TJT CAPITAL GROUP
REGISTERED INVESTMENT ADVISOR

On Our Radar – December 2025

The longest government shutdown in U.S. history ended after 43 days, with little tangible progress to show for it. Congress essentially kicked the can down the road, as key appropriations bills must still be resolved by January 30, 2026. During the shutdown, volatility increased across U.S. equity markets: the S&P 500 Index fell roughly 4.6 percent before staging a late-month rally that left it up about eight points at 6,849. A mix of disappointing earnings guidance, concerns over the massive borrowing required to finance artificial intelligence (AI) data-center buildouts, and a comment from OpenAI's Chief Financial Officer referencing potential government "backstops" contributed to sharp swings in stock prices.

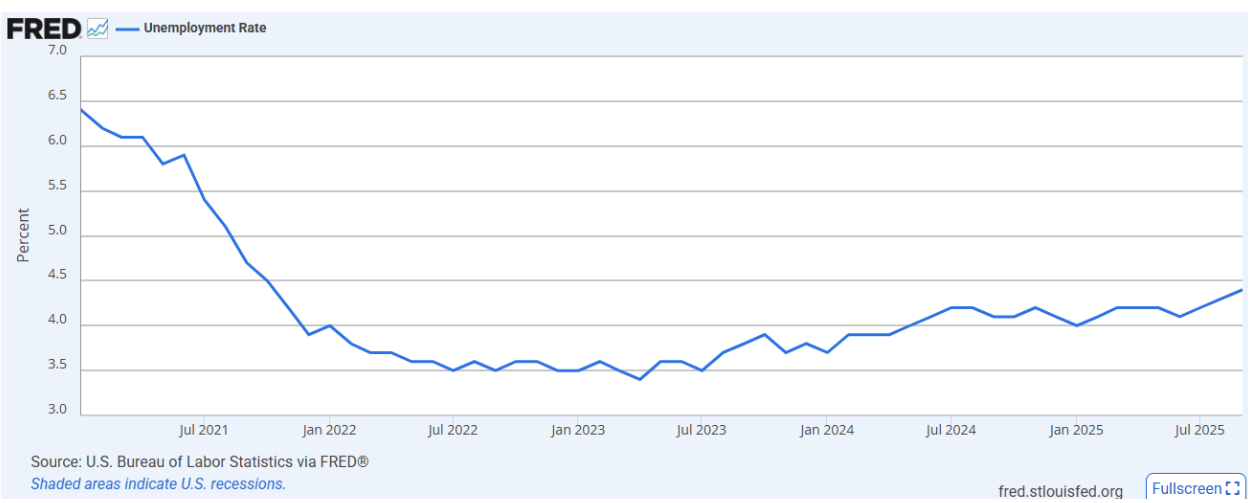
Meanwhile, the yield on the 10-year Treasury note declined to 4.02 percent from 4.11 percent at the end of October. Oil prices slid from nearly $62 a barrel to $58.55, while gold surged to $4,217 an ounce.

TJT Capital Group's InVEST Risk Model ® has helped our clients participate in bull markets and protect capital from the devastation of bear markets by focusing on 5 indicators that really matter when it comes to determining the health and direction of markets. The following is the most recent update.

Interest Rates (Monetary Policy)

The Federal Open Market Committee (FOMC) is scheduled to meet on December 9–10, 2025, to determine whether any adjustments to interest rate policy are warranted. The effective federal funds rate currently stands at 3.88 percent, while the yield on the 2-year Treasury sits at 3.47 percent. This suggests that policy may be roughly 41 basis points (0.41%) tighter than it should be.

Several Federal Reserve Governors have already indicated publicly that they would support a 25-basis-point rate cut, citing a weakening labor market and monetary policy that is increasingly burdensome for consumers. Still, it is quite possible that the apparent softening in employment is being driven, at least in part, by productivity gains resulting from corporate adoption of AI technologies, which would not necessarily be addressed by an interest rate cut.



On the inflation front, the delayed Consumer Price Index (CPI) rose 3.0 percent year-over-year, still well-above the Fed's 2 percent target. Even so, a number of Fed officials, including Christopher Waller and John Williams, have expressed support for lowering rates at this month's meeting, pointing to the latest unemployment reading of 4.4 percent - the highest since late 2021 - as evidence that economic conditions are softening.

