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ARGUS ECONOMIC COMMENTARY

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October Lives Up to its Rep: Our Monthly Survey of the Economy, Interest Rates, and Stocks

Historically, October has been one of the stronger stock-market months. On the S&P 500, October ranks fourth (behind November, April, and December) among the 12 months for all years from 1980 through 2024. The market has had a strong return so far in 2025, but it has been a turbulent year with uncommon volatility. The turbulence has radiated out from the tentpoles of tariff reveal day in April and tariff enforcement day in August.

Some months with bad stock reputations have shined in 2025, while some perennially winning months have underperformed. The strong 2.3% gain recorded in October is above average – but not as good as in September, which is usually the worst stock month of the year.

The U.S. central bank met expectations when it cut the fed funds rate by 25 basis toward the end of October – its second cut in little more than a month. But the Fed chair warned investors that the Fed would remain data-dependent, and that a December cut was not a given. Still, stocks barely blinked at the Fed's potential return to the sidelines.

A key contributor to September-October strength was expectations for and deliverance of strong calendar 3Q25 earnings. Stocks also benefited from the absence of likely weak non-farm payrolls data, which would have reminded a giddy and greedy market that the investing environment is not perfect.

The Economy, Interest Rates, and Earnings

The third-quarter 2025 GDP report has not been released due to the government shutdown. The third (final) report of second-quarter 2025 GDP indicated growth of 3.8%, representing sharp recovery from a 0.5% decline for 1Q25. Both first and second-quarter GDP featured distortions in the imports and private inventory categories due to trade positioning ahead of the August implementation of tariffs. Imports plunged in 2Q25 after soaring in 1Q25; private inventories did the inverse. The third quarter of 2025 was expected to feature the first "clean" GDP report in which those two categories did not distort the underlying trend in consumer and business spending.

In the absence of hard data, the Atlanta Fed's GDPNow model currently estimates that third-quarter GDP grew by 3.9%. That estimate, which has been stable for the past several weeks, represents a sharp upward revision from 2.3% about one month earlier.

Argus Director of Economic Research Chris Graja, CFA, has been encouraged by the economy's resilience while monitoring consumer and business caution. Chris believes that solid GDP growth continued in the third quarter of 2025. The Argus model estimates 3Q25 GDP growth at 2.6%, below the Atlanta Fed estimate though within the broad 1.7%-3.8% consensus estimate.

Argus is modeling that 3Q25 personal consumption expenwditures (PCE) rose in the low 2% range. In 2Q25, PCE rose by 2.5%. The widely discussed K-shaped economy is resulting in solid spending by the middle- and upper-income consumers, but a slower pace of spending and a shift to bargain goods by lower-income consumers. Restaurants are reporting that visits by younger consumers and families have dropped off as tariffs and inflation stretch budgets. Consumers on the bottom leg of the "K" are being forced to redirect spending away from discretionary items and to necessities. Services, which is the biggest category in PCE, is being impacted by this trend.

Argus is forecasting that non-residential fixed investment, the proxy for corporate capital spending, grew at a 4.5% rate in 3Q25. Non-residential fixed investment rose by 7.3%

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in 2Q25. That is a step-down from 9.5% in 1Q25 but still very solid. Chris notes that the old economy drivers of the business cycle, housing and manufacturing, are "stuck in the mud." Amid the AI boom, Chris estimates that business investments in intellectual property and equipment may have added seven-tenths of a point to GDP growth.

PCE and non-residential fixed investment normally constitute 80%-85% of GDP. With the pre-tariff positioning and trade distortions of 1Q and 2Q now behind, these two categories may have contributed 2.0-to 2.5-percentage points to 3Q25 GDP growth.

The government shutdown began a day after the third quarter concluded. Government spending was down 0.1% in 2Q25 after being down 1.0% in the final 1Q25 GDP report. Chris is modeling a 0.2% decline in 3Q25 government spending, with state and local still positive and federal trending down. Imports and exports are tough to model without government input and amid ongoing trade positioning, given that tariffs were not fully settled at quarter's end. Argus is modeling exports as running slightly higher than imports while creating an overall net neutral effect.

