

U.S. EQUITY MARKET OUTLOOK

NAVIGATING Q3 2025



The market landscape has transformed dramatically in just a few short months.

The second quarter demonstrated remarkable market resilience and volatility. The S&P 500 delivered impressive gains of 10.5% during this period, a surprising turnaround following the sharp 15% selloff triggered by tariff announcements in early April. This dramatic recovery saw the index climb 28% from its April trough, pushing year-to-date performance into positive territory at 6%.

International markets experienced varied impacts from trade policy developments, though many outpaced U.S. equities in the first half of the year. This outperformance was amplified by the dollar's 11% weakening. European markets particularly excelled with 24% gains in dollar terms through June, while emerging markets posted solid 16% returns.

Trade negotiations remain fluid, suggesting ongoing market volatility ahead. However, financial markets appear to have absorbed much of the initial shock as negotiation parameters have become clearer. Attention may now shift toward other policy initiatives including corporate tax changes and regulatory adjustments in technology and financial sectors, which could provide upward momentum for domestic equities.

The evolving policy environment has prompted questions about corporate and consumer adaptation strategies. Research suggests the economy has demonstrated notable flexibility during this transition period.

Market participants seem to be adopting a longer-term perspective rather than responding to individual economic releases. Risk appetite measurements showed recovery starting in May, returning to pre-volatility levels by summer. This sentiment improvement may signal increased confidence in policy direction and support for sustained market optimism.

European equity performance has shown mixed results across sectors. Future gains will likely depend on broader fundamental-driven stock selection and successful implementation of structural reforms and investment programs regionwide.

Looking toward the latter half of 2025, expectations point to persistent volatility alongside positive long-term equity prospects. Geopolitical developments and economic indicators will likely maintain market uncertainty. Given the complex policy and global landscape, broad market exposure may prove less reliable for returns, potentially elevating the importance of specialized analytical capabilities and differentiated investment strategies.

Current US Equity Valuation Analysis Shows Modest Overvaluation

Morningstar’s comprehensive analysis of more than 700 US-listed securities indicates the domestic equity market is currently priced at approximately 1% above intrinsic value as of late June 2025. This slight premium, while manageable, places current valuations in territory that has been exceeded less than 30% of the time since 2010.

This valuation level represents a significant shift from early spring conditions when equities were trading at a substantial 17% discount to calculated fair values. The rapid price appreciation has brought market pricing much closer to fundamental valuations.

Style and Size Considerations

Value-oriented securities continue to present opportunities, with our analysis showing these stocks trade at a 12% discount to fair value. Conversely, growth stocks appear stretched at an 18% premium to intrinsic worth. Such elevated growth premiums are uncommon historically, with the most recent comparable instance occurring in late 2024 before technology sector corrections began.

From a capitalization perspective, smaller companies offer the most compelling risk-adjusted opportunities, trading 17% below estimated fair value. Mid-capitalization stocks appear reasonably

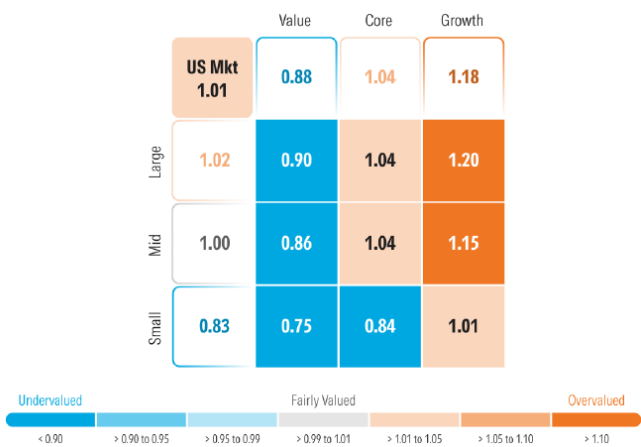
priced near fair value, while large-cap securities carry a modest 2% premium.

Strategic Implications

These valuation disparities suggest tactical allocation adjustments may be warranted. The discount in small-cap valuations relative to large-cap premiums presents a potential opportunity for investors willing to adjust portfolio weightings accordingly. Similarly, the substantial gap between value and growth stock pricing may favor style rotation strategies.

Current market conditions require careful consideration of valuation metrics alongside other fundamental factors when making investment decisions.

US Stock Market Trading Above Fair Value Estimate
Valuations of Morningstar’s equity research coverage by equity style box.



