WestStar
Wealth Management

WEALTH WATCH

2025 Fourth Quarter Review
& 2026 First Quarter Outlook

One classic television show still beloved to this day for its campy, low-budget allure and catchy theme music is the live-action Batman series of the late 1960's—called to mind presently by the market-dominating stocks of 2025 which comprised the acronym "BATMMAAN" and included **B**roadcom, **A**pple, **T**esla, **M**icrosoft, **M**eta, **A**mazon, **A**lphabet, and **N**vidia. In the alphabet soup of acronyms, the matters affecting the market of 2026 may more closely align with another pop culture favorite, Star Wars and its main antagonist Darth Vader.

From BATMMAAN to VADER

In 2025 the dominance of the so-called **BATMMAAN** stocks was directly attributable to the artificial intelligence revolution and compels comparison to another era from both a technological advancement and market strength perspective—the "Dot-Com Bubble" between 1997 and 1999. Defined by the advent of a new technology (the internet), that market experienced a tremendous run which made it relatively expensive and was concentrated among a small number of companies—all amid an environment of declining interest rates and geopolitical upheaval that included the end of the Cold War, international trade issues (NAFTA), culture wars, and a presidential impeachment. The stock market peaked in March 2000 and tumbled over the following two years.

As we enter 2026, current conditions strike several similarities to the Dot-Com era and we must consider **V**aluation, **A**I technology, the political ramifications of the advent of the "**D**onroe Doctrine," the mid-term **E**lection, and a potential market **R**eversal—all combining to give rise to a new theme-driven acronym, **"VADER"**. Accordingly, Star Wars will guide us as we explore the universe of 2026.

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What You Need To Know:

- All major investment categories were positive in 2025
- International stocks were the best performers, with Emerging Markets nearly doubling the U.S.
- The U.S. stock market is relatively expensive & AI/tech stocks comprise a record proportion
- Geopolitical tensions have inflamed due to trade wars & the advent of the "Donroe Doctrine"
- Mid-term election years tend to experience weaker market performance
- Market declines are normal & an intra-year correction does not portend a negative year overall
- Adherence to your long-term strategy despite near-term noise is key to achieving your objectives

Asset Class Index Performance* 2025

STRONGEST

International Emerging Market Stocks
33.57%

International Developed Market Stocks
31.22%

US Large Cap Stocks
17.88%

Commodities
15.77%

US Small Cap Stocks
12.81%

Real Estate (REITs)
10.70%

International Bonds
8.85%

High Yield Bonds
8.62%

US Investment-Grade Bonds
7.30%

Alternative Investments
6.04%

Money Market (Cash)
4.20%

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A Long Time Ago: 2025 Market Recap & Valuation

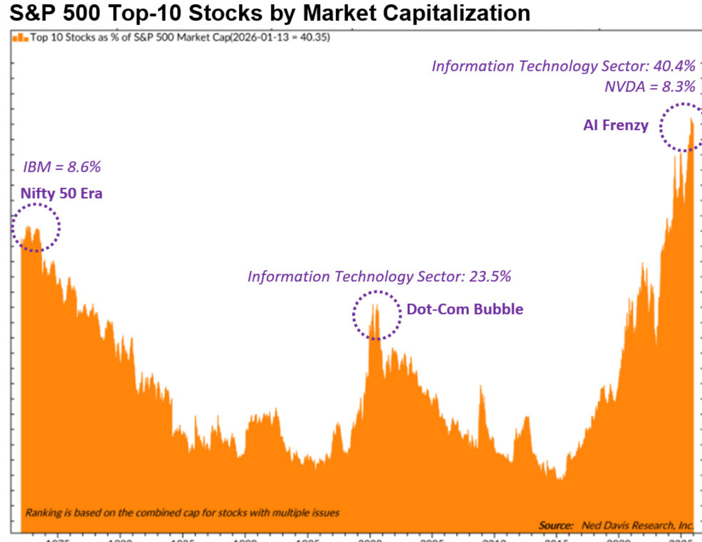
One year ago, we noted in the January 2025 Wealth Watch that, despite two consecutive years of 25%+ stock market returns and 57 all-time highs in 2024, we were expecting another strong year. We likened the environment to 1995 due to three factors: sub-3% inflation allowing Fed cuts, strong corporate earnings, and a technology-driven productivity boom. We were correct in our assessment. Had the S&P 500 ended the year only 2% higher, it would have been the second time in history of three back-to-back years of 20%+ returns (the other instance was the Dot-Com Bubble). International stocks shined as we expected, with Emerging Markets stocks nearly doubling the S&P's impressive result. That said, the exceptional multi-year run in the US stock market has led to its extended valuation and its current expensive state. The chart at right shows that currently the market's forward Price-to-Earnings (P/E) ratio is more than one standard deviation above its long-term average and not far from the "Dot-Com Bubble" level (the higher the figure the more expensive the market). Leading the charge has been the aforementioned "BATMMAAN" and "Magnificent 7" stocks which, as indicated on the table above, have accounted for the lion's share of market performance over the past several years. While said performance contribution has waned from 63% in 2023 to 46% in 2025, the artificial intelligence theme continues to dominate.

