

MARKET OUTLOOK

AT A GLANCE

Markets continued their rally, driven largely by ongoing enthusiasm for AI-related investments. Yet headwinds are beginning to surface—from a tightening labor market to persistent inflation and rising geopolitical tensions. In this evolving environment, our team is focused on identifying opportunities that align with today's shifting market dynamics and positioning portfolios to capitalize on them.

ECONOMY / FIXED INCOME

Fed Funds Rate ↓0.25%

The market now expects an additional 0.50% in cuts by year-end as the Fed prioritizes the labor market.

EQUITY

POSITIVE Q3

S&P 500	+8.11%
S&P 600	+9.11%
S&P Kensho	+14.75%

PRIVATE MARKETS

Private equity firms are increasingly focused on long-term value creation over asset stripping—recognizing that sustainable growth strategies often lead to stronger, more enduring returns.



OUR TEAM IS DEDICATED TO UNCOVERING
UNIQUE INVESTMENT OPPORTUNITIES
THAT ARE BOTH TIMELY AND RELEVANT—
GUIDED BY RESEARCH, DISCIPLINE, AND
A FORWARD-LOOKING PERSPECTIVE
TO HELP CLIENTS NAVIGATE TODAY'S
DYNAMIC AND EVOLVING LANDSCAPE.

Christopher Zabel
Portfolio Manager

POSITIONING FOR A LATE CYCLE ECONOMY

SUMMARY:

The Fed has resumed rate cuts, citing slowing job gains and downside risks to employment. This comes despite elevated inflation and a still-growing economy.

OUR PERSPECTIVE:

The fiscal dominance (when deficits and debt dynamics limit monetary policy's room to maneuver) described in the third quarter outlook is now being met with more accommodative monetary policy in light of the economic headwinds faced by a tighter labor market.

The market response to the resumption of rate cuts by the Fed has presented an opportunity to reposition the fixed income allocation of most multi-asset portfolios to take advantage of yield curve steepening and higher term premiums (the extra yield investors demand to hold longer bonds).

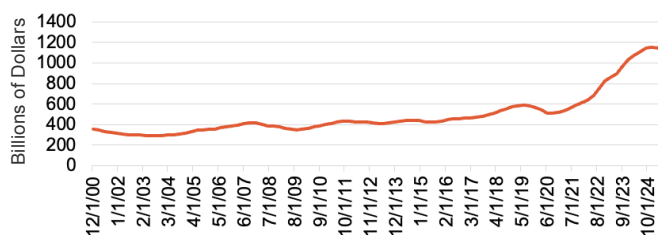
IS POLICY LATE – OR RIGHT ON TIME?

The second and third quarters of the year have been bookended by fiscal actions that have added significant difficulty to the work of the Fed in restoring price stability within the economy.

First and ongoing has been the use of trade policy as a diplomatic tool. The trade-weighted average tariff rate currently stands at 18% (8% if we exclude court-challenged tariffs) domestically. This situation adds burdensome challenges to businesses that require stable input prices in order to make long-term investments and commit to capital projects.

This was followed by debate over the persistently large and growing fiscal deficit, a more significant portion of which has become the interest on the debt used to finance it. This is not only a US problem, but a problem for the bulk of the Group of Seven (G-7) economies around the globe.

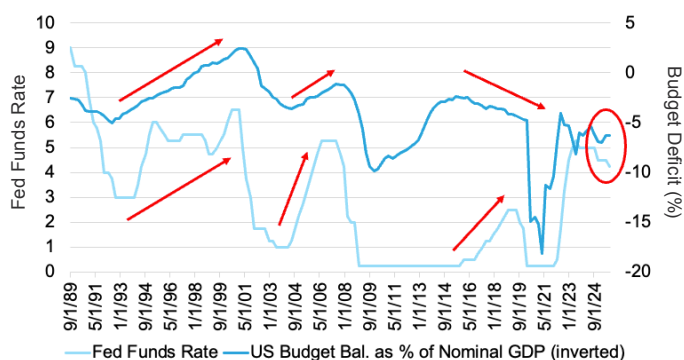
US Debt Interest Payments



Source: Bloomberg

This is the situation in which the Federal Open Market Committee (FOMC) finds itself. After remaining on pause and assessing the cumulative impact of the 1% rate cut delivered in 2024, the FOMC resumed cuts in September, lowering the overnight rate by 0.25%, penciling in two more quarter-point rate cuts for the remainder of this year and two more for 2026.

