



Charts and Smarts®

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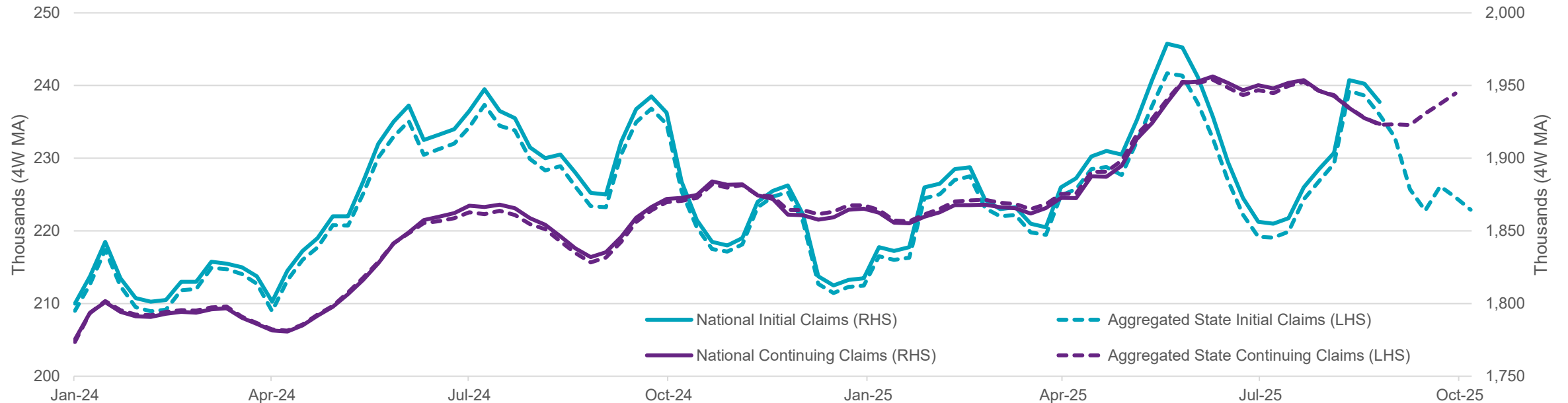
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Almost Cut My Hair

Jobless Claims: National vs Aggregated State Claims (12/29/23–10/31/25)

