

Commerce Trust Market Brief with Scott Colbert

Market Questions Timing of Next Fed Interest Rate Cut and AI Momentum

Recorded November 19, 2025

Scott Colbert: Good morning. It's Wednesday, November 19th, and the markets are open and trending slightly higher after having had a rough week or two since we've last talked. The S&P 500 (Index) is still up, not as much as it was, but still up a positive 13.76%. The smaller stocks have not participated. The average stock price is only up 7% when it comes to the S&P 500 (as measured by the S&P 500 Equal Weight Index). And the Russell 2000 (Index) is up closer to 6.5% when you dive into the smaller 2000 stocks in the country.

International stocks still continue to be standouts, but they've given up a bit of their peak returns. The large cap (capitalization) developed market stocks now are only up 24.12% (as measured by the MSCI EAFE Index), and the emerging markets are still the winner, up 29.17% year-to-date (as measured by the MSCI Emerging Market Index).

The fixed income markets have also participated positively as interest rates have come down a bit this year. The broadest measure of the market, the Bloomberg Aggregate (Index), is up 6.72%. And municipals (municipal bonds), which were mostly flat for most of the year, are now up a solid 4% (as measured by the Bloomberg Municipal Index) plus return on a tax-free basis.

So there are effectively two things troubling the markets that have produced this recent modest correction. The first is: will the Fed (Federal Reserve) or won't the Fed cut interest rates? And the second is: how frothy is all of the AI (artificial intelligence) momentum in the market?

When it comes to interest rates, we can see that the Fed, having cut interest rates twice already this year, has pulled the short end of the market down. The two-year Treasury has rallied from 4.25% down to something closer to 3.6%, or basically 65 basis points so far this year.

The ten-year Treasury has also followed suit, but not quite as much, having fallen from about 4.5% to something closer to 4%, basically about a 50-basis-point reduction in the ten-year Treasuries. Out in the long end of the market, the 20- and 30-year part of the market. It's barely budged, mostly because those aren't terribly impacted by short-term interest rate decisions.

So what is holding the Fed back? Well, clearly, it's still sticky inflation with some Fed governors more focused on that than they are the job slowdown. You can see that the core CPI (Consumer Price Index) and PCE (Personal Consumption Expenditures Price Index) has made very little progress over the past year. And the core PCE, the Fed's favorite measure of inflation, flat at 2.9%, really showing no improvement at all over the past 12 months.

Of course, not helping to lower inflation at all are all the near-term tariffs. There have been a lot of renegotiations recently on the tariffs, but we still think that the average import price has probably increased about 15%. Fortunately, we're not importing quite as much, and we don't think the inflationary impact of tariffs is nearly going to be as strong as initially thought.



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While we initially thought that the tariffs might push inflation up in the neighborhood of 3.6% to 4%, it's pretty clear that the inflation impact is coming on slower. It may last a little longer, but it's not likely to be as acute as initially thought. We still believe that inflation by the end of next year will likely be trending down.

And while the Fed is concerned about inflation, they're also concerned about the sharp slowdown in job growth. The reason that they worry about the sharp slowdown in job growth is because when job growth turns negative, typically a recession ensues. You can see the historical correlation between job growth and recessions on the chart provided.

If we zoom in on that job growth chart a bit closer, you can also see the recent precipitous drop in job growth. Thus, the Fed's willingness to cut interest rates at all when inflation is still stuck at the 3% level, about 100 basis points higher than their targeted 2% range.

So where is this job slowdown coming from? If we look a little closer, it's pretty clear to see that the agricultural sector of our economy didn't hire nearly as many workers as they normally do, mostly because those workers were not there to hire. And we know with certainty that government job growth has slowed as well. We're not actually sure what the impact of AI is, but it's clearly been negative. And of course, the tariffs have also directly slowed production in the country, at least initially.

Those four sectors, agriculture, government, AI, and direct tariffs probably account for about half the job loss. But we would basically suggest that the other half of the job loss is basically related to the tariff malaise that businesses are trying to work their way through and the uncertainty that it creates.

So, where does that leave the Federal Reserve and our expectations for short-term interest rate cuts? Well, they're clearly balancing these two risks: sticky inflation but a tremendous slowdown in job growth. Right now, the market is estimating that the first cut has been pushed out all the way to March of next year. We would still suggest that the weak economic indicators likely to be provided as the government reopens and they catch up on all of the economic statistics, are likely to suggest that the economy is a bit weaker than it was when the government shut down.

And we do believe that this will also probably pull the Federal Reserve into moving interest rates a bit lower, a bit sooner than the market expects. So, there's an awfully lot of economic news to digest, and we'll keep you up to date on all the financial markets moving forward.



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