Fed Funds Rate vs Primary Budget Deficit



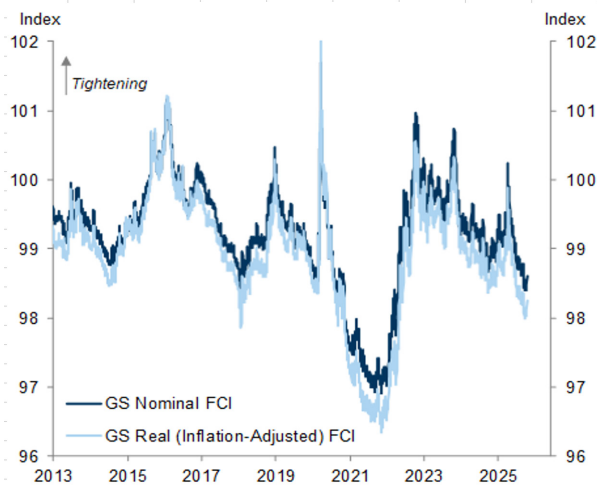
Source: Bloomberg

GROWTH FIRM, LABOR SOFTER: THE SPLIT SCREEN

It's unusual that fiscal and monetary policy are loosening while the economy is growing at 3.8% in inflation-adjusted terms, but that is the current situation.

In fact, evidence is mounting that financial conditions have become looser, and economic data has generally surprised to the upside, especially as services inflation continues to march lower incrementally. This is despite the fact that there are credible and tangible signs of a weakening in labor market conditions, which have largely served as the rationale for the FOMC's recent moves.

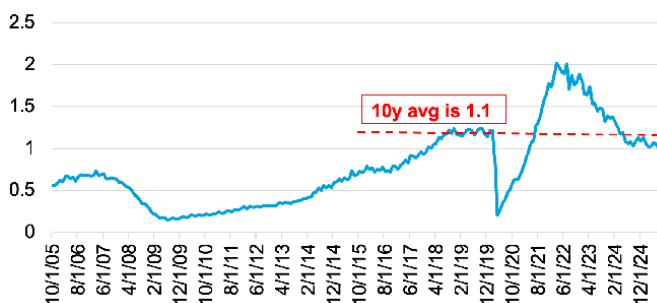
GS US Financial Conditions Indices



Source: Goldman Sachs Global Investment Research

What's more, Jason Thomas, Carlyle Group's (a major private equity firm) head of Global Research and Investment Management, recently stated, "What's so interesting about the moment we're in is the discrepancy between payrolls and the other economic indicators we're looking at," referring to the weakening jobs data despite other indicators broadly portraying resilience.

Jobs/Workers Gap



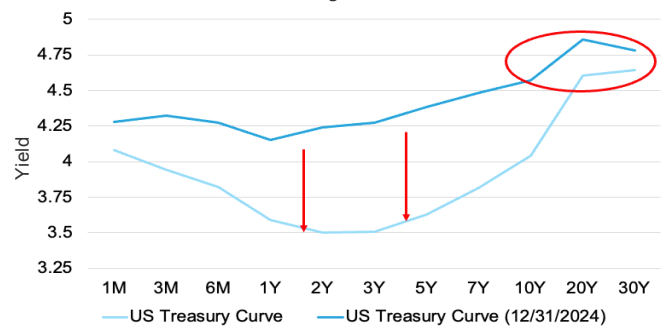
Source: Bloomberg

Recently, the number of jobs available to unemployed workers dipped below 1 to 0.98. The jobs/workers gap, as the measure is more colloquially known, is a key barometer of labor supply and demand and is often cited by FOMC members in the context of the health of the labor market. Additionally, the number of temporary help services payrolls, a leading indicator of labor market health, has deteriorated to about 2.5 million. These levels are similar to those of late 2012, when the economy was still recovering from the financial crisis.