S&P 500 Valuation: Forward Price-to-Earnings Ratio

Attack of the Clones: Artificial Intelligence

The advent of and corporate investment in AI technology has had a tremendous impact on a number of areas. Note that in the first half of 2025, approximately 92% of economic growth was driven by AI-related data center investment. Likewise, echoes of the Dot-Com era have emerged amid the vast outperformance of technology stocks in recent years. The chart below reflects the percentage the top 10 largest stocks represent in the S&P 500 Index. The present period, which Ned Davis Research describes as the "AI Frenzy," has seen a record high reading on this metric, with the top 10 stocks comprising 41% of the market—eclipsing the Dot-Com era reading. At that time analysts were concerned about the concentration of the Tech sector being over 23% of the market; currently it is over 40%. Finally, the company synonymous with the AI revolution, NVIDIA, is now itself over 8% of the S&P 500 index—a phenomenon not seen since IBM in the mid 1970's. In summary, the market's current expensive state and disproportionately tech-heavy composition may render it vulnerable to a correction—particularly if the productivity and profitability promises of AI fail to soon meaningfully materialize.

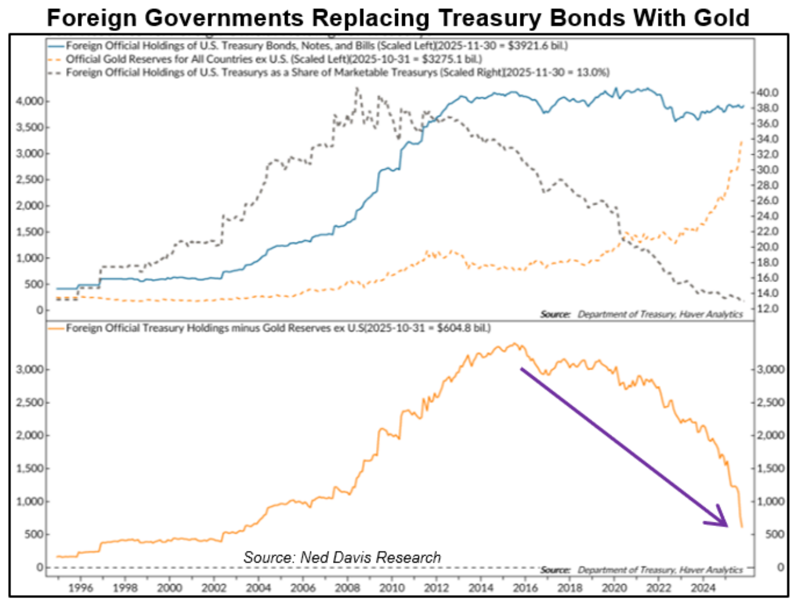
S&P 500 Top-10 Stocks by Market Capitalization



*Large Cap: S&P 500 Index; Small Cap: Russell 2000 Index; Int'l Developed: MSCI EAFE Index; Int'l Emerging: MSCI Emerging Markets Index; US Inv-Grade Bonds: Bloomberg Aggregate Index; Int'l Bonds: Bloomberg Global Aggregate ex-USD Index; High Yield: Bloomberg US Corporate High Yield Index; Cash: BofA Merrill Lynch 3-Month US Treasury Index; Real Estate: FTSE EPRA/NAREIT Developed Index; Commodities: Bloomberg Commodity Index; Alternatives: Wilshire Liquid Alternatives Index

