

Key Insights

- **Historic Recovery Continues:** S&P 500's 38.21% surge from April lows through October completed 2025's remarkable turnaround, with Nasdaq rocketing 55.94% and Magnificent 7 delivering exceptional 69.02% gains that erased February-April declines and pushed indices beyond previous highs.
- **Technology Dominance Returns:** Tech sector commanded October with 6.68% gains while growth stocks dominated decisively (+3.46% vs Value +0.43%), extending year-to-date leadership to 20.84% for growth versus 11.96% for value as large-caps outperformed with Russell Top 50 gaining 3.63% in October.
- **Earnings Surpass Elevated Expectations:** 85% of S&P 500 companies exceeded Q3 estimates with ~12% earnings growth versus 7.7% consensus-strongest since 2021-though cyclically adjusted P/E exceeding 40 signals dot-com bubble territory valuations.
- **Fed Cuts Amid Policy Uncertainty:** October 29th quarter-point cut to 3.75-4% and December 1st end to quantitative tightening created supportive liquidity, but Powell's cautionary stance dropped December cut probability to 60% amid sustained economic strength and above-target inflation.
- **International and Gold Lead Alternatives:** Emerging markets surged 4.19% in October (33.55% YTD) while gold's 3.73% gain extended remarkable 52.52% year-to-date return despite intra-month volatility, as crypto declined 7.60% and dollar strengthened 1.71% (-6.78% YTD).
- **China's Rare Earth Leverage Persists:** Trump-Xi one-year trade truce provides tactical supply chain relief but doesn't resolve China's 70% mining and 92% processing monopoly, with Beijing's demonstrated willingness to weaponize rare earth controls.

Monthly Recap

The S&P 500 Index delivered a solid 2.34% gain in October, continuing its remarkable recovery from the April 8th trough. The Nasdaq Index advanced 4.72% while small-caps posted modest gains with the Russell 2000 Index rising 1.81%. The "Magnificent 7" tech giants delivered a strong 4.93% gain in October, maintaining their position as the dominant force in the market's historic rebound.

The Recovery Story Accelerates: From the April 8th bottom through October, equity markets have posted extraordinary gains with the S&P 500 surging 38.21%, the Nasdaq rocketing 55.94%, and the Russell 2000 climbing 41.83%. The Magnificent 7 index has delivered an exceptional 69.02% recovery, completely erasing the steep February-April declines (S&P 500 -18.75%, Nasdaq -23.77%) and pushing indices substantially beyond previous highs.

Growth vs Value and Market Cap Dynamics: October saw growth stocks dominate decisively, with Russell 3000 Growth advancing 3.46% versus value's 0.43% gain. This widened the year-to-date leadership gap to 20.84% for growth versus 11.96% for value. Large-caps continued their strong performance with the Russell Top 50 gaining 3.63% in October, extending their year-to-date advantage to 20.69% versus small-caps' 12.38%.

Sector Performance: October sector leadership was commanded by Technology (+6.68%), which posted strong gains after its August decline. Health Care showed solid strength with +3.65%, followed by Utilities (+2.17%). Industrials added 0.54% while Consumer Discretionary gained 0.12%. On the downside, Materials declined 4.41%, Communication Services fell 3.01%, Real Estate dropped 2.92%, Financials declined 2.78%, Consumer Staples fell 2.67%, and Energy slipped 1.35%. Year-to-date sector leadership shows Technology dominating at 29.91%, followed by Utilities (20.16%) and Communication Services (19.64%), with Consumer Staples the only negative sector at -1.11%.

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International Markets Advance: International markets posted solid gains in October, with MSCI Emerging Markets delivering an impressive 4.19% versus the S&P 500's 2.34%, while MSCI World ex-US gained 1.09%. Year-to-date, international outperformance remains dramatic: emerging markets +33.55%, international developed markets +27.42%, both substantially ahead of the S&P 500's 17.50% return. From April's recovery bottom, emerging markets have advanced 42.32% while international developed markets gained 29.95%.

