



Friends,

Merry Christmas to you. This is the time of year for thankfulness and reflection on the key relationships in our life. As we celebrate our 25<sup>th</sup> Christmas at Blue Waters, we are reminded that the BWAG Community and our Client Relationships mean everything to our business. While building financial plans and making money is our job (and we love doing it well for you), the main joy for us is our connections with you and how we go about serving you. We are thankful for your trust and friendship over the last 25 years.

***1 Chronicles 16:34 “Give thanks to the Lord, for he is good; for His lovingkindness is everlasting”***

**BWAG 2026 SERVICES IMPROVEMENT UPDATE:** 2025 was a year of improvement for us, both in the management of your investments, as well as in the service and communication we provide around that management. In 2026, we will continue to improve our visuals for you to see the results and the planning platforms of what we are trying to communicate about your plan designs and accomplishments.

This Past Year (felt like 5 yrs worth of headlines)

So many changes have occurred:

- Interest rates and Fed Tightening have started to get *reduced*
- *Tax reduction* packages and capital flows from global trade restructuring
- Major stock market sell off and recovery, connected to *tariff uncertainty*
- New Policy and corporate push for *tech and infrastructure* boom
- New *Capital Rules* starting in the banking system and Fed restarting its add to the balance sheet

Questions for 2026

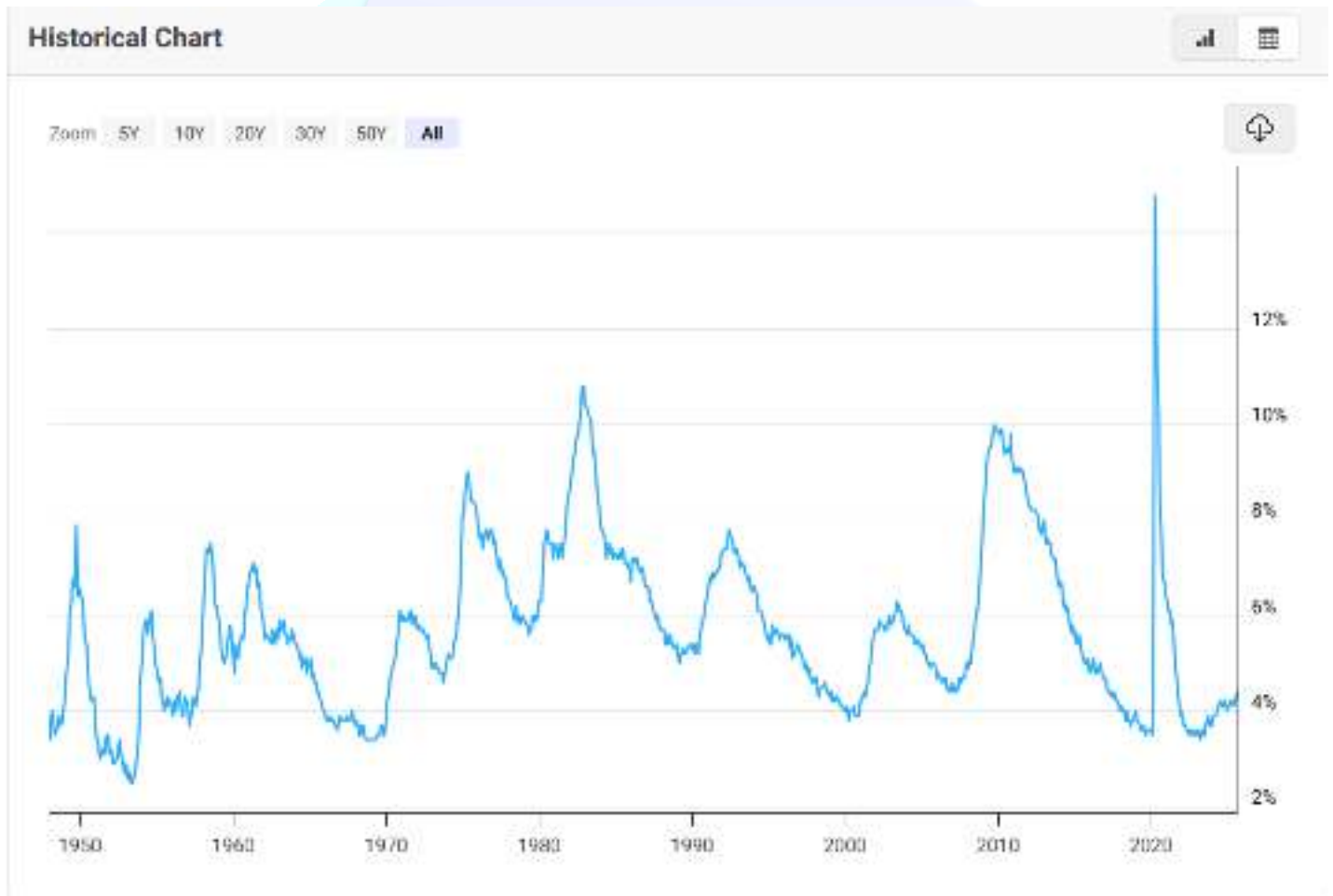
- Will the AI/Other Capital Events employment growth offset near term employment losses
- How much Tax Breaks will help with overall spending and employment
- Will we receive more Rate Cuts and see some new life in the private and real estate markets
- Will growth outperform the elevated Valuations

