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"The essence of risk management lies in maximizing the areas where we have some control over the outcome while minimizing the areas where we have absolutely no control."

— Peter Bernstein
Renowned economic consultant and historian, author of over
10 best selling books on markets and investing.
January 22, 1919 – June 5, 2009

Peter Bernstein was educated at Harvard and later served on the research staff at the Federal Reserve Bank of New York. After a career as both an economics professor at Williams College and later an investment manager at Bernstein-Macaulay, Bernstein became the first editor of the Journal of Portfolio Management, the industry gold standard for scholarly financial publications for both investment managers and academics. He authored over ten books over the course of his life and was an evangelist of the efficient market hypothesis.

While we are clearly living through a period of heightened policy change in the U.S., and its impact on financial markets is undeniable, these periods are not unusual. In fact, current levels of market volatility are lower than we would have expected given the speed and scope of the policy changes underway.

We know many of our clients' fear of the unknown drives them to change portfolio allocations based on short term views or perhaps their own personal disagreement or support of the current direction of public policy. While we understand the nature of these feelings, we would urge clients to avoid acting on emotion, whether positive or negative. Such decisions can have a high likelihood of undermining long term return potential.

We have long maintained that portfolios should be constructed around an investor's risk tolerances rather than predictions about future market prices. In that context, probabilistic thinking, rather than deterministic forecasting, offers a more dependable framework. Even as artificial intelligence (AI) becomes increasingly woven into everyday life, we remain skeptical that the future can be forecast with any consistent reliability. Consequently, our core recommendation continues to be diversification across a broad set of risk factors, we take some comfort in the fact that nearly all major economists misjudged the likelihood of a recession in 2025, and we are equally confident that such forecasting errors will recur.

FIGURE 1

RETURNS (AS OF 12/2025)	1 YEAR	3 YEAR	5 YEAR	10 YEAR
S&P 500	17.88%	23.01%	14.42%	14.82%
Dow Jones Industrial Average	14.92%	15.36%	11.58%	13.11%
Russell 2000	12.81%	13.73%	6.09%	9.62%
MSCI EAFE	31.22%	17.22%	8.92%	8.18%
MSCI EM	33.57%	16.40%	4.20%	8.42%
Bloomberg US Aggregate	7.30%	4.66%	-0.36%	2.01%
Bloomberg US Municipal 5 Year	5.03%	3.49%	1.05%	1.93%
HFRX Equity Hedge	10.06%	8.25%	6.61%	4.75%
Barclay BTOP50	1.59%	1.70%	5.86%	3.02%

Source: eVestment

HIGHLIGHTS OF 2025

As we look back on 2025, it was a year that began with optimism among market participants, then quickly soured, before turning more positive as sentiment improved. The year kicked off with enthusiasm surrounding the 2024 election results, particularly Donald Trump's return to the White House and the Republican majority in both the House and Senate. Markets anticipated a pro-growth, pro-business, reduced regulatory framework, and a more laissez-faire agenda out of Washington, D.C. There was also optimism around a potential curtailment in government spending, driven by the newly created Department of Government Efficiency (DOGE), led by Elon Musk.

What ensued was far different. Instead of the anticipated tax cut and regulatory roll back, the market was met with what Trump labeled "Liberation Day," the introduction of a new tariff regime, at rates not seen in the US in more than a century. The tariff rates initially unveiled approached 20%, and the market reaction was decidedly negative. After a period of reconsideration, the administration pivoted to lower rates, with the current average total tariff rate closer to 11% (Source: Strategas Securities, LLC; Quarterly Review in Charts, Mon. Jan. 5, 2026).

In June, Musk and Trump had a public falling out. That quickly ended the DOGE experiment, with little results to show for it. It reminded us of the Simpson Bowles Commission back in 2010, significant fanfare, but not much in terms of actual results. This is lamentable as we have concerns that the US remains on an unsustainable path of deficit spending.

Following the pivot on tariffs, the administration turned its focus to taxes over the summer, culminating in the passage of the OBBBA (One Big Beautiful Bill Act). As the name suggests, this legislation was wide ranging. The most impactful components included accelerated depreciation for businesses on capital expenditures and the increased limit of SALT (State and Local Tax) deductions. The stimulus created by this tax relief nearly offset the new tax burden imposed by the new tariffs, a dynamic the market was quick to capture.

International equities, both emerging and developed markets, vastly outperformed US equities for the year, driven by two primary factors - First, the US dollar depreciated nearly 10% against a basket of other major currencies. The second was a step up in deficit spending in Europe, primarily around defense spending. This spending was initiated to support both the Ukrainian forces battling against the now four-year-old Russian invasion, as well as bolstering their own European forces to meet new higher NATO spending guidelines encouraged by President Trump, who pressed Europe to shoulder a higher share of the cost to safeguard the continent.