Fixed Income Gains and Mixed Alternative Assets:

Bonds showed positive performance with the Bloomberg US Aggregate gaining 0.62% and 20+ Year Treasuries rising 1.38%, benefiting from rate expectations. High-yield corporates added a more modest 0.16%. The Bloomberg Galaxy Crypto Index declined 7.60% in October after its extraordinary recovery run, though remains up 7.56% year-to-date and a remarkable 83.85% from the April lows. Commodities continued their positive trajectory with 2.56% October gains, extending their year-to-date return to 8.65%, while the Bloomberg US Dollar Spot strengthens 1.71% in October, down 6.78% year-to-date. Gold continued its stellar performance with 3.73% October gains, extending its remarkable 52.54% year-to-date return and 34.18% recovery from the April lows. However, gold exhibited significant intra-month volatility in October, surging from \$3,858.96 at the end of September to an all-time high of \$4,356.30 on October 20th before pulling back to \$4,002.92 by month-end, demonstrating both the precious metal's appeal as a safe haven and its susceptibility to profit-taking after sharp rallies.

Market Outlook: October's performance reinforced one of the most compelling comeback stories in recent market history, with technology and growth stocks reasserting their leadership. The complete round-trip from February's peak through April's trough to new recovery highs demonstrates extraordinary market resilience. With technology leading the charge, robust international performance particularly in emerging markets, continued strength in gold and bonds, and most major asset classes participating in the rally, the recovery that began in April continues to establish new precedents for market durability and breadth.

Corporate Strength Provides Solid Foundation

Corporate America is delivering results that exceed even elevated expectations. Approximately 85% of S&P 500 companies have surpassed third-quarter profit estimates, marking the strongest performance since 2021-particularly impressive given that analysts had raised their forecasts

heading into earnings season. JPMorgan Chase strategists project earnings growth of roughly 12% for the quarter, well above the 7.7% consensus. This strength spans multiple sectors, from financial institutions like Citigroup and Morgan Stanley to industrial giants like General Motors, which raised guidance on strong truck sales, and cConsumer sStaples companies like Coca-Cola, demonstrating pricing power despite elevated costs. Large corporations are expressing confidence about navigating regulatory uncertainty and maintaining robust capital expenditure plans, providing a crucial anchor of stability during periods of economic data uncertainty.

The AI Revolution Accelerates

The artificial intelligence (AI) investment boom continues to intensify rather than plateau. Tech giants Microsoft and Alphabet have acknowledged falling behind in building capacity to meet signed contracts, while Nvidia's CEO reports visibility into over \$500 billion in orders for current and next-generation chips over the coming five quarters. The Magnificent Seven 7 tech companies alone are expected to deploy approximately \$350 billion in capital expenditures this year, driven by AI infrastructure demands. Importantly, the benefits are beginning to spread beyond the mega-cap technology names – Advanced Micro Devices recently surged on an AI infrastructure partnership with OpenAI, while Industrials and Consumer Discretionary sectors also show strong performance, suggesting the market rally is gradually broadening beyond its initial narrow leadership.

Monetary Policy: Supportive Yet Uncertain

The Federal Reserve's (Fed) recent actions have created favorable conditions for risk assets, though the path forward remains cloudy. The Fed delivered a quarter-point rate cut on October 29th, lowering rates to 3.75-4%, and announced the end of quantitative tightening beginning December 1st. This combination of less restrictive rates and cessation of balance sheet reduction by the Fed is generating a rising tide of liquidity that strategists believe points risk assets "heavenwards." However, Fed Chair Jerome Powell tempered enthusiasm by indicating a December rate cut is "far from" certain, causing an immediate market reaction. Traders now assign only 60% probability to a December cut, down from near certainty before the meeting. The Fed appears to be easing despite sustained economic strength and above-target inflation, a dynamic that could fuel asset price appreciation if it continues.