Because of the long federal government shutdown, the Bureau of Labor Statistics (BLS) has canceled the October 2025 Employment release, and the November unemployment report will not be released until December 16, 2025, after the Fed's interest rate decision.

Valuation

U.S. equity markets appear richly valued when measured against traditional historical benchmarks. Yet the forces driving today's environment are far from typical. Consider that U.S. federal debt has surged from approximately $23 trillion before COVID to over $38 trillion today - a roughly 65 percent increase. This unprecedented expansion has helped lift a wide range of asset prices, including gold, silver, real estate, and equities.

At present, the S&P 500 trades at about 23 times projected 2026 earnings. With the Federal Reserve widely expected to cut interest rates next week, and corporate earnings forecasts pointing higher, the combination could continue to support stock prices. Still, high valuations come with elevated expectations, and even a small disappointment can leave little room for error.

Economic Cycle

As of now, there is still no official estimate for third-quarter Gross Domestic Product (GDP). Private forecasts suggest growth of roughly 4 percent, but the effects of the shutdown have led many economists to expect a mild contraction in the fourth quarter.

The Institute for Supply Management (ISM) Manufacturing Index fell for the ninth consecutive month, down to 48.2 - another 0.5 percentage-point decline from October. New orders dropped for the third straight month, and prices paid rose 0.5 percent to 58.5.

Retail sales increased 0.2 percent month over month, but it is important to note that these figures are not adjusted for inflation - meaning the gain may simply reflect higher prices rather than increased consumer demand. The economy remains uneven: households with assets are generally holding up well, while lower-income families continue to struggle as higher prices squeeze their budgets.

To illustrate the divide, the University of Michigan Consumer Sentiment Index has fallen to its second-lowest level on record - surpassed only during the COVID-related shutdown - and now sits even lower than its trough during the 2008 global financial crisis.

One factor still supporting the economy is the substantial capital spending directed toward the rapid expansion of AI data centers. However, if that investment slows or if supply bottlenecks delay the buildout, the elevated valuations of many companies could quickly come under pressure.

Sentiment

Investor sentiment often mirrors recent market performance, but it tends to be most informative when readings reach extremes on either end of the spectrum. While bullish sentiment has remained largely range-bound for the past few months, late October saw the percentage of bearish advisers drop to roughly 13 percent - the lowest level in nearly seven years.

Such extremes are often followed by a counter-reaction, which appears consistent with the recent 5 percent pullback in the S&P 500.

Technical Factors

Beneath the headline market indices, several areas have already experienced meaningful corrections, with many individual stocks down 20 percent or more in recent months. This weakness is evident in market breadth measures: the percentage of stocks trading above their 50-day moving averages has fallen from nearly 60 percent in early October to below 40 percent by the end of November. Despite this deterioration, the major indices have held up reasonably well, suggesting that capital has been rotating among sectors rather than exiting the market altogether

Outlook

The past few months have seen the markets experience significant turbulence, with material swings in both directions. Several factors have contributed to this choppy action, including a notable revenue and earnings miss by a prominent "neocloud" company – a term referring to cloud computing firms providing AI-based infrastructure amid delays in new physical plant development.

Concerns about borrowing for capital expenditures to support AI infrastructure growth have also weighed heavily on investor minds. Major tech giants, including Amazon, Alphabet (Google), Meta (Facebook), and Oracle, have collectively raised tens of billions of dollars in debt to fund their AI ambitions. This shift from using cash flow and balance sheet cash to heavy borrowing has sparked worries about the sustainability of such capital expenditures, causing some investors to question the long-term viability of these investments. For instance, credit default swaps on Oracle's 5-year debt have risen to 125 basis points ($125,000 annually to insure $10 million worth of bonds), reflecting the market's growing unease.

While global AI infrastructure spending could potentially reach $3 trillion to $5 trillion by 2030, the path is unlikely to be linear, and not all companies will emerge as winners in the AI race.

The sheer size of the financial markets means that when one area becomes overextended, it can have far-reaching implications, often influencing the economy rather than the other way around – especially when leverage is high and valuations are stretched.

Additional concerns surround the tariffs imposed by President Trump under the International Emergency Economic Powers Act (IEEPA), which grants the President broad powers to impose tariffs during a national emergency. With a Supreme Court ruling on the matter expected in the coming months, an adverse decision could further fuel market volatility.

As year-end approaches, liquidity is likely to become increasingly scarce, and the popularity of leveraged exchange-traded funds may contribute to sustained volatility. (12.2.25)

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