

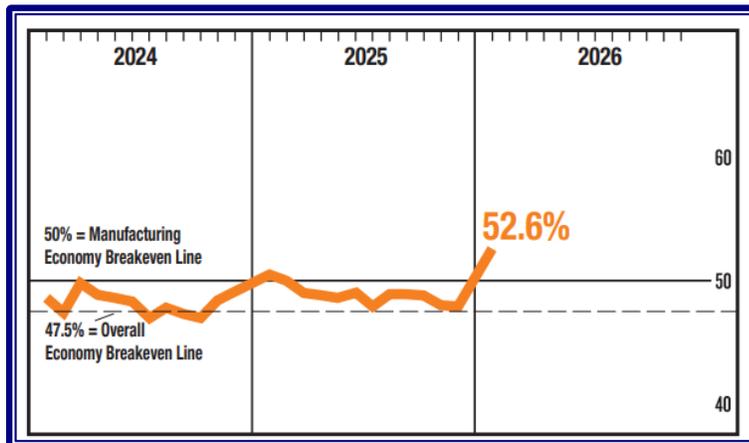
IN FOCUS:

Economic growth picked up at a 4.4% annualized pace in Q3, accelerating from 3.8% in Q2. The latest expansion was fueled by strong consumer spending, exports, and increased government outlays. We are awaiting a delayed Q4 GDP report, due to the government shutdown. Meanwhile, the Federal Reserve Bank of Atlanta's model GDP growth, that is based upon available economic data, suggests a strong 4.2% annualized real GDP growth rate for Q4 2025, a downward revision from its previous estimate of 5.4%. This estimate suggests a resilient U.S. economy, potentially driven by AI-related investment, net export contributions and strong consumer spending.

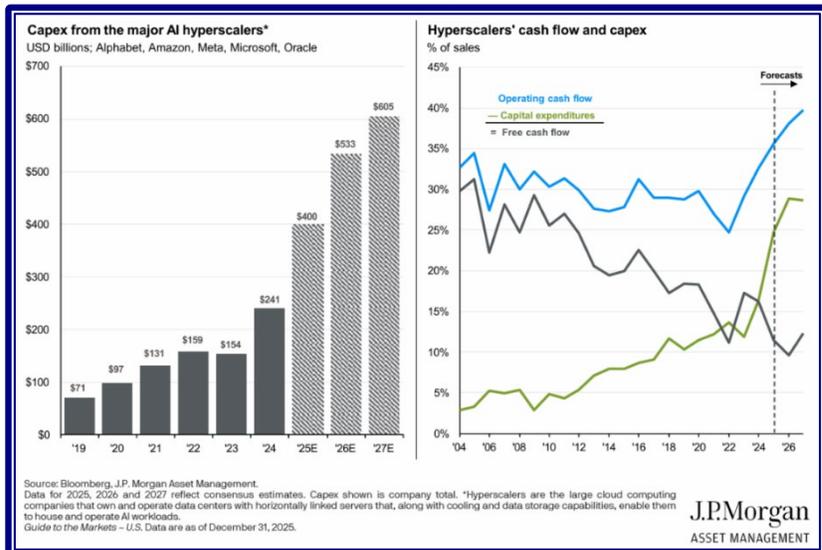
In a surprise reading, January ISM manufacturing PMI came in at 52.6 or 4.7 points above the prior month's reading. Manufacturing has been in retreat over the past year although it remains in expansion territory. Of the 5 main sub-indexes, only employment and inventories remain in contraction territory.

Employment is reflecting staff reductions across multiple industries, as managers delay hiring decisions in a continuously uncertain environment. Overall inventories remain at a level consistent with an expansion,

ISM Manufacturing PMI
First Uptick in 12 months
 Source: Institute for Supply Management



signal above-potential GDP growth, while the Redbook's same-store sales gauge shows the consumer in spending mode. Amidst all the anxiety associated with the U.S. job market, initial unemployment claims continue to trend lower with last week's report coming in worse than expected.



