technology, real estate, alternative, and conventional energy companies throughout the economy.

With the tentacles of AI investment and spending reaching more and more of the economy and its growth, we have seen these effects appear in GDP numbers over the past several quarters. The AI contribution to GDP has grown each quarter since 2023 and now stands (depending on exact estimate) somewhere between 30% and 50% of total GDP growth. These statistics hammer home the point that in order for the US economy to grow near the current pace and for the stock market to work overall (at the index level), AI needs to retain good growth through 2026 and actual consumer/enterprise usage must increase materially.

The above reflects Traphagen's diversified and defensive investment in this sector over the past 2-3 years. We continue to have high conviction and exposure in the infrastructure and electric grid area as we think regardless of AI, this sector will experience a decade of growth along with defensive characteristics and a good dividend yield. We also have some allocation in the private markets where most 'pure play' AI companies on the application layer reside. These have been much less impacted by public market/retail 'froth' and continue to grow as we await possible IPOs.

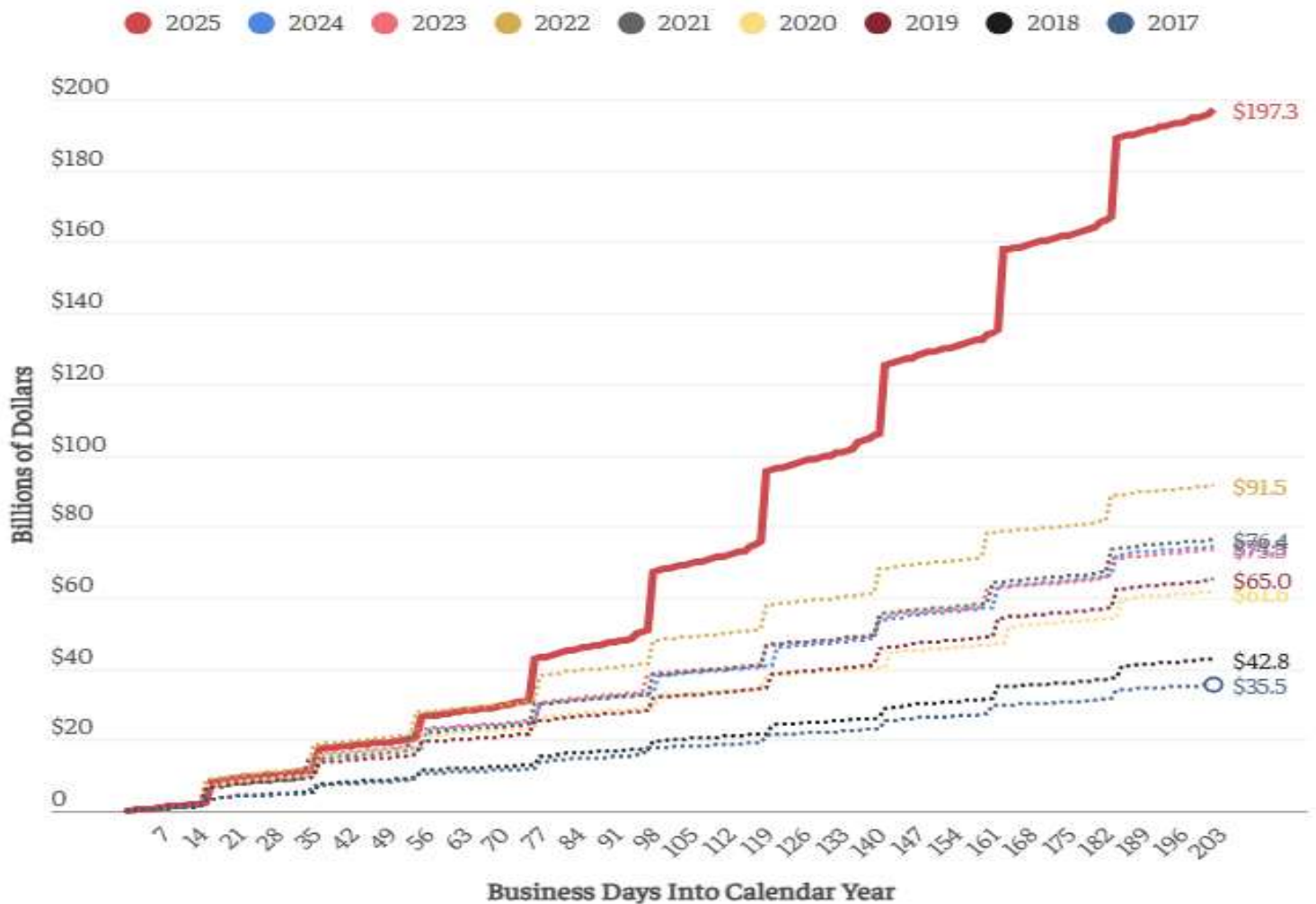
In terms of chip design, manufacturing, and other more speculative AI companies we have ample exposure through broad US stock and higher growth focused ETFs. Depending on how you view/define it, AI centric/focused stocks make up anywhere from 35% to 50% of the SP500 index, with Nvidia alone worth \$5 Trillion (or 8% of the total US stock market).