Risks That Cannot Be Ignored

Despite positive momentum, significant headwinds loom. U.S. equity valuations have reached extreme levels, with the cyclically adjusted price-earnings ratio exceeding 40-territory last visited during the dot-com bubble's peak in 2000. Vanguard research characterizes U.S. markets as historically expensive even under optimistic assumptions about sustained profit margins, and notes that American valuations are substantially elevated relative to global peers. Geopolitically, while President Trump and Chinese leader Xi Jinping agreed to a one-year trade truce, markets reacted with indifference, viewing it as temporary stabilization rather than resolution of fundamental tensions. The specter of tariff-driven inflation persists, with one CEO warning that as retailers exhaust pre-tariffed inventory and gradually raise prices, a "major shock to retail and the economy" could materialize next year. Adding to the cautionary signals, gold's surge suggests parts of the market are seeking safe haven amid concerns about hidden credit market losses.

The market thus presents a paradox: strong fundamentals and supportive liquidity conditions argue for continued gains, yet elevated valuations and unresolved macro risks counsel prudence. Investors must weigh robust earnings momentum and transformative AI investment against euphoric valuations and geopolitical uncertainties that could quickly alter the trajectory.

Topic of the Month: Rare Earth Elements

Rare earth elements represent one of the most critical and strategically vulnerable segments of the global technology supply chain. China's near-monopoly position, controlling approximately 70% of mining and 92% of processing capacity, creates unprecedented geopolitical leverage that is actively being weaponized in the ongoing U.S.-China trade conflict.

The current escalation in export restrictions, license requirements, and supply chain controls marks a fundamental shift in how critical minerals are being used as instruments of economic statecraft.

Following Trump-Xi Jinping talks in South Korea, the U.S. and China have agreed to a one-year trade truce that includes a settlement of the rare earths dispute. While some may argue that the dispute is settled, the agreement is more accurately described as a tactical pause rather than strategic resolution. Both nations are buying time to reduce mutual dependence, with China retaining what

former Commerce Ministry adviser Tu Xinquan describes in the Financial Times as a "trump card" that has "seized America's weak spot."

Key Investment Considerations

- One-year trade truce provides temporary supply chain stability but does not resolve structural dependencies or strategic vulnerabilities
- China's demonstrated willingness to weaponize rare earth controls validates Western diversification efforts despite near-term normalization
- The truce buys time for both sides – China to consolidate advantages, U.S. to develop alternative supply chains requiring 3-5 years
- Markets likely to experience reduced volatility near-term, but structural risks remain with potential reemergence post-truce expiration
- Long-term investment thesis for supply chain diversification remains intact despite tactical détente

Market Overview & Strategic Importance

What Are Rare Earth Elements

Rare earth elements (REE) comprise 17 metallic elements including the lanthanides, scandium, and yttrium. Despite their name, these elements are relatively abundant in the Earth's crust, with cerium more plentiful than lead or tin. However, their geographic dispersion and extraction complexity make commercial mining technically challenging and capital intensive.

REEs are classified into two critical categories with distinct supply characteristics and strategic implications:

- **Light rare earths** (lanthanum to samarium) – More abundant but still strategically important for clean energy and industrial applications
- **Heavy rare earths** (europium to lutetium) – Scarcer, harder to substitute, and critical for advanced defense applications and high-performance electronics

The distinction between light and heavy rare earths has profound market implications. Heavy rare earths command premium pricing due to scarcity and their irreplaceable role in military systems, aerospace, and next-generation semiconductors.

Critical Applications Across Strategic Sectors

Sector	Strategic Applications
Clean Energy	Permanent magnets for EV motors and wind turbines (neodymium, praseodymium)
Defense & Military	F-35 fighter jets, Tomahawk missiles, guidance systems, radar, sonar. Samarium critical for military magnets. Dysprosium and terbium for heat regulation in aerospace applications.
Electronics & Technology	Smartphones, computers, AI chips, semiconductors, displays, batteries
Automotive	EV batteries, electric motors, catalytic converters (cerium). China sole producer of certain small magnets used in vehicles.
Healthcare	MRI scanners, advanced imaging, cancer treatments

China’s Strategic Monopoly

Global Reserve Distribution & Production Control

Country	Reserves (MT)	Production Position
China	44 Million	~70% mining, 92% processing
Brazil	21 million	Future challenger
India	~7 million	Growing production
Australia	~5.7 million	Stable infrastructure
United States	~1.9 million	Mountain Pass mine; 96% processing in China

