MONTHLY MARKET UPDATE
July 2023

Highlights:
- The S&P 500 Index advanced 6.6%, but the narrowness of the market continued. Roughly 200 of the 500 stocks are negative for the year, despite a +16.9% index return.
- After some flattening in prior months, yield curve inversion intensified in June, with 2-year Treasury bonds yielding 100 basis points more than 10-year bonds.
- The Federal Reserve skipped raising rates for the first time in a year; markets now expect one or two more hikes before year-end and are bracing for "higher for longer."

At month end most of the Midwest was suffering under a blanket of wildfire ash and smoke, an apt climate for our sense of the economic and investing landscape. While visibility might have been clouded, investors continued to pile into stocks, with the S&P 500® Index rising 6.6% for the month, pushing the year-to-date return to 16.9%. Short-term bonds and money markets also attracted flows as yields pushed 5%. Optimists could cite resilient corporate earnings, robust housing starts and new home sales, strong employment numbers, steadfast consumer spending, and a slow but steady drop in inflation. First quarter GDP growth was revised upwards from an annualized 1.3% to 2%. The Federal Reserve contributed to the mood by skipping an opportunity to raise rates at their June meeting for the first time in a year.

A deeper look gives reasons for our sense of a more mixed outlook. The narrowness of the market continued. Close to 200 of the 500 stocks in the S&P 500 didn't keep up with the average and are negative so far this year. A few hot technology stocks continued to carry the load, even with extended valuations. While new homes were being grabbed, existing home sales were sluggish as homeowners balked at abandoning existing, low-rate mortgages. New home sales were also concentrated on the high end, only emphasizing the bifurcation in fortune between top earners and the bulk of Americans struggling with the impacts of inflation. Consumer spending, constituting 70% of the economy, appeared to be fueled by dwindling household cash reserves as the bubble of savings stowed during the Covid crisis headed back towards modest, pre-pandemic levels. Another sign of household budget strain: rising levels of credit card debt. Add the consensus likelihood of another Fed rate increase in July with one more possible before year end.

All of these factors lead to our cautious stance on equities, although we continue to see opportunities in the bond market. The sharply inverted yield curve is just one of the historical predictors of an impending recession. The prospect of even higher interest rates, a consumer base with dwindling spending capacity, and a Fed that has explicitly stated the job market will be impacted as it attempts to return inflation towards its 2% targets through restrictive monetary policy all point toward the possibility of rougher times ahead.

Some of these contradictory indicators will eventually resolve, and we should have a clearer perspective on the future. In the meantime, we believe the best course is prudence as we manage through the remainder of 2023 and into 2024.

PORTFOLIO MANAGER Q&A - MADISON SUSTAINABLE EQUITY TEAM

The market's price-to-earnings multiple continues to expand this year while earnings estimates are falling. Are you concerned about the market trading at an above-average multiple while the Fed is still trying to slow down inflation?

Dave Geisler and Maya Bittar
Sustainable Equity Portfolio Managers

Maya Bittar: I would describe this a bit differently. As we entered the year, earnings were falling. But since the first quarter, earnings estimates have actually stabilized. The market is likely looking through to 2024. As you know, the market is a discounting mechanism. Earnings estimates for 2024 call for 10% earnings growth, resulting in a 17.7 times price-to-earnings multiple for the market. If you look at other periods when interest rates were at this level, the market traded 15 to 18 times. So, at 17.7 times, it is not cheap, but also not extremely expensive. When we look at earnings growth based on consensus estimates, we see that earnings are expected to bottom out in the second quarter, which will be reported in just a couple of weeks, and then grow in the third quarter and fourth quarter and into 2024. It's important to look at how individual stocks are priced because the market multiple is based on the entire market. If you look individually at stocks, we're still finding attractively priced stocks in sectors like healthcare, financials, and industrials.

The Fed paused in June after ten consecutive interest rate hikes. And in the second quarter, the stock market rallied on the promise of artificial intelligence. Which of these topics do you think will be more pronounced on upcoming earnings calls?

