

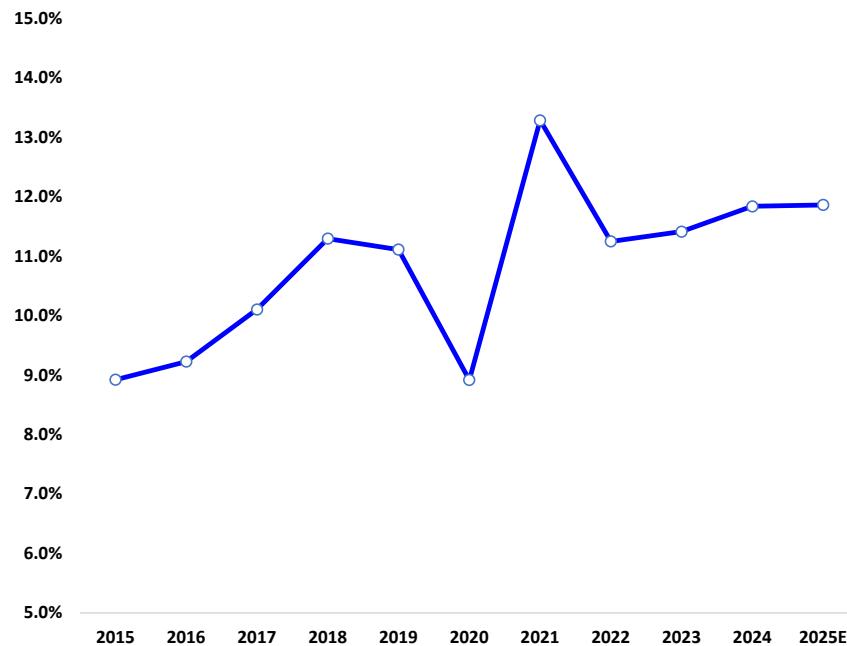
Andrew's Weekly Comment – June 2, 2025

Nvidia's quarterly earnings announcement was the dominant market event this week. While we could explore the specifics, including concerns regarding export curbs, the key takeaway is that end user demand remains robust, which is expected to continue for the foreseeable future. This has significant implications for the broader market given that such a large percentage of the S&P 500 is comprised of the largest technology companies leading the AI revolution. In addition, we expect massive productivity gains to accrue across companies within virtually every sector as AI adoption continues to scale quickly, boosting long-term profitability and broad-based economic growth. We'll expand on this topic further in this week's piece.

Major innovative shifts have historically shaped the economic landscape by increasing productivity, allowing businesses to generate a higher level of output more efficiently. Over time, this drives greater economic growth as more efficient technologies and processes are broadly adopted. Inventions that led to more efficient transportation methods, such as the steam engine or the airplane, for example, allowed goods to be delivered more quickly and at larger scale. This greatly reduced friction costs for businesses and consumers who ultimately benefited due to productivity gains. In our view, the modern-day equivalent is taking shape through AI technology, which we believe has the potential to greatly enhance output levels across both goods and services sectors. The current AI revolution, from our perspective, will ultimately have a similar impact to the industrial revolution that was essential in shaping our modern economy.

The market implications from AI include first, second, and third order effects. First, the companies leading the charge on the AI front will greatly benefit from strong end user demand through exponential revenue growth. That's already occurring and has driven a significant share of profit growth across the market in recent years. The second effect includes the efficiency gains for end users due to widespread AI adoption, which should lift profit margins over the long term. The third order effect includes more optimal capital allocation for companies as they compound higher profits to drive greater shareholder value. Therefore, we are optimistic regarding the outlook for American businesses given our view regarding continued margin expansion and tailwinds supporting profit growth over the medium to longer term.