JUST DO THE TWIST

The proposed fiscal solution to the issues of trade, deficits, and the cumbersome debt servicing costs has been to skew treasury issuance to the short end of the yield spectrum. The observed effect has been a stickiness in long-term rates, albeit lower than one would otherwise expect, and a steepening in the yield curve.

US Treasury Yield Curve



Source: Bloomberg

Separate from issuance strategy choices, the uncertainty around whether trade will be freer and/or austerity measures taken makes it exceedingly difficult for a central bank with an explicit dual mandate of price stability and full employment to operate. Thus, the FOMC has elected to prioritize the employment side of its mandate, while alluding to the risks associated with its often-overlooked third mandate of maintaining moderate long-term interest rates.

Given the moves in rates over the past nine months, the team felt that it would be optimal to reposition fixed income allocations to take advantage of these realities. The 3- to 7-year maturity portion of the Treasury curve (the 'belly') appears to be fully valued at this juncture; thus, we elected to take profits and reallocate these proceeds into mortgage-backed securities (MBS), long-maturity US Treasuries, and short-dated asset-backed securities (ABS).

MBS carry a desirable yield of 4.5% and provide protection should rates move higher. Longer-dated Treasuries, as discussed earlier, carry yields that have remained relatively high, and ABS, while possessing similar protections against rising rates, carry a yield closer to 5%.

It's important to note that these changes further enhance the resilience of client portfolios by focusing the already limited credit risk on the very short end of the yield curve, while interest rate sensitivity is added via the allocation of long-end Treasury notes.

This positioning should allow our clients to take advantage of the steepening of the yield curve, while also hedging against any prolonged weakness in labor market conditions. We will continue to monitor these developments in the macro economy and reposition fixed income allocations to serve as a source of safety and liquidity.

By Emil Suqi, CFA®

EMERGENT THEMES AND ATTRACTIVE VALUATIONS

SUMMARY:

With mega-cap technology stocks driving a substantial share of equity market returns in recent years and many mid- to small-cap companies struggling to keep pace in earnings growth, our team is introducing new equity themes designed to broaden selective technology exposure and add a natural resource allocation. These adjustments aim to enhance portfolio balance and improve diversification amid an evolving market landscape.

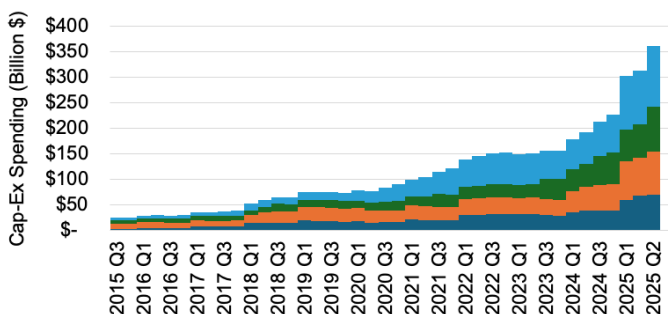
OUR PERSPECTIVE:

As companies pour massive resources into building the infrastructure behind artificial intelligence (AI), some investors are starting to wonder whether big tech firms will be able to translate these investments into sustained long-term profits.

AI INFRASTRUCTURE SPENDING

The legacy business models of major technology firms are evolving as competition intensifies in the race to build out artificial intelligence infrastructure. Companies such as Meta (Facebook), Google, Microsoft, and Amazon are significantly expanding their capital expenditure budgets to develop massive data centers dedicated to AI. While these firms have achieved remarkable revenue and earnings growth under their traditional models, it remains too early to tell whether their new AI-driven investments will deliver comparable profitability. The chart below highlights the amount of capital expenditures (Cap-Ex) from those four companies, showing how much it has increased recently.

Capital Expenditure Spending
Meta, Google, Microsoft and Amazon (In Billion \$)



Source: Bloomberg

Following an extraordinary 10–15-year rally in these mega-cap tech stocks, our team views this as an opportune time to take some profits and reallocate toward areas that stand to benefit from the next phase of the AI buildout. It's not to say that there is no more room for these large tech firms to continue to rally, but our focus is more on risk management and new emerging opportunities.

