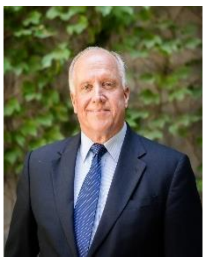
2025 – 2nd Quarter Review & Outlook

Economic and Investment Review



Mark Anderson

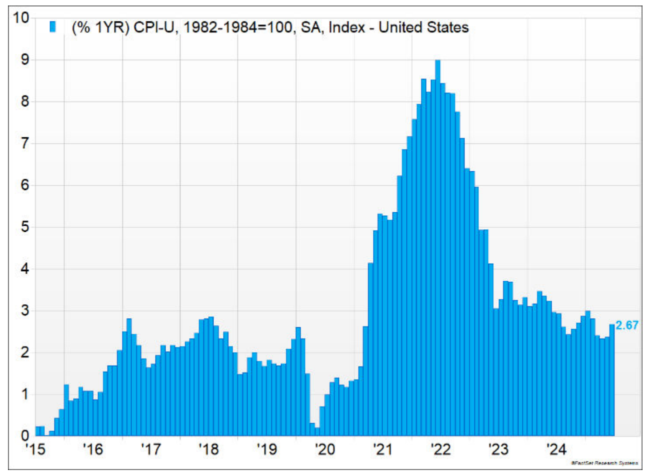
Chief Investment Officer

Economic Growth: The consensus forecast for 2025 GDP has declined from 2.1% at the beginning of the year to 1.50% currently. Q1 GDP contracted -0.5% due to high levels of pre-tariff imports, tariff uncertainty, lower growth in consumer demand, and federal government cutbacks. GDP for the remainder of the year is expected to be relatively low but positive.

The consumer accounts for over 2/3 of GDP, and related issues are accumulating that will likely be a drag on economic growth. The Consumer Confidence Index measures the degree of optimism that consumers have in the overall economy and in their personal financial situation. An index value below 100 indicates that consumers are generally pessimistic about the economy. The index was at 93 in June and has been below 100 since March. Economists expect that consumer spending may be muted due to lower confidence levels.

The probability of a recession in 2025 has declined due to the de-escalation of some trade tensions. Passage of the "Big Beautiful Bill" and reduced regulation should add stimulus to the economy in 2026. The "Big Beautiful Bill" makes the 2017 tax cuts permanent, extends a larger standard deduction, eliminates most taxes on tips and overtime, and adds an additional deduction for seniors. The law also makes permanent deductions for capital investment. The result should be greater spending and investment, but will also likely raise the deficit.

Inflation: Inflation rose 2.7% on an annualized basis in June compared with 2.4% in May. The increase



Source: FactSet

could be an indicator that tariff-related costs may be making their way to the consumer. Jan Hatzius, Chief Economist at Goldman Sachs, estimates that each 1pp in tariff hikes will add about 0.1% to core PCE but that the impact will fade in 2026-2027. David Kelly, Chief Strategist for J.P. Morgan Asset Management, expects CPI inflation to rise to 3.5%, year-over-year, by the fourth quarter and then trend toward the 2% Fed target in the second half of 2026.

Many retailers have held off raising prices, but may have less ability to do so in the future. If consumer spending slows, it may keep inflation on simmer rather than boiling over. The proof will be in the pudding when numbers are released for the next few months.

Interest rates: The Fed has maintained the federal funds rate in the 4.25% to 4.50% for the first half of the year. The Fed and the market expect two 0.25% rate cuts by year-end. David Kelley/JPMorgan expects the Fed to remain on hold for the next few months and perhaps deliver just one 0.25% rate cut by the end of the year. He identifies uncertainty surrounding tariffs, immigration, budget deficits, and inflation as potential reasons for just one rate cut. Jan Hatzius/Goldman Sachs also expects just one rate cut.

The European Central Bank has lowered its key interest rate eight times since June 2024 to 2.00%.

Labor: Unemployment has been in a range of 4.0% – 4.2% over the past year. The June reading of 4.1% indicates a continued healthy labor market. A slower-growing economy will likely result in slower job growth. However, the reduction in available immigrant labor will work to keep the unemployment rate low even in a slowing economy.

Global: The World Bank projects global growth to slow to 2.3% in 2025, nearly half a percentage point lower than expectations at the start of the year. If the forecast from the World Bank for the next two years materializes, average global growth in the first seven years of the 2020s will be the slowest of any decade since the 1960s. M. Ayhan Kose, the World Bank's Deputy Chief Economist, stated that "emerging-market and developing economies reaped the rewards of trade integration but now find themselves on the frontlines of a global trade conflict.