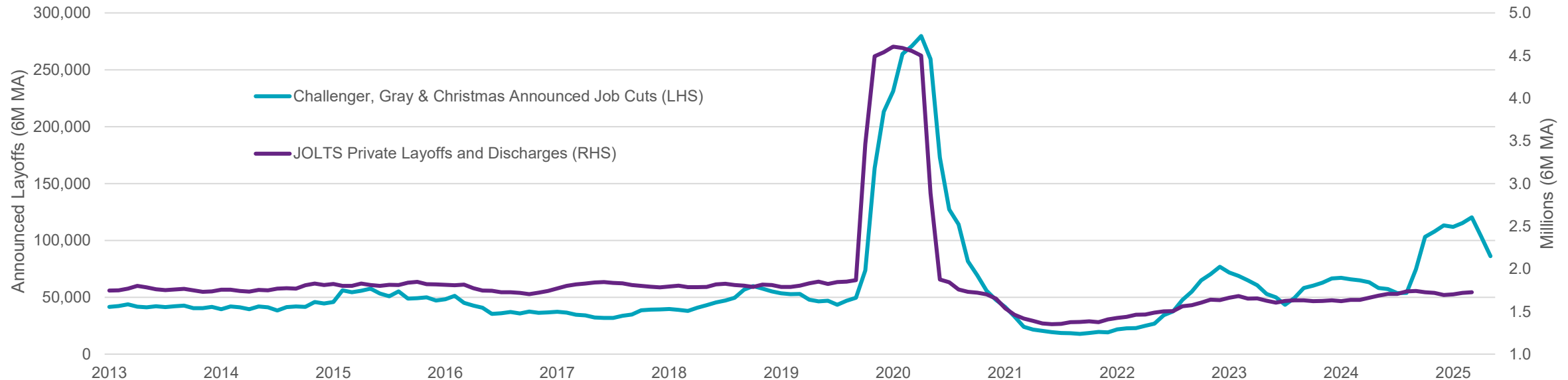


Throughout the duration of the shutdown, investors and policymakers haven't so much been flying blind as they've been flying using third- and fourth-tier instruments. That task has been particularly challenging on the inflation front, given the lack of reliable private-sector data sources by which to gauge near-term aggregate price trends. And on the other side of the Fed's dual mandate, the much-maligned ADP report has been elevated in importance along with a collection of other private sector employment data providers. But, while government data releases have paused, one key data release has continued to be available to investors, if they know where to look. Weekly jobless claims are simply a cumulative tally of claims released by each state's unemployment insurance system and, fortunately for us, state governments aren't shut down. We don't need the Department of Labor to do basic arithmetic for us. Summing each state's weekly claims data and applying the seasonal adjustment factors that are publicly available from the Bureau of Labor Statistics leaves a series that tracks almost exactly with the official national claims data. So, what does the data tell us? Much the same as it did before the shutdown. Initial claims remain benign, largely oscillating between 220k and 250k on a 4-week moving average basis, with prints over the past 6 weeks creeping back toward the lower end of that range. Still no sign of a material uptick in layoffs as the low hire, low fire environment persists, as evidenced by the resumption of a gradual grind higher in continuing claims. The unemployment rate bathtub continues to slowly fill up as an anemic hiring rate can't keep pace with what, for now, remains a modest trickle of inflows into the ranks of the unemployed. Risks remain clearly skewed to the downside, but for now, the labor market remains a story of a linear cooling, not an outright collapse.

Source: Portfolio Analysis & Consulting, Bloomberg. 4WMA represents 4-week moving average.

Carry On

Announced Job Cuts vs Layoffs and Discharges (6/30/13–10/31/25)