S&P 500 Profit Margins: 2015-2025 (Estimated)

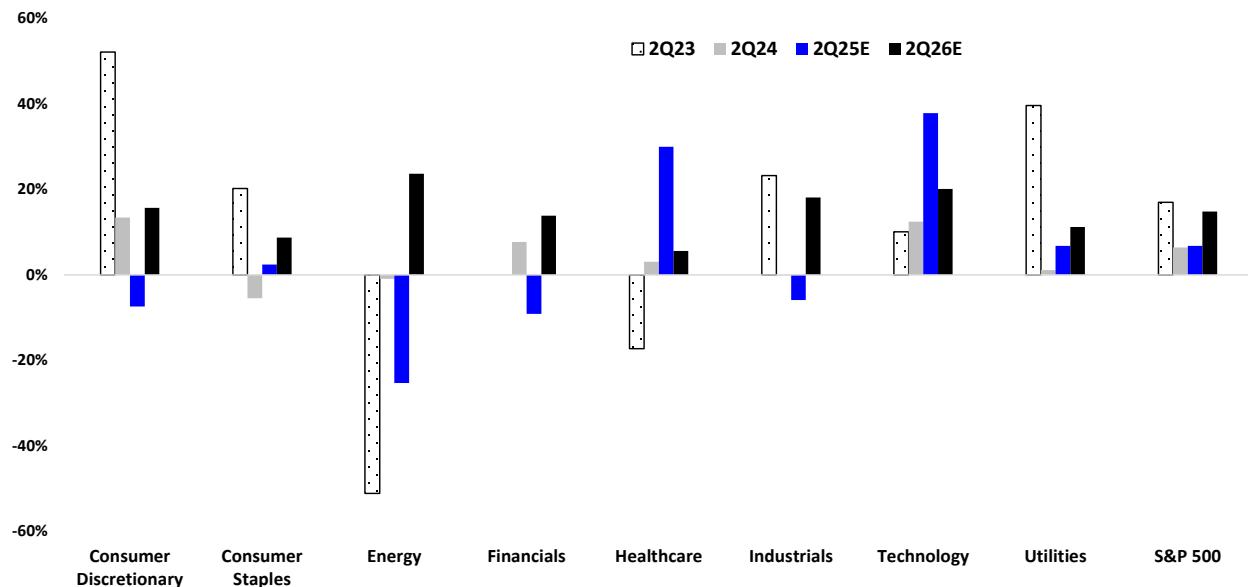


Source: S&P Global

We believe it is always helpful to take both a micro and broader view when analyzing market events. This can include the implications from a specific company's financial results and commentary, economic data, or an external shock event. As investors, it is our job to interpret a constantly evolving landscape and data points when managing client portfolios, positioning both tactically and in accordance with longer-term strategic objectives. As portfolio managers, separating the noise from material developments is key when assessing future implications for specific companies, sectors, and asset classes.

During these weekly updates, we generally like to share our thoughts regarding the broader market backdrop versus diving into a specific company's developments. However, when a company's earnings, commentary, or guidance has wide-ranging impacts, we also want to share our thoughts regarding broader implications. We are closely monitoring profit growth expectations across sectors, parsing for clues regarding the health of the economy and shifts in business and consumer demand. Overall, most forecasters expect profit growth to remain strong through the end of next year. Not surprisingly, much of this profit growth is driven by the largest technology companies, which has been the case since this bull market began in late 2022.

S&P 500 Earnings Growth By Sector: 2Q23-2Q26 (Estimated)



Note: Excludes 2Q23 growth for the financial services sector

Source: S&P Global

Going forward, we are looking for evidence that profit expansion has broadened outside of large-cap technology companies to other sectors such as consumer goods, industrials, and financial services. Higher levels of personal income growth and further tax cuts would support rising corporate profits across all sectors over the near term. While there have been some small cracks in the labor market recently (i.e. slight uptick in weekly jobless claims), the economic data appears to be currently holding up well. As we turn the calendar into June, with 2025 nearly half over, the S&P is roughly flat for the year, although well off the lows which occurred in April shortly after “Liberation Day.” While the secular tailwinds from AI adoption outlined above support our long-term optimistic view, we also believe companies will need to deliver robust earnings growth over the near term to satisfy investors and drive this market meaningfully higher given current valuation levels.

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