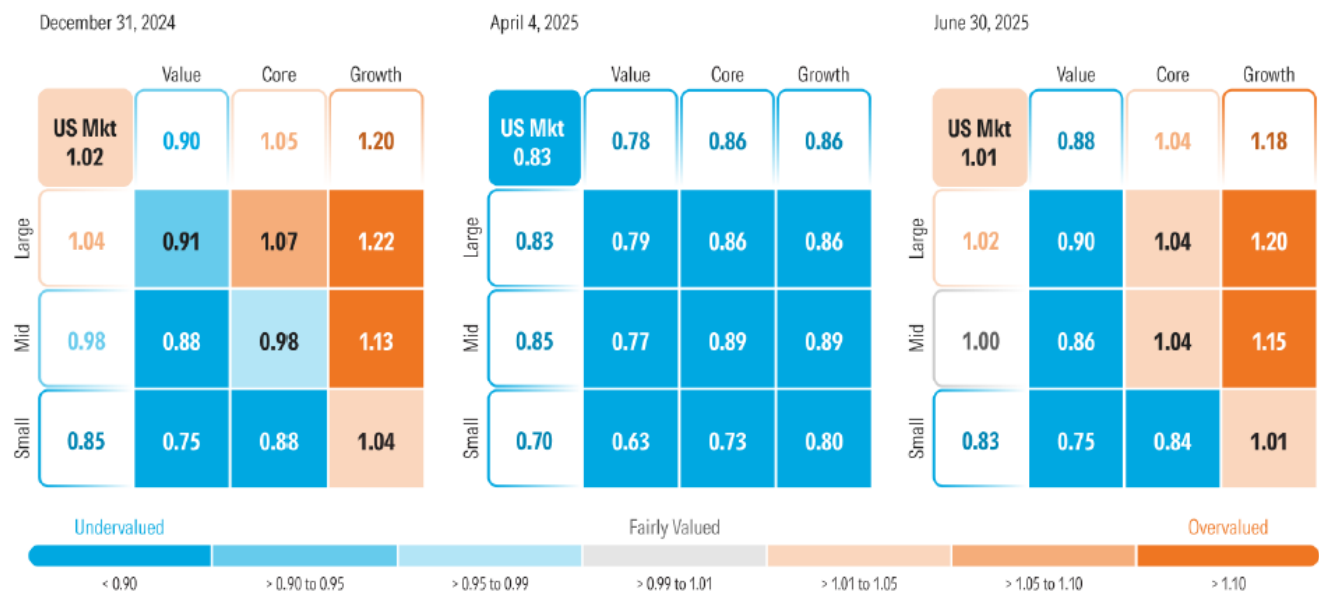
Dramatic Market Volatility Cycle Concludes with Return to Premium Valuations

The equity market experienced an extraordinary valuation cycle during the first half of the year. Beginning from elevated levels where stocks traded above fundamental estimates, markets underwent a sharp correction that drove valuations to deeply discounted territory. The selloff reached its most severe point in early April, with equities trading at a substantial 17% discount to calculated fair values on April 4th.

This dramatic undervaluation proved short-lived, as markets quickly reversed course and embarked on a powerful recovery rally. The rebound was as swift and decisive as the preceding decline, ultimately propelling stock prices to new record highs. By the end of this volatile period, the market had completed a full cycle, returning to trade at a modest premium above fundamental valuation estimates.

This sequence of events highlighted both the market's capacity for rapid repricing and its tendency to overshoot in both directions during periods of uncertainty. The speed of both the decline and subsequent recovery underscored the dynamic nature of equity valuations in response to changing conditions and investor sentiment.

Change in Morningstar Equity Research Coverage Price/Fair Value Estimates Over the Course of the Year



Market Resilience Emerges After Challenging Second Quarter

Major U.S. equity indices, including the S&P 500 and NASDAQ, reached record levels during the second quarter despite experiencing significant volatility following trade policy announcements in early April. Although policy uncertainties and global tensions persist, cautious optimism appears warranted as markets enter the latter half of the year.

Much of the recent market movement stems from sentiment shifts rather than deteriorating corporate fundamentals. This environment presents challenges for investors navigating complex conditions and addressing common concerns.

Should I invest when markets are at record levels?

Investors often face psychological barriers whether markets are declining or advancing. During downturns, there's fear of further losses, while at peaks, concerns about buying at the top emerge. Historical evidence suggests that precise market timing rarely proves beneficial, and maintaining consistent investment discipline typically outperforms attempting to time entries and exits, especially when underlying fundamentals remain sound.

