Monthly Market Update

July 2025

Madison INVESTMENTS

Highlights:

- Markets reached new highs in June, but gains were narrow and lacked broad enthusiasm, with the S&P 500 now up 6.2% year-to-date.
- Mega-cap tech stocks led the market in June, driven by strong profitability and renewed enthusiasm for AI, while international stocks maintained their sizable lead over domestic equities year-to-date.
- The yield curve steepened in Q2 as short-term rates dipped in anticipation of possible Fed cuts, while long-term rates rose amid concerns about inflation and budget deficits.
- With inflation likely to rise, confidence falling, and Fed policy uncertain, investors face potential volatility, making fundamentals and valuation critical heading into the second half of 2025.

As the major stock indices ticked up to new all-time highs in late June, something seemed to be missing: euphoria. For one, the S&P 500 Index's 5.1% return in June brought the year-to-date gain to 6.2%, a modest figure compared to the 20%+ returns of the past two years. But more fundamentally, the return of a narrow, tech-driven market overshadowed the less buoyant majority of stocks and didn't reflect the emerging concerns for the remainder of the year. Last month, we remarked on how quickly the market had absorbed and then discounted the surprising tariff regime announced in early April. In June, we saw a similar story as the shock of the U.S. attack on Iran was quickly accepted, and the ramifications dismissed. We believe that investors will be well served by addressing these concerns and remaining vigilant to the potential consequences that issues such as tariffs and acts of war may yet pose. But first, a deeper look at the market.

The familiar mega-cap tech stocks returned to leadership in June, and not without reason. They continue to be extremely profitable and retain the cutting edge in AI development and its necessary infrastructure. However, they weren't the only game in town, as international stocks continued their sizable lead over domestic equities year-to-date. The prospects of the emerging Republican budget bill were particularly daunting to health care companies, and that S&P sector was down sharply in the second quarter. Small and mid cap stocks had a bounce in June but remained well behind the large cap indices for the year. The yield curve steepened over the second quarter as short-term rates dipped in anticipation of a possible second-half Federal Reserve rate cut, while long-term rates rose with the potential tariff-induced inflation and fears of a growing deficit.

Given the characteristics of the market rise in June and the second quarter, broadly diversified and risk-conscious portfolios did not keep up with the cap-weighted indices. At this point in time, with so much unpredictability around trade policies, immigration actions, geopolitics, and the budget, keeping up with the Mag 7-heavy indices is less of a concern than the risks ahead. The Fed is watching whether tariffs re-ignite inflation, while depressed small business and consumer confidence portend an economic slowdown. This scenario puts the Federal Reserve in a bind, reflected in Chairman Powell's hesitancy to predict easing and his constant invocation of the term "uncertainty." With the market price-to-earnings well above historic averages we see an increasing chance of downside volatility, which could hit the highest-valued stocks the hardest. Staying focused on company fundamentals, including valuation, remains our priority as we enter the second half of 2025. Still, the U.S. economy remains the world's strongest and most resilient, and so with an eye on long-term returns, we are investing with a heightened awareness of the potential for market shocks and the resulting selloffs.

Portfolio Manager Q&A - Stuart Dybdahl

U.S. stocks have rallied over 20% since April 8. What's been driving the gains, and when you look below the surface, what's actually working?

The S&P 500 successfully climbed the proverbial "wall of worry," which was built in the form of trade policy uncertainty, interest rate volatility, and geopolitical risk. The initial pivot on April 9th was attributed to a 90-day pause instituted shortly after the tariffs were announced, and subsequent trade deal announcements sent risk assets higher. What's worked since markets bottomed in early April has been a familiar story. Within US equities, growth has outpaced value by 15% and large caps have outpaced mid and small caps by over 2%. Within fixed income, investment-grade and high-yield have outperformed treasuries and securitized sectors.

Stuart Dybdahl, CFA, CAIA
Multi-Asset Solutions
Portfolio Manager & Analyst

As we approach the July 9th tariff implementation, do you think markets are fully pricing in the potential impact of trade policy? What are you watching most closely?

At 22x forward earnings, markets have seemingly priced out anything other than a positive outcome from the trade policy and are somewhat unprepared for a disappointment on this front, as net tariffs will likely be higher after July 9th.

At this point, markets are likely looking beyond trade policy and turning their focus on the remaining policy priorities of the administration, which will likely be more constructive for both the economy and markets moving forward in the second half of this year, as deregulation and tax policy continue to advance.

In light of the evolving trade and tax policies, we continue to monitor a challenging dynamic that has developed between the U.S. dollar and long-term Treasury rates, as the dollar has continued to weaken despite long-term Treasury rates moving higher. Given that this dynamic has historically been experienced in emerging markets, it is definitely a concern and worth monitoring moving forward.

With bond yields now offering income above cash, plus the element of diversification versus riskier assets, how are you positioning fixed income within portfolios?