I will highlight some potential headwinds, as well as positive realities that likely will impact the economy in 2026. Amid all the likely events the market is pricing in and valuation challenges, we believe the economy will grow and stabilize in many areas, such as potential GDP outperform and FED balance sheet improvement.

## CONCERNS FOR 2026

### **FURTHER TARRIFS = POTENTIAL SHORT TERM RISE IN UNEMPLOYMENT**

Tariffs, intended to protect domestic industries, can inadvertently hurt jobs in the short term through several economic channels, often outweighing any short-term gains in protected sectors. Primarily, they raise costs for imported goods, which burdens U.S. companies and consumers with higher prices.



However, countervailing tariff hikes (e.g., 19–60% on China/EU imports) introduce headwinds: projecting a possible 4–6% long-run GDP drag, 5% in wage suppression, and potential \$1,200+ annual household costs from higher prices.

Net effect: Modest growth acceleration (2.6–2.8% in 2026) if investments outpace trade frictions, but risks of inflation (up 1%) and global slowdown (trade growth to 2.3%).

<https://bipartisanpolicy.org/explainer/tariff-tracker/>

## POTENTIAL ECONOMIC DISRUPTIONS

There are always potential disruptions, and 2026 has a few that could cause some sort of economic volatility. The main two at the forefront for the investment managers seem to be: World Geopolitics and the Federal Debt/Deficit. Geopolitics would be a clear black swan. It is impossible to predict any escalations of wars and other highly disruptive things that could come our way, but if any occur it would be an immediate adjustment need for the portfolio.

### Fed Balance Sheet getting better but still a Big Concern

I will focus on the Feds balance sheet and debt, as that could keep longer rates higher for longer and cause some future Government bond issuance and credit problems in the future. Fed Assets have grown over the last 6 years substantially (see chart below), however the debts have come down over the last 12 months.



### Financial volatility if US Supreme court over turning Tariffs in 2026

- **Massive Refund Obligations:** The government might be on the hook for refunding billions of dollars (potentially exceeding \$100 billion) in tariffs already collected, which could create a significant, sudden budget shortfall for the U.S. Treasury.
- **Market Volatility and Uncertainty:** The immediate aftermath of an overturn could hit financial markets with uncertainty about the future of U.S. trade policy and the administration's next steps. While some

sectors (like retail and small caps) might see a short-term boost from lower costs, the overall disruption could cause instability.

- Disruption to Trade Negotiations: The ruling could weaken the U.S. negotiating position in ongoing international trade talks, as other countries might question the President's authority to make credible tariff threats.
- Impact on Businesses and Consumers: While an overturn could lead to lower prices for consumers in the long run, businesses that paid the tariffs would face a complex, time-sensitive process to recover their money. Companies that absorbed costs or reorganized supply chains would need to adjust again

There are a couple solutions that economists see happening to offset. We can grow our way out of debt by having policies that help the growth rate stay higher than the fed funds rate (positives). We can cut costs at the federal budget level. The new administration has made a priority to cut federal employment, excess expenditure, and reduce expenses related to regulations.

