BOYD WATTERSON
ASSET MANAGEMENT

A BOYD WATTERSON GLOBAL COMPANY

Boyd Watterson Investment Outlook

October 2025

Our Firm:

Boyd Watterson Asset Management, LLC is an SEC-registered investment advisory firm with approximately $19.1 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

Check out our latest blog posts: www.boydwatterson.com/insights/

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The Macro View

Economic activity in the United States appears to be well-positioned for another positive quarter, demonstrating remarkable resilience amid soft job growth, elevated inflation, and on-going fiscal and monetary policy uncertainty. On the growth front, the Atlanta Fed's latest GDPNow estimate projects 3.9% growth for the third quarter, up from the revised 3.8% GDP figure reported in the second quarter. Inflation, as measured by the PCE Price Index, increased 2.7% year-over-year in August and is expected to move higher in September, driven by sticky services prices and rising goods prices. At the same time, signs of a slowdown in the labor market began to emerge, rapidly drawing the attention of investors and policymakers.

Performance for Periods Ending September 30, 2025

	QTD	YTD	1-Year	3-Year	5-Year
2-Year Treasury	1.01	3.72	3.51	3.81	1.21
10-Year Treasury	1.81	6.93	1.35	2.85	-3.08
Bloomberg Aggregate	2.03	6.13	2.88	4.93	-0.45
Corporate Investment Grade	2.65	6.96	3.92	7.24	0.55
Corporate High Yield	2.41	7.09	7.23	10.94	5.51
Leveraged Loans	1.68	4.69	7.09	9.72	6.88
Mortgage Backed Securities	2.40	6.64	3.26	5.01	-0.18
S&P 500	8.12	14.83	17.60	24.93	16.47
MSCI EAFE	4.77	25.14	14.99	21.70	11.16

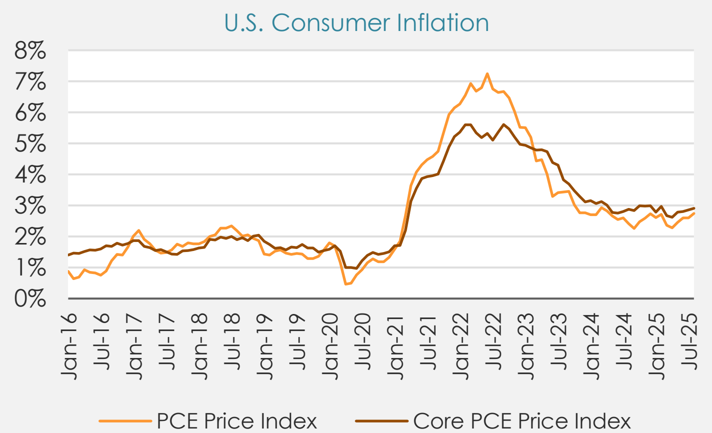
Source: Interactive Data, Bank of America/Merrill Lynch/Bloomberg.

A scenario like this, where the Fed's policy objectives are becoming increasingly unbalanced, has created a challenging environment for monetary policy, further complicated by mounting pressure from the Trump administration on the Federal Open Market Committee (FOMC) to lower interest rates. Additionally, the administration's efforts to remove Fed Governor Lisa Cook due to allegations of mortgage fraud, coupled with the unexpected resignation of Fed Governor Adriana Kugler in August, forced investors to consider the impact that one or more new Trump appointments to the Board of Governors could have on the future path of monetary policy. These developments also stirred debate over the Federal Reserve's independence. Of particular concern were the potential implications for financial markets should that independence be compromised, particularly in relation to the stability of the U.S. dollar, the level of interest rates, the shape of the yield curve, and the broader inflationary outlook.

The FOMC left interest rates unchanged at their July policy meeting, despite the rare occurrence of two dissenting Governors, who advocated in favor of a rate cut. Just two days later, the monthly employment report showed softer payroll growth, accompanied by sharp downward revisions to the prior two months, increasing concerns of growing weakness in the labor market. That report, coupled with Trump's nomination of Stephen Miran, an outspoken advocate for lower interest rates, to fill the vacant seat on the Fed's Board of Governors, fueled market expectations for more interest rate cuts in the coming months. The economic and monetary policy set up was beginning to look similar to last summer, where softening labor market trends resulted in the FOMC easing one hundred basis points in the last four months of 2024. By the time the September policy meeting arrived, it was widely anticipated the Committee would lower rates, however, investors were more interested in the FOMC's economic and policy rate outlook.

