

Welcome to NorthStar Capital's Q3 2025 Newsletter!

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## **Economic**

- The Consumer Confidence Index continues to drift lower, falling to 94 in September
- Retail sales continued to show modest gains, rising 4.8% year-to-year
- U.S. job growth has slowed, with the addition of only 22,000 jobs in August, and no data since then
- Unemployment rate is holding steady at 4.3%
- Labor Participation rate holding steady at 62.3%
- The price of crude oil has dropped to \$61 per barrel, reflecting a steady year-long decline
- University of Michigan Inflation Survey reflects diminished but still persistent tariff fears
- 30-year fixed mortgage rates have fallen from 6.7% to 6.3% in recent months
- Mortgage delinquency rates remain low, but private credit problems are appearing

## **Inflation**

- U.S. CPI in August rose to 2.9%, well above the Fed's target of 2%
- Used car and truck price index has shown a modest increase in 2025
- Health Insurance costs have risen sharply and are expected to spike with Obamacare expirations

## **Monetary Policy**

- Federal Reserve cut rates in September, and may do so again in October and December
- Fed is focused less on inflation and more on the full employment portion of the "dual mandate"
- An additional 2-3 rate cuts are expected in 2026

## **International**

- Japan elects Sanae Takaichi as a Conservative and the nation's first female Prime Minister
- European Central Bank keeps rates low, with the marginal lending rate at 2.4%
- Multiple wars ended and hopes raised regarding the war in Ukraine and the hostilities in Gaza
- International markets have shown steady growth during 2025, valued more cheaply than U.S. markets

## **Interest Rates**

- 10-year U.S. Treasury yield now at 3.96%, marking a continued decline over the year
- 15-year fixed mortgage rate holding flat at 6.00%, with home prices beginning to soften
- SOFR drifted down to 4.18% during Q3

## **Earnings**

- Traditional banking business improving, with generally modest valuations
- AMD strikes \$100 billion deal with Open AI
- Auto results mixed, with record quarter from GM, but disappointing EV earnings from Ferrari
- Healthy but modest earnings growth expected from S&P 500 companies in both 2025 and 2026

## **Market Outlook**

- Jamie Dimon, CEO of JP Morgan, highlights risks in private credit, and we share his concerns
- European defense stocks have strong outlooks, due to heavy EU spending
- Stable legacy tech businesses poised for growth, while speculative and "hyped" stocks slip back
- Despite investor concerns, in Q3, the S&P 500 grew 8.1% while the Nasdaq grew 11.4%
- IPO activity picking up, with tech stocks, communications services, and consumer discretionary leading

## **Current Investment Outlook**

Despite widespread concerns about tariffs and overvaluation, it is now clear that 2025 is proving to be a very good year for stocks. While we expressed a view that valuations were a little high as we entered the year, we most certainly did not want to be out of the market. Since some frightening days in April, it is now clear that the trade and tariff negotiations have not spun out of control, the economy is generally quite strong, and the market is allowing stocks overall and some stocks in particular to do very well. Third quarter gains were 8.1% for the S&P 500 and 11.4% for the Nasdaq, bringing the year-to-date returns to 14.8% for the S&P 500 and 18.0% for the Nasdaq. Our typical client account has done significantly better than that.

As we explained in our last quarterly letter, we take very seriously the responsibility of presenting our market forecasts. This exercise provides us with a foundation for our investment outlook and planning. It helps us determine when to invest and where. And, it serves as a roadmap of sorts for our clients. Most importantly, it helps us to stay in the market. The cardinal sin of investing is to get out of the market and miss the greatest returns which are on offer. An investor who suffers losses with the market can ride out the storm. The investor who gets out and stays out cannot. It takes courage to stay in a frightening market, but it is almost always the right thing to do.

There is a great deal of attention at present given to the question of a possible AI (Artificial Intelligence) bubble. Have the leading tech stocks risen to overinflated levels? And, is the underlying business activity reflecting an unsustainable level of enthusiasm and optimism? We believe that AI and other forms of high speed and data intensive computing represent a significant technological breakthrough. But, just as there were many companies vying for a top position in the automotive, personal computer, and internet markets, there are companies today that will thrive and others that will come in second or third. The biggest challenge today is that the investments to stay relevant are massive. Some of these investments will prove to be profitable and others won't. In other words, unsurprisingly, there is ferocious competition in AI. For the winners, there can be significant rewards. Just as is the case in every other industry, investors would be well advised to stay with the leading one or two or possibly several companies. That's the challenge.

The domestic economy continues to show healthy growth. As described by Mike Wilson, Chief Investment Officer of Morgan Stanley, we have been in a rolling recession for the past several years, and now we have moved into a rolling recovery. We are not at full employment and there are risks of inflation gathering strength, but we are moving in a positive direction. The economy continues to be led by technology companies who have strong demand and are making significant investments. The non-tech economy is stable but relatively flat. So, we have a healthy economy with modest growth, and a few areas of booming demand. This is a very investable market.

Inflationary expectations have been on hold for some time. They had been declining since early 2022, but they rose in the midst of the tariff fears. Expectations have fallen off since then, but they have not yet reached the Federal Reserve goal of 2%. The bond market has had a cautious view on inflation, with the 10-year Treasury holding for months at about 4.5%, but since the end of July, the yield has dropped to its current level just below 4%. On the other hand, commodities like gold and

silver are hitting new highs and ringing alarm bells. With lessened concerns about inflation and a more worried view toward employment, the Fed seems determined to be on a path to drop rates as much as 150 basis points over the next year or so, which is more than the bond market expects.

With strong leadership in tech, healthy levels of consumer spending, and mostly stable results in the rest of the economy, our GDP is expected to produce growth at just below a 2% rate. There are a number of warning signs, however. Private credit has expanded extremely rapidly and clearly incurred some significant risks. Tricolor Holdings and First Brands have collapsed in the face of adverse business results and with possible fraudulent activities. These will not be the only failures in this area and it is unclear how widespread and how large the problems will be. Overall, business is good, but there are pockets of bad business practice and high risk, drawing parallels to the commercial real estate market in 2022.

For once, the international news is almost uniformly positive. For better or for worse, the “peace through strength” philosophy seems to be working, at least for the time being. Despite being our most hated President ever (in some quarters), Trump has been able to end numerous wars, maybe even to include the hostilities in Gaza. Whether he can do the same in the Ukraine or not is still unclear. As a result, the international business climate is improving.

Despite the modest pace of growth in domestic GDP, the outlook is for healthy growth in the earnings of the S&P 500 companies, with lowered estimates of about 10% gains in both 2025 and 2026. That would place the price-earnings (p/e) ratio for the S&P 500 at 24.5 times 2026 earnings. This level of valuation is lofty and leaves little room for error. We see continued broadening out in the market, but technology stocks continue to lead with strong earnings growth. Communication services and consumer discretionary stocks are also showing strength. Very few individual companies are showing any expectation of a recession. We are still finding stocks with rising earnings and valuations which are fair or even low. We are optimistic on balance and continue our search for success.

Thank you for taking the time to read NorthStar Capital's Q3 2025 Newsletter. In compliance with FINRA Rule 2210, our extensive security analysis, specific information pertaining to market data, and additional investor information have been redacted from this document.

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