2. Continued Progress in Trade Deals/Global Framework & Recent China Issues

Q1's tariff escalation rattled markets significantly with a quick 20% drawdown, but in Q2/Q3 we had a sharp reversal of these tensions across the globe outside of China.

a)Over the past six months the US has constructed a largely stable and comprehensive trade structure with most of our major trade partners. This includes Canada, Mexico, the European Union, Japan, Indonesia, Philippines, Vietnam, South Korea, and the UK. Most of these region's tariffs (outside of some specific product exclusions) are tariffed at between 10% and 20%. Although these tariff rates are much higher than rates pre-2025, for the most part, consumers and US corporations have been able to absorb these without a spike in inflation or lower profit margins.

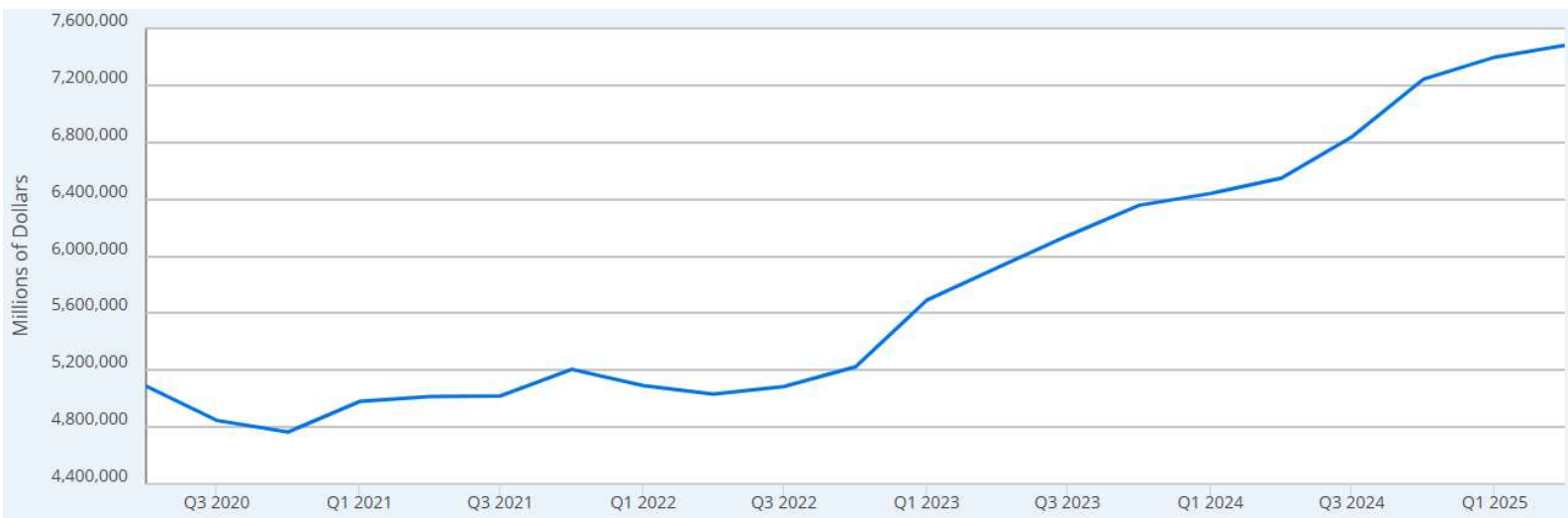
b)Still outstanding, and in many ways the most important, is China. In recent weeks the tensions between both countries have increased notably, causing some volatility in the equity markets. There are extremely high tariffs threatened against China starting November 1st (more than 100%), but hopefully this is more of a negotiation technique (similar to prior moves) and after President Trump's and President Xi's recent meeting it seems this is the case. For at least the current moment in time, lower tariff rates than originally threatened and some de-escalation look likely.



Above: Tariff revenue received by the US government by year.

A somewhat surprising positive to the new global tariff regime, is the large tariff revenue being received by the US government. In August 2025, roughly \$30B was received in tariff revenue, which on an annualized basis equates to \$360B per year. This revenue, although nowhere near enough to reverse the course of increasing fiscal government deficits alone, is certainly a material help.

3. Changing Federal Reserve Policy & Lower Rates: The federal reserve, for the first time in 2025, lowered short term interest rates in September by 0.25% and another 0.25% in late October. It is expected that over the next 6-12 months the Fed will continue to reduce rates by another 0.25% to 0.5%, and that will get short-term rates near 3%. This (all else being equal) is a tailwind to risk assets and stocks as investors approach a yield on savings net of inflation near 0%. This should push cash in money markets, CDs, and savings, into higher returning investments. Longer term bonds, real estate, and certain types of rate sensitive stocks could be standout beneficiaries of this trend. Currently, there is around \$7.5T in money market funds that could be looking for a ‘home’ over the next year or so if rates continue to drift downwards.