We're excited about the opportunities available in fixed income today as we are able to achieve desirable levels of income without having to sacrifice credit quality or take on additional interest rate risk, which, for much of the decade preceding 2022, were the only ways to achieve similar yields to those available today in the investment-grade landscape.

Specific to our positioning, the relative valuations and credit enhancements available in the securitized sector combine to make it an emphasis across portfolios today. The bulk of our duration exposure remains in the 1-10 year part of the curve, as we're intentionally underweight longer-term Treasuries due to the uncertainty within the bond market, particularly around the challenging fiscal policy dynamic moving forward.

How are you thinking about active versus passive management in today's market? Are you leaning more in one direction than the other?

From our perspective, the opportunity set for active managers truly couldn't be better, as elevated interest rates, changes to trade policy, and upcoming changes to tax policy will continue to create an environment that benefits some companies more than others and rewards management teams that can adapt and manage accordingly. Combined with a bifurcated valuation backdrop, the opportunity for active management is really attractive moving forward.

For example, on the valuation front, the S&P 500 is trading at 22x forward earnings, which is at the top end of its historical range. Meanwhile, the equal-weighted index is trading at under 17x forward earnings, and the S&P 400 Mid Cap index is trading just under 16x. So, while valuations are stretched at the headline level, there is plenty of opportunity below the surface.

Within fixed income allocations, we prefer to be active and employ active managers within credit, as spreads are currently tight. There are numerous intricacies in the bond marketplace today that we believe experienced fixed income teams are better positioned to capitalize on than purely passive strategies.

So ultimately, across portfolios today, we are expressing this view by allocating more to active managers and enhanced strategies, while de-emphasizing purely passive exposure at this time.

U.S. Equities (%)

	June	QTD	YTD	1 Year	3 Year	5 Year	10 Year
DJ Industrial Average	4.5	5.5	4.6	14.7	15.0	13.5	12.1
S&P 500	5.1	10.9	6.2	15.2	19.7	16.6	13.7
Russell 1000	5.1	11.1	6.1	15.7	19.6	16.3	13.4
Russell 1000 Value	3.4	3.8	6.0	13.7	12.8	13.9	9.2
Russell 1000 Growth	6.4	17.8	6.1	17.2	25.8	18.2	17.0
Russell Midcap	3.7	8.5	4.8	15.2	14.3	13.1	9.9
Russell 2000	5.4	8.5	-1.8	7.7	10.0	10.0	7.1

U.S. Equity Characteristics - S&P 500

	June	2024
Price/Earnings Ratio (NTM)	22.2	21.6
Weighted Avg. Market Cap ($B)	1,145.2	1,117.1
Dividend Yield (%)	1.2	1.3

U.S. Equity Sectors - S&P 500 (%)

	June	QTD	YTD	Weight
Communication Services	7.3	18.5	11.1	9.8
Consumer Discretionary	2.2	11.5	-3.9	10.4
Consumer Staples	-1.9	1.1	6.4	5.5
Energy	4.9	-8.6	0.8	3.0
Financials	3.2	5.5	9.2	14.0
Health Care	2.1	-7.2	-1.1	9.3
Industrials	3.6	12.9	12.7	8.6
Information Technology	9.8	23.7	8.1	33.1
Materials	2.3	3.1	6.0	1.9
Real Estate	0.2	-0.1	3.5	2.0
Utilities	0.3	4.3	9.4	2.4

International Equities (%)

	June	QTD	YTD	1 Year	3 Year	5 Year	10 Year
ACWI	4.5	11.5	10.1	16.2	17.4	13.7	10.0
ACWI ex USA	3.4	12.0	17.9	17.7	14.0	10.1	6.1
MSCI EAFE	2.2	11.8	19.5	17.7	16.0	11.2	6.5
Emerging Markets	6.0	12.0	15.3	15.3	9.7	6.8	4.8
China	3.7	2.0	17.3	33.8	3.1	-1.0	2.1
Japan	1.7	11.4	11.7	13.9	15.0	8.8	6.1
Germany	2.3	16.3	34.4	40.3	25.6	12.5	7.0
United Kingdom	1.4	8.7	19.3	20.0	15.2	14.0	5.5
India	3.1	9.2	6.0	0.9	15.7	18.2	9.2

Key Asset Prices

	June	2024
EUR/USD	1.17	1.04
USD/CAD	1.37	1.44
USD/JPY	144.74	157.37
GBP/USD	1.37	1.25
Bitcoin ($)	107,135.3	93,429.2
Gold ($/oz)	3,309.0	2,608.0
Crude Oil (WTI) ($/bbl)	66.3	72.4

Fixed Income (%)

