

Good morning,

What's in this week's Report:

- Taking Stock of the Four Pillars of the Rally Ahead of 2026
- Weekly Market Preview: Can Year-End Window Dressing Push Stocks Higher?
- Weekly Economic Cheat Sheet: Another Quiet Week, But The Labor Market Will Stay in Focus
- A Historical Look at Bubbles

Futures are modestly lower following a mostly quiet weekend of news, as the Trump/Zelensky meeting failed to produce meaningful progress toward peace in Ukraine.

Geopolitically, markets were hopeful that the Trump/Zelensky meeting over the weekend would yield a formal agreement. Still, it did not (just more "progress"), and oil prices are rising moderately (2%) in response.

Notably, gold, silver, and copper are all down 2% - 4% pre-market, but that's likely due to year-end positioning.

Today, the calendar is generally quiet, so focus will be on any signs of geopolitical progress (Russia/Ukraine). Oil remains the best barometer for geopolitical concerns. Despite the bounce in oil this morning, market concerns remain low (despite numerous unsettled situations, including Russia/Ukraine, China/Taiwan, and now Venezuela). There is also one economic report today, Pending Home Sales (E: 0.9%), but that shouldn't move markets.

Market	Level	Change	% Change
S&P 500 Futures	6,959.75	-19.50	-0.28%
U.S. Dollar (DXY)	98.12	0.10	0.10%
Gold	4,472.90	-79.80	-1.75%
WTI	58.16	1.42	2.50%
10 Year	4.117%	-0.014	-0.34%

Stocks

Last Week (Needed Context as We Start a New Week)

The stock market steadily rose to new record highs over the holiday-shortened Christmas week as traders shrugged off rising geopolitical tensions amid renewed AI enthusiasm with year-end in sight. The S&P 500 rose 1.41% on the week.

Equities rallied to start the week last Monday as trading desks were already thinning out ahead of the midweek holiday break. News that NVDA plans to begin shipping H200 chips to select Chinese customers by mid-Q1, paired with a TSLA-friendly decision by a Delaware court, rekindled a bid in mega-cap tech stocks. At the same time, markets remained wary of tensions between the U.S. and Venezuela. The S&P 500 gapped higher and closed up 0.64%.

The bullish momentum persisted on Tuesday thanks to net-positive economic data, including a robust Q3 GDP report and a solid Durable Goods release, which tamped down recession worries. Meanwhile, dovish commentary from the

White House by President Trump and NEC Director Hassett, who both called for lower interest rates, left bets on Fed rate cuts in 2026 intact. The S&P 500 added another 0.46% to close above 6,900.

The rally persisted through Wednesday's early close as AI enthusiasm continued to firm, driven by a strong Taiwanese Industrial Production print (the nation produces over 60% of the world's semiconductor chips). In contrast, recession fears continued to dwindle amid another sharp pullback in initial jobless claims. The S&P 500 rose another 0.32% to a new record.

The major indexes hit all-time highs early Friday, driven by news that NVDA and AI startup Groq had agreed to a licensing deal, in what was otherwise a quiet session with a dearth of catalysts, thin attendance, and low volume. The S&P 500 gave back early gains to end the session with an incremental loss of 0.03% on Friday.

Taking Stock of the Pillars of the Rally as We Start 2026

With Christmas behind us, investor focus will now turn towards the new year. While trading will be slow this week (and won't really pick up until next Monday), I wanted to take advantage of this potential lull in market activity to review the state of the pillars of the rally, i.e., those factors that powered stocks higher not just in 2025, but in some cases, for the past few years.

For reference, the four pillars of the rally are: 1) AI Enthusiasm, 2) Expected stable economic growth, 3) Ongoing rate cuts, and 4) General tariff stability.

Pillar 1: AI Enthusiasm. The positive impact of AI Enthusiasm on markets in mega-cap tech stocks (and the broader tech sector) is both subjective and objective. Subjectively, the idea that AI is the next iteration of the internet or next industrial revolution has spiked interest and excitement in stocks to levels we haven't seen since the early 2000s (dot-com bubble). Objectively, the robust earnings growth of the largest stocks in the market (the Mag 7) has pushed the market multiple for the entire S&P 500 higher. That's allowed the index to trade above levels previously considered sustainable. Additionally, the massive AI infrastructure capex (meaning hundreds of billions being spent on data centers, networking, compute power, etc.) is acting like a private-market economic stimulus plan, supporting broader economic growth. If there is one factor most responsible for this remarkable three-year run in stocks, it's AI Enthusiasm.

