BOYD WATTERSON
ASSET MANAGEMENT
A BOYD WATTERSON GLOBAL COMPANY

Boyd Watterson Investment Outlook

July 2025

Our Firm:

Boyd Watterson Asset Management, LLC is an SEC-registered investment advisory firm with approximately $18.8 billion of assets under management.[1] Over the last 90+ years, Boyd Watterson and its predecessor companies have successfully managed a broad range of fixed income and real estate strategies for institutions and individuals alike.

With a focus on the management of money and a dedication to the satisfaction of our clients' expectations, we offer the benefits of a boutique firm but with the resources usually attributable to a much larger asset management firm.

[1]Including real estate assets managed in separately managed accounts and advisory-only unified managed accounts (UMA). SEC registration does not constitute an endorsement of the Firm by the SEC nor does it indicate that the Firm has a particular level of skill or ability.

For information about Boyd Watterson's investment strategies, insights, philosophy and teams, please visit our website, www.boydwatterson.com

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The Macro View

The U.S. economy demonstrated modest resilience in the second quarter of 2025 as GDP growth likely turned positive, despite persistent inflation, softening labor market conditions, and a challenging global backdrop. Beneath the surface, however, growing tensions around trade policy, rising geopolitical risks, and intensifying political pressure on the Federal Reserve have complicated the near-term outlook and introduced new risks to the future path of monetary policy.

Performance for Periods Ending June 30, 2025

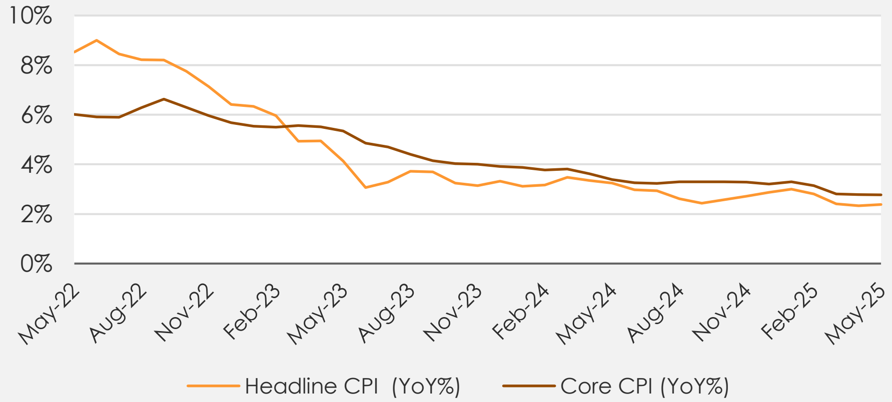
	QTD	YTD	1-Year	3-Year	5-Year
2-Year Treasury	1.10	2.68	5.40	2.87	1.02
10-Year Treasury	0.98	5.03	5.25	0.08	-3.42
Bloomberg Aggregate	1.21	4.02	6.08	2.55	-0.73
Corporate Investment Grade	1.79	4.20	7.03	4.47	0.36
Corporate High Yield	3.57	4.57	10.22	9.81	5.98
Leveraged Loans	2.33	2.96	7.50	9.54	7.39
Mortgage Backed Securities	1.13	4.14	6.42	2.28	-0.63
S&P 500	10.94	6.20	15.16	19.71	16.64
MSCI EAFE	11.77	19.45	17.73	15.97	11.16

Source: Interactive Data, Bank of America/Merrill Lynch/Bloomberg.

The Federal Reserve continues to face a difficult balancing act given the current risks to both sides of their dual mandate - maximum employment and price stability. More recently, this challenge has been complicated by the Trump Administration's increasing pressure on the Federal Open Market Committee (FOMC) to cut short-term interest rates. FOMC Committee members have emphasized the importance of central bank independence – as its loss could have significant consequences for the U.S. dollar, U.S. Treasuries, and financial markets more broadly.