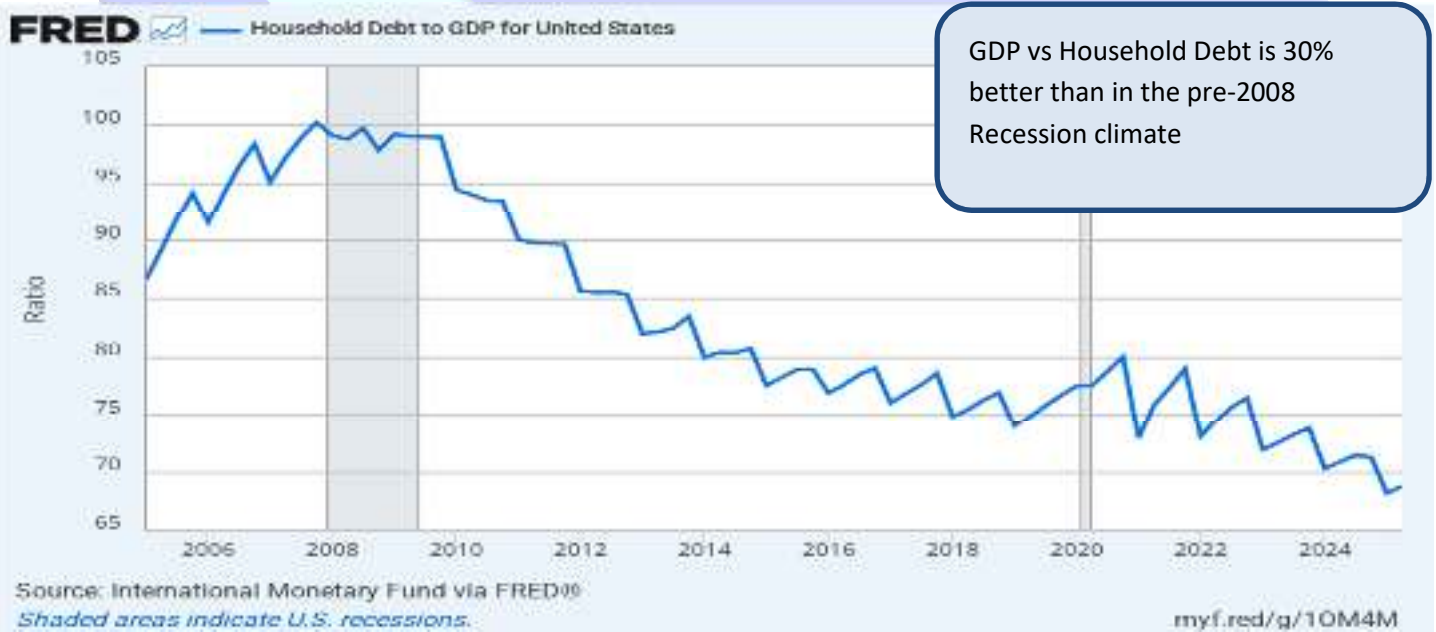
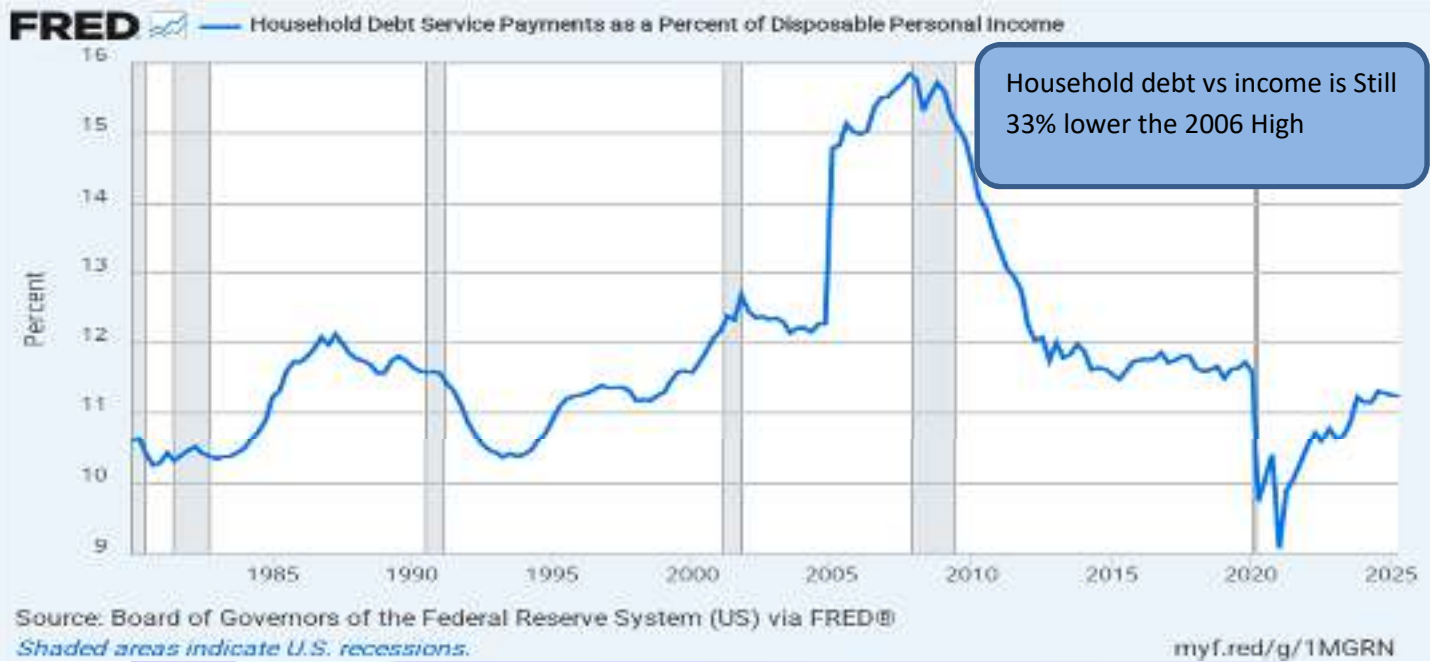
See implication in this article printed last week, it has great commentary on the Federal jobs cut (as a part of the jobs disappointment) and benefits to private payroll down the line: [nonfarm-payrolls-increased-64,000-in-november](#)