The September FOMC meeting ended with a 25-basis point reduction in short-term interest rates, with newly confirmed Governor Miran dissenting in favor of a 50-basis point cut. The Committee's comments acknowledged that downside risks to the labor market had increased, yet their median economic projections for 2026 showed modestly stronger growth, higher inflation, and a lower unemployment rate relative to their June projections. Chair Powell emphasized that there are currently risks to both sides of their dual mandate, indicating there is not a risk-free path for monetary policy currently. Their 'dot plot' reflected a median projection for two additional interest rate cuts this year, one in 2026, and one in 2027, bringing their policy rate down to 3.1% by 2027.

Looking ahead, there are a few ways we can track the durability of our expectations for inflation and consumption in the coming months. If current tariff policies remain unchanged, we expect import prices and producer prices to rise further. Over the next twelve to eighteen months, businesses impacted by tariffs will look to adjust their strategy if margin pressure ensues, which will likely result in the majority of producer price increases being passed on to the consumer. For the consumer to continue spending at a pace above inflation, hiring trends must stabilize and wage growth must keep pace with inflation. For that environment to unfold, the breadth of businesses with positive earnings needs to continue to grow. Underpinning this developing economic setup will be the impact of pro-growth tax policies set to take effect in 2026.

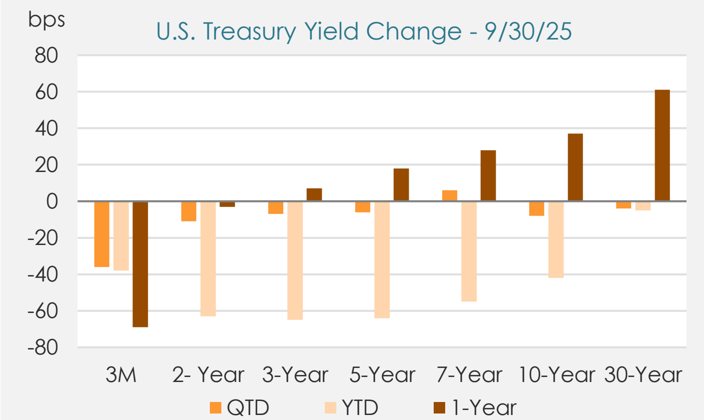


Source: Macrobond

The fourth quarter may prove to be a critical inflection point where headline growth and inflation measures have been increasing, despite some recent negative news in the labor market. We expect the U.S. economy to continue growing at a modest pace, with inflation gradually increasing over the near term. We anticipate the FOMC will lower their policy rate further over the coming months, but given the current set up, we do not believe it will necessarily be a series of consecutive cuts or to the magnitude currently reflected in the futures market.

Fixed Income

Interest rate volatility remained elevated throughout the third quarter, with Treasury yields rising in July while the yield curve flattened, only to see the opposite occur in August, largely due to the weakening employment outlook and increasing expectations for more policy rate cuts. The third quarter ended with Treasury yields modestly lower and the yield curve slightly steeper; the federal funds futures market had fully priced in one additional rate cut this year, with a 74% probability of a second cut by year-end.



Source: Bloomberg

Risk assets in the fixed income market performed well in the third quarter, with both investment grade and high yield credit spreads tightening 10 and 16 basis points, respectively, ending the quarter near the tighter end of historical ranges. Similarly, spreads tightened across all three securitized sectors: asset-backed, agency mortgage-backed, and commercial mortgage-backed securities. As a result, excess returns relative to similar duration Treasuries were positive for the quarter across the corporate bond and securitized sectors.

Our portfolio positioning did not change materially from the prior quarter. All fixed income strategies began the third quarter with a short duration bias and, despite the sharp swings in interest rates, we maintained that modestly short duration position throughout the quarter. The Core and Intermediate strategies sustained their bulleted maturity structure, with the focus on the 3 to 7-year part of the yield curve. We continue to see room for further steepening of the yield curve given the market's expectations for a series of additional interest rate cuts and our expectation of inflation remaining persistently above the FOMC's 2% target over the near term.

