

Dear friends of Arcus Capital Partners,

We hope this letter finds you well as we enter the new year. Q4 2025 saw equities extend their advance, though gains were uneven and increasingly reliant on central bank guidance rather than improving fundamentals. Fixed income returns were muted, with Treasury yields largely sideways despite two rate cuts. The U.S. dollar quietly strengthened, and commodities were mixed: weakness in energy and soft commodities were offset by exceptional strength in metals. Economic growth slowed unevenly, inflation remained elevated, the housing market cooled, and consumer spending displayed a pronounced K-shaped divergence—all underscoring the complex backdrop policymakers and markets must navigate heading into 2026.

### I. Market & Economic Overview

Equities extended their advance in Q4, but beneath the surface the tone was far less robust than headline index returns might suggest. While the S&P 500 finished the quarter modestly higher, momentum stalled meaningfully after October, with gains increasingly dependent on policy signaling rather than improving fundamentals.

Volatility reemerged around key inflection points, most notably the late-October FOMC meeting, where a surprisingly hawkish pivot by Fed Chair Jerome Powell—when markets had been pricing in multiple rate cuts through early 2026—combined with the ongoing government shutdown to cause equities to hit a wall. From that point, the S&P 500 sold off more than 5% peak-to-trough before being effectively rescued on the morning of November 21, the regular monthly options expiration, when New York Fed President John

Williams stated that a December rate cut was still “on the table.” At the time of those remarks, the S&P 500 was down roughly 1.5% premarket after a 3.5% high-to-low drop the prior day<sup>1</sup>.

While Fed communication ultimately helped stabilize equities, fixed income markets were notably less impressed. Despite two Fed rate cuts during the quarter, Treasury yields ended modestly higher at the long end, and bonds largely traded sideways overall<sup>1</sup>. The market’s reluctance to embrace the Fed’s pivot appears rooted in lingering inflation concerns and unease over the durability of a dovish stance amid still-elevated price pressures. Commodities likewise churned, with weakness across the energy complex offsetting continued strength in metals<sup>1</sup>. Gold and silver pushed to new all-time highs during the quarter, reinforcing their alignment with the prevailing secular regime. Meanwhile, the U.S. dollar quietly strengthened for a second consecutive quarter—an outcome at odds with the prevailing narrative of easing policy, expanding liquidity, and imminent dollar weakness<sup>1</sup>.

Macro visibility was unusually poor during the first half of the quarter, as the longest government shutdown in U.S. history effectively blinded markets to the evolving state of the economy<sup>2</sup>. While the shutdown likely contributed to a modest slowing in activity, its more immediate impact was informational: the near-total absence of government data left investors flying blind just as growth, inflation, and labor market dynamics were becoming more contested. Once data flow resumed, the picture that emerged suggested an economy losing momentum—but not collapsing<sup>2</sup>.

Economic growth slowed in Q4 from the robust pace seen earlier in the year, though the deceleration was uneven. Manufacturing stabilized though remained in contraction, while services



activity maintained its robust expansion<sup>3</sup>. Consensus estimates for Q4 GDP drifted lower over the course of the quarter, settling into the low-1% range by year-end, reflecting the combined effects of fiscal drag, tighter real financial conditions, and fading post-pandemic tailwinds<sup>1</sup>.

Inflation remained the central complicating factor. While headline inflation cooled modestly on energy weakness, underlying pressures proved more persistent. Goods disinflation stalled—in fact, the November reading was the highest core goods inflation since 2012—shelter inflation remained elevated (3.5% year-over-year) but continued to trend lower<sup>4</sup>. Core CPI and core PCE both remained well above the Fed’s 2% target, reinforcing concerns that inflation is proving more structural than cyclical. This persistence helps explain why markets responded so skeptically to the Fed’s easing cycle, even as policy rates moved lower.

The housing market continued to cool. Elevated mortgage rates, stretched affordability, and rising inventories weighed on both new and existing home sales. Construction activity slowed further, price appreciation decelerated meaningfully, and several previously resilient metros slipped into outright year-over-year declines. Housing, once a stabilizing force in the post-pandemic expansion, increasingly looks like a modest drag on growth heading into 2026<sup>5</sup>.

