

Week in review and ahead (vol.45)



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November 9, 2025

The past week was volatile as risk-off sentiment overtook markets amid continued hawkish commentary from FOMC members, continued government shutdown, now the longest on record, and generally elevated valuations. Bitcoin prices, which can be viewed as proxy of risk (sentiment) and somewhat correlating with the tech-heavy Nasdaq, were very much in focus with prices falling below \$100K, a highly watched support level by many, the first time since June'25 - the last time it experienced heightened volatility. Bitcoin and the market's price action appeared to stabilize on Friday with the former trading above \$100k at the time the markets closed, but down -7% on the week. As of writing this update, prices were trading above \$104K. The coming weeks will be notable to determine if the underlying momentum remains intact, however. Generally, markets perform well as the holiday season nears, with the S&P500 posting gains 15 of the last 20 years.

All major indices in the US decline for the week, with the tech-heavy Nasdaq leading with the steepest decline of -3% for the week. The S&P500, Dow Jones, and small-cap Russell-2000, saw declines in the week of -1.6%, -1.2%, and -1.9%, respectively. The declines did not impact all sectors, however, with the more defensive sectors within the S&P actually advancing (i.e. consumer staples, utilities, financials, healthcare, materials, energy, and real estate), underscoring the pronounced decline and sell-off of high-beta risk assets like the tech sector that declined by -4.2% on the week.

With the exception of China and Honk Kong that advanced 1.1% and 1.3%, respectively on the week, all major global equity indices followed suit and saw declines for the week lead by Japan's Nikkei that declined by -4.1% after record setting weeks.

Cryptocurrency Performance

Bitcoin (BTC) and Ethereum (ETH), indexed to 100

Sources: Clearnomics, Bloomberg
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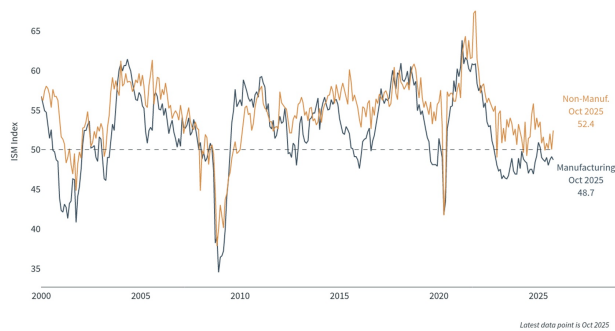
The government shutdown continues and is now the longest on record, depriving markets (and the Fed) of critical macroeconomic data. While private employment data is being reported on a recurring basis and offers a glimpse of the state of the labor market, inflation data and other data are more difficult to attain. Absent the government providing key macroeconomic data, reports from the Institute of Supply Management ('ISM') and S&P on the overall state and health of the economy, including inflation, however, did provide pertinent data for October taking on even more significance than usual.

ADP reported that private payrolls increased by 42K in October compared to estimates of 22K, and certainly significantly better than the decline of -29K in September. With the labor markets undergoing structural changes (i.e. immigration enforcement, labor force participation, and AI adoption) some economists believe the low-end estimate to maintain the current unemployment rate (of 4.3%) is about 30K, which if accurate, would mean that private payrolls alone exceeded it and may signal some stabilization in the labor market after months of declines and downward revisions to job growth. For reference, the mid-range estimate is 70-100K, while the high end is about 153K. Even

Similarly, the ISM reported that employment in the service and manufacturing sectors in October improved sequentially to 48.2% (from 47.2%) and 46% (from 45.3%), albeit both remained well in contraction territory (with readings below 50%). While the reading on the overall manufacturing sector continues in contraction territory and declined sequentially to 48.7% (from 49.1%), ISM's survey for the service sector surprised with a reading of 52.4%, well above expectations of a neutral reading of 50%, and certainly better sequentially (from 50.5%) as ISM reported with its PMI index for both sectors. Besides the PMI index for the service and manufacturing sectors, markets focused on the prices paid. While readings for both continue to show increasing trends in prices paid, it was the reading for services of 70% that caused some concern likely for FOMC members as well. The last time ISM's service price paid were at these or higher levels was in Oct'22 that saw the reading at 70.7%, at a time the Fed was aggressively raising rates to curb inflation. The reading for manufacturing did improve sequentially with a reading of 58% (down from 61.9%), however, it is the services impact that is a concern for most. Many FOMC members expressed concerns about re-accelerating inflation within services, and which certainly contributed to diverting stances on monetary policy during the most recent meeting.

Economic Activity Indices

ISM Manufacturing and Non-Manufacturing Indices
Numbers above 50 represent economic expansion



Sources: Clearnomics, LSEG, ISM
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Corporate earnings season continued favorably last week. Through Friday, with about 91% of all S&P500 companies having reported, 82% of those companies reported positive earnings surprises, well above the 10-year average (of 75%), matching the levels last seen in Q3'21. Per FactSet the aggregate earnings surprise of 7% above estimates currently matches the 10-year average, but comes in below the 5-year average of exceeding estimates by 8.4%. It should be noted that the averages used for comparison and reference, however, do reflect all 500 companies and as such offer some insight but may somewhat be distorted at this juncture. Corporate earnings continue next week but the

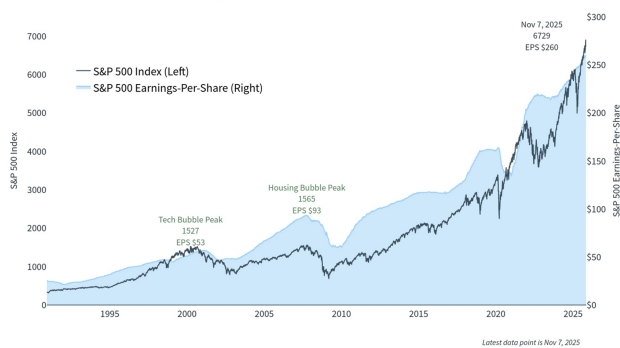
current reporting season is winding down.

Markets will focus on the price action of high-beta and risk asset classes to determine if the risk-off sentiment was one of caution or if it may undermine the current bull market. So far, many view the pullback as "healthy" and integral to any bull market. Admittedly, since April markets have been on a tear and have not really seen drawbacks of observed last week.

Finally, markets will look to Washington to see if the shutdown may be near its end. Besides depriving markets of critical datapoints, many governmental employees are now well beyond the 30-days of getting paid exacerbating personal hardship and that undoubtedly will negatively impact the US economy as a whole.

The Stock Market and Earnings

S&P 500 Index price and trailing earnings-per-share since 1990



Sources: Clearnomics, LSEG, Standard & Poor's
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If you have questions about how this may impact your investments, or how you should be positioned, please do not hesitate to contact us at claudio@caladocapital.com.

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