



3rd Quarter North American Market Commentary – 2025

Key Take-aways:

- In August, U.S. Headline CPI rose to +2.92% YoY, marking a +25basis point sequential acceleration from June 2025. Core CPI was reported at +3.11% YoY, representing a +18basis point sequential acceleration from June 2025.
- The US economy, following a short contraction in Q1, rebounded in the second quarter bouncing back to 3–3.3% annually, and the Atlanta FED's GDP model currently projects Q3 growth at a stable 3% pace.
- The U.S. unemployment rate sits at 4.3%, jobs growth is slowing, continuing claims continue to grind higher, and private payrolls (ADP) have declined for 2 consecutive months for the first time since the 2020.
- The FED cut its benchmark rate by 25bps on September 17th. The next interest rate announcement is scheduled for October 29th. Markets are beginning to anticipate that the FED will lower interest rates further, which could further boost borrowing, investment, and the economy's momentum well into 2026.
- In Canada, employment gains have slowed markedly, unemployment rate sits at 6.9%. The Bank of Canada reduced its overnight rate by 25bps on September 17th to 2.50%. The next interest rate announcement is scheduled for October 29th.

Positioning:

- Post Q3 equity markets entered the month of October with bullish momentum, but on October 10th we were reminded by President Trump that trade relations with China remain fragile. In response to ongoing global uncertainty and the effects of financial repression, demand has grown for alternative stores of value and large cap growth.
- The CBOE Volatility Index (VIX) edged higher in October, currently around 24 (historical average of approximately 19.5) leading to a wave of deleveraging. We continue to believe that the floor for the VIX will remain structurally higher compared to prior years, particularly in an environment where a single headline or tweet has the potential to trigger sharp market reactions. In this environment, prioritizing robust risk management focusing on investable volatility, is crucial.
- For Q4 2025 the U.S. economy appears to be shifting from a period of stagflation toward a more pro-growth, pro-inflation environment. The M2 money supply is expanding at its fastest pace since 2022, signaling renewed liquidity. This inflationary momentum continues to erode consumer purchasing power, particularly for households with limited asset exposure. In this environment, financial resilience increasingly depends on holding assets that appreciate faster than the rate of inflation.



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In the U.S., the August Headline CPI was reported at 2.92% YoY, representing a +22basis point sequential acceleration from July and +25basis points higher than in June 2025. Due to the government shutdown, there is a delay in releasing the September figures. Our outlook for a sustained reflationary trend through November remains supported by the diminishing deflationary effects of energy commodities and our baseline expectation of faster core goods inflation, further reinforced by the delayed impact of tariffs. The August release reflected a continued softening of the deflationary impulse from energy, alongside waning shelter disinflation. Adding to this, food-at-home inflation accelerated, and core goods inflation picked up—driven primarily by strength in utilities and transportation commodities. Headline CPI measures the total change in the cost of all goods and services purchased by households. This includes all categories, such as food, energy, housing, apparel, transportation, medical care, recreation, education, and other goods and services. In contrast, reported Core CPI excludes food and energy prices and includes all other categories, such as housing, apparel, transportation (excluding fuel), medical care, recreation, education, and other goods and services. Core CPI is often used by policymakers, like central banks, to gauge underlying inflation trends and to make decisions about monetary policy. It is considered, by them, to be an appropriate

measure for setting interest rates because it is less affected by transitory price shocks, such as weather conditions and geopolitical events. We argue that their choice of CPI measure makes the extent of price increases and currency debasement less obvious. The Core CPI was reported at 3.11% YoY in August, representing a +5basis point sequential acceleration from July and +18basis points higher than in June 2025. From September through December, we continue to anticipate that the inflationary trend will be driven by accelerating core goods inflation as well as the diminishing deflationary impulse from energy commodities and the fading disinflationary momentum in shelter.