Above: Total assets held within US money market funds over the past five years (Trillions)

Traphagen 2025 Portfolio Changes & Performance Update

In 2025 we made several new investments that we will summarize below.

2025 Portfolio Adjustments/Security Changes:

- **‘COWG’ US large cap growth stock purchase:** This ETF is a growth focused fund that focuses on the most efficient companies in the US in terms of producing free cash flows. Between our initial purchase in January/February and a subsequent purchase in April (near market lows) we are up roughly 10% on the position. We continue to like this theme a great deal and are currently researching the attributes of ‘COWG’ vs. a similar ETF ‘GFLW’. ‘GFLW’ is similar in looking for high free cash flow margin companies with good growth but utilizes different metrics and has had superior performance since launch. It is possible we will replace or compliment ‘COWG’ as we

move into 2026 with this newer fund.

- **Deployment of funds into ‘AAA’/‘A’ rated CLOs and securitized loans:** Both JAAA and JSI are high quality investment grade corporate bond ETFs, (A/AAA rated) that have little to no interest rate risk and a yield (at current base rates) around 5.6%. These continue to perform as we expected with little/no volatility (even when the stock market goes through downturns) while paying out its monthly income. These are also liquid, which allows us to rebalance at any point if we feel there is an opportunity.
- **Creation and purchase of new Alternative/Private Asset Manager ETF (GPZ):** As we communicated in our last newsletter, earlier this year we partnered with Van Eck to create a new ETF that concentrates purely on alternative/private asset managers (Blackstone, KKR, Ares, Apollo, etc.). We are pleased to report that this ETF has reached \$100M as of early October and is the 4th quickest to reach that level in Van Eck’s history. We invested in this for our clients shortly after launch in June, and are up roughly 5% on the position, although in recent weeks there has been a material drawdown and volatility due to market wide credit concerns. There have been two high profile subprime auto related bankruptcies over the past month, however at this point we do not see a wider credit issue and little to no impact on any of our holdings.

Overall Portfolio Performance

Traphagen’s portfolios through September of 2025 were generally up between 6.0% and 13%. The SP500 was up 14.8% in the same period with the ACWI up 18.6%. We are extremely pleased with our portfolio performance, as much like 2024, all pillars are performing at or above our long-term targets with significant defenses already in place. Even if stocks remain unchanged for the remainder of the year, most of our client portfolios are able to obtain a final return of 10% or more for most clients with additional cash income. Just as importantly, when the stock market was down around 20% in early April, most client portfolios were only down 2% to 7% depending on strategy. This level of total returns and protection is not easy to achieve and the way we have obtained it is unique to Traphagen.

2025/2026 Market and Economic Outlook Update

Looking ahead through the end of 2025 and into 2026, we maintain a generally optimistic stance with two meaningful headwinds in mind. Several positive factors support this view, including good clarity in a new global trade framework (outside of China), lower interest rates, stimulus through the new tax bill, and corporate earnings strength. However, risks are present (as is always the case).

Key Risks

The table below outlines the risks we are monitoring, along with their potential impacts on portfolios, and the mitigation strategies we are using to reduce any possible impact:

Issue/Risk	Importance	Potential Portfolio Impacts	Mitigation Strategy
Tariff/Trade Policy	Low/Moderate	China Tied Stocks/Tech	Hold sectors with little tariff impact / High Alternative exposure
Stock Valuations	High	Stocks (especially AI/Spec)	Value/free cash flow stocks / concentrate on fundamentals
Recession Risk	Low/Moderate	Most risk assets	High alternative exposure/AA bonds
Inflation/Rates	Low/Moderate	Real Estate, Bonds	Infrastructure, certain stock sectors, Alternative exposure
Geopolitical Tensions	Low	Select stocks in short term	None taken (only short-term impact)
Slowing Employment	Moderate	Most risk assets/Consumer	Defensive stock exposure / AA bonds / Alternative exposure

We expect a continued balanced approach—combining opportunities in select growth and defensive/value areas of the market (healthcare, utilities, some software) with downside protection (namely AAA/A rated bonds and alternatives)—will be key to navigating the remainder of 2025 and early 2026. Our firm will be gradually pivoting from being invested in all areas of the AI ecosystem over the past 2 years to being more selective and defensive in the theme. As we progress over the next several months, we expect to make portfolio changes to reflect this shift in strategy. In addition, we might look to proactively take profits in certain alternative/private investments after years of good performance and reallocate elsewhere.

Conclusion

Q3 2025 has been a period of continued improvement in almost all financial markets and continued improving clarity around tax and trade policy. We are pleased that client performance has been above long-term estimates this year, while at the same time providing significant protection with elevated stock valuations and some excess speculation present. As we look forward to 2026, we will likely be making material changes to portfolios to reflect the changing landscape of the economy, interest rates, and market opportunities. Enjoy the holiday season and we hope the best for all as we enter the near year.

Best regards,
Your Traphagen Investment Team