Finally, Chris and Argus are modeling 3.0% growth in the core PCE price index (excluding food and energy). This number is consistent with the 3.1% annual rise in September core PPI. Employees of the Bureau of Labor Statistics were called back to their offices briefly to compile this number, which was then used in the calculation of the COLA rise in Social Security for 2026.

Outside the GDP accounts, the government shutdown has also eliminated access to the most widely watched economic release in any month, non-farm payrolls. The last such report was from August, when the U.S. economy generated just 22,000 new non-farm jobs for the month. Three-month average jobs growth was just 29,000 as of the end of August. The unemployment rate was 4.3% for August, up from 4.2% for July and 4.1% in June. Average hourly earnings grew 3.7% annually, moderating from the 4% annual growth trend of the past several years.

The consensus for September and October non-farm payrolls is predictably wide. Chris Graja believes September non-farm payrolls growth increased from August levels but remained subdued. He is modeling 56,000 growth in September non-farm payrolls, while the consensus is lower at 51,000.

Chris is estimating that October non-farm payrolls were up in the 25,000 range. Many federal worker laid off by DOGE ran out of severance at the end of September; some may have retired or been hired elsewhere, but some of the furloughed will figure in non-farm payrolls and unemployment calculations. Chris estimates that the unemployment rate as of October end is in the 4.2%-4.4% range. His estimates are based on weekly initial unemployment claims, JOLTs job openings, Challenger & Grey layoff data, and other privately compiled data.

The breakeven level of jobs growth required to hold the unemployment rate steady is now lower than it was in recent years because of trends in population growth. Due to sharply reduced immigration and the secular decline in native-born birth rates, the St. Louis Fed now estimates breakeven employment growth of 32,000-82,000 per month. Thus, job gains in the neighborhood of the Argus estimate would likely keep unemployment stable.

In the absence of government data, economic releases from private sources have taken on extra weight. Several of these reports are sentiment surveys or diffusion indices. The business community appears guardedly optimistic but frustrated by ongoing economic uncertainty, given the slowing jobs economy compounded by tariffs and the government shutdown.

Overall business sentiment remains guarded but is off its worst levels. The ISM's manufacturing purchasing managers' index (PMI) edged up to 49.1% in September from 48.7% in August and 48.0% in July. Purchasing managers indicated that contraction in new orders and in employment is being offset partly by higher production.

ISM's services PMI, however, unexpectedly fell from 52.0% for August to 50.0% for September. That put the service PMI at the breakeven point between expansion and contraction for the first time since 2010. In the large services category of accommodations & food services, survey respondents complained that tariff impacts on food input costs were leading to customer loss. In the construction sector, respondents worried that higher materials costs along with high mortgage rates were keeping would-be buyers sidelined.

The Small Business Optimism Index from the National Federation of Independent Business (NFIB) slipped to 98.8 in September from 100.8 in August. The index remained above its 51-year average of 98.0, but is well down from 105.1 in December 2024, right after Donald Trump's election win. The uncertainty index for September rose sharply to its fourth-highest reading ever, according to NFIB Chief Economist Bill Dunkelberg.

Consumer sentiment is also up from tariff-shock lows but has been more volatile than business sentiment. The University of Michigan consumer sentiment survey remained at 55.0% for October after falling to 55.1% in September from 58.7% in August. That same consumer sentiment was 70.5% a year earlier in October 2024. The Conference Board's Consumer Confidence Index fell to 94.2 for September from 97.4 for August. Within this series, the Expectations Index reading of 73.4 remained below the 80 threshold – as it has since February 2025 – that tends to signal a recession ahead.

Despite the absence of 3Q25 GDP data and the employment report for September, Chris has raised his 2025 GDP growth forecast given the solid growth trend across the two middle quarters of the year. Argus has raised its 2025 GDP growth forecast to 1.9% from a prior 1.5%. Our forecast assumes moderation to sub-2% growth in 4Q25, which could be impacted by the loss of government spending and suspension of SNAP benefits, which will cut into consumer spending. Argus believes GDP is likely to remain fairly steady next year, and Chris recently raised his GDP growth forecast for 2026 to 1.9% from 1.7%.