Inflation is often (and in our view correctly) attributed to expansive monetary policies and the printing of money. While the rate-of-change of price levels in the economy is always a tug-of-war between inflationary and deflationary forces, our expectations remain, we must adjust our expectations and processes for higher inflation regime. While central banks and governments may spin up new narratives, inflation is an actual policy and is intentional. Since 1999, the U.S. money supply has grown at an annual rate of 6.26%. The extent of currency debasement globally since 1999 is remarkable. While the U.S. has seen a 78% debasement of the dollar, averaging 6.26% annually since 1999, it is not the most extreme case. Canada has experienced an even greater erosion, with an 81.5% reduction in purchasing power and



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a 7.1% annual increase in its money supply since 1999. The destruction of fiat currencies purchasing power from excessive government spending is undeniable. Politicians are happy to promise more free stuff by endlessly spending because they know they won't pay for it and that it will make citizens and businesses more dependent and submissive to political power. No government can truly reduce debt without cutting spending. More government debt means lower growth, more taxes generate weaker receipts, and more government spending perpetuates inflation. Governments worldwide are collectively devaluing fiat currencies, thereby diminishing their purchasing power. Underlying inflation remains elevated, and the continued decline in purchasing power of both U.S. and Canadian dollars is a growing concern for consumers and investors. Given that this trend is likely to continue, with nations persistent on printing money and devaluing their currencies, it is unsurprising that individuals and corporations are increasingly seeking refuge in alternative assets like gold, bitcoin, and real estate.

Gold is now trading above US\$4,100 oz and has overtaken the Euro as the second largest asset after the US dollar in global central banks. In fact, gold has appreciated about 60% year-to-date, which is the best performance in nearly a half century. Bitcoin, on the other hand, has shown investors and citizens that a decentralized currency can

gradually become a generalized means of payment and a unit of measurement. As global citizens see Bitcoin as an increasingly viable alternative to fiat money, more are using it to store value and protect themselves against inflation. These two assets are not in competition with each other, but rather they serve as a team in the fight against currency debasement.

Cumulative inflation reflects the total percentage increase in prices over a period, accounting for compounding effects. In the U.S., cumulative inflation since 1999 now approximates 91.93%. This means that today's prices are 1.9193 times as high as average prices since 1999. In Canada, cumulative inflation since 1999 is 72.20%. This means that today's prices are 1.7220 times as high as average prices since 1999. Inflation is a regressive tax, impacting households regardless of income, yet doing so with varying degrees of relative magnitude, is gradual and cumulative. As such, disinflation from record-high price levels offers little relief. Costs are not deflating; they are simply inflating less. Inflation for each person is individualized and cumulative. Real inflation simply means the destruction of the purchasing power of the currency. Consumers are not focused on what Wall Street is focused on which is the rate of change from M/M, Q/Q, Y/Y or the different categories. They are focused on the level of inflation on 'needs' and 'wants' and how things are drastically more expensive. The point is underlying inflation has



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remained elevated and the cumulative decline in purchasing power of US and CDN dollars remains a major concern for consumers and investors. The M2 money supply is expanding at its fastest pace since 2022, signaling renewed liquidity. This inflationary momentum continues to erode consumer purchasing power, particularly for households with limited asset exposure. In this environment, financial resilience increasingly depends on holding assets that appreciate faster than the rate of inflation.

Slowing GDP in Canada point to renewed stagflation risks, helping explain broader USD strength as US GDP re-accelerates. Canada's economy remained under considerable strain in the third quarter of 2025, with growth prospects clouded by persistent inflation uncertainty and heightened trade frictions. Domestic demand showed little improvement, and output continued to contract in key sectors. Real GDP stagnated in July and August, posting two consecutive months of flat growth, before edging down by 0.1% in September, highlighting ongoing economic weakness. Employment gains slowed markedly, with just 22,000 jobs added (+0.1%) in September, keeping the employment rate largely unchanged at 61.0%. The national unemployment rate is 6.9%, remaining a concerning statistic, this current government must seriously address.

The Bank of Canada reduced its overnight rate by 25 basis points on September 17,

2025, bringing it to 2.50%. Policymakers justified the move as a precautionary measure to support slowing economic momentum and counter persistent weakness in domestic demand. However, the Bank signaled limited scope for further easing, citing risks of renewed inflation pressures from elevated energy prices and ongoing U.S. trade tariffs. Broader structural challenges—stagnant productivity, widening fiscal deficits, and the absence of a tabled federal budget—continue to hinder growth prospects. Until these fundamental issues are resolved, the outlook for the Canadian economy and the dollar is expected to remain subdued.

This quarter's major macro event was the FOMC's 25-basis-point rate cut in mid-September, marking its first decrease since late 2024. Although the markets had largely expected this move, it highlighted the FED's delicate balancing act. Chair Powell stressed the committee's cautious approach, as they weigh a cooling labor market against persistent inflation. Employment risks now outweigh inflation concerns. The bond market is now fully pricing in 2 rate cuts by year-end and 3-4 more cuts in 2026. That would bring the FED Funds Rate below 3.00%.

