

# FORTITUDE CAPITAL MANAGEMENT

**Independence • Integrity • Insight**

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*"We cannot solve our problems with the same thinking we used when we created them."* – Albert Einstein

*"Beware geeks bearing formulas."* – Warren Buffett

Fellow Investors:

Now that 2025 is in the books, we can look forward to a calm, predictable 2026, right? Not a chance. We are living in a world of rapid change, and change that only seems to be accelerating. However, change brings opportunity and those opportunities flow through to our investments.

In the equity markets, the year can be bifurcated into before and after “Liberation Day” (April 2, 2025), when the initial tariff program was announced. The S&P 500 was down 15.28% on 4/8/2025 but finished the year up 16.44%. As in recent years, the return of the S&P was heavily driven by a handful of large tech companies. The “Magnificent 7” accounted for 46% of the total return of the S&P. While still an alarming concentration of index returns, the percentage accounted for by these seven companies is down from the 55% and 63% of S&P returns for 2024 and 2023 respectively. A broadening of returns would be healthy for the economy and investors. The other 493 companies returned 13% for 2025 and the equally weighted S&P 500 had a total return of 11.1% for the year.

Other indices performed in a similar pattern. The NASDAQ Composite returned 20.08% for 2025, having been down 20.94% on 4/8/25. The Russell 2000 was down 18.83% post Liberation Day and turned in a full year return of 11.29%. International markets outperformed US markets, assisted by a 9.7% decline in the value of the dollar (measured by the ICE US Dollar Index). All of this decline occurred prior to April. The MSCI EAFE returned 27.92% for 2025 and only reached a low point of being down 5.26% in April. When considering foreign markets, it is important to remember that the US equity markets represent 64% of world markets by capitalization.

Interest rates trended down throughout the year. The 10-year treasury finished the year at 4.14%, down 0.43% for the year although it did hit a high of 4.79% and a low of 3.97% over the course of the year. The two-year came down 0.80% during 2025, finishing at 3.45%. Lower interest rates partially reflect the lower inflation rate of 2.68% for 2025, a big improvement from the inflation experienced in recent years which peaked at 9.06% in June 2022. A big assist in the inflation fight came from lowering energy costs and bringing the growth of the money supply (M2) back to a more normal rate of 4.25%.

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Going back to the opening of this letter, how will the opportunities present themselves to investors? As we survey the “experts”, one hears a wide range of predictions. We have seen predictions for 2026 Gross Domestic Product (GDP) growth as low as 1.5% and as high as 5% plus. We are not relying on any of these for decision making for the simple reason that the track records of the prognosticators are rather abysmal. The factor on everyone’s mind, of course, is artificial intelligence (AI). While in the near term the focus is on the mega-cap companies and their capital spending, the longer-term effect on the broader economy will be where the average investor benefits. Improved productivity, information and data analysis, scientific research, logistics, customer service, etc. are examples of where we are already experiencing the benefits. As more businesses incorporate AI into their everyday procedures, the benefits will improve the bottom line, which should flow through to benefit shareholders. Of course, there will be disruptions, winners, and losers, but we expect the expanding benefits to lead to a broadening of market performance.

Markets do not only go up, of course. There is a lot of commentary regarding high equity valuations and the risk to investors of a market correction. First of all, corrections occur, and reacting to them, or worse, trying to predict them, does not have a good track record. Currently, the forward price/earnings (P/E) ratio of the S&P is about 22 times, compared to the average for the prior 30 years of 16.8 times. The concentration of the largest 10 companies in the index affects this as the forward P/E of the top 10 companies is 29.0 times, resulting in the remaining 490 companies in the S&P having a forward P/E of 19.3 times, still high compared to the 30-year average, but at a much more reasonable level. While using historical comparisons is useful, in this fast-changing economy we find using past comparisons less applicable. AI is a disruptor. The enormity of the upfront capital investment is beyond any historical comparison. The markets are trying to sort through the meaning and eventual results from these investments. As with past disruptors from the steam engine to the internet, the US economy adapts, incorporates the technology, and moves onward and upward.