NEXT GENERATION OF INNOVATION

While much of the market's attention remains on artificial intelligence, investors may be underestimating the potential of other emerging technologies that could unlock new opportunities. The accelerating pace of change in the global economy continues to separate companies that lead in innovation from those struggling to keep pace. From an investment standpoint, identifying the firms best positioned to benefit from these shifts is increasingly complex. To gain broad exposure to this evolving landscape, our team recently allocated to an ETF that tracks the S&P Kensho New Economies Index, providing a diversified, index-based approach to capturing innovation-driven growth.

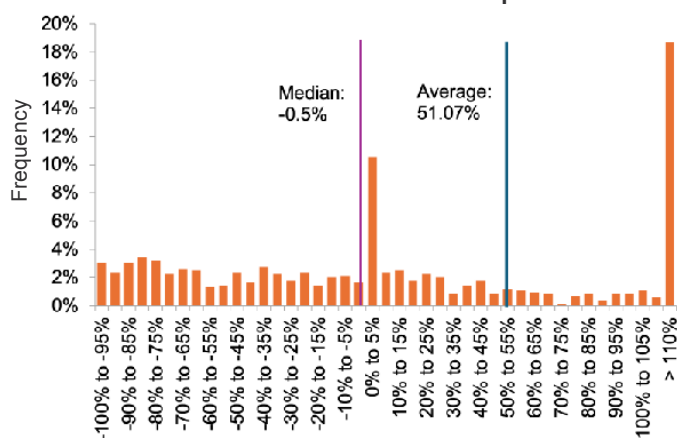
This index identifies key themes in the early stages of the Fourth Industrial Revolution and the publicly traded companies best positioned to benefit from them. Many of these areas are expected to be highly disruptive to traditional business models, though it remains too early to determine which companies will emerge as long-term winners. Because profitability for many of these firms may still be years away, their valuations tend to be sensitive to interest rate movements. As bond yields decline, the present value of those future cash flows increases—a dynamic that helped drive a strong rally in this index during 2020–2021, before those gains reversed as rates rose sharply. With the current level of interest rates, this may create a great entry point to this allocation.

A summary of the key subsectors of this index is shown below.

- | | |
|------------------------------|----------------------------|
| 1) Space | 14) Sustainable Farming |
| 2) Robotics | 15) Genetic Engineering |
| 3) Clean Energy | 16) 3D Printing |
| 4) Cyber Security | 17) Nanotechnology |
| 5) Smart Borders | 18) Smart Factories |
| 6) Wearables | 19) Smart Grids |
| 7) Drones | 20) Adv. Transport Systems |
| 8) Clean Tech | 21) Electric Vehicles |
| 9) Virtual Reality | 22) Alternative Financing |
| 10) Smart Buildings | 23) Future Payments |
| 11) Autonomous Vehicles | 24) Distributed Ledger |
| 12) Digital Communities | 25) Digital Health |
| 13) Enterprise Collaboration | |

Investing in emerging themes can be challenging because not every company will become a long-term winner. Yet the few that succeed often deliver extraordinary returns that more than offset the losses of others. This pattern has been evident within the S&P Kensho New Economies Index from December 2018 through September 2025. While the index rose by approximately 150% during that period, the median stock actually declined slightly (−0.5%). The gains were driven by a small group of standout performers—seven stocks with returns exceeding 1,000%, creating a strong positive skew in results. As the chart below illustrates, this dynamic highlights how capturing even a few of these breakthrough successes can have a meaningful impact on overall portfolio performance.