Equity Markets

The U.S. large-cap equity market, as measured by the S&P 500, rebounded significantly since the tariff provoked a decline in April. The index was up 11.6% in Q2 and 6.2% year-to-date through June 30th.

2025 Q2 Returns				
EQUITY	**Q2 2024**	**YTD 6.30.25**	**1 Year 6.30.25**	**3 Years Annualized**
S&P 500	11.57	6.20	15.09	19.70
S&P 500 Value	4.77	6.00	13.63	12.76
S&P 500 Growth	17.94	6.09	17.13	25.75
Dow Jones Ind Avg	6.04	3.64	12.66	12.73
NASDAQ Composite	17.59	5.48	14.80	22.69
S&P Mid Cap 400	6.92	0.20	7.49	12.82
S&P Small Cap 600	5.41	-4.46	4.58	7.65
MSCI EAFE	11.78	19.45	17.73	15.97
MSCI Emerging Mkts	11.99	15.27	15.29	9.70

Source: FactSet

Easing of trade tensions, strong earnings, and an AI tailwind pushed the index higher.

The weight of the top 10 stocks in the S&P 500 dropped and quickly rebounded in Q2. The top 10 stocks now represent more than 38% of the market capitalization of the entire index.

Source: FactSet, Refinitiv Datastream, Standard & Poor's, Thomson Reuters, J.P.Morgan Asset Management.

The top 10 stocks have been trading at higher P/E multiples than the remaining stocks as a group for some time. They have also been trading at a higher percentage relative to their average until recently.

Source: FactSet, Refinitiv Datastream, Standard & Poors, Thomson Reuters, J.P.Morgan Asset Management

The entire index is now trading at a significant premium to the long-term average. This broadening performance could be looked at as a positive.

It is generally dangerous to state that it is different this time, but there are justifications for the current premium valuation. Todd Ahlsten, CIO for the Parnassus Core Equity Fund, identifies the following as supports for the premium.

- American exceptionalism.
- There are many great companies in the S&P 500 that are powering earnings growth.
- The earnings structure is durable.
- U.S. companies are best positioned to benefit from AI development and implementation.
- Significant liquidity is helping to drive P/E multiples.

We have increased our year-end forecast for the S&P 500 to 6450 and 6650 for twelve months. Goldman Sachs forecasts 6600 for 2025 and 6900 for twelve months. Raymond James feels that there may be some weakness as the economy slows, resulting in a year-end forecast of 5875, but expects improvement over the twelve-month period to 6375. Ed Yardeni of Yardeni Research thinks we could reach 7000 by year-end.

Mid-cap and small-cap stocks performed well in Q2 but continue to lag their large-cap counterparts. The S&P Mid-Cap 400 was up 6.92% in Q2 but was only up 0.20% year-to-date. The S&P Small-Cap 600 rose 5.41% in the quarter but remained in negative territory, at -4.46% YTD. Some of the reasons pointed to for the underperformance include:

- Smaller technology sector weightings.
- Greater economic sensitivity.
- Greater reliance on borrowing and a higher cost of capital.
- High cost of implementing AI into operations.
- A difference in strength and quality from large-cap.

On the other hand, international stocks matched large-cap domestic stocks in the quarter and have led the way on a year-to-date basis. The MSCI EAFE index moved up by 11.78% in Q2 and 17.73% YTD. International performance has been driven by lower relative valuations, re-allocation, increased government spending, and a decline in the value of the dollar relative to foreign currencies.

Sector returns for the quarter were led by Information Technology, up 23.54%, and Communication Services, up 18.48%. Energy and Health Care were the worst laggards, -8.40% and -6.79% respectively. Industrials led on a year-to-date basis (through June 30th), increasing 11.96%, followed by Communication Services at 10.62%. Consumer Discretionary and Health Care were the worst year-to-date performers, down -4.22% and -2.01% for the period.

Fixed Income Markets

Taxable investment-grade fixed Income had its best performance in some time. The Bloomberg US Aggregate Bond index was up 1.21% in Q2 and 4.02% YTD. High Yield returned 3.68% in the quarter and 4.87% YTD.