Fixed income investors experienced respectable returns over the course of the year, though not without bouts of volatility. Early in the year, long-rates climbed amid concerns around persistent inflation and a Federal Reserve (Fed) on pause, awaiting clarity in what became a rather uncertain period. That veil of uncertainty began to lift in the third quarter. Fears that tariffs would fuel further inflation abated, as it became clear they functioned largely as consumption taxes and ultimately would have a deflationary impact quelling consumer demand through higher costs. We also began to see signs of weakness in the labor market. These two factors spurred the Fed back into action in September and we saw further easing throughout the remainder of 2025. This resulted in returns of just over 5% for the Bloomberg 5-year Municipal Index, and just over 7% for the Bloomberg US Aggregate Index.

THE YEAR AHEAD

While we make no claims to have better insight than our industry peers, we are seeing trends that have taken hold in markets and some near-term events on the horizon that we suspect will be of consequence to markets.

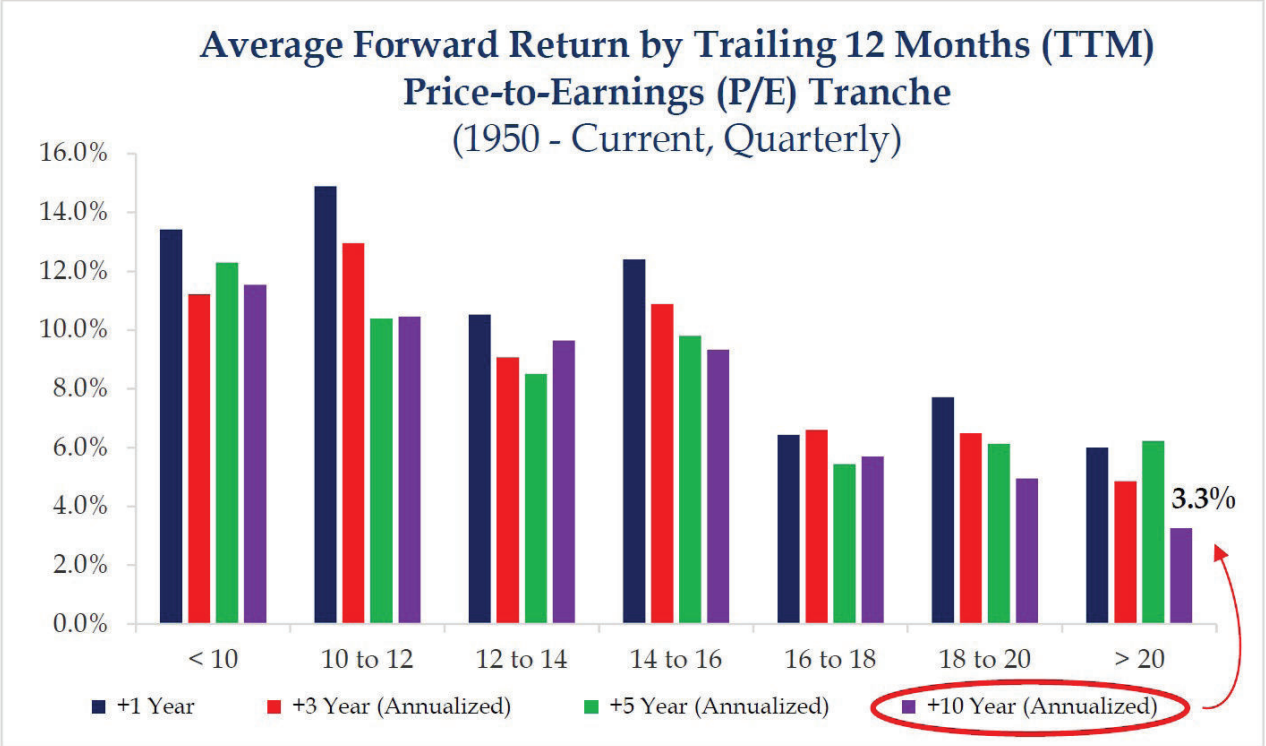
Federal spending remains unsustainable in the long term. The current solution appears to be an ambition that supply side fiscal stimulus will spur higher levels of growth and productivity. At minimum, we believe this elevated level of fiscal stimulus could contribute an incremental .5 to 1% of GDP growth in 2026 the two most significant components are accelerated depreciation allowances for business capital expenditures, and the increased tax refunds consumers are expected to receive in the first quarter of the year. The refunds could spur further retail spending, a shot of adrenaline for our consumer led US economy. This could be focused on lower- and middle-income wage earners who, based on the most recent retail data, are most in need of this stimulus. The accelerated depreciation holds the prospect of a greater long-term enduring economic impact. The hope is that this spending generates productivity gains sufficient to drive economic growth at a pace that exceeds the rate of government spending. The risk, of course, is that we do not achieve sufficient productivity gains, and we simply have a resurgence in inflation, similar to what we saw during the high levels of fiscal stimulus during the Covid-19 pandemic.