The U.S. Federal Reserve is tasked with the dual mandate of optimizing employment while keeping inflation in check. After raising rates aggressively throughout 2022 and early 2023, the Fed maintained its policy rate at 5.25%-5.50% from September 2023 until August 2024. Beginning in August, the Fed cut rates by a cumulative 100 bps over the next three FOMC meetings into year-end 2024.

The central bank cut the fed funds rate in September 2025 for the first time in nine months. It then cut rates again by a quarter point at the end of October. The Fed in September broadly hinted at two additional rate-cuts by year-end. But after the October meeting, Fed Chair Powell stated that a widely anticipated rate cut in December was "not a foregone conclusion." Commentary following the October cut reminded investors again that any further monetary easing will be data-dependent – even amid data scarcity.

Assessing the delicate balance act between jobs growth and pricing pressures, the Fed appears to have determined that the balance of risks had shifted away from rising prices and toward weakness in the employment economy. The latest CPI data, published amid the government shutdown to help set the Social Security COLA for 2026, signals that inflation remains elevated. But the recent trend in monthly non-farm payrolls growth, along with downward revisions to most of 2024 and early 2025 jobs data, signals real weakness in the employment situation.

The Fed has become more divided than in the past. One voting member, Jeffrey Schmidt, preferred no rate cut in October, while Stephen Miran, the newest member of the Fed, would have preferred a half-point cut. With non-farm payrolls and GDP data not available, the Fed (like the rest of us) is flying somewhat blind.

U.S. market interest rates have been volatile but ended October little changed from September. The 10-year Treasury yield was 4.11% as of the end of October 2025, compared with 4.18% as of the end of September. The cycle peak for the 10-year yield was 4.9% in October 2023; the 10-year yield briefly slipped below 4% following the employment benchmark revisions in mid-August 2025. The two-year Treasury yield was 3.61% as of the end of October 2025, vs. 3.64% as of the end of September. The cycle peak for the two-year yield was 5.2% as of October 2023.

The extended period of yield-curve inversion is decisively finished. Over time, Argus expects short-term yields to move lower from current levels. Long yields over time are expected to widen their relative premium to short yields.

Notwithstanding Fed Chair Powell's ambiguity about any further policy action in 2026, Argus Fixed Income Strategist Kevin Heal continues to model one remaining rate cut in 2025 (in December) following the reductions in September and October. According to the CME FedWatch tool, the probability of a rate cut at the December FOMC meeting is now 63%; that is down several percentage points on the post-FOMC commentary.

Argus acknowledges the possibility that, after the September and October cuts, the Fed moves to the sidelines for the remainder of 2025. The Fed is mindful that tariffs are historically associated with higher goods prices. Were inflation to rise from current levels, the Powell Fed might be inclined to hold rates steady, particularly if nonfarm payrolls growth recovers into year-end.

In the absence of government data, calendar 3Q25 earnings season has had an outsized and largely positive impact on stocks. With over one-half of companies having reported quarterly results as of 10/31/25, the blended annual growth rate for calendar 3Q25 earnings is in the 10%-12% range, up a few percentage points in the past few weeks as actual results displace consensus estimates. Blended earnings growth rates combine both actual results for companies that have reported with estimates for companies yet to report. Estimates tend to be based on conservative guidance, whereas actual results are often above guidance.

As actual results replace estimates, the final calculation of EPS growth for any quarter tends to be several percentage points above the blended estimate from early in the reporting period. Nearly 90% of companies have reported earnings above the pre-reporting consensus, which is higher than the long-term 75% average. The magnitude of the EPS beat against expectations, in the high single digit range, is also at the high end of the long-term range of 5%-9%.

The Financial sector kicked off earnings season with high-teen percentage growth from 3Q24. Bank activity is benefiting from improved business confidence and lessened tariff anxiety, which is leading to increased loan activity, higher M&A and IPO deal-making, and increased equity and fixed-income trading volumes. Other sectors that are outperforming consensus expectations so far include Information Technology, Materials, and Industrial.

