Stirling Bridge
Wealth Partners, LLC

MARKET COMMENTARY – October 1, 2025

No bird soars too high, if he soars with his own wings. ~ William Blake

We came across this quotation recently and, of course, immediately thought of Icarus. Remember the old tale of a man who wanted to fly and so built himself a set of wings. And he succeeded! But hubris (it is so often hubris that brings about troubles for mankind) led him to soar toward the sun. Heat melted the wax that held his contraptions together. His wings disintegrated and he plummeted to his death.

The quotation also made us think of today's markets and whether they, like Icarus, are flying a little too close to the sun. Are markets overvalued? The chairman of the Federal Reserve suggested last week that asset prices across the board were "fairly highly valued." Is he right? Partly right? Wrong?

Let's start with metals like gold, silver, and copper. Gold is often used by investors as a potential hedge against inflation. It is popular, especially in its digital form via ETFs because in calamitous times gold tends to zig when other assets zag. It is bouncing around an all-time high of roughly $3,800/oz. Since gold is a commodity, its price should trend close to its cost of production. The cost to mine an ounce of gold is about $1,800. By this simple metric, gold is expensive. Similar comments can be made for silver. Yet we continue to hold the gold we bought for clients earlier this year for two reasons. First, profligate government spending policies continue unabated. Second, investors' inflation expectations have not yet leveled or come down. This implies more potential buyers in the future despite what is likely a high price today.

Copper is different from gold and silver because few buy it as a pure inflation hedge. Copper has essential industrial uses in our modern society and therefore its price is driven by supply and demand for the production of things and economic growth. Its price is certainly elevated compared to ten years ago. But it is down about 15% from the highs experienced as we exited lockdowns. At the moment, copper is not embroiled in a speculative frenzy and appears fairly valued.

Let's now turn to bonds. The real interest rate is calculated by taking today's yield and subtracting inflation. Real interest rates that are near zero or even negative mean that buyers expect no inflation in the future or they are paying too much for bonds. Today's real interest rates are around 1.5% which is middle-of-the-road for the past quarter century. And so, unless inflation truly spikes again, treasury bonds are not over-

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valued. There are pockets here and there in the corporate and municipal spaces that are a little on the pricey side since some of those rates fail to compensate buyers for the extra credit risk taken on by owning them.

At last, let's touch on stocks. We're only going to comment on broad indices here, not any individual names, which can be expensive while the market is cheap and vice versa.

A Wall Street Journal article in the past month expressed concern about how expensive the S&P 500 was when looking at its price-to-sales ratio over time. It correctly stated that this particular valuation measure is near historic high-water marks. But there is more to the story. You see, profit margins of companies in the S&P 500 have increased from around 9% to about 14% over the course of our investing careers. That means companies bring more of their sales to the bottom line than ever before. That also means that any rational investor should be willing to pay more for every dollar of those sales, all else being equal.

Once again, we need to dig a little deeper. The current average forward price-to-earnings ratio of the S&P 500 is 22.2x. The average for the past 30 years is 17.0x. We're clearly elevated in this case. BUT earnings for the average company in the index have become more predictable, more subscription-based, more reliable. There is, of course, still risk to those earnings, but less than in the early parts of our career. These more reliable aspects of the "e" in the PE ratio means that a rational person should be willing to pay more. Admittedly, our back of the envelope calculations suggest that the proper number is still only about 19-20x. By this measure, the S&P is about 11% ((22.2-20)/20) overvalued. Expensive, but not dire.

There are a host of other metrics for stocks (big and small caps), but they demonstrate similar findings. The stock market, especially the biggest of the big, is likely a little expensive compared to history. But since the direction of rates is downward at the moment, revenue growth among companies is sound, earnings growth is even firmer, and the One Big Beautiful Bill Act has small stimulus measures that kick in next year, there is not an explicit reason today why stocks <u>should</u> fall.

But let us always remember, they <u>could</u> fall at any time. That need not bother us if we have set our allocations between stocks and bonds appropriately. Especially, if we haven't done something foolish like borrowing someone else's wings (borrowing money to invest) to soar too close to the sun ourselves.

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Finally, to our earlier question on the Fed chairman's assertion that asset prices are "fairly high." We think he is right enough not to quibble. Some air could stand to be let out of our balloon. Though the animal spirits currently at play in the market make that seem unlikely.

Stirling Bridge Wealth Partners, LLC is fortunate to count many of you as clients. In the good times and bad, we remain committed to providing customized investment solutions and robust financial planning wrapped in a package of exceptional service. We thank each of you for your dedication to us and for your trust.

Sincerely
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