Another key development was the White House's appointment of Stephan Miran to the FOMC, making him the first executive branch member to serve since the 1930s. While Miran is just one of 12 voting



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members, his role in the administration could amplify his influence. With the administration pushing for rates to drop by 3%, Miran's presence may shape future decisions. Looking ahead, President Trump will have the opportunity to appoint a new FED chair when Powell's term concludes in May 2026, potentially aligning future FED leadership with his monetary policy goals.

Looking ahead, despite analyst estimates showing upcoming YoY GDP growth deceleration, the U.S. economy continues to outperform its peers, showing broad-based strength and signs of accelerating growth. Consensus recession predictions have proven overly pessimistic. After a brief contraction in Q1, real GDP rebounded to 3–3.3% in Q2, with the Atlanta FED's model projecting steady 3% growth for Q3. Growth has been supported by resilient consumer spending, firm business investment, and restrained government expenditure. Investors increasingly expect the FED to respond with rate cuts, potentially reinforcing borrowing, investment, and economic momentum through the beginning of 2026.

Equity markets remain dominated by concerns over trade tensions and the imposition of reciprocal tariffs. Many tariff arrangements remain unresolved, and their eventual implementation or extension could destabilize financial markets, which currently show underlying fragility despite the S&P 500's record highs post-Q3. This

fragility, coupled with persistently high volatility in bond markets, creates an environment where the Trump Administration may shift negotiating postures dynamically. When markets are strong and volatility is low, the Administration tends to adopt a more aggressive tariff stance. Conversely, deteriorating market conditions could pressure a retreat on tariffs to stabilize financial markets. Market participants may be underestimating tariff-related risks, risking complacency ahead of potentially impactful political and trade developments.

The M2 money supply is expanding at its fastest pace since 2022, signaling renewed liquidity. Washington appears to be reverting to its historical pattern of expanding deficits and debt after attempts to reshape fiscal policy, raising concerns echoed in the bond and dollar markets. These markets exhibit warning signs including rising inflation expectations, elevated credit risk, and signals of declining U.S. global economic dominance.

Markets should be recognized for their complexity, dynamism, and unpredictability, with volatility fluctuating and often behaving unexpectedly over time. Risk is ever-present, even when it is not immediately visible. The biggest overhang continues to be the uncertainty around tariffs and their impact on the global economy. On October 10th, tensions between the U.S. and China escalated after President Trump announced



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that, following months of stable relations, China had taken a more confrontational stance. He suggested that a planned in-person meeting with President Xi might be canceled and warned of a significant tariff increase. Markets reacted swiftly—stocks declined, and notably, the dollar index also fell. This inverse move suggests that investors did not view the dollar as a traditional haven amid the renewed trade uncertainty. Risk quickly reemerged in the market, though much of it faded as headlines shifted. Additional trade flare-ups remain likely in the months ahead. The picture remains highly uncertain.

The market had grown increasingly vulnerable to a volatility shock, with systematic positioning at multi-year highs and realized volatility near record lows. The events of October 10th highlighted these structural fragilities in real time. A sharp rise in short-term volatility (1M RV exceeding 3M RV) triggered volatility-control and risk-parity funds to systematically reduce exposure, amplifying selling pressure. This deleveraging created a self-reinforcing feedback loop—selling driving more selling—a hallmark of systematic drawdowns. Although risk assets have largely recovered from the October 10th decline, the higher-volatility regime has remained in play.

While there are several moving parts to tracking structural flows, we broadly break them down into three main subgroups: passive funds, the options markets, and systematic strategies. While most investors have at least some awareness of these categories, many are still surprised by how large they've become, collectively representing more than \$20 trillion, or roughly half of the investable market. The key thing to remember about non-discretionary flows is that they have virtually zero connection to fundamental, sentiment, or macroeconomic analysis. For these strategies, fundamentals simply aren't part of the algorithm.

If volatility continues to build this would be bearish for risk assets. For now, conditions remain stable, but sustained upward trends in volatility could again force systematic funds to sell. While the current stance remains risk-on with a growth bias, structural convexity still tilts risks to the downside. We are navigating unprecedented circumstances, and patience continues to be a key component of our investment strategy.

"Far more money has been lost by investors preparing for corrections than has been lost in the corrections themselves."

Peter Lynch



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Sincerely,

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The Portfolio Management Team

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