On the monetary front, a new Federal Reserve Chairman will take office in May. President Trump has been clear expressing his desire for a more dovish approach than the incumbent Chairman Powell has pursued. While rate decisions are ultimately determined by the Federal Open Market Committee rather than the Chair alone, presidential influence is not insignificant. History suggests Trump does not afford long honeymoon periods, and the incoming Chair may experience that dynamic firsthand.

Chairman Powell, himself a Trump appointee, has endured sustained criticisms from the president for the past year. We would expect the new Chair to be tested rather quickly as he or she tries to navigate the Fed's dual mandate of stable prices and full employment under the pressure to ease rates aggressively from President Trump.

Domestically, equity markets are trading at elevated valuation levels, making a rotation in market leadership, away from large-cap tech and toward sectors that have not materially participated in the rally or perhaps further down the market-cap spectrum, more likely today than in the recent past. Historically, when trailing price to earnings (P/E) ratios exceed 20x—and at roughly 25x today—subsequent 10-year market returns have been well below average, at approximately 3.3%, only modestly above the current rate of inflation.

FIGURE 2



Source: Strategas Securities, LLC

DEGLOBALIZATION

We have written about deglobalization for several years, and our investment focus around this theme has centered on two primary areas. First, how deglobalization drives the creation of new supply lines and nearshoring. Second, how advances in AI impact the economy, global energy demand and productivity. We continue to view these themes as actionable and actively evolving in real time.

What has come into clearer focus, and something we discussed in our last letter, is how the Trump led "America First" agenda is accelerating the pace of deglobalization. While the forces driving deglobalization were in place prior to Trump, his policy actions are accelerating the process. One such action is the reassertion of the Monroe Doctrine. As the name suggests, this doctrine was originally articulated by President James Monroe in 1823. Its core premise was that the Western Hemisphere was not open to future colonization by European powers. At the time, however, the US was a fledgling power, and that position was further weakened by the US Civil War which was the bloodiest war in our nation's history, limiting America's ability to enforce this doctrine. However, this doctrine later got reasserted by President Teddy Roosevelt at the turn of the 20th century as the US then had become a more significant naval force and could project power abroad.

The US never formally abandoned this doctrine, though it evolved post World War II. Following the war both the Allied powers and the Axis militaries were destroyed, or significantly weakened, and the US stood as the new world power, having supplanted the UK and its then sunsetting British Empire. The US effectively expanded this doctrine as it took charge of security policy for those nations that agreed to align with it, in direct opposition to the newly created Soviet Union. Essentially, the Monroe Doctrine expanded to include the Eastern Hemisphere as well.

Following the Cold War, the US has gradually migrated toward a more inward-looking focus. President Trump's reassertion of hemispheric claims—most notably the Monroe Doctrine—reflects this shift. He referenced the doctrine, during a press conference at Mar-a-Lago following the capture of Venezuelan President Nicolás Maduro and his wife, Cilia Flores. We see additional evidence in this reassertion. One example is President Trump's recent comments about Greenland, which he has described as critical to US strategic defense, both for the strategic minerals contained there, as well as its geography to build his "Golden Dome" missile defense system to safeguard the US from Russian ICBMs (Intercontinental Ballistic Missiles).

Other examples include the US and others either seizing or sinking shadow fleet ships engaged in transporting sanctioned oil, largely from Russia, Iran and Venezuela. Several of these vessels were sunk by Ukraine in the Black Sea, while Sweden has also interdicted a Russian shadow vessel in the Baltic Sea.

We see several market ramifications stemming from these events. The buildout of the US industrial complex-aimed at reshoring manufacturing and shortening supply chains away from China is likely to be inflationary. Market volatility will likely move higher from its current below average levels. As geopolitical risk premium rises, traditional flight to safety assets, including gold, will potentially see further demand. These dynamics could also drive US long rates higher as dollar denominated reserves are not needed to the degree they would have been by foreign central banks before this deglobalization trend began.

CONCLUSION

As we mentioned at the onset of our letter, these geopolitical events can be both encouraging, filled with hope and opportunity, as well as, at times, unsettling. We encourage you to reach out to your advisor at FineMark should you wish to discuss any of these matters and how they could impact your portfolio. Risk management is something we can focus on, the news of the day and its impact on markets is something that is difficult to predict.

Thank you for your continued confidence in FineMark and for trusting us to manage your wealth.



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