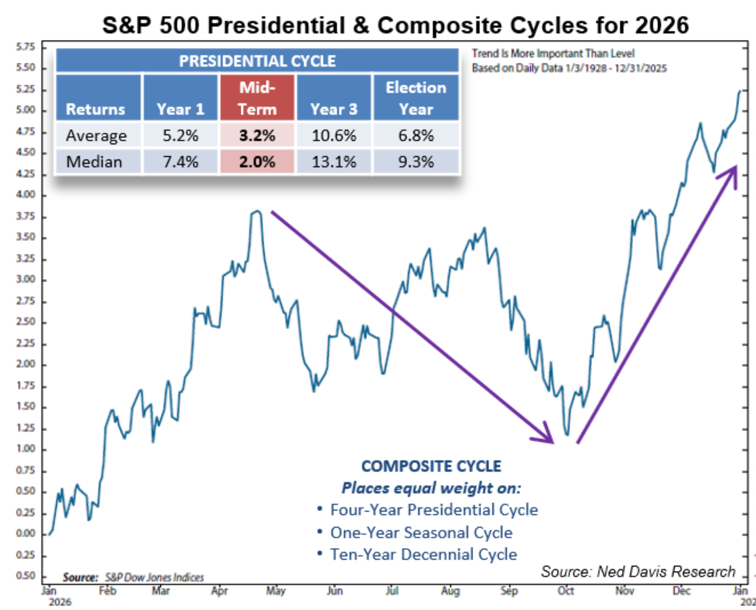
The Force Awakens: The "Donroe Doctrine"

In 1823 President James Monroe established a new foreign policy intended to curtail European colonialism in the Americas. What came to be known as the Monroe Doctrine, and the evolution thereof, focused on U.S. interests in the Western Hemisphere and sealed its position as the dominant force therein. Now, 200 years later, the Trump administration has reasserted the policy, dubbing it the "Donroe Doctrine" and invoking it as justification for the bombing of alleged drug boats, the capture of Venezuelan President Nicolas Maduro, and the threatened annexation of Greenland. While at the time of this writing President Trump has ruled out military force in his pursuit of Greenland, tensions between the U.S. and other NATO countries have intensified. Meanwhile, the erratic and increasingly aggressive nature of U.S. trade and foreign policy is leading to a realignment of global economic alliances, with new trade deals established between Canada and China as well as between the European Union and South America (Mercosur). Indeed, amid escalating Greenland pressure, the EU most recently suspended its trade deal with the US and has signaled willingness to employ its Anti-Coercion Instrument—the so called "trade bazooka"—in retaliation. This contentious climate is thought to also be a root cause of foreign nations replacing their US dollars and Treasury holdings with gold. As seen on the chart at right, the gap between official foreign Treasury and gold holdings has narrowed significantly.



The Phantom Menace: Elections & Reversals

Among the vast array of data we curate, two recurring elements in the Wealth Watch are the presidential election cycle and the broader annual cycle composite. The table at right shows the typical stock market return during each of the four years of a presidential term, noting that the mid-term election year tends to be the weakest. Additionally, the chart at right, which incorporates the presidential cycle along with seasonality and the ten-year average, illustrates that a market downturn between the second and third quarters of 2026 might be expected. When we also consider the previously stated extended valuation, sector and company concentration, and geopolitical uncertainty, it would not be surprising to see a reversal of the soaring stock market of the past three years. That said, it is always important to remember that such corrections are normal. Historically on average the market experiences a correction of 10% every 12 months and of 20% every 3.5 years. Furthermore, note that, should the market hold true to historic averages, a mid-year decline could be followed by a late-year rally subsequent to the election.



PRESIDENTIAL CYCLE				
Returns	Year 1	Mid-Term	Year 3	Election Year
Average	5.2%	**3.2%**	10.6%	6.8%
Median	7.4%	**2.0%**	13.1%	9.3%

A New Hope: Investing in 2026

Beyond the factors already discussed, the "k-shaped" nature of the economy presents another risk. Wealthier people have been doing better than their lower income counterparts, with the former benefitting from recent outstanding market performance while the latter are contending with major affordability pressures. This has led to record low consumer sentiment and could be economically problematic should overall consumer spending slow. That said, consumers are projected to receive large tax refunds in the first half of 2026 due to tax cuts within the "One Big Beautiful Bill Act," and the extra cash should stimulate the economy. While these stimulative effects may wane later in the year, there is no current indication of recession in the near term. All considered, we are maintaining our neutral tactical strategy for our actively-managed clients at this time but stand ready to shift as data warrants and as the year progresses. As always, adhering to your long-term strategy is the most prudent and effective way to achieve your objectives, despite near-term noise.

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