Five of the Magnificent 7 stocks reported in the trading week beginning 10/27/25: MSFT, AAPL, AMZN, META, and GOOGL. The five names straddle three separate S&P sectors, and all dominate their sector reporting. The five stocks grew calendar 3Q25 earnings at a more than 20% average rate, surpassing consensus expectations. Investors panned the META and MSFT reports, sent GOOGL and AMZN higher, and were neutral on AAPL.

Sector and index growth estimates are based on year-over-year simple-average EPS growth rate calculations, not the relative weight of individual company net-income growth.

Given that these giant companies generate significant net income on a dollar basis, their contribution to earnings growth is under-counted in a simple-average EPS calculation. Nonetheless, the enormous net income these companies generate is plowed into the economy and contributes meaningfully to U.S. economic growth.

Argus came into 2Q25 earnings season modeling the high-single-digit to low-double-digit earnings, and results approximately matched our expectations. We are reiterating our forecasts for S&P 500 earnings from continuing operations of $270 for 2025 and $300 for 2026.

Domestic and Global Markets

Stocks hit their 2025 trading year lows in the aftermath of President Trump's "Liberation Day" tariffs announced early in April. Stocks have since staged a six-plus month rally, punctuated by a few selling spasms. The major indices rebounded from selling triggered by weak August non-farm payrolls to start September, recovered as September progressed, and rallied strongly in the historically good month of October. After an above-average September, gains in October were fueled by favorable 3Q25 earnings; there was also the absence of weak employment data to rain on anyone's parade.

The S&P 500 was up 18% year to date at the end of October after being up 14% at the end of September. With AI mania back in full swing, the Nasdaq was up 24% year to date at the end of October after being up 17% at the end of September. The Dow Jones Industrial Average finished October up 13% after being up 10% year-to-date at the end of September.

Wilshire Large Cap Growth was up 25% YTD as of the end of October; Wilshire Large Cap Value relatively underperformed and widened the growth vs. value performance gap to 14 percentage points as of the end of the month. The Russell 2000 was up in low-double-digit percentages for the year at the end of October, after surging into positive territory in August.

The Barclays Bloomberg U.S. Bond Index was up 6.5% year to date at the end of October 2025, its highest level of the year. Bond returns, which bounced around all through 2024, could continue higher if the Fed cuts rates again in December 2025.

For much of 4Q24 and early 1Q25, investors rotated away from traditional growth leadership and toward defensive, interest-rate-sensitive, and cyclical sectors. In the second quarter of 2025, growth stocks came back into favor on stock-price weakness for well-known names and renewed enthusiasm for the AI trade. Even with some late-September profit-taking, growth sectors clearly won the third quarter. Growth remained in vogue in October. Other parts of the market also participated in the uncommonly strong summer-into-fall stock rally. And with tech and AI stocks looking expensive, investors are finally pivoting to some of the most oversold sectors of 2025.

Just one month in, the best sector in 4Q25 to date has been Information Technology, up 6%. The surprising next-best sector is Healthcare, up 3.5% in October. Healthcare is still a bottom-two sector for all of 2025. Other positive sectors for the month included Utilities and Industrials. Multiple sectors were down for October as investors focused on AI stocks and lower rate beneficiaries (Utilities and REITs).

Given the recent rotation benefiting Healthcare, every sector is now positive for 2025. Only four sectors, however, are doing better than the S&P 500. The 2025 top sectors include two traditional growth leaders, Information Technology and Communication Services; the cyclical Financial sector; and the rate-sensitive Utilities sector.

On a granular basis, the AI trade continues to drive overall stock-market returns. But it is not the only theme, particularly now that some AI exhaustion and profit-taking is setting in. Enduring AI enthusiasm along with broad-market bargain-hunting creates a positive set-up that could enable the market to build on existing gains into year-end 2025.