The consumer picture in Q4 was increasingly bifurcated. Aggregate spending held up reasonably well, as measured by core retail sales, but that resilience masked a pronounced K-shaped dynamic beneath the surface, with higher-income households continuing to account for a disproportionate share of consumption while lower-income consumers faced mounting strain. Rising credit card balances and increased reliance on short-term financing suggest that consumption at the lower end of the income spectrum is increasingly being sustained through leverage rather than income growth. This divergence helps explain how headline consumption can remain firm even as underlying financial stress builds and represents a potential vulnerability should labor

market conditions weaken further or financial conditions tighten<sup>6</sup>.

The labor market showed tentative signs of softening in Q4, most visibly in the unemployment rate, which rose from 4.3% to 4.6%<sup>7</sup>—a development that helped reinforce the Fed’s dovish pivot. That said, the broader set of labor indicators painted a more mixed picture: job openings increased and initial claims declined, while private payroll data weakened even as nonfarm payrolls remained modestly positive<sup>1</sup>. Taken at face value, these gains do not yet point to a material downturn in labor demand.

By year-end, the Federal Reserve had cut rates twice during the quarter, ended quantitative tightening, and begun signaling a return to asset purchases—albeit without clarity on scale, duration, or exit strategy. This combination of easing policy, persistent inflation, and slowing growth leaves markets entering 2026 with more questions than answers, and increasingly dependent on central bank reassurance to sustain risk appetite.

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## II. Global Equities

On the surface, U.S. equities posted a solid quarter, with gains of 2.7% in the S&P 500, 2.5% in the Nasdaq 100, 2.1% in the Russell 2000, and 1.4% in the equal-weighted S&P 500<sup>1</sup>. Yet most—if not all—of that performance was heavily front-loaded in October. Over the balance of the quarter, market momentum faded considerably; in fact, the Nasdaq 100 declined by 2.2% across November and December.

That lack of follow-through over the final two-thirds of the quarter was notable given the liquidity tailwinds ostensibly supporting equities. The Fed cut rates twice, ended quantitative tightening, and initiated what appears to be largely open-ended asset purchases. While the Fed has suggested these purchases will be wound down in Q2 2026, it offered little specificity around the timing or mechanics.



Offsetting those liquidity tailwinds, however, were a moderation in economic growth expectations—partly related to the government shutdown—a deceleration in earnings growth expectations from roughly 15% year-over-year realized growth in Q3 to an expected 8% in Q4<sup>8</sup>, and steadily deteriorating investor positioning<sup>9</sup>. Institutions began selling equities in late September, just ahead of the shutdown, and continued to do so throughout Q4. Retail traders, by contrast, crowded into leveraged long ETFs while largely eschewing leveraged short exposure<sup>10</sup>. Those imbalances suggest emerging headwinds for equities in the weeks and months ahead.

Sector performance reflected these crosscurrents. Health care led with an 11% gain, while technology and financials rose roughly 2% apiece. Utilities (-1.3%) lagged, likely pressured by rising long-duration bond yields<sup>1</sup>.

Another notable development was the growing dispersion within the AI trade, rather than the broad, uniform price appreciation that characterized earlier phases of the cycle. Google rose 29% following the introduction of its tensor processing units (TPUs), which reduce reliance on Nvidia chips, alongside the strategic advantage of its vast proprietary training data embedded within Google Workspace<sup>1</sup>. In contrast, Oracle—up 57% in Q2 and 29% in Q3—fell 30% in Q4 as investors began questioning the scale, capital intensity, and leverage associated with its aggressive AI-infrastructure push<sup>11</sup>. Meta (-10%) and Microsoft (-6%) also declined during the quarter, while Nvidia, long the emblem of the AI trade, finished essentially flat<sup>1</sup>.

Outside the U.S., developed market equities had a strong fourth quarter, rising 6%, while emerging markets added 1%<sup>1</sup>. After years of underperformance—and years of strategists invoking mean reversion—non-U.S. equities finally delivered meaningful relative outperformance in 2025. Developed markets outpaced U.S. equities by roughly 1,500 basis points, while emerging markets outperformed by about 700 basis points. Given the still-wide

valuation gap, this episode of outperformance is unlikely to be the last over the coming decade.