2025 Q2 Returns

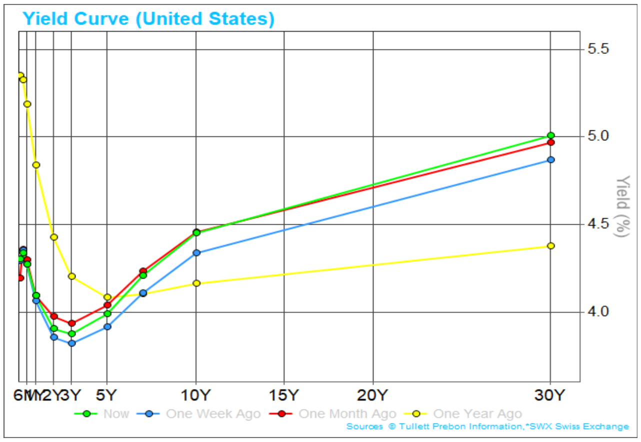
FIXED INCOME	Q2 2024	YTD 6.30.25	1 Year 6.30.25	3 Years Annualized
Bloomberg US Agg Bond	1.21	4.02	6.08	2.55
ICE AMT-Free Nat'l Muni	0.00	-0.51	1.06	2.37
Markit iBoxx USD Liquid High Yield Index	3.68	4.87	10.68	9.80

Source: FactSet

Companies issuing investment-grade fixed income generally have high-quality balance sheets, putting them in a better position to withstand economic turbulence.

Municipal bonds have lagged due to a surge in issuance, volatility in the bond market, changing expectations for Federal Reserve policy, and related ETF outflows. However, fundamentals remain strong, which should support municipal bonds going forward. Intermediate-term and long-term municipal bonds provide a significant after-tax income advantage for high-tax bracket individuals.

The short end of the U.S. Treasury Yield Curve will decline in response to Fed rate cuts; however, the intermediate and longer areas of the curve will not likely follow due to the amount of government debt outstanding and perceived declining credit quality.



Real Assets

The Dow Jones Real Estate Index was down -0.40% in Q2 and up 2.92% YTD. The index was up 11.02% for one year. The GSCI commodities benchmark was down -2.81% in Q2 and up 1.94% YTD. The one-year return was relatively flat at 0.25%. Crude oil prices

2025 Q2 Returns				
REAL ASSETS	Q2 2024	YTD 6.30.25	1 Year 6.30.25	3 Years Annualized
Dow Jones U.S. R/E	-0.40	2.92	11.02	4.27
S&P GSCI	-2.81	1.94	0.25	-0.37

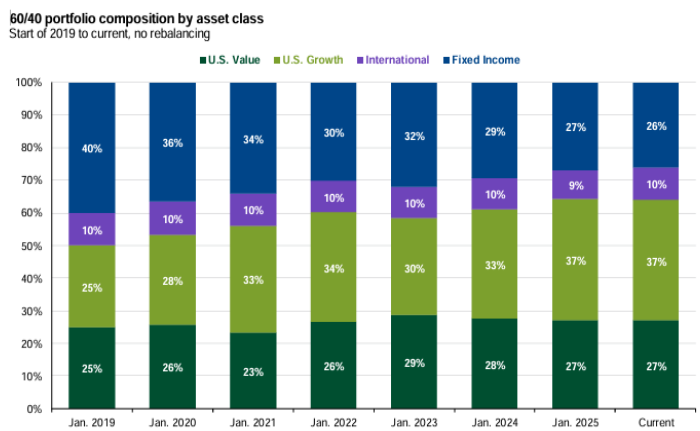
Source: FactSet

have trended down over the past year while gold prices have shot up.

Asset Allocation

Asset allocation decisions are among the most important factors affecting total portfolio volatility. By choosing the right mix of assets, overall portfolio risk is potentially reduced and the return stream should be smoother. Asset allocation should be used primarily for risk management and secondarily for return generation.

Except for 2022, the last six years have had very strong equity returns. Investors have enjoyed the ride; however, portfolios have become riskier over time if they have not been rebalanced periodically. A portfolio considered reasonably balanced with a 60% equity and 40% fixed/bonds allocation in January 2019 would have been modified to a more growth-oriented 73% equity and 27% fixed allocation today if no rebalancing took place during the time period.



Source: Bloomberg, FactSet, MSI, Russell, Standard & Poor's, J.P.Morgan Asset Management

The modified allocation may not be appropriate for investors with less appetite for risk or with shorter time horizons. It may make sense to rebalance over an appropriate period of time.

Disclosures

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