The Consumer Price Index (CPI) rose 2.4% year-over-year in May, the first acceleration since January, while the core CPI remained elevated at 2.8%, primarily driven by housing costs that remain stubbornly high. Wage growth continues to outpace inflation, supporting real household income and spending; however, the recent rise in inflation and the threat of tariff related price pressures has lowered the chances of near-term interest rate cuts.

U.S. Inflation Trends



Source: Macrobond

At the same time, the labor market is showing signs of softening. Payroll growth has slowed, and labor force participation declined modestly during the quarter. The unemployment rate leveled off at 4.2%, and while initial jobless claims remain low, hiring activity has become more cautious as evidenced by the rise in continuing jobless claims. Tighter immigration enforcement may also distort employment data over the next several months, complicating the Fed's ability to assess labor market health in real time.

Trade policy re-emerged as a significant driver of market volatility during the quarter. The U.S. imposed new tariffs on countries around the world in an effort to rebalance the global trade landscape and support domestic production. While the immediate economic impact has been limited, the tariffs have begun to affect pricing—particularly in the auto sector, where consumers pulled forward purchases ahead of expected price increases. Concerns are mounting that a broader trade war could ensue if current negotiations falter, posing additional risks to vulnerable supply chains and adding upward pressure on inflation. The return of tariff-based trade friction adds uncertainty to the economic outlook, especially at a time when global manufacturing is already under pressure.

Geopolitical tensions also remained elevated, adding complexity to the economic outlook. The ongoing war in Ukraine and renewed instability in the Middle East continued to influence commodity markets and investor sentiment. While the recent de-escalation between Israel, Iran, and the United States has eased some immediate concerns about military conflict and energy supply disruptions, the relationship remains fragile. Earlier fears of sanctions and oil market volatility contributed temporarily to higher inflationary expectations, and markets remain sensitive to further developments.

The fiscal landscape also shifted in the second quarter. The budget bill currently working its way through Congress has sparked renewed concerns about debt sustainability and its potential impact on market yields. Increased federal spending may boost GDP in the short term, but a resulting rise in debt levels could trigger crowding-out effects, alter the shape of the yield curve, and complicate future monetary policy decisions. Bond markets are now weighing the inflationary implications of higher spending and budget deficits against expectations for eventual Fed rate adjustments.

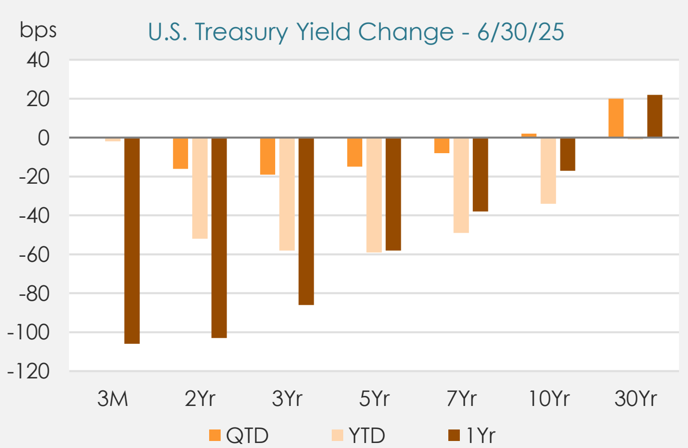
Looking ahead, the third quarter is likely to bring continued moderate growth, persistent inflation, and heightened policy uncertainty. Trade tensions and geopolitical developments remain key risks, particularly if they lead to further supply chain disruptions or retaliatory measures. The Federal Reserve is expected to maintain a cautious stance, focusing on inflation, while closely monitoring labor market dynamics. While the U.S. economy continues to expand, it does so in an increasingly complex environment. For now, the path forward is one of cautious optimism, tempered by an increasingly uncertain fiscal, monetary, and geopolitical outlook.

