

The S&P 500 closed above 6500 for the first time on Thursday, followed by a Friday sell-off ahead of the holiday weekend. Nvidia's quarterly earnings release on Wednesday afternoon was the main event last week given the wide-ranging implications across the market. The key takeaway - AI-related spending remains robust with no signs of a slowdown. Given the magnitude of capital expenditures earmarked for investment across the AI ecosystem, ensuring that this secular trend remains firmly in place is critical for the bull market's go-forward longevity.

The other major headline of the week, which hit after the close on Friday - a federal appeals court ruled that most of President Trump's tariffs are unconstitutional. The broad-reaching tariffs will be allowed to remain in place until October 14, and it's likely the administration will appeal to the Supreme Court. If the higher duties are ultimately invalidated, this would be a welcome relief for American businesses and likely a positive for both corporate profits and the broader economy.

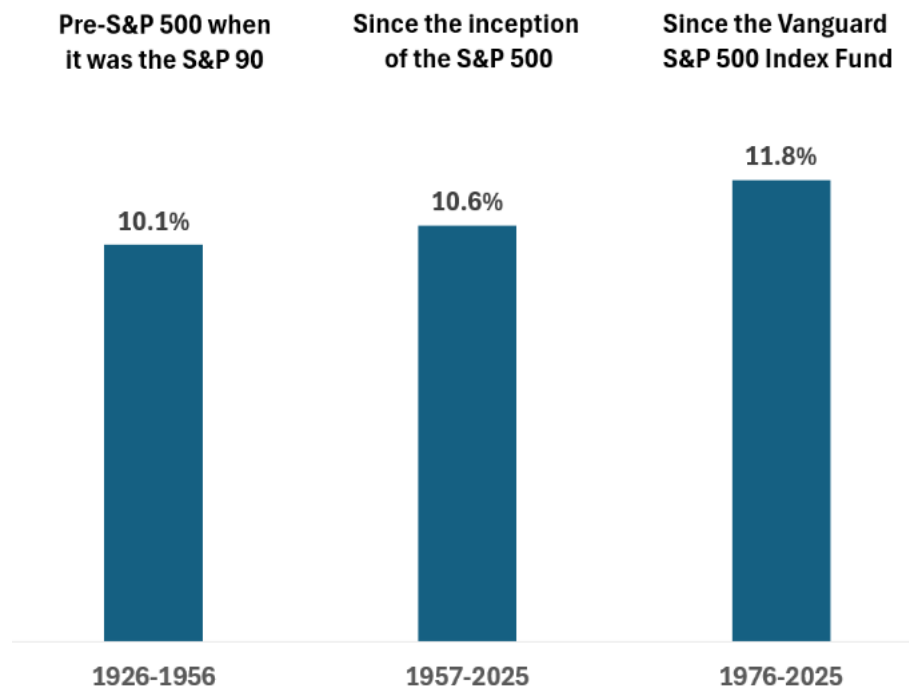
The persistent claim I hear from bears is that the current bull market is overextended. Since 2009, they argue, we've been in a long secular uptrend that is ripe for a steep reversal. The more extreme pessimists suggest that an early-2000s style meltdown, when the S&P 500 lost 49% of its value over roughly 2.5 years, is a major risk. At first glance, this claim appears to have merit; stock valuations are elevated compared to their historical norm, and it's been 17 years since the last severe bear market. While we've had some bumps and bruises along the way (i.e. Covid crash, 2022 bear market, some meaningful corrections / growth scares), temporary declines have generally been short-lived, and the S&P is nearly 10x higher compared to the low-point in early 2009. Furthermore, the bears draw parallels between the speculative technology-fueled bubble that formed in the late 1990s to what's currently taking place.

However, I believe these concerns are misplaced. Firstly, while the market has generally performed well since 2009, this immediately followed one of the worst extended bear markets in history between 1999 and 2009 (arguably, the secular bear market ended in 2013 when stocks finally reached new highs after nearly 14 years). Thus, we were due for a sustained and powerful multi-decade rally, which has occurred since.

Taking a longer view, however, U.S. stocks (S&P 500) have only generated roughly 8% annualized returns during this century, which is now more than a quarter old. Despite recent gains, this reflects one of the poorest 25-year stretches going back to the Great Depression. Thus, the argument that we are simply due for an extended bear market isn't credible in my view. While valuations are somewhat extended relative to history, given projected profit growth over the near to medium term, I don't believe that stock prices in the aggregate are especially overvalued.



#### **S&P 500 Annualized Returns By Historical Time Period**



Source: *A Wealth of Common Sense*

Furthermore, I also don't believe the comparisons between the current technology boom and the 1990s speculative bubble are warranted. Unprofitable (or low margin) tech firms,

often with unsustainable business models, which attracted investor interest in the 90s drove valuations to much higher levels. For example, at the high point in early 2000, formerly leading companies such as Qualcomm, Yahoo, and Cisco traded at price to earnings multiples of 192x, 739x, and 134x, respectively. Current market leaders aren't in the same zip code from a valuation perspective. Today's AI revolution is led by the largest and most profitable companies, with productivity gains spreading to other sectors. The internet boom of the 90s was built on hope for widespread internet adoption but often without concurrent profit expansion as capital flowed indiscriminately.

For the bears' fears to be realized, it would very likely require a corporate earnings recession. I don't see that forming on the horizon. Profit estimates are now trending higher, which reflects confidence regarding the go-forward prospects for the largest American companies. Generally speaking, it is difficult to imagine an earnings recession occurring simultaneously against a capital investment boom, especially one of this magnitude. As long as the outlook for profits remains rosy, I believe the longer-term bullish trend is likely to remain intact.

While I remain optimistic over the long-term, there are potential headwinds that are worth noting over the near-term. As we've written about previously, there are signs that the labor market is meaningfully softening. In addition, elevated tariffs, fully implemented for now, threaten to hit corporate profit margins and consumer wallets. Whether American companies and consumers will prove resilient and nimble enough to absorb an additional roughly \$500 billion in annual costs remains to be seen. However, on Friday, the personal income and spending data released for July reflected consumer strength while unemployment claims (released last Thursday) ticked slightly lower. Both of these data points were reassuring regarding the current health of the American consumer despite the negative pull from tariffs and a weaker jobs market.

If nothing is certain in life but death and taxes, bulls and bears are two of the market's few certainties. Regardless of the fundamental backdrop, there will always be those which forecast impending doom while others see only bright skies on the horizon. This dynamic is what makes a market function. I'd argue that the bearish camp, while correctly acknowledging several risks across the market and U.S. economy, may be currently missing the forest for the trees. However, their perspective performs the crucial function of curtailing speculative excesses. It was in short supply during the late 1990s (i.e. Greenspan's "irrational exuberance" reference in late 1996), and the sharp decline to kick off the 21<sup>st</sup> century was the price to be paid. I, for one, am thankful the bearish voices are louder today, which helps prevent "irrational exuberance" from fueling unsustainable market bubbles.

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