Dec. 2018 – Sep. 2025 Skewness for S&P Kensho New Economies Composite



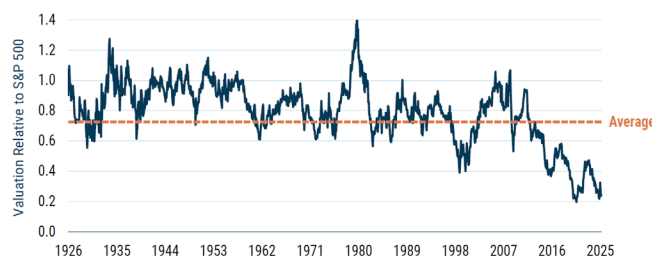
Source: S&P Kensho

BALANCING GROWTH AND VALUE WITH NATURAL RESOURCE EXPOSURE

As valuations across the broader US equity market continue to climb—driven in part by enthusiasm surrounding artificial intelligence—other segments of the market still offer compelling opportunities. The S&P 500's forward price-to-earnings (P/E) ratio ended the third quarter near 25x, well above its 25-year average of approximately 18x.

In contrast, natural resource equities are trading near historically wide valuation discounts relative to the S&P 500, as shown in the chart below. This discount presents a potential opportunity: if valuations revert closer to their long-term averages, the sector could experience a meaningful period of relative outperformance.

Valuation of Energy/Metals Companies Relative to the S&P 500



Source: S&P, MSCI, Moody's, GMO

Beyond valuation considerations, the natural resources allocation also provides a potential hedge against US dollar weakness. Because most commodities are priced globally, they tend to benefit when the dollar declines in value. With increasing global discussion around alternatives to the US dollar as the primary reserve currency, this exposure can serve as a useful diversifier in the event of a prolonged period of relative dollar weakness.

Another key advantage within this segment is the high dispersion of returns between individual commodities and the equities tied to them. This variability creates meaningful opportunities for skilled active managers to add value through selective positioning. While index-based strategies remain effective in many areas of equity exposure, our team believes that active management can play an important role within natural resources, given the complexity and volatility of the underlying markets.

By Ryan Lange, CFA®, CAIA

WELCOME TO MIDLAND WEALTH MANAGEMENT!

Please join us in welcoming:

- **Nick Gibson** – Director, Wealth Management Sales
- **Steve Kelly** – Wealth Advisor
- **Lindsay Savage** – Trust Officer
- **Joshua McCammon** – Associate Wealth Advisor
- **Karen Johnson** – Senior Wealth Advisor
- **Amy Riley** – Financial Advisor
- **Hunter Bukowy** – Portfolio Implementation Analyst

PRIVATE EQUITY: FROM LEVERAGE TO LEADERSHIP

SUMMARY:

Private equity has transformed from asset-stripping tactics to long-term value creation, emphasizing operational improvement, strategic growth, and sustainable portfolio management.

OUR PERSPECTIVE:

Private equity firms create value not through financial engineering, but by strengthening operations—driving efficiency, expanding margins, and building more resilient businesses that deliver sustainable, long-term returns for investors and stakeholders alike.

THE RISE AND FALL OF THE BARBARIANS

In our inaugural Private Markets article, we briefly debunked some of the misconceptions of what private equity firms do—primarily that they are chop shops that lever up companies, buy the whole, and sell the parts. It's worth taking a closer look at how the private equity landscape has evolved—from one often viewed as aggressive to one increasingly focused on firm-level growth and value creation.

Private equity firms employed tactics that were often perceived as predatory throughout the late 1970s and into the 90s. Firms would set out to find undervalued firms where the whole was worth far less than the sum of its parts and utilize borrowing or leverage to buy out (LBO) the firm. From there, the firm would begin cutting costs and selling assets—whether by divesting business divisions, laying off workers, or liquidating the tangible assets. Private equity firms used these proceeds to pay down debt, thereby increasing the value of their investors' equity positions.

Returns generated by the buyouts were not driven by the growth of the firm, but rather by financial engineering. Leverage often exceeded 80% of the deals, magnifying losses during downturns, but also providing massive upside for equity holders. One cautionary tale was KKR's purchase of RJR Nabisco in 1989, where 80% of the buyout

was financed with borrowed funds. The weight of the debt caused the firm to struggle with its cash flow, hindering its ability to grow. While KKR was eventually able to work through the investment, it took substantially longer and yielded returns below expectations.

As competition among private equity firms intensified and returns from traditional LBOs began to fade, the industry evolved. The new playbook emphasizes active management over financial engineering.

