

Q3 2025 OUTLOOK: FEAR AND HOLDING ON WALL STREET

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“In the fifteenth century, Giovanni Pico della Mirandola claimed to have read every single published text in general circulation, which back then amounted to maybe a gigabyte of data. We currently produce that much information every thirty milliseconds.” – Sam Kriss

It was somewhere around 10:29 AM when her Zoom ended with a wave at the camera. Not even enough time to grab a coffee before her 10:30. Megan frowned. Then scowled at the ticker running across her third monitor. The life of a financial advisor is not for the faint of heart.

She put on a professional smile to greet Dr. Oscar Z. Acosta Jr., her newest client.

“Long week?” Megan asked, as they shook hands, noting the dark circles under his eyes.

The doctor exhaled and collapsed into a chair. “Every time I get a news alert, I feel a bit lightheaded. I’m averaging 300 a day. How long can I maintain, I wonder? If Powell sneezes, my phone vibrates.”

Megan paused and leaned forward. “Why follow the news?”

He paused. “Well, if I don’t, then I lose my edge.”

A smirk flashed over Megan's face. Her old sales manager would not have approved. "Your edge? Markets price new data in picoseconds, you can't beat that."

"So you're saying my information edge is... nonexistent?" he said with a resigned smile.

"I'm saying your edge is deciding where not to look. As your financial advisor, I suggest that your information diet needs Ozempic. I'm here to worry about the market for you. Buy the ticket, take the ride. Let's try it my way."

Three months later they met again.

Megan: "How are you doing Oscar?"

Oscar: "I've received twelve alerts today. Four from you, eight from my patent attorney."

Megan: "Patent attorney?"

Oscar: "Turns out when you're not glued to market noise, you have time to finish a side project. My high-powered coronary stent prototype is being considered for mass production. The royalty check is funding a new 'alts sleeve.'"

Megan smiled. "See! Your attention compounded faster in your lab than it ever would on a trading app."

A hard lesson for investors to learn is that passive investing isn't 'doing nothing.' It's protecting the bandwidth that earns money. Markets compound capital; people compound skill. Sometimes the smartest trade is to receive less information and let time in the market do its work.

Below we recap Q2's market moves below and then look ahead to what the second half of 2025 might have in store.

U.S. Economic Performance

- **GDP Rebound:** Real GDP is on track to grow by 2.6% in Q3 2025, according to the July 9th from the Atlanta Fed's GDPNow Model. This reflects continued recovery, supported by steady consumer spending and improved export activity, though momentum has slowed from the prior quarter.
- **Job Market Remains Steady:** Total payrolls increased by 147,000 in June, with unemployment edging down to 4.1%. Hiring remained resilient, led by health care and hospitality, despite softer gains in manufacturing and government.
- **Consumer Confidence Slips in Q2:** Sentiment weakened after a brief rebound in Q1. The Conference Board's consumer confidence index fell 5.4 points in June to 93.0, as concerns over inflation, tariffs, and job prospects weighed on both current conditions and future expectations.
- **Trade Tensions Escalate:** A new tariff deadline has been set. After Aug. 1 tariffs of up to 40% on 14 nations are threatened. While no deals were finalized, markets held steady as investors viewed the deadline as flexible, though extended uncertainty around enforcement and sector-specific rates still weighs on sentiment.

Monetary Policy

- **Fed Holds Steady, Signals Caution:** The Federal Reserve kept interest rates steady at 4.25%–4.5% through Q2 2025, as core inflation remained elevated and growth showed signs of cooling.
- **Rate Cuts or Rift:** The June 2025 dot plot projects a 50 bps cut by year-end, but Fed officials are split. Governor Waller, seen as a possible Trump pick to replace Powell, backed a July cut, citing muted tariff effects, while Powell and others prefer to wait amid lingering inflation and uncertainty.

- **Deficit Pressures Build:** U.S. debt remains above \$36 trillion, and the federal deficit is expected to rise to 6.4% of GDP in 2025. The “One Big Beautiful Bill” could add \$2.4 trillion to the deficit over the next decade, with over \$1 trillion expected in just 2026 and 2027.
- **Inflation Slowed, Though Friction Remains:** Price growth slowed steadily but unevenly, with headline PCE inflation dropping to 2.1% in April, down from 2.6% at year-end. Core PCE also eased to 2.5%, though new tariffs and persistent cost pressures suggest inflation may remain slightly above the Fed’s target.