Critical Processing Bottlenecks:

While reserve distribution shows some geographic diversity, processing capacity reveals China’s true chokehold. The separation and refining of rare earths require complex chemical processes, extensive technical expertise, and facilities that take years to develop. China’s dominance in this segment creates the most severe vulnerability:

Geopolitical Weaponization & Trade Conflict

China’s Export Control Evolution

China has systematically escalated rare earth export restrictions as a direct weapon against U.S. tariffs and

semiconductor controls, targeting critical supply chain vulnerabilities with increasing sophistication:

- Late 2024: Initial restrictions on gallium, germanium, antimony, and tungsten exports to U.S. in retaliation for Washington’s semiconductor curbs
- April 2025: Export licenses required for seven rare earth elements and permanent magnets, creating immediate supply uncertainty
- October 2025: Expanded restrictions to five additional rare earth elements, broadening scope of controls
- Military targeting: End-use certification requirements with “in principle” denial of applications for military production. Samarium exports for military magnets effectively halted for months
- Intellectual property and equipment lockdown: Rules preventing transfer of rare earth technical secrets, experienced personnel, and export of essential processing equipment and chemicals, blocking Western supply chain development

Strategic Leverage Mechanisms

While the truce provides near-term supply chain predictability, China’s structural control mechanisms remain in place:

Extraterritorial Control System

China’s most innovative control mechanism extends its authority far beyond territorial borders. The licensing system requires permission for cross-border movement of any magnets containing Chinese-origin rare earths representing at least 0.1% of value – even if those magnets were manufactured in third countries. This creates:

- Complex compliance challenges for global manufacturers who must track and document Chinese content across intricate supply chains
- Potential to block allied countries from supplying weapons to conflict zones, as any military equipment containing Chinese rare earths requires Beijing’s approval
- Comprehensive mapping of global rare earth demand patterns through required documentation, providing China’s Commerce Ministry a detailed “road map” of Western vulnerabilities

Trade Negotiation Dynamics

Rare earths function as primary leverage in U.S.-China trade negotiations. Framework agreements have temporarily unlocked rare earth flows and secured pauses

on new export controls, typically following high-level diplomatic engagement. Treasury officials have explicitly acknowledged China's strategy, noting agreements to "keep tariffs low if you keep the rare earths flowing."

However, experts caution this represents tactical maneuvering rather than strategic resolution. China's willingness to defer export control tightening provides negotiating flexibility while maintaining structural control. Beijing is unlikely to withdraw the licensing system entirely, meaning fundamental Western dependence remains unresolved despite periodic truces.

Supply Chain Disruption & Economic Impact

Immediate Effects of the Truce

The trade agreement immediately altered market dynamics that had been severely disrupted during the October escalation:

- **Production resumption:** Automakers and manufacturers that exhausted inventories during the crisis can resume normal operations. Ford Motor Co. and other companies that temporarily shuttered facilities expect to restart production
- **Price stabilization expected:** Gallium prices that increased 2-3x in the West versus China should moderate. Anticipated dysprosium price surges likely postponed
- **License processing normalization:** The "untenable" backlog of export license applications should clear as China adopts more permissive approval stance during truce period
- **Defense supply concerns reduced:** Near-term military production delays avoided, though stockpiling efforts likely to intensify during the one-year window

Long-Term Structural Implications

Critically, the truce does not alter fundamental supply chain vulnerabilities or strategic imperatives:

- **Diversification imperative reinforced:** China's demonstrated willingness to weaponize rare earth controls validates Western efforts to develop alternative supply chains. Government and private investment in domestic capabilities likely accelerates rather than diminishes
- **Timeline pressure intensifies:** The one-year truce creates urgency for Western nations to advance mine-to-magnet capabilities. Projects requiring 3-5 years face pressure to accelerate development

- **Capital deployment continues:** Substantial capital investment in mining, processing facilities, and recycling capabilities proceeds despite near-term supply normalization
- **Technology development accelerates:** research and development spending on substitution technologies, efficiency improvements, and recycling advances maintains momentum as insurance against future restrictions
- **Economic risk persists:** The \$150 billion potential economic output loss from 10% supply disruption remains relevant risk scenario post-truce expiration

The market is essentially bifurcating into China-controlled supply chains and nascent Western alternatives, with the transition period creating significant volatility and opportunity for investors who correctly anticipate timing and winners.