Fixed Income

President Trump's 'Liberation Day' tariff announcement kicked off the second quarter with country specific tariff levels significantly higher than expected, which resulted in a broad sell-off across financial markets. While the 'reciprocal' component of the tariffs (excluding China) was suspended for 90 days a week later, a series of subsequent events continued to unsettle investors. These included escalating trade tensions with China followed by a temporary pause for negotiations, Moody's downgrade of the United States' sovereign credit rating from Aaa to Aa1, and the brief military conflict involving Israel, Iran, and the United States. All these developments combined to create a whirlwind of market fluctuations throughout the quarter.

The tariff announcement added to an already uncertain economic and fiscal outlook, prompting fears among investors about the potential for slower growth (or a recession) and higher inflation. These concerns also extended to the Federal Reserve, as the growing risk of a stagflationary environment further complicated its policy decisions. The FOMC maintained its patient stance on future policy rate adjustments, as it awaits greater clarity on the outcome of tariff negotiations before assessing the potential impacts on inflation, growth, and the labor market. Monetary policy was left unchanged in the second quarter, however the Committee's median economic projections for 2025 and 2026, released following the June meeting, reflected slower growth, higher unemployment, and higher inflation, relative to their projections in March. The Committee's 'dot plot' continued to project a median estimate for two interest rate cuts in 2025 yet lowered their projection for 2026 to one rate cut, down from two previously.

The steady flow of political and economic headlines kept interest rate volatility elevated, with key intermediate and long-term Treasury yields fluctuating within ranges of 40 to more than 60 basis points during the quarter. By quarter-end, short-to-intermediate term Treasury yields were flat to lower, while long-term Treasury yields rose, leading to a further steepening of the yield curve.



Source: Bloomberg

During the quarter, risk assets in the fixed income market experienced a period of heightened volatility. Credit spreads initially widened sharply following the announcement of new tariffs but gradually narrowed back toward the tighter end of historical ranges as investor confidence slowly increased that tariffs would likely be negotiated significantly lower in the coming months, leading to a return of risk appetite. As the quarter progressed, resilient economic data, a slowing pace of new issuance, and attractive all-in yields supported strong demand in the corporate bond sector. Both investment grade and high yield corporate bond spreads ended the quarter tighter, resulting in positive excess returns relative to comparable maturity Treasuries. The same held true for the securitized sectors, as asset-backed, agency mortgage-backed, and commercial mortgage-backed securities all posted positive excess returns relative to Treasuries for the second quarter.

We began the second quarter with a short duration bias across all our fixed income strategies; however, following the 'Liberation Day' tariff announcement, and subsequent spike in Treasury yields, we took advantage of the higher interest rate environment by extending portfolio durations to a neutral position relative to their respective benchmarks. The Core and Intermediate strategies maintained their bulleted maturity structure given our expectation for further yield curve steepening. As interest rates moved lower late in the quarter, we slightly reduced portfolio durations in longer-term strategies while allowing the intermediate and short-term strategies to drift modestly below their respective benchmarks.

Our sector positioning was generally unchanged for the quarter, with only minor additions to our corporate bond allocations. We continue to have overweight positions in corporate bonds and asset-backed securities, and an underweight position in U.S. Treasuries. Additionally, the Core strategies have a modest overweight allocation to agency mortgage-backed securities.

We expect volatility to remain elevated over the near-term as investors await clarity on the tariff outlook, the budget bill, and current geopolitical risks. July will likely be an important period as resolution (or considerable progress) is expected on several of these issues, which could have a significant impact on the economic and monetary policy outlook. We continue to expect a slower growth environment coupled with higher near-term inflation readings, which we believe will result in fewer interest rate cuts than the market currently expects this year. As a result, we believe our portfolios are appropriately positioned to take advantage of any volatility, as we expect to remain patient and await greater clarity before adjusting our current risk profile.

Real Estate

A volatile second quarter which created significant uncertainty but offered some stability leading into the third quarter has the commercial real estate sector optimistic for the remainder of the year. The Trump administration's tariffs (and threatened tariffs) created volatility in the debt and equity markets and slowed the commercial real estate market as uncertainty on the U.S.'s economic trajectory caused many companies to pull back on investing. Towards the end of the 2nd quarter, however, equity markets had snapped back, liquidity had returned to the debt markets and there was more comfort that the most extreme tariffs threatened by the administration would not come to fruition. This has set the stage for the commercial real estate market to potentially take off in the 2nd half of the year, with potential interest rate cuts and fairly strong demand on the leasing front combined with very little new supply being brought on across asset types fueling improvements in the market.