But as we start 2026, it's fair to say that AI Enthusiasm is under as much scrutiny as it's been since ChatGPT burst onto the scene more than three years ago. Concerns about too much cap-ex spending and poor ROI on hundreds of billions in data center investment (best monitored by ORCL stock), concerns that Google Gemini 3 AI model will cut into ChatGPT market share and undermine the \$1 trillion in spending commitments from OpenAI, worries about end-user adoption (will regular people pay for AI?) and data center overcapacity have all combined to increase concerns that AI is in a bubble. And for much of the fourth quarter, we saw those bubble concerns weigh on the tech sector and act as a headwind on the S&P 500.

Bottom line, AI Enthusiasm is still alive and well as we start 2026, and it is a bullish force for stocks. But we should expect that 1) AI Enthusiasm will be more fractured this year, with specific stock and sub-sector winners and losers, as opposed to the entire tech sector and any stock that mentions AI in their quarterly call. 2) Because of that, AI Enthusiasm likely won't carry the market higher by itself, as it did for times in 2025 (and more forcefully in 2024).

While AI Enthusiasm remains a bullish force for markets in 2026, the rest of the economy and markets will have to do some heavy lifting if we're going to see the major indices repeat 2025's stellar performance. **Verdict: In place, but not as strong as years past.**

Pillar 2: Stable Economic Growth. Stable Economic Growth was the unsung hero of 2025, as we and others have demonstrated that when growth is stable (it doesn't have to be spectacular), the rest of the market can hold up even if AI Enthusiasm isn't a powerful force.

As we start 2026, the reality is that growth is stable. Virtually all growth metrics (ISM PMIs, retail sales, durable goods) are showing solid activity, and none of them are in danger of implying that growth could suddenly stall. The labor market, however, is a bit of a different story, as the unemployment rate is at a 4-year high of 4.6%. For now, that's not a problem. But if that unemployment rate rises to 5.0% or higher, that will be an obvious economic warning sign. At that point, it leaves the market very vulnerable to any AI disappointment, because if AI disappointment is combined with growth worries, few (if any) sectors will be able to hold up. **Verdict: Still in place, but the labor market needs to be watched.**

Pillar 3: Ongoing Rate Cuts. Expectations for Fed rate cuts were a bullish factor for stocks, especially in the second half of 2025, but there's clear uncertainty as we start 2026. The Fed has tweaked forward guidance in a more hawkish direction and 1) Signaled no near-term rate cuts and 2) Just one cut in 2026. Usually, that'd be a hawkish (and negative) turn for markets. However, these are not normal times.

The new Fed chair (regardless of who) is expected to be substantially more dovish than Powell, and that is keeping expectations for a dovish Fed in place as we start 2026. **Verdict: Still in place, but it all rides on a dovish new Fed chair actually cutting rates.**

Pillar 4: Tariff Clarity. Markets surprised everyone last year by ignoring the largest tariff increases in decades, and, ultimately, tariff policy clarity helped markets look past the higher rates and rally. However, we start 2026 with potential significant tariff uncertainty.

The Supreme Court IEEPA tariff decision is expected early in 2026. If tariffs are struck down (as most expect they will be), that will cause potentially significant uncertainty around 1) Tariff refunds and 2) The reimposition of tariffs using other statutes.

The key here will be the 10-year Treasury yield. If the IEEPA decision pushes the 10-year yield above 4.50%, that will be a new market negative. **Verdict: Still in place, but risk of damage early in 2026.**

Economic Data (What You Need to Know in Plain English)

Last Week

There weren't many economic reports during the holiday-shortened week, but the Report we received continued to show a generally solid economy. That key Report was the final Q3 GDP print, and it was stronger than expected, rising 4.3% vs. (E) 3.2%, while consumer spending was also strong, rising 3.5% vs. (E) 2.7%. The Q3 GDP is a dated report to be sure (it's from July-October), but it just joins a long list of economic indicators showing stable growth.

To that point, the other two notable economic reports from last week, Durable Goods and jobless claims, also showed solid growth. While the headline durable goods figure was a touch soft, it is often skewed by the timing of airplane orders. The more important New Orders for Non-Defense Capital Goods ex-Aircraft (NDCGXA) rose 0.5% and logged another solid gain after September's 1.0% rise. Again, this is a dated report (October), but it still reinforces that we aren't seeing any major signs that growth is wavering.