Key Risk Factors

The one-year trade truce fundamentally alters the risk timeline but does not eliminate underlying vulnerabilities. Investors must carefully weigh multiple risk dimensions across different time horizons.

Truce-Related Risks

- **Expiration cliff risk:** One-year timeline creates hard deadline after which restrictions could snap back to pre-truce levels or intensify further. Markets may underprice this tail risk during stability period
- **False security:** Supply chain normalization may create complacency, reducing urgency for diversification efforts precisely when time is most critical. Western governments and companies may deprioritize alternative development
- **China's strategic positioning:** As Tu Xinquan noted, China is using this year to consolidate advantages. Beijing may enhance processing capabilities, secure additional resources, or develop new control mechanisms during the pause
- **Truce fragility:** Agreement could collapse before expiration if other trade disputes escalate. Taiwan conflict, technology controls, or tariff disagreements could trigger rare earth restrictions resumption

Geopolitical and Policy Risks

- **Post-truce escalation:** When this agreement expires, both sides will have had time to harden positions and develop alternatives. Renewed confrontation could be

more severe than the 2025 October crisis as both sides feel better prepared

- **Taiwan scenario:** Conflict over Taiwan would likely trigger immediate and complete rare earth cutoff regardless of truce, with catastrophic effects on Western technology and defense manufacturing
- **Third-party disruptions:** Alternative supply chain development in unstable regions (Africa, Latin America) faces political risk. Government changes could disrupt Western rare earth projects.

Market and Price Risks

- **Volatility compression/expansion:** Truce likely compresses price volatility near-term as supply normalizes. However, post-expiration volatility could exceed pre-truce levels as uncertainty returns with higher stakes
- **Demand destruction:** One-year window provides time for manufacturers to implement substitution technologies and efficiency improvements, potentially permanently reducing rare earth consumption
- **Oversupply risk timing:** If Western supply chains mature just as truce normalizes Chinese exports, market could face oversupply crushing prices and stranding investments

Development and Operational Risks

- **Timeline mismatch:** Western processing facilities require 3-5 years, but truce expires in one year, creating vulnerability window where restrictions could return before alternatives become operational
- **Capital intensity:** Projects require hundreds of millions in upfront investment with uncertain economics if Chinese supply normalizes permanently
- **Technical expertise gap:** Western companies still face steep learning curves.

Conclusion

The Trump-Xi trade truce represents a significant tactical pause in rare earth tensions but not a strategic resolution. China's actions demonstrate Beijing's clear understanding

of the leverage provided by rare earth controls and their effectiveness in targeting critical American vulnerabilities. The mutual agreement to step back reflects that both nations faced substantial economic consequences from the escalating confrontation, validating the potency of China's strategic position while also revealing its costs.

The one-year timeframe creates a critical window with divergent implications. For manufacturers, it provides breathing room to rebuild inventories and stabilize operations. For governments and investors, it offers time to advance alternative supply chains that remain 3-5 years from maturity. For China, it allows consolidation of advantages and strategic positioning. Neither side views this as permanent settlement – both are buying time to strengthen their positions for renewed competition.

Investors should not interpret near-term supply stability as resolution of structural vulnerabilities. The October crisis validated fears about China's willingness to weaponize rare earth dominance, lending urgency to diversification efforts despite the current pause. Western nations now understand they face an adversary with demonstrated intent and capability to disrupt critical supply chains, creating sustained political will for alternative development even as immediate threats recede.

Market participants should expect continued geopolitical maneuvering, periodic supply disruptions, and dramatic price swings as this strategic competition unfolds. Success requires not only understanding technical and economic fundamentals but also monitoring geopolitical developments and policy evolution across multiple jurisdictions. The rare earth market has moved beyond traditional commodity dynamics to become a key battleground in great power competition, with implications extending far beyond the elements themselves to the technological and industrial systems they enable.

Sincerely,

The James Research Team



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