As we enter Q1, equities continue to benefit from meaningful liquidity support, but that support is increasingly counterbalanced by positioning and valuation headwinds. For now, positioning does not argue for aggressive downside, but it also offers little foundation for a strong, sustained advance—suggesting a market that remains vulnerable to catalysts but not yet resolved in either direction.

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### III. Fixed Income

Bond volatility retreated further in Q4, following its collapse in Q3—which itself was a normal reversion after the extreme fixed income volatility in Q2 surrounding Liberation Day. This muted volatility helped support equities, but it did little for fixed income returns. Bonds across the curve were essentially flat for the quarter, despite two Fed rate cuts<sup>1</sup>.

Specifically, the 2-year Treasury gained 0.2%, the 5-year 0.1%, the 10-year 0.1%, and the 30-year fell 0.3%<sup>1</sup>. Even after Powell's hawkish pivot in October, the subsequent rate cuts in October and December appear to have unsettled the long end of the curve, likely reflecting market concern about the inflationary impact of the Fed's easy stance—rate cuts, an end to quantitative tightening, and renewed asset purchases with uncertain exit guidance. Even amid moderating inflation, a cooling labor market, and slowing growth, long rates seemed to remain wary of a potential resurgence in inflation.

By the end of Q4, the 30-year yield stood at 4.84%<sup>1</sup>, just shy of the psychologically significant 5% level that in the past has triggered tighter financial conditions, increased bond volatility, and equity selloffs. Stretched equity valuations, particularly among long-duration equities such as unprofitable tech names, are ill-suited to elevated rates; the inability of rates to fall meaningfully likely constrained equities in Q4.



Credit spreads, like interest rates, were largely sideways over the quarter, though intra-quarter swings were notable<sup>1</sup>. With the U.S. fiscal backdrop still fragile—rising deficits and accumulating debt—policymakers are unlikely to tolerate a sustained rise in long-term yields that could destabilize the system. Against this backdrop, long-duration Treasuries remain richly priced relative to a secular environment of persistent inflation and are likely to deliver negative real returns over the cycle. While tactical rallies in longer-dated bonds will occur in the normal ebb and flow of markets, we continue to favor shorter maturities and inflation-protected securities.

#### IV. Dollar, Commodities, and Precious Metals

At first glance, the dollar continues to wear a veneer of weakness. That perception is reinforced by the fact that it finished Q4 nearly 2% off its mid-November highs, a drawdown large enough to keep the “weak dollar” narrative alive. And yet, beneath the surface, the tape tells a different story. The dollar quietly ended the quarter up just under 1%, following a 1.4% gain in Q3, and it remains firmly anchored to both intermediate- and long-term technical support<sup>1</sup>. This resilience is notable given the Fed’s decidedly dovish posture—rate cuts, an end to quantitative tightening, and renewed asset purchases—particularly when contrasted with the comparatively more hawkish stance adopted by several other major central banks. Under a more conventional framework, that policy divergence would be expected to pressure the dollar. Instead, the dollar’s durability has coincided with a renewed rise in long-end interest rates, suggesting markets may be increasingly attuned to the inflationary implications of the Fed’s easy stance. This dynamic bears watching, as a sustained rise in both the dollar and long-end rates would likely act as a constraint on investors’ appetite for equities.

Broad commodity indices ended Q4 modestly higher—up roughly half a percent—as they continued a nearly four-year consolidation following their 250% advance from April 2020 to June 2022<sup>1</sup>. Exceptional strength in metals was

offset by weakness in energy and soft commodities (e.g., cotton, sugar, and cocoa). That said, zooming out reveals a clear, steady upward drift in commodities since mid-2023<sup>1</sup>.

Energy has been the primary drag on the broader commodity complex over the past several years, with crude oil grinding lower from its post-Ukraine-invasion peak near \$120–\$130 to the mid-to-high \$50s<sup>1</sup>. At those levels, however, questions naturally arise as to how much further prices can fall before U.S. shale production becomes uneconomic. Moreover, any escalation in global tensions—whether involving Russia-Ukraine, Israel-Iran, or China-Taiwan—would almost certainly place upward pressure on energy prices as participants move to secure supplies.