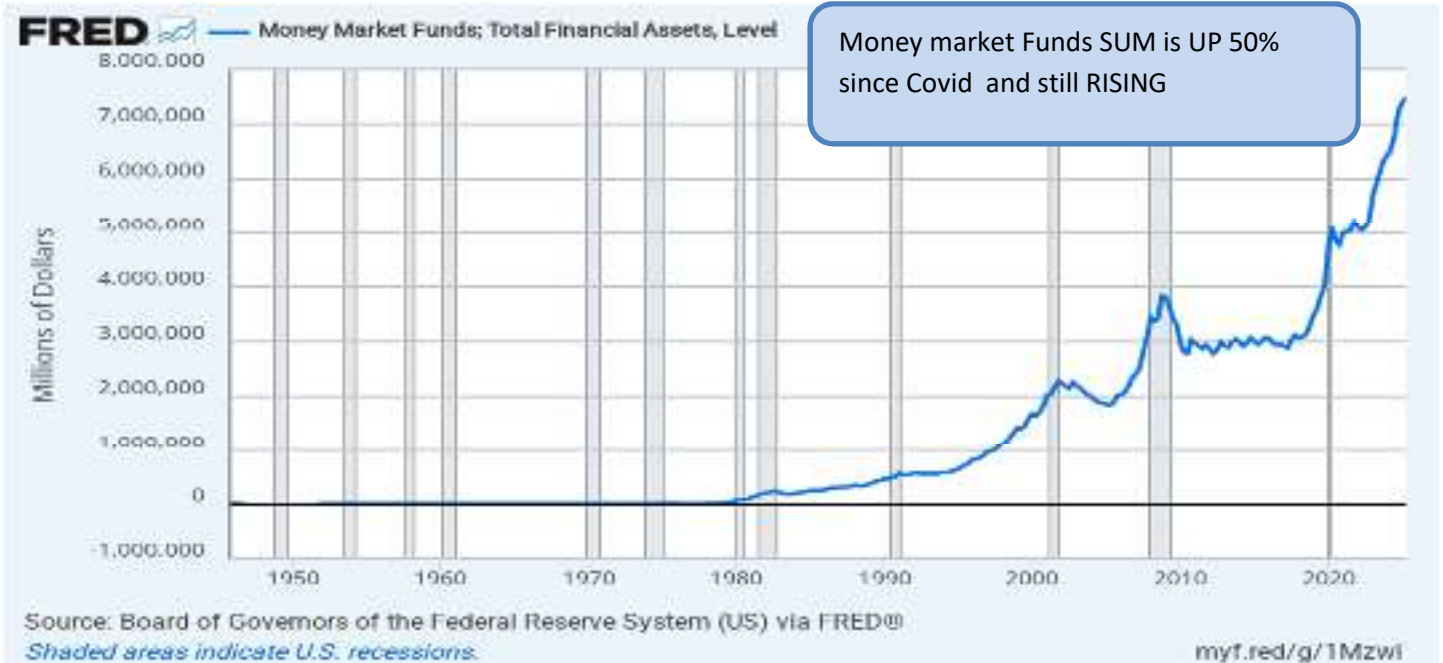
These measures won't do it alone, but it will certainly help eliminate the increase in budget deficit and allow for the growth the begin to chip away at it