Data demonstrates that purchasing at local market peaks has minimal impact on subsequent one-, three-, and five-year returns. New market highs occur

regularly, with the S&P 500 averaging 18 record closes annually since 1957, making them a normal market feature rather than cause for concern.

What volatility should we expect going forward?

Continued market fluctuations appear likely given ongoing policy uncertainties, Federal Reserve decisions, and geopolitical developments. However, volatility often creates opportunities in fundamentally strong companies. While some corporations have withdrawn earnings guidance amid macro uncertainty, management commentary generally indicates limited trade-related impacts. Current consensus expectations project 5% earnings growth for Q2 and 9% for full-year 2025.

Analysis reveals that stock price volatility historically exceeds earnings volatility, suggesting market reactions to macro concerns often exceed actual business impact. This dynamic emphasizes the importance of careful stock selection and building portfolio resilience during uncertain periods, particularly when markets trade near highs.

How can portfolios be strengthened for resilience?

Three core elements enhance portfolio durability: quality, valuation, and diversification.

Quality Focus Companies with consistent earnings histories represent

prudent choices amid mixed economic signals. Quality enterprises typically maintain strong cash generation, solid balance sheets, and pricing power that helps preserve market position during economic pressures.

Dividend payment records serve as additional quality indicators. Dividends demonstrate lower volatility than both stock prices and earnings, as management teams typically avoid cuts that might alarm investors. This discipline has historically helped dividend-paying stocks, particularly those with growing payouts, outperform during downturns.

Valuation Considerations Investment success depends on the relationship between price paid and value received. Many fundamentally strong large-cap stocks currently trade below their earnings potential, as markets have favored select AI-beneficiary companies.

However, large-cap growth stocks shouldn't be dismissed solely on price. Leading technology companies often display quality characteristics including high profitability and cash generation that may justify premium valuations. This distinguishes them from more speculative growth investments that expose investors to significant downside risks.

Diversification Benefits Portfolio balance becomes more valuable during dramatic market reversals. Sectors and factors most affected during April's

decline subsequently led the recovery. Portfolios combining traditionally defensive sectors like healthcare with growth-oriented technology exposure may better withstand sentiment-driven volatility than those with concentrated risk exposures.

Strong innovation potential in both sectors supports long-term growth prospects while offering stability elements. Today's technology sector, particularly software, functions as essential infrastructure for modern life. Healthcare segments outside pharmaceuticals, including services and medical devices, exhibit quality characteristics with stable earnings, growth potential, and attractive valuations.

Accepting Market Reality

Stock markets respond to macro concerns and investor reactions, sometimes dramatically. However, corporate fundamentals and earnings capabilities prove less erratic and historically drive long-term investment outcomes.

Volatility and accompanying new highs need not disrupt long-term investment objectives. Emphasizing resilience can strengthen portfolios while providing investors the confidence to navigate turbulent markets. The key principle: maintain investment discipline through prudent portfolio construction

Sector Outlooks – Summary

Basic Materials: The sector underperformed in Q2 but remains attractive, with many names trading below intrinsic value. Chemicals stand out, where domestic cost advantages and stabilizing crop-protection sales provide long-term growth drivers despite tariff uncertainty and slowing durable goods demand.

Communication Services: Meta and Alphabet continue to dominate digital advertising, though growth rates are maturing. While ad volumes have slowed, both retain significant network effects and AI capabilities to defend share. Canadian telecoms remain undervalued, and Warner Bros. Discovery's planned split could unlock value.

Consumer Cyclical: Despite a strong quarter, the sector still trades at a discount to fair value, particularly in travel/leisure and apparel. Weakness in airline traffic reflects corporate travel cutbacks, but leisure demand remains resilient. Investors can find bargains among well-positioned brands and service providers.

Consumer Defensive: Defensive stocks are mixed. Food producers and packaged goods companies look undervalued as they improve margins and supply chains. Some large retailers trade at stretched valuations, but select names offer

attractive entry points.

Energy: Oil's retreat weighed heavily on the sector, with integrated majors dragging returns. That said, select refiners and service providers look cheap relative to fundamentals. Medium-term demand and cost discipline could support a rebound.

Financial Services: Large banks remain undervalued, particularly those with strong efficiency and diversified models. While rate cuts may pressure margins later this year, capital return policies and normalized credit costs should underpin earnings.