Absent a recession, these dynamics suggest energy commodities may be carving out a floor near current levels. In that context, we would expect the gradual upward drift in commodities to persist, eventually giving way to a renewed uptrend that would mark the next leg higher in the secular commodity bull market.

Precious metals continued to perform strongly in Q4. Gold rose 12% (64% on the year), silver surged 50% (145% on the year), and both palladium and platinum advanced roughly 25% (up 74% and 124%, respectively, for the year). Gold miners broadly kept pace with bullion, gaining 12% in Q4 and finishing 2025 up approximately 155%<sup>1</sup>. The magnitude of the rally has been notable, with both gold and silver repeatedly pushing into new highs as the advance unfolded.

As we enter Q1, positioning remains meaningfully bullish for precious metals, though less extreme than it was from late September through mid-December<sup>9</sup>. The sector continues to align with the inflationary secular backdrop. Gold appears increasingly reflective of an evolving monetary regime, supported by sustained central bank accumulation and the growing use of gold in bilateral trade settlement among BRICS nations. Silver, meanwhile, continues to benefit from persistent structural supply deficits and robust industrial demand tied to solar energy, electric



vehicles, defense-related applications, and the ongoing buildout of AI data center infrastructure<sup>12</sup>.

While the path forward will almost certainly include periods of elevated volatility, sharp corrections, and cyclical bear markets, the underlying structural forces now in place suggest the coming decade remains fertile ground for continued precious metals appreciation.

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## V. Looking Ahead

As we noted at the conclusion of our Q3 commentary, “The macro environment remains complex.” That assessment remains apt as we enter Q1 2026.

On the surface, one might reasonably expect a more overtly bullish market backdrop. The Fed has cut rates, ended quantitative tightening, and begun largely open-ended asset purchases. Meanwhile, the administration continues to run the economy hot, with no apparent end to deficit spending.

And yet, U.S. large-cap equities have gone essentially nowhere for more than two months. Interest rates have risen over that span, perhaps reflecting market unease with the Fed’s accommodative stance and its potential inflationary consequences. Smart Money has been steadily selling since just ahead of the government shutdown—gradually and persistently, rather than in short, aggressive bursts—while retail participation has skewed increasingly bullish. Valuations remain extreme by many measures, composite equity relative sentiment is slightly bearish<sup>9</sup>, and the AI trade appears to be losing momentum as investors focus more on rapid data center depreciation and the absence of clear incremental returns on capital.

Taken together, these dynamics suggest that the easy money conditions of the past three years may be approaching their limits.

What could reawaken markets from their current torpor? Favorable inflation readings in the months ahead and/or better-than-expected earnings

results. The former could help relieve upward pressure on interest rates; the latter could temper valuation concerns.

Even in the event of renewed upside, however, it seems likely that Smart Money would continue to sell into strength, gradually pushing positioning toward a more decisively bearish extreme.

It is also worth noting that positioning in both the dollar and long-duration bonds sits on the verge of turning unfavorable for equities<sup>9</sup>. Should those shifts occur, the bias would likely be toward tighter financial conditions and renewed upward pressure on rates, with the 30-year yield again threatening the 5% level—an environment that has historically proven challenging for risk assets.

If composite equity positioning were more decisively bearish, the case for an outright pullback would be more straightforward. Instead, with positioning near the center of its historical distribution—where equities often churn rather than trend—the more probable outcomes are continued choppiness or, in a more extreme scenario, a blowoff move that fails to sustain and ultimately retraces. Adding another layer of complexity, President Trump has demonstrated a keen awareness of market dynamics and is unlikely to remain passive in the face of equity weakness during a midterm election year.

All told, it seems premature to expect sharp equity downside from current levels. At the same time, meaningful headwinds remain that would likely prevent a durable, sustained advance absent a clear catalyst from inflation data or earnings.

For now, we will continue to monitor how these dynamics evolve as markets return to a more normal rhythm of data releases and corporate reporting over the course of the quarter.

As always, we are available to discuss these topics and address any questions. Thank you for the trust you have in our firm.

Sincerely,

**Arcus Capital Partners**



**Sources:**

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9. CFTC & Relative Sentiment Technologies
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12. [Saxo](#)

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