## **POSITIVE EXPECTATIONS FOR 2025**

### **CONSUMER FINANCIAL HEALTH/JOBS/LIQUIDITY:**

The relative health of the US consumer at end of 2025 is intact. There is still a large U.S consumer discretionary income (See Chart below). 11.5% debt payments/Household is at the 40 yr Low, since the start of the 90s and 2000s booms. The locked-in nature of a vast majority of the mortgages market back in the covid lows has set the cost of owning a home at such low levels, making the general cash flow for families stronger over the long term. Also, most of the meaningful debt is held by the top 20% of the economy, in addition the mortgage is the majority of the debt that a middle-class household absorbs, thus showing a very healthy ratio.





Nearly 40% of the Houses in this country are paid off and have no mortgage. That means ½ the housing supply have no debt constraint.

According to an Article by *Realtor.com*, 56% of the current mortgages are locked in below a 4% Interest rate and 75% are under 5% Interest.

### **TAXES DECREASES COMING:**

The new administration lowered tax on corporations, service providers, and individuals as well as make the prior tax reductions permanent tax law, eliminating the fear of the tax jumping in the next 2 years (See Link Below with a summary of the proposals).

I think will be the biggest stimulant for the economy is the proposal to reduce corporate taxes for all companies that build and hire in America. That will be a double stimulant in that it increases cash flow and spending for the corporation, while also creating more spending and employment in the US.

### **Tax Changes for Individuals**

- **Permanent Tax Rates and Brackets:** The current individual income tax rates (e.g., the top rate of 37%) are made permanent, preventing them from reverting to higher pre-TCJA levels.
- **Increased Standard Deduction:** The higher standard deduction amounts are made permanent and adjusted for inflation (e.g., \$31,500 for married couples filing jointly in 2025).

- **Child Tax Credit:** The credit is permanently set at \$2,000 per child, but temporarily increases to \$2,200 per child for tax years 2025 through 2028.
- **No Tax on Tips and Overtime (Temporary):** The bill allows an above-the-line deduction for up to \$25,000 of tip income and up to \$12,500 of overtime pay annually through 2028, subject to income phaseouts.
- **Additional Senior Deduction (Temporary):** Individuals age 65 and older can claim an additional deduction of \$6,000 from 2025 through 2028, also subject to income limitations.
- **State and Local Tax (SALT) Cap:** The cap on the SALT deduction is temporarily increased from \$10,000 to \$40,000 per taxpayer through the end of 2029.
- **Electric Vehicle (EV) Credits Repealed:** Tax credits for new and used clean vehicles (30D and 25E) are no longer available for vehicles acquired after September 30, 2025.
- **Trump Accounts:** A new type of tax-deferred individual retirement account is created for newborns (2025-2028), with a government contribution of \$1,000 upon account opening and annual contribution limits.

## Business Tax Changes

- **Bonus Depreciation:** The 100% bonus depreciation for qualified property is permanently restored and expanded.
- **R&D Expensing:** Taxpayers are once again allowed to immediately deduct domestic research and development (R&D) expenditures, reversing a prior amortization requirement.
- **Qualified Business Income (QBI) Deduction:** The 20% QBI deduction for pass-through businesses is made permanent.
- **Opportunity Zones:** The existing favorable treatment for gains from investments in qualified opportunity zones is made permanent.

### How These Cuts could support Economic Investment:

- Corporate investment rise ~11–20% in the years after enactment
- Reverse a decade-long decline in business fixed investment
- Add an estimated 1 percentage point to annual GDP growth pre-pandemic
- Help create ~4.9 million jobs before COVID (including 1.1 million in manufacturing)
- Increase capital spending on factories, equipment, and technology
- Provide long-term certainty for businesses (especially with permanent corporate provisions)
- Incentivize investment in Opportunity Zones for distressed communities

[housecallpro.com/resources/one-big-beautiful-bill](https://housecallpro.com/resources/one-big-beautiful-bill)

