Fayez Sarofim & Co. Large Cap Equity Strategy

SEPARATELY MANAGED ACCOUNTS | MANAGER COMMENTARY | Q2 2025

MARKET REVIEW

"We expect volatility to continue as markets await further clarity on the potential impacts of tariffs and the direction of monetary and fiscal policies."

The S&P 500 gained 10.94% in the second quarter to reach new record highs; however, these strong gains mask the heightened volatility throughout the period due to tariff policy uncertainties. Announced U.S. trade policies triggered a global equity sell-off in April, driven by concerns of potential trade wars, rising consumer prices, and the heightened risks of a broader economic slowdown. However, markets recovered in the second half of the quarter as investors welcomed a de-escalation in trade tensions, along with strong corporate earnings reports, resilient consumer spending data, and accommodative central bank policies.

At the beginning of April, President Trump announced sweeping tariffs on America's trade partners, stating a goal to lower America's trade imbalances and achieve bilateral trade deficits of zero. Specifically, these policies would include tariffs on China (34%), the European Union (20%), and Asian trade partners, such as Vietnam, Japan, Taiwan, and South Korea (with tariffs ranging from 20-46%). For countries where the U.S. runs a trade surplus, a baseline 10% tariff was announced. Investors were shocked and rattled; stocks sold off as the magnitude of these tariffs were far more pervasive than initially anticipated. A week later, a 90-day pause was instituted, and a universal 10% baseline tariff was enacted to allow for further negotiations.

The only country excluded from the 90-day pause was China, which saw a 145% tariff applied (a level reached through a series of escalations); China responded by levying a 125% tariff on American-made goods. After trade representatives from the U.S. and China met in May, the U.S. trimmed Chinese tariffs from 145% to 30% and China cut its tariffs on American-made goods from 125% to 10%. This de-escalation between the world's two largest economies set the stage for further negotiations and drove a rebound in global equity performance. As similar patterns emerged in trade negotiations with countries across Asia, the E.U., Canada, and elsewhere, equity markets rallied, and market participants expected that trade deals with the U.S. were ultimately achievable, despite the Trump administration's tough initial stance.

The U.S. Federal Reserve chose to hold rates steady in the quarter, as the agency anticipated an uptick in inflation with businesses potentially passing on higher tariff costs to consumers via price increases. In contrast, America's tariff announcements would likely challenge growth prospects for an already stagnant Europe and export-dependent Asia. In response to trade tensions, major central banks across Europe and Asia cut their respective interest rates to ease credit conditions in a shift of their collective focus from fighting inflation to supporting economic growth.

During the first quarter earnings season, corporations reported better-than-expected earnings growth and addressed key investor themes, including the consumer outlook, continued artificial intelligence (AI) investments, and strategies to navigate a dynamic tariff environment. Consumer packaged goods companies discussed ways to shift manufacturing closer to end markets to minimize tariff costs while not alienating price-sensitive consumers. Companies that cater to discretionary spending categories, including companies in the luxury, automotive, beauty, spirits, cruise lines, and restaurant sectors, have reported a slowing in consumer spending. Overall, consumer spending remained strong and undeterred by the myriad tariff threats in the first quarter. However, companies have issued more cautious outlooks and have paused investment plans. Many are opting for a "wait-and-see" approach, preferring finalized trade deals to be signed before implementing price adjustments or reorganizing supply chains.

The large technology companies within the S&P 500 reported strong earnings and continue to spend on AI infrastructure. These tech giants reported continued demand for their AI hardware and services, which was driven by efficiency gains and product improvements in the quarter. Consequently, they issued better-than-expected guidance and higher capital expenditure plans to expand AI computing capacity in the year ahead, which drove equity gains and positive sentiment.

The S&P 500 recovered from the tariff shocks, but uncertainty related to global trade policies continues to weigh on investor sentiment. Geopolitical risk re-entered the conversation as conflict between Israel and Iran erupted, but the two nations quickly agreed to a ceasefire. This caused volatility in the price of crude oil globally, but didn't derail the stock gains that were driven by tariff de-escalation and strong earnings.

PERFORMANCE REVIEW

An underweight allocation in the utilities sector boosted relative performance in the quarter. Positive allocation and stock selection effects within the real estate and industrials sectors contributed positively to relative results.

Conversely, the dual impact of negative allocation and selection effects across the financials and energy sectors detracted from relative performance. A negative stock selection effect within the consumer discretionary sector also detracted from relative results in the quarter.

TOP CONTRIBUTORS

The top contributors to relative performance include **Microsoft, NVIDIA, Amazon.com, Meta Platforms, and Intuit.**

TOP DETRACTORS

The top detractors from relative performance include **UnitedHealth Group, Apple, Chevron, Eli Lilly, and Progressive.**

MARKET OUTLOOK

Fayez Sarofim & Co. investment philosophy remains steadfast during periods of heightened uncertainty. While we expect volatility to continue as markets await further clarity on the potential impacts of tariffs and the direction of monetary and fiscal policies, we have conviction in the long-term strength of the capital markets. We believe that our portfolio companies, which are comprised of what we consider to be global industry leaders, are well-equipped to navigate near-term market challenges.

Top 10 Equity Holdings (6/30/25)*	
Microsoft	8.00%
NVIDIA	8.00%
Amazon.com.	5.75%
Apple	5.00%
Meta Platforms	4.50%
Alphabet	4.00%
Visa	3.50%
Intuit	3.00%
BlackRock	2.50%
Intuitive Surgical	2.50%

*Source: Fayez Sarofim & Co. Top 10 equity weights are based on a representative model account, exclusive of cash. Individual accounts may vary. There is no assurance that the securities will remain in the portfolio or that other securities have not been purchased.

The holdings listed should not be considered recommendations to purchase or sell a particular security. It should not be assumed that securities bought or sold in the future will be profitable or will equal the performance of the securities in this list. Fayez Sarofim & Co. will provide a list of all securities purchased and sold during the past year upon request.

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RISKS

Equities are subject to market, market sector, market liquidity, issuer, and investment style risks, to varying degrees. Investing in **foreign denominated and/or domiciled securities** involves special risks, including changes in currency exchange rates, political, economic, and social instability, limited company information, differing auditing and legal standards, and less market liquidity. These risks generally are greater with emerging market countries**.**

Index Definition

The **S&P 500® Index** is a widely accepted, unmanaged index of U.S. stock market performance. An investor cannot invest directly in any index.

Definitions

Q is quarter. **FDIC** is Federal Deposit Insurance Corp. **SEC** is US Securities and Exchange Commission. **UMA** is unified managed account.

Artificial intelligence (AI) refers to computer systems that can perform tasks typically requiring human intelligence, such as visual perception, speech recognition, decision-making, and language translation.

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