Healthcare: The sector was hurt by policy concerns and the sharp selloff in UnitedHealth, which accounted for most of the weakness. Still, pharma and med-tech companies with wide moats offer long-term opportunities at attractive valuations.

Industrials: Solid performance continues, driven by aerospace and defense. Infrastructure spending and corporate investment are supportive tailwinds. Valuations vary widely, but select contractors and manufacturers trade below fair value.

Real Estate: Still pressured by higher financing costs and uneven demand, though some REITs with quality portfolios trade at significant discounts. Office

remains challenged, but residential and healthcare-oriented REITs show relative strength.

Technology: Tech led markets higher, powered by mega-caps. AI-driven demand is strong, but valuations are stretched in certain names. Opportunities exist among select semiconductors, software firms, and service providers

transitioning effectively to cloud models.

Utilities: Unexpectedly the best-performing sector in the first half, benefiting from falling interest rates and AI-related infrastructure demand. Valuations have risen but remain reasonable for some regulated players.

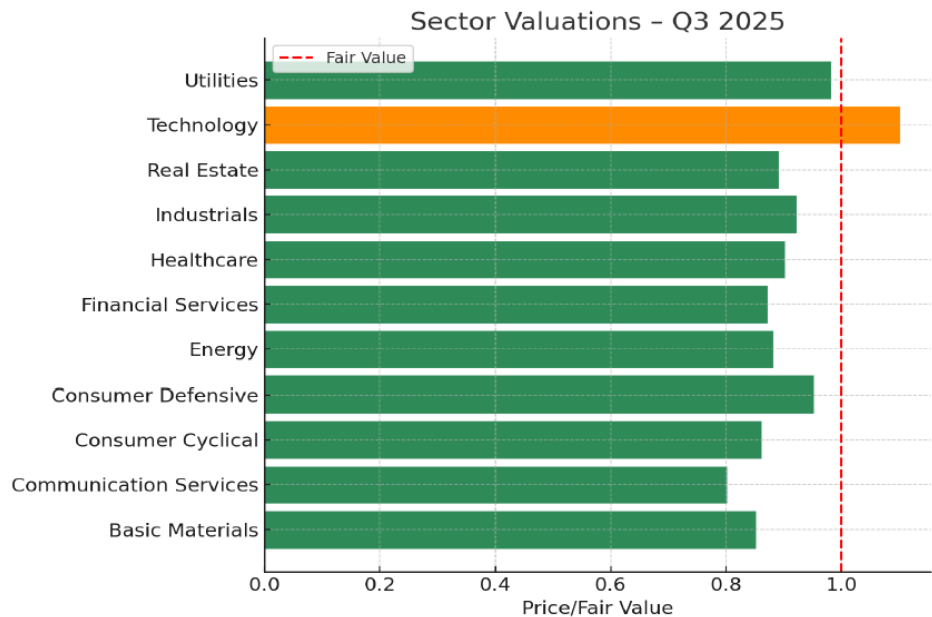
Sector Snapshot – Overview

Sector	Outlook Summary
Basic Materials	Underperformed but chemicals and crop protection offer long-term growth; many names undervalued.
Communication Services	Meta/Alphabet still dominant though maturing; Canadian telecoms cheap, WBD split could unlock value.
Consumer Cyclical	Sector rebounded; travel/leisure and apparel discounted, leisure demand resilient despite corporate travel pullback.
Consumer Defensive	Food and packaged goods improving margins; some large retailers stretched, select value remains.
Energy	Oil weakness hit majors; refiners and service firms undervalued, cost discipline may drive rebound.
Financial Services	Large banks still cheap; efficiency and capital returns supportive even as rates ease.
Healthcare	Dragged down by UNH; wide-moat pharma/medtech remain long-term buys at discounts.
Industrials	Strength in aerospace/defense and infrastructure; some contractors/manufacturers undervalued.

Real Estate	Higher rates weigh, but quality REITs trade at discounts; office challenged, residential/healthcare stronger.
Technology	Mega-caps drove rally; AI demand strong, valuations stretched. Semis/software/cloud leaders still offer opportunities.
Utilities	Top performer in H1; benefited from falling rates and AI infrastructure demand. Valuations up but selective value remains.

Source: Morningstar Equity Research, June 30, 2025 | Compiled by Together Forward Capital

Together Forward Capital | Market Insights



This chart illustrates the relative valuations of each sector, expressed as Price/Fair Value ratios. Bars in green indicate sectors trading below fair value (undervalued opportunities), while orange highlights those trading above fair value (potentially overvalued).

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