The commercial real estate market appears to be at its bottom, with depreciation in the ODCE index flat to slightly positive after approximately three years of declines. Boyd's funds have seen similar trends in its appraisals, with Q2 depreciation expected to be minimal and recent quarters seeing declining depreciation. After a wave of new supply hit in the industrial and apartment markets last year which hurt rent growth, there are fewer completions expected in the next few years which should allow those markets to stabilize and continue to grow. The office sector appears to have bottomed as well with several positive indicators. According to CBRE, office conversions or demolitions will exceed new supply coming onboard for the first time in 25 years this year, which will help reduce the amount of vacancy in the market. Many buildings that have been stuck in limbo due to bad capital structures have been sold to new owners at a much lower basis, allowing for new investment into new uses. Secondly, leasing velocity has picked up in many markets and there has been a slowdown in the downsizing trend that has been prevalent for the past several years as companies adjusted to new work arrangements. Thirdly, there continues to be momentum for office users returning to work, with Placer.ai, which measures foot traffic, indicating that Tuesday through Thursday foot traffic has actually exceeded 2019 levels in New York City and many other cities approaching those levels. Many prominent companies as well as the federal government and many state and local governments have ordered workers back to the office with more frequency, which has improved utilization rates and the number of people in office.

All of these trends bode well for Boyd Watterson's funds, which will benefit from increased office utilization, particularly by the government, as well as a stabilized economic and interest rate environment. The current administration's posture towards workers returning to the office will help the broader office market but also Boyd's funds directly and as the government seeks to unload federally owned properties, there will be more leasing opportunities for the firm's funds to capitalize on. Boyd has also seen a pickup in leasing velocity- in Q2 one of the firm's funds filled a 220,000 square foot vacancy in Jacksonville, Florida and is in negotiations to fill another large vacancy, which would boost fund occupancy and cash flow. Additionally, we have heard anecdotally of government tenants who do not have enough room in their existing space to accommodate all of the workers returning to office and we are proactively offering up leasing solutions in an effort to fill vacancy while building even better relationships with the government. The funds are well situated to help with a large, diverse portfolio of properties that few, if any, of our competitors can match and the firm is optimistic about the outlook in the coming years.

Equities

All the major equity indices rebounded in the second quarter of 2025, with the NASDAQ leading the way, up nearly 18%, followed by the S&P 500 up just under 11%, and the Dow Jones Industrial Index up nearly 5%, resulting in all three indices ending in positive territory on a year-to-date basis. This followed the announcement of higher-than-expected tariffs on 'Liberation Day' in April, which triggered a 688-point drop in the S&P 500 over the next three trading days. The market began to recover after the administration announced a 90-day pause or relaxation of tariffs on most countries and signaled a willingness to negotiate a more realistic outcome with China.

Growth outpaced value in the quarter, with the S&P 500 Growth Index up 18.73% while the S&P 500 Value Index was up only 2.96%. Large cap stocks led the way versus midcap and small cap stocks, as measured by the Morningstar Large Core Index, which was up 11.34% while the Morningstar Small and Mid-Cap Core indices were up 7.92% and 7.88%, respectively.

Despite strong second quarter returns in U.S. equity markets, foreign markets such as the UK's FTSE 100 and Germany's DAX, delivered even stronger year-to-date returns, rising 9.45% and 20.09%, respectively, in local currency terms. When converting those results into U.S. Dollars, the returns jump to 19.90% and 35.91%, respectively.

The rebound in U.S. equities has resulted in valuations of the S&P 500 rising above its long-term averages, with the price-to-earnings ratio exceeding 22 times, versus a long-term average of 15 to 20 times. While earnings growth expectations have improved, the market's current valuation suggests that future returns may be more limited.