Sector positioning across our strategies was broadly unchanged as well. We continue to have overweight positions in corporate bonds and asset-backed securities and an underweight position in U.S. Treasuries. Additionally, Core strategies hold a neutral to modest overweight position in agency mortgage-backed securities. With valuations rich across the fixed income landscape, our focus has turned more toward security selection, while remaining patient with any larger adjustments to our relative risk positioning amongst sectors.

As we enter the final quarter of the year, uncertainty remains elevated, with politics playing an increasingly significant role in shaping financial market dynamics. We are closely monitoring developments related to the FOMC and the effects they could have on the path of monetary policy. The administration's desire for lower short and intermediate-term interest rates is unlikely to subside, raising questions about alternative tools they could utilize beyond the FOMC to accomplish their goals. Given the heightened degree of uncertainty, we believe our portfolios are positioned appropriately for the current environment and will continue to remain patient with our positioning as we await additional clarity on the fiscal and monetary policy outlook.

Real Estate

The commercial real estate sector appears to have finally reached a bottom after a three-year decline caused by higher interest rates and slow return-to-work following the Covid pandemic. Boyd's real estate strategies and the broader NFI-ODCE index have had four straight quarters of positive returns with essentially flat appreciation, and the expectation is for the market to have slow but steady growth in the coming years.

The first sign that life is returning to the real estate sector is that liquidity is returning to the market. Transaction activity has been extremely muted for several years but Q3 saw an increase in activity that is expected to continue through the end of the year and into 2026. CoStar is projecting trailing 12-month transaction activity to have increased 14% over the prior year and further increases are anticipated as we move toward year end. Additionally, lenders have been fairly aggressive in putting out capital after several years on the sidelines. Spreads have tightened to levels last seen in 2022 and even office borrowers are starting to see increased interest from lenders after several challenging years. Several high-quality office assets have changed hands recently, which have been among the first to do so in recent years.

Another positive factor for the real estate sector is that interest rates appear to have stabilized on the long end of the yield curve and seem poised to go lower on the short end of the curve. The Fed cut rates in September to a targeted range of 4-4.25%, and the market is now projecting two additional cuts through the end of 2025 and two additional cuts next year.

This will result in lower borrowing costs for those borrowing for the short and middle term (and possibly the long term) as well as floating rate borrowers and will likely further boost transaction activity and values in commercial real estate.

Fundamentals in most sectors appear to have stabilized, including in the office sector, but we do not expect real estate to rocket upwards. PREA's quarterly survey of core fund managers indicates that returns are projected to be in the 6-8% range over the next few years, which signals slow growth in market appreciation. This market environment of slow growth tends to favor investments which rely on income generation for most of their return and are less dependent on appreciation. This sets up well for Boyd Watterson's real estate strategies in the coming years as they are income-oriented vehicles that aren't reliant on appreciation to generate returns. Generally, our strategies have outperformed the NFI-ODCE index in this type of market environment while producing lower volatility. Also, with the Fed cutting rates, we believe the high level of income generated by Boyd's real estate strategies will become more attractive to investors in the coming quarters.

Equities

The S&P 500 Index continued to deliver strong results in the third quarter, gaining 8.12% and bringing the year-to-date return to 14.83%. The NASDAQ Index was up 11.24% for the quarter, led by the computer and health care sectors. Of the eight sectors that make up the NASDAQ Index, only two, insurance and telecom, were negative for the quarter.

The Fed's interest rate cut in September, coupled with the market's expectation that the move was just the beginning of an easing cycle, helped propel stocks higher. Better than expected corporate earnings reports, combined with optimistic outlooks, also fueled the strong returns.

Growth stocks outperformed value, as measured by the S&P 500 Growth Index, which was up 9.77% for the quarter, while the S&P 500 Value Index was up 6.12%. Interestingly, small caps led the way, followed closely by large caps, while mid-caps came in a distant third, as measured by the Morningstar Core indices.

As investors look ahead, they will need to factor in a Federal Reserve that is facing risks to both sides of their dual mandate, a government shutdown, and valuations that appear stretched across nearly all major measures.