Like the U.S. market, global stocks did better in 2023 than they did in 2022; and most carried that momentum across 2024. In 2025, overseas markets have generally been doing better than the U.S. market. Tariffs have both scared foreign investors out of U.S. equities and realigned global leadership. All nine global bourses in our tally are positive for the 2025 year as of the end of August, but leadership has changed since early in the year.

Most regions strengthened in October from third-quarter-ending levels. Some of the worst markets in 2024, such as Mexico (with a 31% gain so far in 2025), are near the top of the leaderboard in 2025. Conversely, some of 2024's winners such as India are relatively underperforming in 2025; India alone is lagging the U.S. market (S&P 500) for the year to date.

In terms of our themes, Resources economies and Asian markets are both up 27%. Americas markets are up 24%, fueled by recovery in Mexico and Canada. Mature economies, which led in 2024 and 2023, are up 23%; this group had the best October as trade-related tensions appeared to wind down. BRICs-minus-Russia are up 18% year to date.

Conclusion

The calendar 3Q25 earnings season has been a big hit, led by sometimes-astonishing growth predictions from AI participants. Is the AI trade at risk of rolling over? We do not think so, given that the AI trade appears to be widening out.

AI momentum was formerly centered in AI training for large language models (LLMs) deployed by the hyperscalers (the largest cloud service providers) and conducted in their data centers. AI is broadening out in multiple directions, including the AI technology itself; technology hardware and software niches that will benefit; and the companies and governments just now beginning their AI journeys.

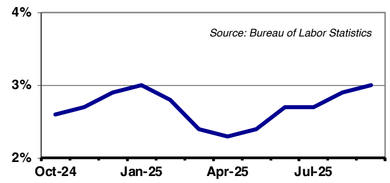
In terms of AI development, inference is a much larger opportunity than training. Whereas training enables an AI to learn, AI inference enables an LLM to actually function and be useful. Inference will require massively more compute capacity than training. So too will agentic AI and physical AI (robotics). Beyond the initial focus on compute for massive GPU clusters, there are now vertical opportunities in data storage, networking, and services – all the elements needed to get AI services from the data center and out into the world. And there are endless horizontal opportunities across enterprises in every industry and in sovereign, or nation-sponsored, AI.

Despite its terrific, AI-driven start, third-quarter earnings season is at risk of ending with a fizzle. Much as the big banks always kick off earnings season, retailers always sweep up the parade and may have a chilling message to share. In this K-shaped economy, the upper income brackets are doing well, based on rising home prices and investment asset values. At the lower end of the economy, consumers are strained after years of inflation; jobs availability is shrinking; tariffs are pushing up prices; and government policy is making healthcare more expensive and food assistance harder to obtain.

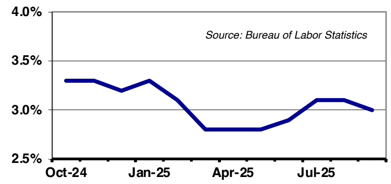
Despite those concerns, we expect stocks to finish a turbulent year with further upside, as the remaining bears capitulate and lagging managers window-dress client portfolios. The year 2025 may prove to be a tough act to follow, if tariffs do prove to be inflationary, the economy starts shedding jobs, and the AI trade starts to unwind. But those are concerns for next year. In the current rallying market, investor won't worry about 2026 until January 1.

Jim Kelleher, CFA,
Director of Research

Release:	**Consumer Price Index**
Date:	11/13/2025
Month:	October
Previous Report:	3.0%
Argus Estimate:	3.0%
Street Estimate:	NA



Release:	**CPI ex-Food & Energy**
Date:	11/13/2025
Month:	October
Previous Report:	3.0%
Argus Estimate:	3.0%
Street Estimate:	NA



Previous Week's Releases and Next Week's Releases on next page.

Previous Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
3-Nov	ISM Manufacturing	October	49.1	50.1	49.0	**48.7**
	ISM New Orders	October	48.9	50.0	NA	**49.4**
5-Nov	ISM Services Index	October	50.0	51.0	50.7	NA
7-Nov	U. Michigan Sentiment	November	53.6	55.0	54.0	NA

Next Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
20-Nov	Existing Home Sales	October	4.06 Mln.	NA	NA	NA

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