Economic & Market Commentary

WINTER 2026

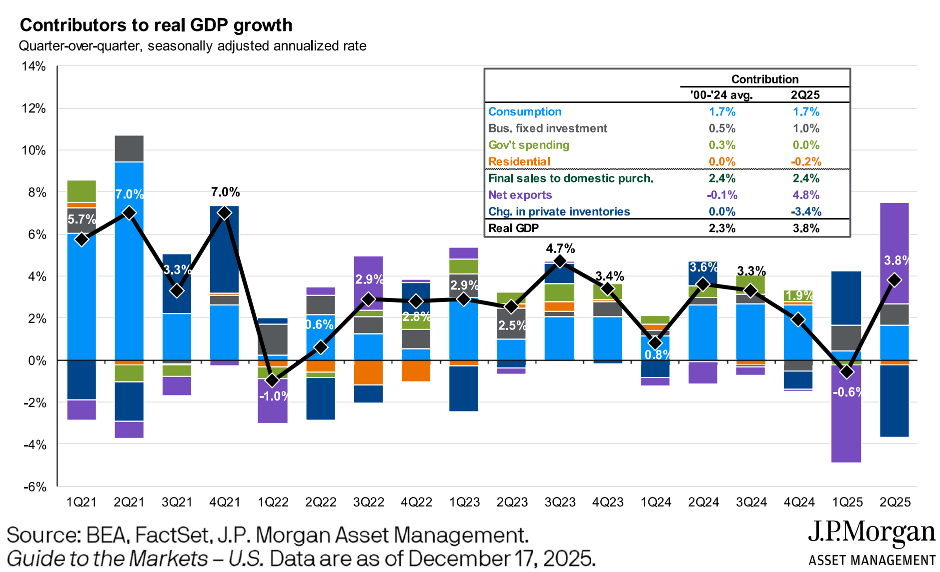
'Diversification is the only free lunch in investing.'
– Harry Markowitz

The core of a rigorous investment philosophy can often be traced back to work of Harry Markowitz (1927-2023). He was a Nobel Prize-winning economist and a professor at the University of California – San Diego. He is best known for his work in modern portfolio theory and the development of an efficient frontier – the identification of a portfolio mix providing the optimal return for a given exposure to price risk.

What this quote means to us is straightforward. There are always opportunities for positive results – if you cast a wide net. While many sectors of the financial markets are expensive by historic measures, others offer low-to-reasonable valuations. Look beyond the popular names and build a low-risk portfolio that will serve you well over time.

Just How Strong is the Economy?

The dearth of economic data during the federal government shutdown added to an already cloudy (and volatile) picture. The first and second quarters were a study in contrasts – both resulting from tariff activities. As shown, negative net exports dragged economic activity into minus territory early in 2025, and a sharp reversal in the second quarter pushed GDP well above generally pessimistic expectations.



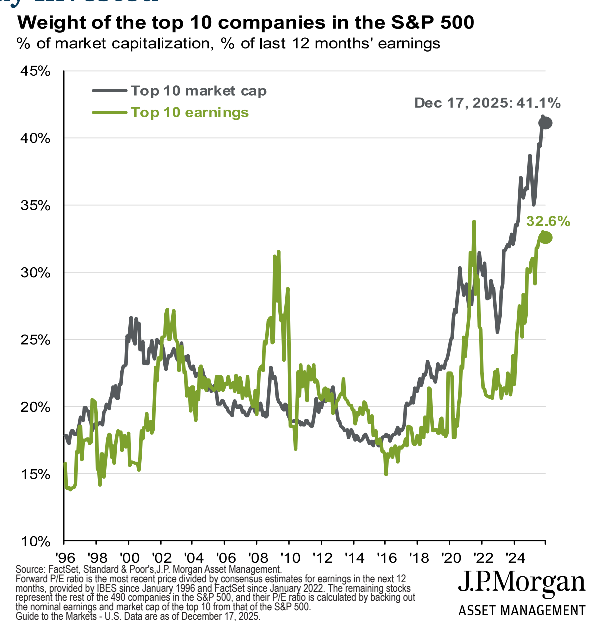
This recovery continued in the third quarter. Preliminary data released in late December showed an annualized 4.3% advance in domestic economic activity. Higher exports and falling imports accounted for about a third of this gain – a continuation of the second quarter pattern. Robust consumer spending (especially for high-end goods and services) was also noted. In all, it was a good report – the highest in two years – and well above market expectations.

At the same time, reasons for caution are present. Much has been written about the likelihood of a 'K-shaped' recovery, where relative weakness in hiring patterns will eventually weigh down prospects for a continuation of strong consumer spending and further dampen prospects for a near-term recovery in housing markets. The Federal Reserve acknowledged this in its December decision to lower its target interest rate and in its projections for future years. Even so, inflation remains sticky, adding to the Fed's cautious stance. In all, the balance of risks is tilted toward the downside for the economy.

We are in general agreement with these views. On the positive side, the fiscal impulse from the 'One Big Beautiful Bill' should keep near-term spending at a healthy level. Longer term, net job creation will evolve in structure and likely lag as AI-enhanced processes partially displace the traditional workforce. Still, we enter 2026 with a much more positive outlook than seemed likely only a few months ago.