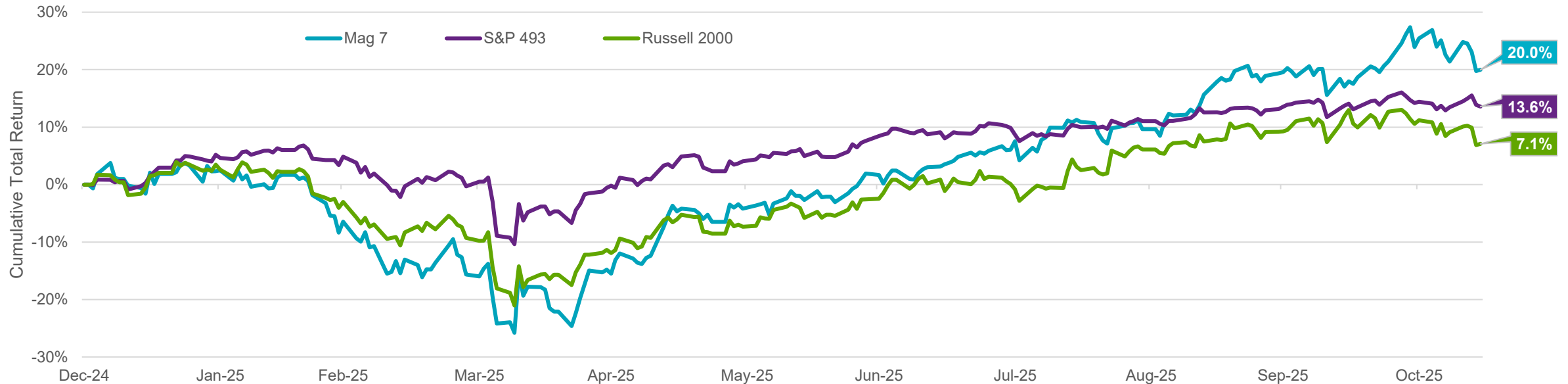


Despite the continued availability of high-quality data that confirms that the low hire, low fire environment persists, investors have been increasingly sensitive to any and all data points during the shutdown-induced data vacuum. One of those data points that caused ripples in the market narrative was the Challenger, Gray & Christmas report – the source of the firmly third-tier Challenger job cuts data. The release saw over 153k layoffs announced in October, a 175% year-over-year increase, and good for the largest monthly total since March and the most layoffs for the month of October since 2003. But there's a good reason the report has long been considered third-tier data. First, the report tracks announced layoffs, not actual discharges. Firms may or may not follow through on those announcements to a tee. Furthermore, those announcements can include non-US employees for large multi-nationals. Finally, there can be a calendar mismatch as well, as layoff announcements can be leading, trailing, or coincident with the actual layoff activity. As a result, layoff announcements can deviate meaningfully not only in size, but in trend from layoff data from larger, more reliable sources, such as the JOLTS survey, as has been the case over the past few years. The final reason to not get swept up the layoff fever: layoffs are a normal part of ongoing labor-market churn. Since 2009, we've averaged 1.74 million layoffs per month while hiring has averaged over 5.3 million per month. In line with the low fire, low hire environment, the three-month average of layoffs stood just shy of 1.7 million as of the latest available JOLTS data, while hires averaged 5.2 million – both modestly below the longer-run average, and well below the pre-pandemic average when expressed as a percentage of total employment. There's little evidence of a sharp spike in layoffs, and what layoffs have been announced and completed appear to be more a reflection of normal frictional churn as opposed to a sharp deterioration in the demand backdrop.

Source: Portfolio Analysis & Consulting, Bloomberg. 6M MA represents 6-month moving average. JOLTS represents Job Openings and Labor Turnover Survey.

Déjà Vu

Magnificent 7 vs S&P 493 vs Russell 2000 (12/31/24–11/14/25)



It's that time of year again. The time when everyone claims the market is only moving higher due to a handful of names and that means the gains can't possibly hold. It feels like it has become an annual tradition for the narrative to become obsessed with market breadth and exclaim that the market is advancing on the backs of only a handful of names, therefore a pullback is imminent. We've debunked this myth each of the past two years, so here we go again. Market breadth refers to a broad swath of measures aimed at demonstrating how many stocks are participating in a given move for an index or exchange. The common wisdom goes that an upward advancing market, driven by just a few stocks as the rest of the market lags behind or even rolls over, is a bearish breadth divergence which must resolve by prices catching down to deteriorating breadth. The problem: narrow market breadth isn't a bug, but rather a feature of markets. The empirical evidence not only reveals that a small portion of names drive the vast majority of wealth creation over the long run, but that these so-called bearish breadth divergences tend to resolve by breadth catching up to price. Narrow breadth is the norm, and recent episodes of acute narrow markets have proven to be a function of tepid, cyclical-risk appetite, focusing flows into areas of perceived strength and quality in equity markets. Chicken beta. That chicken beta has taken the form of megacap tech names, which have benefited not only from robust quality characteristics but secular growth engines that have only been supercharged by the AI capex boom. This year, markets haven't been so much narrow as top heavy. If the S&P 493 and Russell 2000 are sitting near all-time highs, up 13.6% and 7.1%, respectively, that's a pretty good indication that breadth isn't that weak. And there's nothing like a resilient market steadily climbing a towering wall of worry to spur risk appetite and squeeze investors into laggards to cure those narrow breadth fears.

Source: Portfolio Analysis & Consulting, Bloomberg. Performance data shown represents past performance and is no guarantee of future results.

4 + 20

S&P 500® Margin Normalized Forward P/E Multiple (1/31/01–10/31/25)