however relatively low customer inventories reflect caution surrounding volatile trade policies and rising prices. PMI prices continued to climb as tariffs push up prices on imported goods. We expect manufacturing conditions to improve further in the year ahead, which should add resilience to the expansion. However, new orders softened as did employment over the same period, while pricing pressures pressed higher. Hiring was weak in January as reported by the ADP non-farm employment report of only 22,000 jobs vs expectations for 46,000 jobs. The loss of momentum in job creation is evident in the 3-month moving average that dropped to 10,000 jobs vs the prior 18,000. The Dallas Fed's weekly economic index continues to

Financial conditions remain highly accommodative. This is beneficial for risk assets, and further upside for U.S. and global stock/bond allocation ratios, especially given our expectation for healthy global forward earnings growth momentum. Keep in mind that U.S. financial conditions are typically only this easy during or shortly after periods of very weak or weakening global earnings growth momentum.

The dollar continued to weaken in 2025 on the backs of policy uncertainty, a growing U.S. deficit and the expectation of lower interest rates. Communications from the white house about the dollar policy have also been contradictory and pressuring the dollar lower. A weaker dollar makes exports cheaper and consequently could help reduce the trade deficit. However, on the other side of this argument is a weak dollar could destabilize the inflow of foreign capital into U.S. treasuries and equities. For now, the U.S. remains reliant upon foreign capital inflows - and international investor appetite for American assets has remained healthy. This of course could change if foreign investors lose confidence in U.S. trade relations, fiscal or monetary policies, or foreign diplomacy.

We expect the Fed to be measured in its approach to lowering interest rates this year. Even as Fed leadership is due to change hands, the consensus amongst the voting member base seems committed to data-driven decisions. There are, however, a number of factors that could cause long-term interest rates to rise such as: Fed independence becomes compromised, inflation concerns grow, or fiscal sustainability comes into question. Absent any market shocks, we expect this year to be another year in which the expansion continues producing solid profits against a backdrop of rising productivity levels.



Consumer confidence in January fell to its lowest level since 2014, as worry grew over both the Present Situation and future Expectations indices. These indices edged lower, with views on current business conditions hovering just above neutral at +0.1%. Assessments of employment conditions also softened, as the labor market differential (jobs plentiful vs hard to get) continued to ease. All three components of the Expectations Index declined in January. Expectations for business and labor market conditions six months ahead weakened further, and perceptions of future household income growth became more restrained.

Contrary to weak consumer confidence, spending has been robust. In the wake of delayed data from the Census Bureau, we turn to CNBC’s NRF Retail Monitor that examines credit card data from Affinity Solutions. December retail and restaurant sales (excluding autos and gas) came in +1.3% over the prior month and +3.5% year over year. 4 of the 5 categories grew over the prior month with the largest advances in sporting goods/music and bookstores, followed by general merchandise and electronics/appliances. Restaurant spending was the only sector to come in negative, down -0.29%. There could be several reasons for the divergence between spending and sentiment. Cyber Monday landed in December in 2025 and likely provided a boost to monthly reports. Inflation concerns are also fueling a “buy now, ahead of rising prices” effect. Additionally, consumer strength is most evident particularly among higher-income households, who benefit in what is being called a “K” shaped economy – where top earners sustain growth while lower income groups feel more pressure from economic stresses.

This economy highlights the diverging trajectory between high- and low-income earners. More specifically, wealthier households benefiting from soaring stock markets and rising home prices have the flexibility to save more while spending less. As lower income households struggle with affordability, they tend to rely more on debt as they make ends meet, while reducing spending on discretionary items. This disparity can have vast implications for economic and business conditions. The direction of inflation, employment, and interest rates, coupled with technological advancements through AI, will have a lasting impact - each working to help shape the next phase of the economy.

Looking ahead, both fiscal and monetary policy are expected to underpin growth in the coming year, with consensus forecasts pointing to an even stronger U.S. economy in 2026. Corporate tax cuts should support robust capital investment, while elevated equity and home prices may encourage additional spending by higher-income households. That said, downside risks remain: many households are under financial strain, residential investment is weak, and government spending may soften, raising the possibility that GDP growth falls short of expectations. Meanwhile, corporate earnings continue to expand, and the rollout of AI technologies is poised to significantly boost productivity - potentially pushing profit margins to record highs. According to Yardeni Research, current consensus estimates place S&P 500 EPS growth at roughly 14.9%.