Credit Market Performance

- **Default Forecast Steady Amid New Risks:** According to S&P Global, the US leverage loan default rate fell to 1.23% in Q1 2025 but is expected to climb to 1.75% through March 2026. The anticipated rise is driven by growing global trade uncertainty, along with expectations of rising unemployment and inflation.
- **Credit Spreads Tighten Sharply:** In Q2 2025, credit spreads narrowed by 75–150 bps, reflecting improved market sentiment and stronger lender competition despite lingering macro uncertainty.

US and Global Market Summary

- **Market Momentum Builds:** The S&P 500 saw record highs and Nvidia just became the first \$4 trillion dollar company. The economy keeps growing, consumers keep spending, and investors keep buying.
- **AI Infrastructure Spending Surges:** In Q2, escalating demand for AI processing power fueled a 154% year-over-year jump in NVIDIA’s data center revenue, as hyperscalers, enterprises, and governments ramped investment, solidifying AI infrastructure as a long-term capital priority.
- **Earnings and Economy Fuel Optimism:** Q2 S&P 500 earnings rose 4.9% year-over-year, marking the eighth straight quarter of growth. A resilient labor market, easing inflation, and the prospect of Fed rate cuts continue to support investor confidence.

Markets*

	As of 6.30.2025	Q2 Return	2025 YTD
S&P 500	6,204.95 pts	10.2%	5.5%
NASDAQ	20,369.73 pts	16.7%	5.5%
The Dow	44,094.77 pts	5.0%	3.6%
Global Equities		11.5%	7.0%
Emerging Markets		10.0%	15.4%
Energy		-9.8%	-1.0%
Gas	\$3.68/gal	-0.3%	4.3%
Gold	\$3,303.14/oz	6.1%	25.9%
VIX	16.73 pts	-23.2%	-3.6%
10-Yr Treasury	4.228%	5.9 bps	-34.1 bps

*See endnotes.

Alternatives*

	Q2 Return	2025 FY
Direct Lending	-2.7%	-2.0%
CLOs	2.4%	3.8%
Private Equity	6.5%	3.1%
Hedge Funds	2.5%	1.8%
Equity REITs	0.2%	2.9%
Residential REITs	-6.7%	-3.9%
Industrial REITs	-6.6%	-1.8%
Wine & Cheese	-6.1%	-15.1%
Crypto Market	25.2%	-11.7%
SPACs	30.1%	10.8%

*See endnotes.

Tariff Turmoil Turns to Noise

The quarter started off with a thud. When “Liberation Day” tariffs were announced on April 2, the market reacted poorly. The S&P 500 plummeted by a dramatic 12% in a matter of days. Prognosticators predicted chaos, decline, and recession.

Surprising most, equity markets quickly bounced back. Less than a month later, the S&P had recovered. By the end of the quarter, after all the *sturm und drang*, the index was up over 5% year-to-date. Tariffs may be back on the calendar, but the markets have barely reacted.

After a quarter defined by panic and relief in equal measure, the takeaway is clear: staying invested through turbulence remains the better bet.

Recession Fears Fade

As we look ahead, uncertainty persists, but so does the market’s ability to absorb shocks and reset. Financial conditions have caused analysts to decrease their recession probability estimates, albeit modestly. Goldman’s 12-month estimate of recession odds was trimmed from 35% to 30%.

Fund manager expectations of a recession have significantly declined since April, with 36% saying a recession in the next year is “unlikely.”

Recession Expectations Have Peaked

Net % say global recession is likely —



Source: BofA Global Fund Manager Survey

Some Signs of Light Turbulence Ahead

However, employment seems to be softening. Increases in Worker Adjustment and Retraining Notification (WARN) Act notices are concerning. WARN Act notices are filed 60 days before the anticipated layoff event and can be a leading indicator of future unemployment. The number of notices jumped to the highest level since August 2023.