	June	QTD	YTD	1 Year	3 Year	5 Year	10 Year
Government Bond	1.3	0.9	3.8	5.3	1.6	-1.5	1.2
Municipal	0.6	-0.1	-0.4	1.1	2.5	0.5	2.2
U.S. Aggregate Bond	1.5	1.2	4.0	6.1	2.6	-0.7	1.8
Investment Grade Corporate	1.8	1.8	4.2	6.8	4.2	0.1	2.8
High Yield	1.8	3.5	4.6	10.3	9.9	6.0	5.4

U.S. Treasury Yields (%)

	June	2024
3-Month	4.4	4.4
6-Month	4.3	4.2
2-Year	3.7	4.3
5-Year	3.8	4.4
10-Year	4.2	4.6
30-Year	4.8	4.8

"Madison" and/or "Madison Investments" is the unifying tradename of Madison Investment Holdings, Inc., Madison Asset Management, LLC ("MAM"), and Madison Investment Advisors, LLC ("MIA"). MAM and MIA are registered as investment advisers with the U.S. Securities and Exchange Commission. Madison Funds are distributed by MFD Distributor, LLC. MFD Distributor, LLC is registered with the U.S. Securities and Exchange Commission as a broker-dealer and is a member firm of the Financial Industry Regulatory Authority. The home office for each firm listed above is 550 Science Drive, Madison, WI 53711. Madison's toll-free number is 800-767-0300.

Any performance data shown represents past performance. Past performance is no guarantee of future results.

Non-deposit investment products are not federally insured, involve investment risk, may lose value and are not obligations of, or guaranteed by, any financial institution. Investment returns and principal value will fluctuate.

This report is for informational purposes only and is not intended as an offer or solicitation with respect to the purchase or sale of any security and is not investment advice.

In addition to the ongoing market risk applicable to portfolio securities, bonds are subject to interest rate risk, credit risk and inflation risk. When interest rates rise, bond prices fall; generally, the longer a bond's maturity, the more sensitive it is to this risk. Credit risk is the possibility that the issuer of a security will be unable to make interest payments and repay the principal on its debt. Bonds may also be subject to call risk, which allows the issuer to retain the right to redeem the debt, fully or partially, before the scheduled maturity date. Proceeds from sales prior to maturity may be more or less than originally invested due to changes in market conditions or changes in the credit quality of the issuer.

Holdings may vary depending on account inception date, objective, cash flows, market volatility, and other variables. Any securities identified and described herein do not represent all of the securities purchased or sold, and these securities may not be purchased for a new account. There is no guarantee that any securities transactions identified and described herein were, or will be profitable. Any securities identified and described herein are not a recommendation to buy or sell, and is not a solicitation for brokerage services.

Diversification does not assure a profit or protect against loss in a declining market.

Indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only, and do not represent the performance of any specific investment. Index returns do not include any expenses, fees or sales charges, which would lower performance.

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

The S&P 500® Index is a large cap market index which measures the performance of a representative sample of 500 leading companies in leading industries in the US.

The S&P Midcap 400 is designed to measure the performance of 400 mid-sized companies, reflecting the distinctive risk and return characteristics of this market segment.

The Russell 1000® Index measures the performance of the 1,000 largest companies in the Russell 3000® Index, which represents approximately 89% of the total market capitalization of the Russell 3000 Index.

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.

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

Russell 2000® Index is a small cap market index which measures the performance of the smallest 2,000 companies in the Russell 3000® Index.

The Russell Midcap® Index is a mid cap market index which measures the performance of the mid cap segment of the US equity universe.

Russell Investment Group is the source and owner of the trademarks, service marks and copyrights related to the Russell Indexes. Russell® is a trademark of Russell Investment Group.

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.

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

Municipal - Bloomberg US 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.

US Aggregate Bond - Bloomberg US Aggregate Bond Index is a broad-based flagship benchmark that measures the investment grade, USD-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 US Credit Index measures the investment grade, USD-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 US 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.

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.

Bond Spread is the difference between yields on differing debt instruments of varying maturities, credit ratings, and risk, calculated by deducting the yield of one instrument from another.

A basis point is one hundredth of a percent.

Yield Curve: a line that plots yields (interest rates) of bonds having equal credit quality but differing maturity dates. The slope of the yield curve gives an idea of future interest rate changes and economic activity. There are three main types of yield curve shapes: normal (upward-sloping curve), inverted (downward-sloping curve), and flat.

The Magnificent Seven stocks are a group of high-performing and influential companies in the U.S. stock market: Alphabet, Amazon, Apple, Meta Platforms, Microsoft, NVIDIA, and Tesla.

The federal funds rate is the target interest rate range set by the Federal Open Market Committee (FOMC) for banks to lend or borrow excess reserves overnight. It influences monetary and financial conditions, short-term interest rates, and the stock market.

Duration is a measure of the sensitivity of the price of a bond or other debt instrument to a change in interest rates. Duration measures how long it takes, in years, for an investor to be repaid the bond's price by the bond's total cash flows.

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

Madison-763297-2025-07-01

Madison INVESTMENTS