## **US CAPITAL GROWTH INITIATIVES: US INDUSTRY NEW CAPITAL INVESTMENT**

US is aiming to reshore manufacturing, boost fossil fuel production, and foster innovation in tech and finance. Based on analyses from industry reports and policy trackers, here are the industries with the highest potential for expansion in 2026, ranked by projected impact:

Top US Industries Poised for Significant Growth in 2026 Under the Trump Administration Emphasis:

- Deregulation, tariffs on imports (e.g., 25% on steel, autos, and semiconductors),
- Tax incentives-Expensing for equipment/R&D,
- Increased defense spending,
- Energy independence

1. Oil and Gas Deregulation via executive orders declaring a “national energy emergency,” expedited permitting, and removal of barriers (e.g., methane rules delayed 18 months) will accelerate drilling and production. Tariffs on Canadian energy (10%) further protect U.S. producers like ExxonMobil, potentially increasing output by 5-10% and creating thousands of jobs, despite short-term price volatility. This aligns with broader fossil fuel promotion, including LNG exports, positioning the sector for 8-12% revenue growth.

2. Semiconductors and Advanced Manufacturing Onshoring incentives, including a bumped-up advanced manufacturing credit (25% to 35%) and over \$500 billion in commitments, will triple U.S. capacity by 2032, with 2026 as a key ramp-up year. Tariffs (32% on Taiwanese imports) shield firms like Intel and GlobalFoundries, driving factory expansions and AI/data center demand for components. Expect 15-20% growth in domestic production, fueled by trade deals renegotiating USMCA and partnerships with allies like Japan.

3. Aerospace and Defense Boosted by proposed defense budget increases (up 5-7%) and Musk-influenced space initiatives, this sector benefits from tariffs on foreign components and U.S.-focused spending. Companies like Honeywell and Planet Labs could see 10-15% stock and revenue surges, with reshoring rare earth minerals reducing supply risks. Policy carve-outs for domestic sourcing will enhance competitiveness against European rivals.

4. Financial Services and Crypto Rollbacks on regulations (e.g., dismantling CFPB, rescinding SEC’s SAB 121) and crypto-friendly moves like a U.S. bitcoin reserve will spur innovation and dealmaking. A stronger dollar from tariff-induced inflation aids banks like JPMorgan, while fintech sees higher lending to manufacturers. Projections indicate 12-18% growth, with congressional bills by mid-2026 solidifying digital assets as a mainstream investment.

5. Steel, Aluminum, and Critical Minerals Mining 25% tariffs on imports protect U.S. producers, enabling price hikes and plant investments (e.g., steel output up 2% in Trump’s first term). Streamlined mining for rare earths supports batteries and tech, with executive orders expediting permits. This could yield 10-15% production increases, bolstering supply chains for autos and renewables, though global retaliation poses minor risks.

6. Automotive (Domestic Manufacturing) Tariffs on imported vehicles/parts (25%) favor U.S.-based assemblers like Ford and Tesla, prompting expansions (e.g., Toyota’s \$88M investment). EV regulatory easing and tax provisions for equipment will drive margins up 5-8%, with job growth in Rust Belt states. Long-term, renegotiated trade pacts could stabilize exports for 2026.

These sectors are projected to contribute to overall U.S. GDP growth of 2.5-3% in 2026, up from 1.8% in 2025, as trade uncertainties resolve. However, risks like retaliatory tariffs or inflation could temper gains in import-reliant areas. Investors should monitor budget reconciliation for final incentives.

## **NEW US CAPITAL INVESTMENT COMMITMENTS via *WHITE HOUSE AGENDA***

Since returning to office in January 2025, the administration has aggressively pursued bilateral trade negotiations and deals, emphasizing “America First” policies to attract foreign direct investment (FDI) into the U.S. These efforts have yielded announcements of substantial capital commitments, primarily in manufacturing, technology, energy, and infrastructure. However, while White House tallies claim trillions in pledges, independent analyses and fact-checks highlight that many are aspirational, non-binding, or include domestic U.S. investments, with realized FDI likely in the hundreds of billions annually rather than trillions. The administration reports over \$5.8 trillion in foreign investment pledges tied to trade frameworks with more than a dozen partners, spanning 2025–2030

High-Level Summary of Capital Inflows from US Trade Deals:

- Gulf States and Middle East: \$3.2 trillion combined, led by UAE (\$1.4T in tech/aerospace/energy), Qatar (\$1.2T in manufacturing/tech), Saudi Arabia (\$600B in tech/manufacturing), and Bahrain (\$17B general).
- Asia-Pacific: ~\$1.4 trillion, including Japan (\$1T/\$550B in auto/steel/energy/AI; conflicting reports), South Korea (\$450B/\$350B in energy/shipbuilding), India (\$500B in manufacturing), Malaysia (\$70B general), and smaller pledges from Vietnam/Thailand/Cambodia (e.g., \$8B Vietnam Boeing aircraft).
- Europe: ~\$800B, with EU firms (\$600B general) and Switzerland/Liechtenstein (\$200B in pharma/machinery/energy over 5 years).
- Latin America and China - Over the Next 2–3 Years (2026–2028): Specific near-term tranches are limited but total ~\$500–700B if pledges hold.

These inflows, if substantially realized, could supercharge U.S. economic resilience by reshoring supply chains and funding high-growth sectors:

Investments: Prioritizes “friendshoring” in critical areas like AI infrastructure, semiconductors, clean energy, and ports—potentially adding \$1T+ in private capital for factories and R&D. This aligns with CHIPS Act extensions, accelerating domestic production and reducing reliance on adversaries like China.

Economy and Jobs: Could create 500,000–1M manufacturing/tech jobs over 2–3 years (per administration estimates), boosting GDP by 0.5–1% annually through multiplier effects (e.g., each \$1B FDI generates \$1.5–2B in output). Early 2025 data shows 3% Q2 GDP growth partly from import surges and investment surges. Regions like the Rust Belt and Sun Belt stand to gain most.

However, countervailing tariff hikes (e.g., 19–60% on China/EU imports) introduce headwinds: projected 4–6% long-run GDP drag, 5% wage suppression, and \$1,200–\$5,200 annual household costs from higher prices. Net effect: Modest growth acceleration (2.6–2.8% in 2026) if investments outpace trade frictions, but risks of inflation (up 1%) and global slowdown (trade growth to 2.3%).

Overall, a high-reward gamble favoring industrial revival over consumer affordability.

## **FED RATES PROJECTED TO CONTINUE DOWNWARD OVER NEXT 12 MONTHS:**

The new administration and the FED Reserve wants to continue to see lower rates as Inflation projects to be in a range acceptable for inflation and allowing the rate to settle .5% lower than today at 3 – 3.25% Fed Funds Rate over the next year.

The federal funds current target range is currently 3.75%-4.00%. The effective federal funds rate (EFFR) has been trading at approximately 3.89% in early December.

2026- .5% Rate Cut Projected: Most sources anticipate 1-2 additional quarter-point (25 bps) cuts, primarily in the first half of the year, lowering the rate to a median of 3.00%-3.25% by year-end. For instance, Goldman Sachs and Bank of America forecast two cuts (in June and July), targeting 3.00%-3.25%.

The general consensus among Federal Reserve officials, economists, and market analyst's points to a gradual easing of monetary policy through 2026 and into 2027, with additional rate cuts expected to bring the federal funds rate closer to its estimated neutral level. This outlook is shaped by projections of relative cooling inflation (probably above the Fed's 2% target), steady economic growth, and relative stable employment (flashes of employment problems have shown in the near term-Likely from tariffs/AI effects), allowing the Fed to reduce rates without reigniting price pressures.

• • Mid-2027: Expectations call for 1 more cut in early 2027, settling the rate around 2.75%-3.00%. This aligns with the FOMC's end-2027 median of 3.1%, reflecting a slowing pace of easing as the economy stabilizes.

We should see broader growth in these industries such as:

- New Housing starts/Construction boom as the country is still a decade behind in inventory
- Increased remodel projects
- Increased sales of Homes
- Increased sales of Commercial real estate and other private equity
- Trade of used cars for new cars

## **Corporate Profits and Outlook:**

For the recent Q3 2025 earnings season (ending early Dec 2025), the S&P 500 showed strong performance, with around **82-83% of companies beating earnings estimates**, significantly above historical norms, while guidance was also positive, with nearly **60% of companies raising full-year outlooks**, a strong trend.

Earnings growth accelerated to about 13.4% year-over-year, exceeding initial expectations, and revenue beats were solid but less stellar than EPS.

### **Key Figures for Q3 2025 Earnings Season (as of early December 2025):**

- **Earnings Beat Rate:** 82-83% (well above the 75% 10-year average).
- **Revenue Beat Rate:** 77% (also strong, but EPS stronger).