Total JOLTS Hires Rate vs Total WARN Notices

JOLTS: Hires Rate: Total - SA, % 

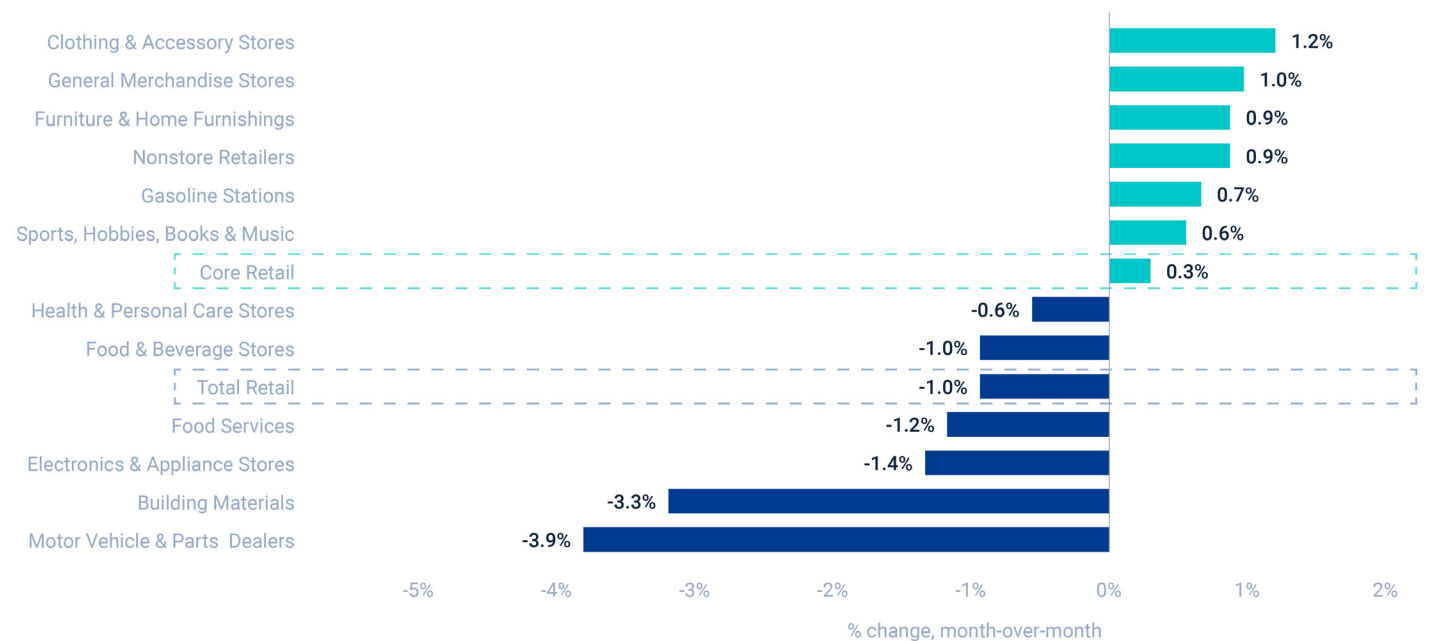
WARN Notices: FRB of Cleveland WARN Number of Implied Layoffs - SA, Number 



Sources: BLS, FRBCLE/Haver

And there are additional signs of economic weakness. Retail sales volumes fell in May, led by auto-related sales declining nearly 4%. Even food and beverage sales, which shouldn't have seen any tariff turbulence, declined.

US Retail Sales Adjusted for Inflation - May 2025



Source: US Census Bureau, BLS, EY-Parthenon

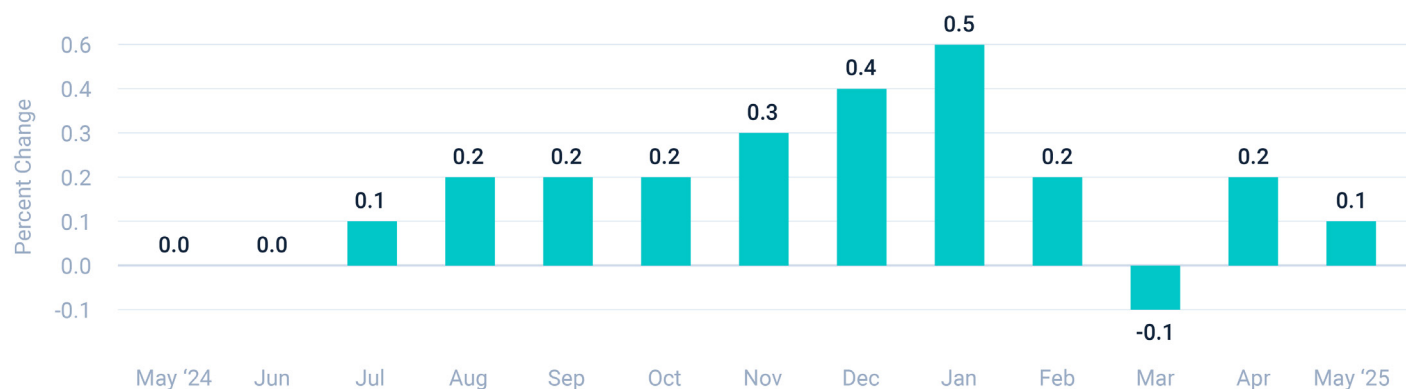
Many investors are now watching inflation prints and consumer spending for confirmation that the rebound is sustainable while, of course, ever-present tariff strife continues to impact the market.