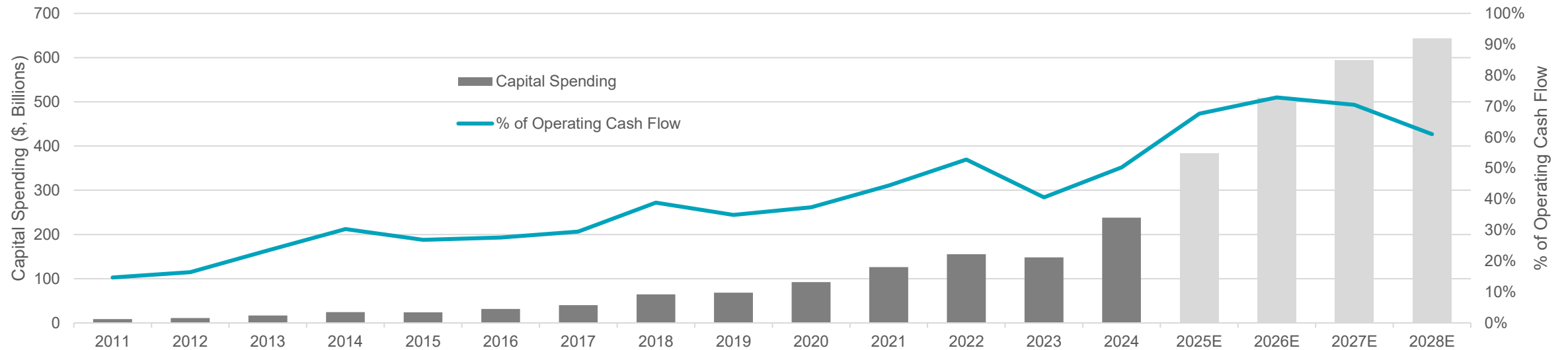


Another narrative that comes up at least once a year it seems: Valuations. Markets push to all-time highs, multiples expand, and we hear a chorus of calls that markets are rich or, our personal pet peeve, “priced to perfection.” This year’s edition of valuation fears has been particularly impressive with investors dusting the cobwebs off the Cyclically Adjusted Price-to-Earnings (CAPE) ratio and the Buffett Indicator and drawing all sorts of parallels to the Dot-com bubble to support the case that markets are too rich and ripe for a pullback. The CAPE ratio has long been put to pasture for a plethora of reasons, not the least of which is that markets discount the future, not the past. And the Buffett Indicator similarly lost its relevance given the multi-national status of so many of the largest US-listed firms. But it’s been particularly challenging for many investors to look past the S&P 500® trading close to 23 times forward earnings and closing in on the Dot-com era peak of 24 times. As we’ve stressed repeatedly, valuations are dynamic and have historically exhibited distinct regimes over time. But more importantly, the composition and quality of the index has changed dramatically, namely through a sharp increase in profitability. Since early 2001, forward return on equity has grown over 20%, from 17% to over 21%, while net margins have surged almost 60%, from 8.9% to 14.1%. Historically, investors tend to pay a premium for quality and profitability as these factors inherently increase predictability. More predictable cash flows warrant greater multiples. Given how dramatically the S&P 500® has shifted to become a less cyclical and higher quality, high-margin index, it only seems fair that the index should garner higher multiples. And indeed, the empirical evidence supports the case that higher margins warrant higher multiples. Adjusting for the sharp increase in margins leaves a multiple that is almost perfectly in line with the long-run average. Hard to argue that valuations are extreme or markets are priced to perfection when the fundamentals justify those multiples.

Source: Portfolio Analysis & Consulting, FactSet. Margin normalized Forward P/E Multiple represents forward P/E multiple divided by consensus forward net margin estimate. Z-Score represents the number of standard deviations each data point is away from the average of the data set.

Our House

AI Hyperscaler Capex (2011–2028E)



While we're dismantling the greatest hits of the shutdown-era bear cases, we might as well cap things off with the emerging skepticism surrounding the AI trade. Circular financing and rising debt issuance to fund the massive build out has increasingly led to concerns around the health and durability of the investment boom. As usual, markets love to take things too far, and the narrative around AI and financing appears to have overshot. While the bubble in bubble talk has certainly cooled down, there remains quite a bit of skepticism around financing arrangements. While massive funding needs for some of the smaller names in the AI space are indeed being met by debt issuance and vendor-financing arrangements, contrary to the emerging narrative the key hyperscalers broadly have plenty of operating cash flow to continue self-financing the bulk of capex spending. Looking out over the next three years, capex from the five major hyperscalers, Alphabet, Amazon, Meta, Microsoft, and Oracle, capex is expected to grow to well over \$650B by 2028. Meanwhile operating cash flow has continued to grow steadily for the hyperscalers, with estimates placing aggregate cash flows at over \$1T by 2028. Indeed, the surge in capex is likely to weigh on free cash flow generation, but it is quite a leap to claim that some compression in free cash flow growth is equivalent to the end of self-financing. However, it is fair to point out that not all hyperscalers are the same, and recent equity market performance highlights those differences. Oracle is the clear outlier of the group and has and will likely need to continue financing capex out of debt issuance, as the firm has posted negative free cash flow in three of the past four quarters. And the underperformance of Meta appears to be less a function of organic capex financing and more a redux of 2022's return on invested capital concerns, as investors worry about a lack of direction for their ever-growing capital spending and operating expenses. In short, while there are indeed some yellow flags worth monitoring, the true risk for the AI trade isn't the popping of a debt financed bubble but rather a shift in the market's reaction function from rewarding capex growth to punishing it as returns remain unknown.

Source: Portfolio Analysis & Consulting. FactSet. As of 11/12/25.

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