Dave Geisler: Many companies we listen to quarterly don't necessarily discuss specific monetary policies. The financial sector, of course, discusses the Fed's outlook on rate policies. But most executives are speaking about underlying economic conditions and the visibility of demand for the end markets in which they operate. Listening to companies during the conference season more recently, they're pointing to more of a soft landing. Executives tend not to stick their necks out and will remain pretty cautious about demand and demand conditions during the second quarter earnings calls. As it relates to artificial intelligence (AI), it's a commonly discussed topic that's becoming more important. Companies tend to discuss how they are starting to use generative AI in their businesses and the type of impact it could have. But it's very early. Companies are beginning to incorporate AI more at an experimental level as opposed to really deploying it in specific use cases.

Is the AI hype overblown, or do you see a path toward durable growth?

Dave: There tend to be short-term market reactions to companies mentioning AI, but we think it's still early. It has significant implications across multiple economic sectors, but it's going to be a long investment cycle behind generative AI. Right now, the market that's being impacted the most is the data center market, which is going through an evolution from being run on traditional CPUs to where AI workloads run on a different type of processor called a GPU. Nvidia, the primary provider of GPUs, has had a very strong stock market reaction. And there are a lot of other components to generative artificial intelligence. It's not just semiconductors. We own some of the generative AI beneficiaries in our strategy today, and we continue to evaluate other opportunities because we think there is a case to be made for durable growth over a multi-year period going forward.

The two of you manage Madison's Sustainable Equity Strategy and have a wide array of clients. You and other sustainable and ESG managers have been caught in the crossfire of fierce public policy debate over ESG investing lately. How do you, and how should investors rise above the politicization of ESG?

Maya: Let me start by saying our main objective is to produce competitive returns while taking less risk over a market cycle. We do that by investing in high-quality companies with durable growth. For us, looking at ESG factors is not a political statement at all. It's about good decision-making and risk management. We want to understand the potential risks and opportunities each of the companies we own could face in the future. We are long-term investors and want to ensure they have a viable, long-term strategy and business model. So, it's more than just looking at the risks in front of us today. It's looking at the long-term risks. For example, Pepsi is working to ensure they have access to the raw materials they need for the long term. That's done primarily through the work that they are doing on agriculture and water. Pepsi is working with its suppliers to educate and implement regenerative agricultural practices so they have all the raw materials they may need long term. And then with water – used in both the agricultural side of the business and the beverage business – they have key efforts around water stewardship. They are developing more efficient ways to use water, replenish water, and increase water access in areas where it's scarce. They aim to reduce the water they use in their production by 50% by 2030. These are business decisions, not political ones. It's about good management.

U.S. EQUITIES (%)

	June	QTD	YTD	1 Year	3 Year	5 Year	10 Year
DJ Industrial Average	4.7	4.0	4.9	14.2	12.3	9.6	11.3
S&P 500	6.6	8.7	16.9	19.6	14.6	12.3	12.9
Russell 1000	6.8	8.6	16.7	19.4	14.1	11.9	12.6
Russell 1000 Value	6.6	4.1	5.1	11.5	14.3	8.1	9.2
Russell 1000 Growth	6.8	12.8	29.0	27.1	13.7	15.1	15.7
Russell Midcap	8.3	4.8	9.0	14.9	12.5	8.5	10.3
Russell 2000	8.1	5.2	8.1	12.3	10.8	4.2	8.3

U.S. EQUITY CHARACTERISTICS - S&P 500

	June	2022
Price/Earnings Ratio	23.6	19.1
Weighted Avg. Market Cap ($B)	680.8	417.5
Dividend Yield (%)	1.5	1.7

U.S. EQUITY SECTORS - S&P 500 (%)