All Eyes on the Fed

For the 4th month in a row CPI came in below consensus expectations, confounding beliefs that tariff driven inflation would materially impact CPI. With muted inflation, will the Fed lower rates? Currently, the Fed is still expected to lower rates by 50 bps sometime this year, which isn't fast enough or low enough for the executive branch. CME futures, the price of which act as implied probabilities, show a 75% chance of lower rates by year end, and a 30% chance of two 25 bps cuts. The US must refinance \$11 trillion of debt over the next year, and if rates stay high, it will add hundreds of billions of dollars in interest payments.

One-Month Percent Change in CPI for All Urban Consumers (CPI-U)

Seasonally Adjusted, May 2024–May 2025



Source: Data, BLS. Chart, CPIinflationcalculator.com

Inflation Isn't Done Yet

One-year inflation expectations dipped to 3.0% in June, down from 3.2% in May, according to the Fed's Survey of Consumer Expectations. But the story might not be that simple. Some analysts think inflation will rise in the second half of the year. Asset manager Guggenheim thinks we are in the "eye of the storm" in that price impact to policy changes have yet to hit. They anticipate an increase of core personal consumption expenditure PCE above 3 percent by the end of the year.

Conclusion

The meeting concluded as dramatic headlines scrolled across the muted office television. Oscar gestured at the TV. "Those things used to phase me. But now I'm too busy to notice; I'm ready to ride this out."

"Exactly," Megan replied. "You're learning. Time in the market beats timing the market; miss the best days and half your gains vanish. Hold steady and let the process run."

The journey to long-term gains does not have to be a savage one. Long-term investing wins because time does the compounding for you; patience is the key. A balanced mix of broad equity indexes, high-quality bonds, and other volatility mitigating assets keeps your portfolio on course when headlines churn. Assets should be owned, not nervously watched.

Endnotes

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"Crypto Market" represented by the Bloomberg Galaxy Crypto Index. "NASDAQ 100" represented by the NASDAQ 100 Index. "S&P 500" represented by the S&P 500 index. "Private Equity" represented by the Invesco Global Listed Private Equity ETF. "Direct Lending" represented by the DLX Direct Lending Index. "US Residential REITs" represented by the MSCI US Residential REIT Index. "CLOs" represented by the Palmer Square CLO Debt Index. "Leveraged Loans" represented by the S&P/LSTA Leveraged Loan Total Return Index. "High Yield Bonds" represented by the Bloomberg Barclays US Corporate High Yield Total Return Index Value Unhedged. "Gold" represented by the SPDR Gold Shares. "Emerging Markets" represented by the iShares MSCI Emerging markets ETF. "Investment Grade Bonds" represented by the Bloomberg US Corporate Bond Index. "Hedge Funds" represented by the Bloomberg All Hedge Fund Index. "Equity REITs" represented by the MSCI World Equity REIT Index "Financials" represented by the Financial Select Sector SPDR Fund. "Telecom" represented by the iShares US Telecommunications ETF. "Utilities" represented by the Utilities Select Sector SPDR Fund. "Commodities" represented by the Invesco DB Commodity Index Tracking Fund. "Oil" represented by the United States Oil Fund LP. "VIX" represented by the Chicago Board Options Exchange's CBOE Volatility Index. "Natural Gas" represented by the United States Natural Gas Fund LP.

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