

**FLAGSTONE**  
FINANCIAL ADVISORS, INC.

**MARKET REVIEW**  
**CALENDAR YEAR 2025**

***What Happened:***

We have closed the chapter on another terrific year of double-digit stock returns and we couldn't be happier. 2025 marked the third straight year of stellar stock performance with the S&P 500 index up 17.9%. Tech giants led the way, but other players also showed plenty of life. In a nice twist, previously beaten down sectors like healthcare caught fire as did small-cap stocks. International stocks continued an impressive run with annual returns of 31.9%. All this happened in the face of many headwinds—a 43-day government shutdown, tariffs, political strife, geopolitical tensions—making this performance nothing short of miraculous. Almost everyone would agree that this three-year rally is largely attributable to enthusiasm over artificial intelligence (AI).

Until recently, AI was a vague concept that lived only in our imagination and a few science fiction books. But now it is on our doorstep and knocking loudly. Businesses are scrambling to incorporate AI into their business models. Like anything new, it will take time to digest the implications of this new technology on our lives and the broader economy. Recent market advances suggest that investors consider AI to hold great promise for business, our economy and our lives in general. We are watching developments closely.

As we mentioned last quarter, the Mag Seven stocks and the overheated AI trade cooled down a bit as 2025 wore on. In fact, the only two Mag Seven stocks to beat the S&P 500 index in 2025 were Nvidia and Google, up 39% and 66%, respectively. Many investors found compelling value elsewhere, in stocks of overlooked and underappreciated companies. The Mag Seven companies are great, but smart investors always seek other opportunities when the mainstream get overheated. The broader market fared well and we expect that trend to continue into the New Year.

***Calendar Year 2025 Performance:***

S&P 500 Index (large stocks)	17.9%
Russell 2000 Index (small stocks)	12.8%
MSCI EAFE Index (international stocks)	31.9%
Bloomberg U.S. Aggregate Bond Index (bonds)	7.3%

***Prognosis:***

After three years of blockbuster stock returns, you may be wondering if there is any gas left in the tank. No one knows for sure, but we see plenty of positives. Corporate earnings growth estimates for 2026 are well into double digits and it would not surprise us to see GDP growth of 3% or more for the year. We expect the continuation of low interest rates and stable inflation. The labor market should improve as the economy strengthens and expands. That all bodes well for stocks.

The impact of AI is more difficult to predict. While we like AI stocks in the long-term, we also like the idea of diversification into areas of the market with more reasonable valuations and less reliance on AI. Our clients' portfolios are well positioned in this regard with some exposure to AI stocks as well as investments in less risky areas of the market. All in all, we are comfortable with our clients' portfolio allocations, and we are excited about the coming year.

We wish you all a happy and prosperous New Year!

*SCK*