	June	QTD	YTD	Weight
Communication Services	2.6	13.1	36.2	8.4
Consumer Discretionary	12.1	14.6	33.1	10.7
Consumer Staples	3.2	0.5	1.3	6.7
Energy	6.6	-0.9	-5.5	4.1
Financials	6.7	5.3	-0.5	12.4
Health Care	4.4	3.0	-1.5	13.4
Industrials	11.3	6.5	10.2	8.5
Information Technology	6.6	17.2	42.8	28.3
Materials	11.1	3.3	7.7	2.5
Real Estate	5.6	1.8	3.8	2.5
Utilities	1.6	-2.5	-5.7	2.6

INTERNATIONAL EQUITIES (%)

	June	QTD	YTD	1 Year	3 Year	5 Year	10 Year
ACWI	5.8	6.2	13.9	16.5	11.0	8.1	8.8
ACWI ex USA	4.5	2.4	9.5	12.7	7.2	3.5	4.7
MSCI EAFE	4.6	3.0	11.7	18.8	8.9	4.4	5.4
Emerging Markets	3.8	0.9	4.9	1.7	2.3	0.9	3.0
China	4.0	-9.7	-5.5	-16.8	-10.3	-5.3	3.0
Japan	4.1	6.4	13.0	18.1	5.7	3.1	5.2
Germany	5.3	2.8	17.9	28.4	5.2	1.8	4.1
United Kingdom	3.9	2.2	8.4	13.2	12.6	2.8	3.9
India	4.7	12.2	5.1	14.2	19.3	8.8	8.9

KEY ASSET PRICES

	June	2022
EUR/USD	1.09	1.06
USD/CAD	1.32	1.36
USD/JPY	144.47	132.78
GBP/USD	1.27	1.21
Bitcoin ($)	30,477.0	16,514.0
Gold ($/oz)	1,926.0	1,827.0
Crude Oil (WTI) ($/bbl)	69.1	80.4

FIXED INCOME (%)

	June	QTD	YTD	1 Year	3 Year	5 Year	10 Year
Government Bond	-0.7	-1.4	1.6	-2.1	-4.7	0.5	1.0
Municipal	1.0	-0.1	2.7	3.2	-0.6	1.8	2.7
U.S. Aggregate Bond	-0.4	-0.8	2.1	-0.9	-4.0	0.8	1.5
Investment Grade Corporate	0.3	-0.3	3.1	1.4	-3.4	1.7	2.5
High Yield	1.7	1.7	5.4	9.1	3.1	3.4	4.4

U.S. TREASURY YIELDS (%)

	June	2022
3-Month	5.4	4.4
6-Month	5.5	4.8
2-Year	4.9	4.4
5-Year	4.1	4.0
10-Year	3.8	3.9
30-Year	3.9	4.0

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The Dow Jones Industrial Average® (The Dow®), is a price-weighted measure of 30 U.S. blue-chip companies. The index covers all industries except transportation and utilities.

The S&P 500® Index is an unmanaged index of large companies and is widely regarded as a standard for measuring large-cap and mid-cap U.S. stock-market performance. Results assume the reinvestment of all capital gain and dividend distributions. An investment cannot be made directly into an index.

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The Russell 1000® Growth Index is designed to track those securities within the broader Russell 1000 Index that FTSE Russell has determined exhibit growth characteristics.

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International Equities Definitions
The MSCI ACWI ex USA Index captures large and mid cap representation across 22 of 23 Developed Markets countries (excluding the US) and 23 Emerging Markets countries. With 1,843 constituents, the index covers approximately 85% of the global equity opportunity set outside the US.

The MSCI EAFE (Europe, Australasia & Far East) Index is a free-float adjusted market capitalization index that is designed to measure developed market equity performance, excluding the U.S. and Canada.

Emerging Markets - MSCI Emerging Market Index – captures large and mid cap representation across 24 Emerging Markets (EM) countries. With 1,138 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country.

China - MSCI China Index - captures large and mid cap representation across China A shares, H shares, B shares, Red chips, P chips and foreign listings (e.g. ADRs).

Japan - MSCI Japan Index - is designed to measure the performance of the large and mid cap segments of the Japanese market.