Turning to jobless claims, they were better than expected at 214k vs. (E) 225k and generally reinforced the idea that we're in a "no hire/no fire" environment. Continuing claims remained above 1.9 million, but that's been the case for over a year, and the reality is that a no-hire/no-fire labor market is indicative of stable growth.

As we look to the start of the year, the reality is that economic growth is solid and that's an important (and unheralded) positive supporting this market (and it needs to stay in place if stocks are going to rally in 2026).

Important Economic Data This Week

This week is another quiet one from an economic standpoint, and barring a major surprise, it won't change the current outlook that growth will be solid as we start the new year.

The key Report is Wednesday's weekly jobless claims (it's a day early because of the holiday), and markets will want to see stability in the data to reinforce that we remain in a no-hire/no-fire environment as we begin the year. Ideally, we'd also see Continuing Claims drop solidly to imply that those looking for work were better able to find it (which means a healthier labor market).

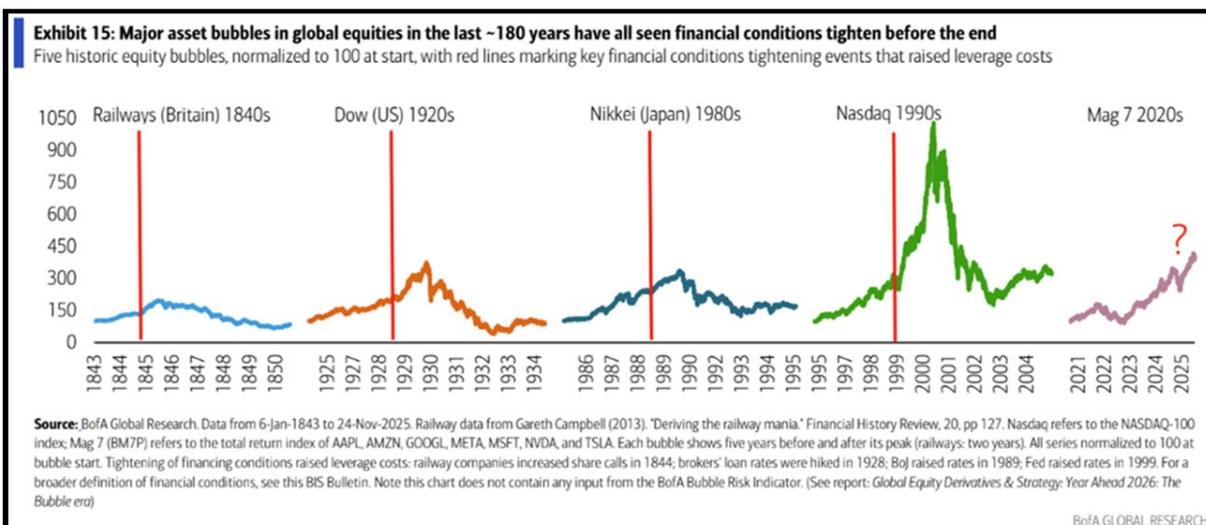
The only other notable reports this week are housing-related: Pending Home Sales today, and the home price metrics (Case-Shiller and the FHFA HPI) on Tuesday. Slowing housing inflation is an important downward force on overall inflation, and that needs to continue if the markets are going to get additional rate cuts in 2026.

Bottom line: this is another quiet week for data, and the more important reports come next week (ISM PMIs and the jobs report). But the numbers this week still matter, and the more they signal stability, the better for markets.

Special Reports and Editorial

A Historical Look at Bubbles

As you can see from the BofA chart here, major asset bubbles in global equities over the last 180 years have all seen financial conditions tighten before their end.



The current “bubble,” whether it’s Mag 7, mega-cap tech, and/or AI, doesn’t have those conditions. And when you combine some facts and statistics, such as:

- Not all long-term investment cycles are bubbles: early industrial revolution (1760s-1830s), U.S. mass transit electrification cycle (1880s-1920s), U.S. interstate highway system (1960s-1990s), personal computer (1980s-1990s), mobile infrastructure (1990s-2010s), etc.
- Based on the constituents of the MSCI ACWI Index, 32 countries are more concentrated than the U.S (based on the market-cap weight of the top five companies).
- While Mag 7 multiples are expanded, they’re nowhere near the extremes of dot-com levels.
- 62% of S&P 500 companies mentioned “AI” in their Q3 earnings calls.
- As Salesforce CEO Marc Benioff said, “Artificial intelligence and generative AI may be the most important technology of any lifetime.”

The point here is that while bubble concerns are valid, this AI movement hasn’t yet reached levels that are similar to other “bubble bursts.”

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