We expect healthy economic growth with some deceleration in 2026. Overall consumer spending has held up so far, but we are concerned by the disproportionate impact of higher prices and weakening employment. Trade policies have yet to stabilize and we continue to await a decision by the Supreme Court that should clarify boundaries, if any, around the executive branch's trade authority. However, we would expect any adverse ruling against the administration to be met with a recategorization of tariff rationale that is accompanied by the extension of said policies for at least a few months. We are encouraged by fiscal support from the OBBBA (One Big Beautiful Bill Act) and the impact it will have on corporate bottom lines. All eyes are on Fed action this year, as they balance a dual mandate for full employment and stable prices. Policy uncertainty will likely continue and will presumably intensify as the mid-term elections approach.

The recent rise in the U.S. 10-year Treasury yield primarily reflects an increase in the real yield. This is consistent with the improving U.S. economy, although it remains moderately below the current level of real GDP growth. Although inflation has nudged modestly higher, it is well below the level that may be appropriate given longer-term upside inflation risks. The 10-year term premium continues to rise, and we would expect this to continue to add upward pressure on the nominal 10-year Treasury yield over the next 6-12 months, reflecting increasing policy uncertainty and risks.

We would expect the Fed to continue to provide support for U.S. Treasuries, despite some uncertainty surrounding the biases of Kevin Warsh, the nominee for the next Fed chair. Warsh has long argued against the growth of the Fed's balance sheet and has been traditionally viewed as being hawkish. Yet his nomination is assumed to come with a promise to President Trump that he would reduce the federal funds rate, if conditions, most notably inflation, would support it. It remains unclear whether a dovish Warsh will influence a majority within the FOMC when he takes charge. Currently, it does not seem likely. There doesn't appear to be a majority stance to steadily reduce the size of the Fed's balance sheet, although the issue is not likely to be a significant driver of Treasury yields in the foreseeable future, in our estimation. As we have stated previously, it is difficult to assume there will be further Fed interest rate cuts, given that inflation is still well above target, economic growth is well above potential, financial conditions are accommodative, and asset prices remain elevated.

The U.S. economy remains resilient amidst the backdrop of mixed economic indicators and an evolving policy climate. However, market expectations of moderating U.S. inflation may be vulnerable to disappointment, given the strength of the economy and the lagged pass-through of tariffs into consumer prices. Gauging monthly CPI or PCE inflation would be impossible at this point given numerous statistical aberrations and assumptions by the Bureau of Labor Statistics. The economy is "running warm", and monetary and fiscal policies are certainly accommodative. Notwithstanding A.I.'s impact on potential productivity, economic fundamentals point to higher, not lower, underlying U.S. inflation in the months ahead.

However, we do remain cautiously optimistic for continued economic growth throughout 2026, albeit at a slower pace than the previous year. We continue to emphasize overweighting cyclical exposure in our equity allocation model. This assumption includes stimulative tax policies stemming from OBBBA, the continuation of independent monetary policy decisions, and the moderation of trade policy headwinds.

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No gross performance returns that are referenced that are calculated after brokerage commissions but before investment counsel fees are presented without the comparable net performance figures after both commissions, investment counseling fees and other custodial charges. The net counseling fees are the actual average counseling fee calculated across all the portfolios included in the composite. All performance figures are presented on a time-weighted total return basis and assume all income is reinvested. The investment advisory fees are disclosed in Part II-A of the Investment Form ADV. Some clients may benefit from available discounting in the management fee schedule associated with the overall size of the portfolio. Management fees will reduce overall returns to the client.

The composites were created in 2001 and the inception dates start on August 17th, 2001. The composites include only discretionary fee-paying accounts managed in the strategies, and additional information associated with the composites are available such as: dispersion in individual portfolio results as well as the % of the firms AUM in the strategy. All performance calculations are presented within the GIPS® guidelines of the CFA Institute. The CFA institute does not endorse or promote this organization nor does it warrant the accuracy of the content herein.

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