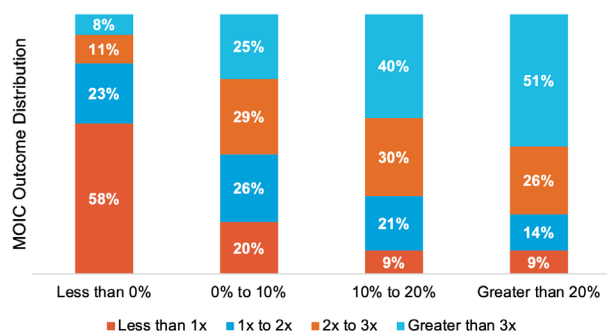
FROM CORPORATE RAIDERS TO VALUE CREATORS

It is important to acknowledge that leverage is still a tactic employed today to generate returns. Buyouts are typically financed with a combination of 50% debt and 50% equity, although this ratio may vary at times. Likewise, asset stripping has not been completely eradicated from the toolbox of private equity firms and funds. It still occurs, but far less often.

One way to measure returns in private equity is by looking at the multiple on invested capital (MOIC), which indicates to investors the value created relative to the amount of capital invested. The two largest drivers of MOIC tend to be revenue growth and balancing out the price paid with the increase in the firm's Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA).

Firms that successfully grow their portfolio company revenues generally achieve higher multiples on invested capital. Between 2000 and 2020, 58% of portfolio companies that experienced zero growth had MOICs less than 1x—meaning their value fell below the original investment amount. In contrast, firms that successfully grew company revenues by 20% or more saw 51% of investments achieve multiples of 3x or higher.

Compounded Revenue Growth Rate



Source: Bloomberg

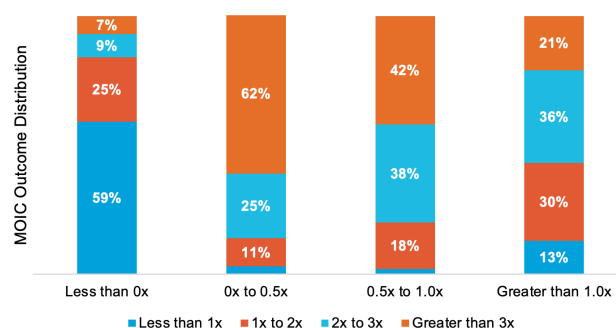
40% of portfolio companies lost investment value if they experienced even a single year of negative revenue growth. In contrast, only 10% of firms have seen their valuations decline while achieving positive revenue growth. Simply put, topline growth is the engine of value creation and higher return multiples.

Private equity firms create value for investors by aligning the price they pay with the true growth potential of a company's operating leverage, as measured by EBITDA. EBITDA growth is driven by two main levers: revenue expansion and margin improvement, the latter often achieved through cost optimization, supply chain efficiencies, and technology-driven productivity gains.

The strongest returns arise not simply from growing EBITDA, but from paying a fair price for genuine growth—nearly half of firms that maintained a purchase price-to-EBITDA growth ratio between 0x and 1x achieved returns exceeding 3x their original investment. By combining sector expertise with disciplined valuation, private equity firms identify and elevate businesses with real potential, driving sustainable

performance and long-term value creation rather than overpaying for the illusion of growth.

Growth Adjusted EBITDA PPM



Source: Bloomberg

Today's private equity landscape looks far different from the era of corporate raiders and balance sheet engineers. As competition intensifies and financing costs remain higher, firms can no longer rely on leverage and asset stripping to drive returns. Instead, the success of the company depends more on an owner-operator mindset—one focused on sustainable value creation, operational efficiencies, and long-term growth. In this environment, the best private equity firms are not those who extract value, but those who build it.

By Jake Stapleton, MBA

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QUARTER 4

MARKET OUTLOOK

INSIDE THIS ISSUE:

ECONOMY / FIXED INCOME

Positioning for a Late Cycle Economy

EQUITY

Emergent Themes and Attractive Valuations

PRIVATE MARKETS

Private Equity: From Leverage to Leadership