There remains much uncertainty among the public and individual investors. Employment has seemingly stagnated, the housing market is tight and expensive, past inflation is still affecting affordability, and government policies are just beginning to take effect. What perhaps is being missed are some sound economic fundamentals. We have heard the job market described as a “no hire, no fire” economy. During a transitioning economy, employers are holding steady until the fog clears. While new hires are low, so are layoff announcements. Past innovations have led to more jobs at the end of the day, not less. Also being overlooked are increases in labor productivity, perhaps an early indicator of what is to come from AI.

Interest rates are only high relatively, not historically. We all became accustomed to the near zero rates following the Great Financial Crisis and the pandemic. Treasury rates are well within historical norms. Mortgage rates are similarly at or even below historic levels outside of the post Great Financial Crisis period.

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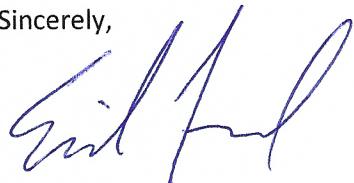
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These factors lead us to have confidence in markets going forward. There will be bumps in the road as always, but as new technologies are adopted, the economy will adapt and patient investors should benefit. We do not change our outlook for maintaining a diversified and risk-conscious portfolio. Regarding diversification, there are opportunities for individual investors to diversify into assets previously available only to the few. Areas like real estate, private credit, hedge funds, and private equity. Just to touch on the latter, 86% of companies with revenues greater than \$100 million are private. In the past, individual investors could not benefit from the success of these private companies.

Diversification and risk control are key aspects of achieving financial goals and we now have a broader (and growing) selection of alternatives to pursue our objectives.

Much is happening in the US, the world, and the markets. Be aware, be educated, and be prepared. Let us all have a healthy and prosperous 2026!

Sincerely,



Erik Ford



Jason Marrs

The Magnificent 7 is comprised of Nvidia, Apple, Meta, Amazon, Alphabet, Microsoft, and Tesla.

The S&P 500 Index, or the Standard & Poor's 500 Index, is a market-capitalization-weighted index of the 500 largest publicly traded companies in the U.S. It is not an exact list of the top 500 U.S. companies by market capitalization because there are other criteria to be included in the index.

The S&P 500 Equal Weight Index (EWI) is an equal-weight version of the popular S&P 500 Index. Although both indexes are comprised of the same stocks, the different weighting schemes result in two indexes with different properties and different benefits for investors.

The term Russell 2000 Index refers to a stock market index that measures the performance of the 2,000 smaller companies included in the Russell 3000 Index. The Russell 3000 is a capitalization weighted index representing approximately 96% of the investable U.S. equity market.

The MSCI EAFE Index tracks large cap and mid-cap companies in developed countries around the world. The index primarily covers the Europe, Australasia, and the Far East regions.

The NASDAQ Composite is a stock market index of the common stocks and similar securities listed on the NASDAQ stock market. Along with the Dow Jones Average and S&P 500 it is one of the three most followed indices in US stock markets. The composition of the NASDAQ Composite is heavily weighted towards information technology companies.

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The ICE US Dollar Index is a geometrically averaged calculation of six currencies weighted against the U.S. dollar: the euro, Japanese yen, British pound, Canadian dollar, Swedish krona, and Swiss franc. Currently, the euro holds a 57% weight in the calculation formula, having replaced 5 previously weighted currencies.

US M2 Money Stock refers to the measure of money supply that includes financial assets held mainly by households such as savings deposits, time deposits, and balances in retail money market mutual funds, in addition to more readily available liquid financial assets as defined by the M1 measure of money, such as currency, traveler's checks, demand deposits, and other checkable deposits.

The price-to-earnings (P/E) ratio measures a company's share price relative to its earnings per share (EPS). Often called the price or earnings multiple, the P/E ratio helps assess the relative value of a company's stock. The forward (or leading) P/E uses future earnings guidance rather than trailing figures. Sometimes called "estimated price to earnings," this forward-looking indicator helps compare current earnings to future earnings and can clarify what earnings will look like without changes and other accounting adjustments.