- **Overall Earnings Growth (EPS):** 13.4% year-over-year (accelerating from Q2).
- **Guidance Beat:** Nearly 60% of companies issuing guidance raised it, double the rate seen earlier in the year.

**What This Means:**

- **Strong Bottom-Line:** Companies are successfully exceeding profit targets, driven partly by AI themes and strong tech performance.
- **Positive Outlook:** Management teams are optimistic, issuing more positive future guidance than usual, signaling confidence.
- **Top-Line Strength:** While earnings are great, revenue growth is good but not as explosive as profits, though still above average

**VELOCITY OF M2 MONEY SUPPLY:**

This concept represents the movement of money in the economy and is a great sign of future growth. The Global money market Liquidity is still substantially higher than the 2007 bull market (see chart below)



The Velocity of money is substantially lower than normal Growing economies. There is inherent optimism in the economic growth projections due to the potential pick up in velocity over the next years. Largely, the capital markets have been halted for the last few years. We haven't seen the Mergers, Acquisitions, and Lending. Also, the liquid Investment capital hasn't translated to US Corporate Economic activity at the levels it could. Liquidity remains high and Movement of money is still relatively low, leaving us with very positive speculation about what is around the corner when the capital markets begin moving more. The movement of money "velocity" creates all sorts of economic windfalls for individuals and corporations in the form of new revenues and margins to spend on new opportunities. The excess liquidity in the world and the potential Next M2 Movement is a big potential stimulus to GDP over the next 3 Yrs. (see charts below).



## **MARKET OUTLOOK FOR 2026**

In summary, we still see continued strong economic growth with spotty disappointments in the U.S in 2026. We can also look forward to an improved financial capital environment along with a more pro-business administration in the white house. Here is what to expect from the Market:

### **HIGH STOCK VALUATIONS – PRECEDE RECESSIONARY MARKETS**

**We see increased Volatility in 2026, with potential sharp sell offs, but buying opportunities**

The Price of a stock in relation to the earnings of that company, is how we can value a company. The higher growth expectations of a company, the higher the Price tends to be. Forward P/Es have trended higher in recent decades due to lower interest rates and growth expectations. Elevated readings (above 20x) have been more common in the post-2000 era and often precede deeper corrections. It's possible that is the reason we have had so many more 15%+ sell offs over the last 5 Yrs.

- Current Forward P/E of the S&P 500 (as of December 6, 2025): 22.4x
- Current Forward P/E of the S&P 493 (as of December 6, 2025): 17.9x (reflecting non-Mag7 stocks)
- Current Forward P/E of the S&P 500 Financials Sector (as of December 6, 2025): 16.0x

## Key Insights:

- Median Forward P/E at peaks of Market: 18.0x. About half of these bear markets began with forward P/Es below 18x, typically during periods of economic uncertainty or rising rates, while higher ones (e.g., 2000 dot-com, 2022 inflation) aligned with optimism turning to reality checks.

## Tailwinds

- Improved Interest rate environment
- More money flow and new capital investment
- Increased Corporate Activity- acquisitions and refinancing
- Relatively Stable inflation over the next year
- Proposed Tax Cut for Businesses
- Proposed Reduction of Regulation
- Employment should stay relatively strong with the new business initiatives that we highlighted above
  - Green shoots in All things Tech, Capital Markets, All things Energy

## THEMES IN 2026

I think the best theme going forward is owning Quality Assets with a slight add to Value Sectors. In the short term I see some sell offs as jobs data shows increased volatility in early 2026, tariffs/results get challenged, and the AI stocks experience increased price scrutiny. We see all sell-offs as buying opportunities for the capital markets, Industrial/infrastructure build out, and Innovative Quality companies. In the end, general consensus is that the markets will end the year positive but not without their challenges. Here is a quick summary of my thoughts:

- We like the Quality Innovative Growth markets, connected to tech/Infrastructure growth
- We like the shorter end of the bond market, focusing on 3-7 years
- I anticipate seeing a broadening out of the market into sectors and sizes that haven't recovered from the rate hikes and thus offer better valuations. Areas of overweight such as:
  - Value, weighted to Capital Markets and Financials
  - Quality Small/Mid Cap, in particular stock that benefit from AI and Financials
  - Industrials focused on Mid cap infrastructure American companies, as well as Tech/Energy
  - Healthcare

We see volatility in early 2026, however the larger market dips should be buying opportunities leading to growth.

**I look forward to serving you in 2026 and the many years to come.**

Clay Carter

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