Search for Value and Stay Invested

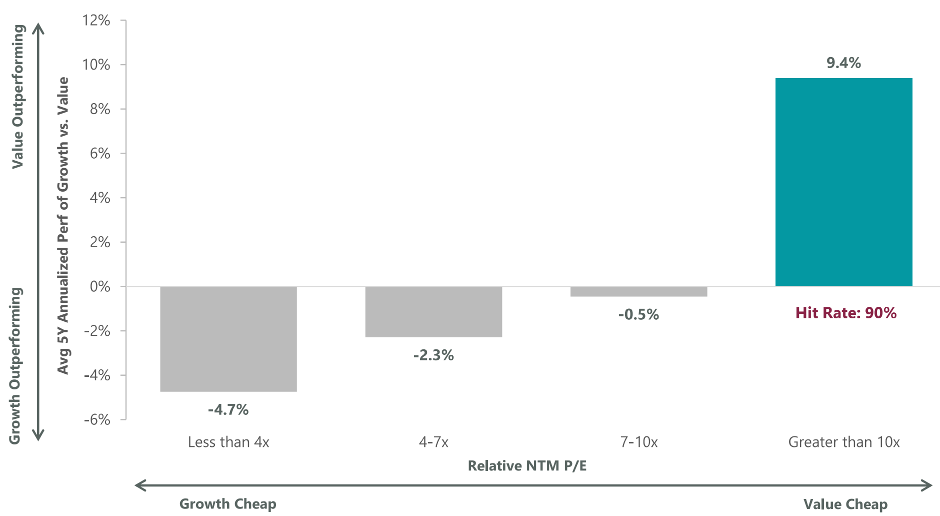
The major theme of investing in recent years was to buy the growth favorites. This has been a successful strategy, but the results are concerning. The ten largest issues in the S&P 500 – almost all technology companies – now comprise 41% of the index's total capitalization, nearly twice the concentration at the peak of the internet bubble in the late 1990s.



Concurrent with this, the valuation gap between growth and value themes has widened dramatically. The broader Russell 1000 Growth index sold at almost 30 times expected earnings at the end of November, while the companion 1000 Value index was priced at about 17.5 times earnings. Growth has not been this expensive relative to value since the aforementioned speculative bubble of the internet era.

Can this pattern continue? Absolutely. It's a well-worn truism that valuation is not a timing device. At the same time, a reversion to the mean is probable. Over the last quarter-century, value has outperformed growth by a wide margin when the 'valuation gap' exceeds ten multiple points.

Performance of Value vs. Growth Based on Starting P/E Differential



▶ **Value has historically outperformed Growth by a healthy margin when the valuation gap (P/E differential) is above 10x. The valuation gap is currently 13.8x.**

ClearBridge

Russell 1000 Growth, Russell 1000 Value, 1997-Present. Data as Sept. 30, 2025. Sources: FactSet, Russell. Investors cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges. **Past performance is not a guarantee of future results.**

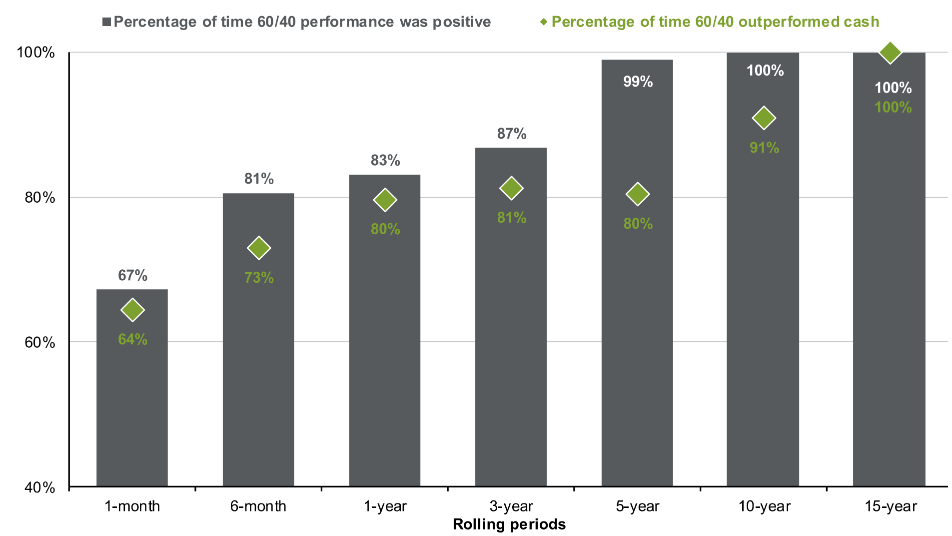
FRANKLIN TEMPLETON

This tells us it's an appropriate time to broaden beyond the growth favorites. And, in addition to the measures discussed above, the opportunities in smaller companies and international markets are equally attractive to those present in traditional value themes. This takes us full circle – diversification is the key to building a portfolio with solid return potential and controlled risk. Plus, don't forget the value of fixed income as a diversifier. Intermediate-term bonds offer a positive real (inflation-adjusted) return to offset the inevitable volatility of stock prices.

Most important, stay invested. Through good times and bad, a balanced portfolio outperforms cash more often than not – and increasingly so over longer time periods.

Percentage of time 60/40 returns were positive or outperformed cash

Rolling monthly basis, 1995 - 2024



Source: Bloomberg, FactSet, Standard & Poor's, J.P. Morgan Asset Management.
A 60/40 portfolio is 60% invested in the S&P 500 Total Return Index and 40% invested in the Bloomberg U.S. Aggregate Total Return Index. Cash is the Bloomberg U.S. 30-day Treasury Bill index.
Guide to the Markets – U.S. Data are as of December 17, 2025.

J.P.Morgan ASSET MANAGEMENT

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Economic & Market Commentary is written by the Investment Services Department at Security National Wealth Management.