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3rd Quarter 2025 Moreno Dye Cervantes Wealth Management Group of Wells Fargo Advisors Quarterly Newsletter

The 3rd Quarter was wonderful for the financial markets as performance was driven by strong momentum, low volatility and economic optimism. We were most pleased to see that stock market performance widened out beyond large cap technology with small cap stocks having the best return of all major asset classes during the quarter. International equities continue to be the best performer of the 2025 after years of underperforming U.S. equities.

	3 rd Quarter	2025 Performance
Dow Jones Industrial Average	5.7%	10.5%
S&P 500 Index	8.1%	14.8%
S&P 500 Equal Weighted Index	4.8%	9.9%
NASDAQ Composite Index	11.4%	17.9%
Russell Mid Cap Index	5.3%	10.4%
Russell 2000 Index (Small Cap)	12.4%	10.4%
MSCI EAFE – International Index	4.8%	25.7%
Bloomberg Barclays US AGG Bond	2.0%	6.1%

*Wells Fargo Investment Institute Capital Market Summary

Lately, investors have turned their focus to positive economic tail winds related to regulatory reduction, pending interest rate declines and significant investment in AI. These positives have thus far drowned out the noise of potential inflation from tariffs and the current government shutdown. S&P 500 earnings have grown 11% through the first half of the year versus beginning of the year expectation of only 4% growth.

There continues to be significant focus on the S&P 500 trading at higher valuations than the historical average. While this is true, when you remove the largest 10 companies from the S&P 500, the price-to-earnings multiples look much closer to historical norms. This is why we are glad to see the stock market performance broaden out beyond Mega Cap Tech/AI stocks, as investors were able to find value in other sectors of the economy. Almost every sector of the economy, outside of Consumer Staples and Energy, have seen better than expected earnings growth this year and with the likelihood of further interest rate cuts, we wouldn't be surprised if earnings continue to report better than previously expected.

In addition to market momentum, we have also seen positive developments around Congress' passing of the One Big Beautiful Bill Act (OBBA). While the permanent extension of the 2016 tax cuts will likely provide minimal economic benefit, we are anticipating a strong increase in capital spending/investment by corporations and small businesses. The OBBA also provided some short-term benefits that will find its way into consumer wallets next year through expanded child tax credits, larger standard deductions and an increase in the state and local tax deduction (SALT). We believe that the primary reason the OBBA has helped the financial markets is by providing longer term fiscal clarity. Business leaders and investors now have a much better line of sight, which is reflected as greater optimism in the financial markets. We cannot overstate the importance that the global financial markets place on legislative clarity.

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Federal Reserve interest rate policy was also a positive catalyst during the 3rd quarter. The FED cut rates by 0.25% in September for the first time since late 2024. We believe that the FED will continue to cut rates during the 4th quarter, but they will maintain a cautious approach to further rate cuts in 2026 as inflation remains closer to 3% than their 2% target goal. Their justification for reducing rates is that inflation has come down and they are beginning to move to a neutral position with rates as opposed to a restrictive posture. It is important to remember that the Federal Reserve has a dual mandate of price stability and full employment, which is why we believe that the FED has to take a measured approach moving forward in an effort keep inflation in check. In our opinion, the financial markets are comfortable with a neutral interest rate policy of not too hot and not too cold while the administration's new tariff policy plays out. We are not convinced that the current FED easing cycle will provide the economic stimulus that we have traditionally experienced in the past. Economic data in the 4th quarter will be very important in determining what if any additional interest rate cuts will be needed in 2026.

Moving into the end of the year, our biggest concerns continue to revolve around potential disruptions related to tariffs implementation and immigration policy. Tariff policy uncertainty is extremely high, and we do not believe that the stock market is pricing in an appropriate risk premium associated with this uncertainty. As of the writing of this letter, tariff policy towards China has flared up again and the Supreme Court has yet to rule on the legality of how the Trump administration is administering tariffs. Our best guess is that the Supreme Court will rule that most if not all of the tariffs will be legal under the President's ability to regulate. That being said, the pending ruling from the courts along with unresolved tariff discussions with major world economies does provide the backdrop for increased volatility as we head towards year-end.

Additionally, the labor market continues to show signs of weakness, which might translate to a reduction in consumer sentiment and confidence. We are already seeing a decrease in demand for "big-ticket" consumer items and housing as well as an increase in sub-prime auto loan defaults. Our expectation is that the national unemployment rate will continue to drift higher and eventually stabilize as we get more clarity around tariffs and immigration policy. Both of those issues have significant influence on supply and demand for labor in the U.S. and we will be paying close attention new labor and unemployment data.

In general, we are very pleased with how portfolio diversification has contributed to overall performance this year. Large cap technology stocks continue to draw the majority of attention this year, but the hidden gem has been international investments. Our allocation to international equities has thus far been crucial to helping overall portfolio performance. Additionally, we are happy to see bonds performing much better of late as the FED has begun easing interest rates again. It is important to remember that the primary benefit of asset allocation is to be able to blend different asset classes together in order to smooth portfolio performance over time. Ultimately, having a smoother and more consistent rate of return should help give you the fortitude to maintain your investment discipline during times of stress. This year has been a poster child for the benefits of diversification and portfolio rebalancing.

It's a bit hard to believe, but here we are heading into the end of yet another year. Time really does seem to fly sometimes!! We hope that you all are preparing for a wonderful holiday season with family and friends. Please don't hesitate to reach out if you have any questions, concerns or would like to talk. And as always, thank you so much for the confidence that you place in our team to help you with your portfolios. We hope that you have a great finish to 2025 and look forward to speaking with you all in the weeks and months to come!

Sincerely,



Jose A. Moreno, CFP®
Managing Director – Investments



Michael B. Dye, CRPC®
Managing Director – Investments



Oliver A. Cervantes, CFP®, CRPC®, RICP®
Managing Director – Investments

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The Dow Jones Industrial Average is a price-weighted index of 30 "blue-chip" industrial U.S. stocks.

The S&P 500/Barra Growth Index is an unmanaged capitalization-weighted index stocks in the Standard & Poor's 500 index having the highest price to book ratios. The Index consists of approximately half of the S&P 500 on a market capitalization basis.

The S&P 500/Barra Value Index is an unmanaged, market-capitalization-weighted index of the stocks in the Standard & Poor's 500 Index having the lowest price to book ratios. The index consists of approximately half of the S&P 500 on a market capitalization basis.

The NASDAQ Composite Index measures the market value of all domestic and foreign common stocks, representing a wide array of more than 5,000 companies, listed on the NASDAQ Stock Market.

The S&P Midcap 400 Index is a capitalization-weighted index measuring the performance of the mid-range sector of the U.S. stock market and represents approximately 7% of the total market value of U.S. equities. Companies in the Index fall between the S&P 500 Index and the S&P Small Cap 600 Index in size: between \$1-4 billion.

The S&P Small Cap 600 Index consists of 600 domestic stocks chosen for market size, liquidity (bid-asked spread, ownership, share turnover and number of no trade days) and industry group representation. It is a market value-weighted index (stock price times the number of shares outstanding), with each stock's weight in the index proportionate to its market value.

The MSCI EAFE Index is designed to represent the performance of large and mid-cap securities across 21 developed markets, including countries in Europe, Australasia, and the Far East, excluding the U.S. and Canada.

Bloomberg Barclays U.S. Aggregate Bond Index is a broad-based measure of the investment grade, US dollar-denominated, fixed-rate taxable bond market.

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