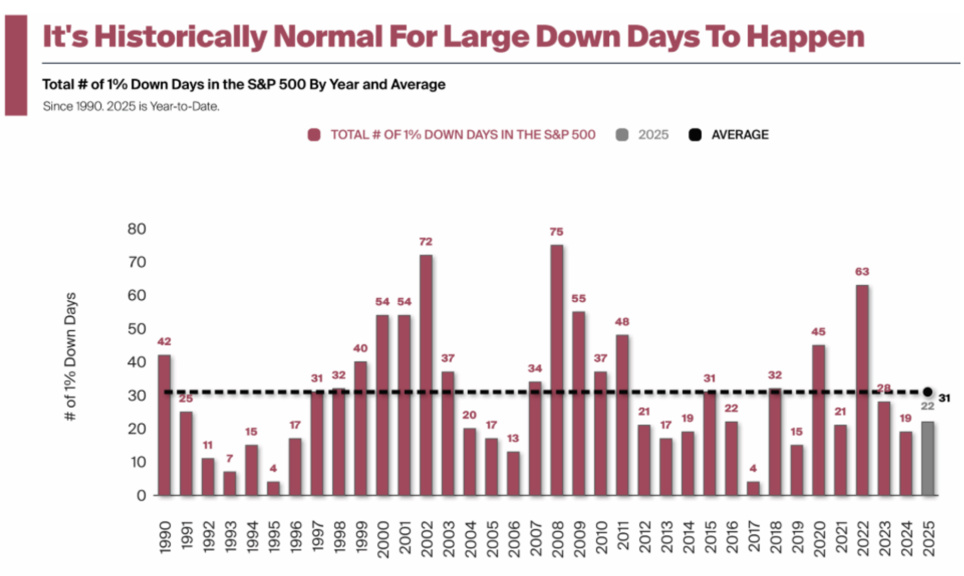
After stocks again reached new all-time highs, the week ended with a sharp move lower. On Friday, President Trump posted on social media that he is considering a sharp increase in Chinese tariffs and potentially other economic countermeasures. He also suggested that the planned upcoming meeting with President Xi may not take place. Given the magnitude of Chinese imports into the U.S., as well as China's rare earths refining capabilities, the sudden re-escalation regarding trade tensions sent stocks into a tailspin after the announcement. Following Friday's close, the President suggested he plans to impose an additional tariff rate of 100% on Chinese goods as well as export controls on "critical software" beginning on November 1.

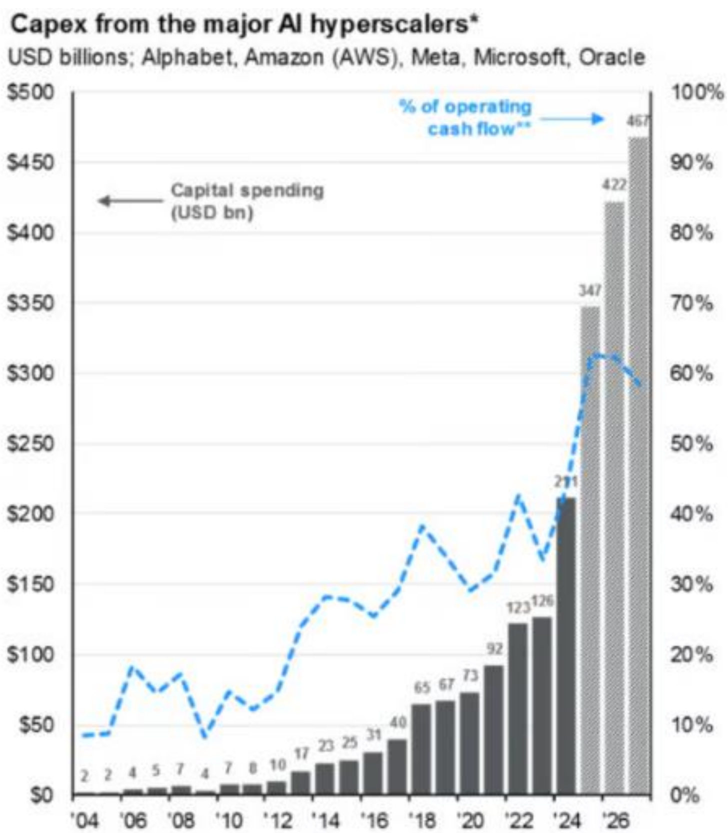
Investors had hoped that the Trump/Xi meeting scheduled later this month would signal progress towards a broader agreement between the U.S. and China. Markets found relief earlier this year when both countries dialed back embargo-level tariff rates and appeared to reach consensus regarding the framework for a trade deal. Should tariff levels again significantly rise, this may meaningfully increase costs for American importers and disrupt supply chains. Furthermore, given that China controls roughly 90% of the global rare earths supply, should they implement strict export controls, this may result in shortages for these critical materials. Following Friday's developments, the administration's stance appeared to soften over the weekend.

Friday's 2.7% decline was the worst day for stocks since April. Given that it's been basically a straight line up since the April lows, markets were likely overdue for a step back. While it remains to be seen if trade tensions will escalate further, a modest pullback from recent highs may be healthy in my view.



Source: A Wealth of Common Sense, FactSet

The set-up heading into year-end remains constructive, especially if tariff levels aren't ratcheted up further or if the Supreme Court strikes down the President's global tariffs altogether. Earnings growth, fueled by booming capital spending, has been robust and is forecasted to accelerate further. The predominate secular trend powering profit growth, AI-related spending, will in all likelihood only strengthen over the coming quarters and years. In essence, corporate earnings show no signs of peaking, which suggests that the current bull market is well supported by underlying fundamentals and likely has more room to run.



Source: A Wealth of Common Sense, Bloomberg

Quarterly earnings announcements start picking up this week, including the large banks on Tuesday and Wednesday. Bank results and credit metrics will provide further clues regarding the health of the U.S. consumer while many other companies will be offering fresh guidance regarding their forward outlooks. While the China question is the geopolitical "elephant in the room," like a bad movie that never seems to end, the on-going feud between our administration and China's leadership may not be fully resolved anytime soon.

Nevertheless, I remain optimistic regarding the fundamental picture for American businesses. While the labor market is somewhat weak, spending behavior and income trends suggest the consumer is holding up well overall. Credit spreads are still near all-time tights, which signals that a broad-based stress scenario is highly unlikely. Overall, while a negative black/grey swan event (i.e. China cutting off the rest of the world from their rare earths supply) is always a possibility, absent a major unforeseen macro event, I remain constructive regarding the outlook heading into year-end and 2026.

If anything, elevated geopolitical risk should encourage heavy domestic investment in critical areas such as rare earths refining, energy production, and defense-related sectors. This would only add to capital spending levels that are being greatly boosted due to AI-related initiatives. Hopefully, the market's recent jitters will be short lived and we can get back to focusing on corporate fundamentals, which currently appear very strong in my view.

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