NADLER FINANCIAL GROUP
Investment and Financial Consultants

Nadler Financial Group, Inc.
155 N. Pfingsten Road • Suite 160
Deerfield, Illinois 60015-4903
Phone: 847.940.4040 • Fax: 847.940.7246
www.nadlerfinancial.com

THIRD QUARTER 2025 ECONOMIC AND FINANCIAL MARKETS REVIEW

The stock and bond markets performed well during the third quarter despite uncertainty regarding tariffs, inflation, legislation, and the economy in general. Investors cheered the fact that the Federal Reserve Board hinted at lowering interest rates in August and then actually lowered them by .25% in September. When the Fed lowers interest rates, it is positive for the economy because it reduces the borrowing costs that many corporations and consumers pay when financing purchases. It also reduces interest rates on many existing loans, providing borrowers with more money to spend on other goods and services. This typically leads to growing corporate earnings, on which stock prices are based. As a result, the S&P 500 Index ended the third quarter up 13.72% year-to-date, while the Dow Jones Industrial Average gained 9.06%. As for the bond market, the Bloomberg Intermediate U.S. Government/Credit Bond Index increased 5.70% year-to-date as of September 30, 2025.

The Federal Reserve Board's interest rate policy is one of the main factors influencing the direction of the economy and financial markets, and the Fed has been weighing the costs and benefits of lowering the federal funds rate throughout this year. The federal funds rate is the interest rate that the Fed sets for banks to lend reserves to each other overnight. It is a short-term interest rate that impacts financing rates on various types of debt, including auto loans, credit cards, and other lines of credit. Adjusting this rate enables the Fed to manage inflation, employment, and other aspects of the economy. In addition to helping corporate earnings grow, lower interest rates are generally positive for stocks because yields get reduced on competing fixed-income investments such as money market funds, bonds, and CDs. However, if the Fed lowers interest rates too much, it can lead to an increase in inflation because the U.S. dollar could weaken and the economy could begin to overheat.

Although the Fed has feared that lowering interest rates too much and too soon could exacerbate inflation, not reducing rates enough could harm an already fragile job market and lead to an economic slowdown or even a recession. The Fed has also been under pressure from the Trump administration to lower interest rates, as the administration believes the economy could perform even better if rates were lower. However, the Fed has been very careful not to lower rates too quickly or too much to avoid triggering unwanted and excessive inflation.

During the third quarter, Congress passed the One Big Beautiful Bill Act of 2025. This bill provided new tax relief for certain taxpayers and extended the existing, relatively low income tax rates already in place. Some argue that lower taxes are beneficial for the economy because they typically lead to individuals and corporations spending more money on goods and services. Lower taxes are also helpful for corporate profits, as they reduce companies' costs. Supporters of the bill cheer the tax breaks and argue that even if tax revenue brought into the government is reduced, it will be offset by an increase in economic activity, spending cuts elsewhere, and tariff revenue received by the U.S. government. Opponents of the bill argue that tax relief only benefits some individuals and that lower taxes will increase the national debt, as the government will be taking in less money.

Bond investors have become concerned that if the national debt increases too much, longer-term interest rates in the Treasury bond market will rise. This is because those individuals, corporations, and other countries that loan money to the U.S. government will now demand higher interest rates for their investments in longer-term U.S. Treasury bonds, which would be seen as riskier than before. Rising long-term interest rates could also harm the stock market as investors sell stocks to buy long-term Treasury bonds that would then pay higher interest. Therefore, even if the Fed continues to lower the short-term federal funds rate, a potential increase in long-term interest rates in the Treasury bond market will be important to monitor over the remainder of this year and into next year.

Finally, the strength of the economy bears watching, as the last several employment reports show that the labor market is weakening. This could be the result of employers delaying the hiring of workers due to uncertainty regarding tariffs, which were under scrutiny from the courts during the third quarter. If investors become even more concerned about the job market, they may sell stocks in anticipation of a weaker economy and lower corporate earnings in the future.

Despite these concerns, we remain bullish on stocks over the long term and believe that any short-term market corrections should be viewed as buying opportunities for investors with long-term time horizons. We continue to overweight large-company stocks, which have outperformed small-company stocks for many years. Smaller-sized companies would be particularly vulnerable if long-term interest rates rise in the bond market, as they tend to rely more heavily on debt than larger companies. We have been allocating more money to foreign stocks for investors with a relatively high risk tolerance because they are generally undervalued compared to U.S. stocks. We still prefer short-term bonds over long-term bonds as this provides the best combination of risk and reward in fixed income.

As always, we will continue to monitor ongoing economic and financial market conditions. In the meantime, please contact us if you have any questions regarding your portfolio or the financial markets in general.

** Index returns were obtained from the Wall St. Journal and Bloomberg on October 1, 2025.*