Germany - MSCI Germany Index - is designed to measure the performance of the large and mid cap segments of the German market.

United Kingdom - MSCI United Kingdom Index - is designed to measure the performance of the large and mid cap segments of the UK market.

India - MSCI India Index - is designed to measure the performance of the large and mid cap segments of the Indian market.

Fixed Income Definitions
Government Bond - Bloomberg US Government Index - measures the performance of the U.S. Treasury and U.S. Agency Indices, including Treasuries and U.S. agency debentures. It is a component of the U.S. Government/Credit Index and the U.S. Aggregate Index.

Municipal - Bloomberg U.S. Municipal Index - covers the USD-denominated long-term tax exempt bond market. The index has four main sectors: state and local general obligation bonds, revenue bonds, insured bonds and prerefunded bonds.

U.S. Aggregate Bond - Bloomberg U.S. Aggregate Bond Index - is a broad-based flagship benchmark that measures the investment grade, U.S. dollar-denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate securities, mortgage backed securities, asset-backed securities and corporate securities, with maturities greater than one year.

Investment Grade Corporate - Bloomberg U.S. Credit Index - measures the investment grade, US dollar-denominated, fixed-rate, taxable corporate and government related bond markets. It is composed of the US Corporate Index and a non-corporate component that includes foreign agencies, sovereigns, supranationals and local authorities.

High Yield - Bloomberg U.S. Corporate High Yield Bond Index measures the USD-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below. Bonds from issuers with an emerging markets country of risk, based on Bloomberg EM country definition, are excluded.

Definitions
Weighted Avg. Market Cap: measures the size of the companies in which the portfolio invests. Market capitalization is calculated by multiplying the number of a company's shares outstanding by its price per share.

Price-to-Earnings (P/E) Ratio: measures how expensive a stock is. It is calculated by the weighted average of a stock's current price divided by the company's earnings per share of stock in a portfolio.

Dividend Yield: the portfolio's weighted average of the underlying portfolio holdings and not the yield of the portfolio.

A basis point is one hundredth of a percent.

Madison INVESTMENTS

All investing involves risks including the possible loss of principal. There can be no assurance the Sustainable Equity strategy will achieve its investment objectives. The portfolios may invest in equities which are subject to market volatility. Equity risk is the risk that securities held by the portfolio will fluctuate in value due to general market or economic conditions, perceptions regarding the industries in which the issuers of securities held by the portfolio participate, and the particular circumstances and performance of particular companies whose securities the portfolio holds. In addition, while broad market measures of common stocks have historically generated higher average returns than fixed income securities, common stocks have also experienced significantly more volatility in those returns.

The Sustainable Equity strategy follows a sustainable investment approach by investing in companies that embed sustainability in their overall strategy and demonstrate adherence to sustainable business practices. In pursuing such a strategy, the strategy may forgo opportunities to gain exposure to certain companies, industries or sectors, and may be overweight or underweight in certain industries or sectors relative to its benchmark index, which may cause the strategy's performance to be more or less sensitive to developments affecting those sectors. In addition, since sustainable investing takes into consideration factors beyond traditional financial analysis, the investment opportunities for the strategy may be limited at times. Sustainability related information provided by issuers and third parties, upon which the portfolio managers may rely, continues to develop, and may be incomplete, inaccurate, use different methodologies, or be applied differently across companies and industries. Madison's framework of sustainable investing will vary from other managers. Further, the regulatory landscape for sustainable investing in the United States is still developing and future rules and regulations may require the strategy to modify or alter its investment process. Similarly, government policies incentivizing companies to engage in sustainable practices may fall out of favor, which could potentially limit the strategy's investment universe. There is also a risk that the companies identified through the investment process may fail to adhere to sustainable business practices, which may result in the strategy selling a security when it might otherwise be disadvantageous to do so.

Prior to 2022, the Sustainable Equity strategy was known as Madison Disciplined Equity. The strategy has evolved over time to the current approach.

Upon request, Madison may furnish to the client or institution a list of all security recommendations made within the past year.