

Monthly Market Update

August 2025

Highlights:

- Markets rose in July, with the S&P 500 up 2.2%, driven by mega-cap tech stocks, while defensive sectors lagged.
- The Fed held off on rate cuts due to tariff-related inflation concerns, but weak job data in early August revived expectations for easing.
- The 10-Year Treasury yield rose 0.15%. In the tax-exempt markets, long-term municipal bonds are trading at yields that have not been seen in decades.
- Looking ahead, risks include high valuations, rising inflation from tariffs, and signs of a softening labor market, all adding pressure to the Fed's policy decisions.

The major market indices moved up in July, led by the familiar coterie of mega-caps that were responsible for two-thirds of the gain. The S&P 500 Index rose 2.2% for the month, led by the Technology sector, which was up 5.2%. As the market tipped into new all-time highs, the driving forces were a resilient economy, some emerging clarity on volatile tariff policies, and robust earnings, particularly among the largest tech companies. Concentrated gains spelled weak returns for other areas, including the historically defensive areas of Health Care and Consumer Staples.

One hurdle the market overcame in July was the Federal Reserve's reluctance to lower rates. The main factor holding back Federal Reserve action was the percolating impact of higher tariffs on consumer prices. The expectation is that we have yet to see the full potential of the inflationary pressures of these new costs paid by importers. Fed Chair Powell's non-committal tone at his July 30th press conference drove investors to price out a September rate cut, only to see markets reverse course following a weak August 1st non-farm payrolls report, which showed a significantly slowing job market. We had already seen some early-indicator signals from the job

market, including a dip in job openings and increased worker hesitancy to leave positions, and now it seems the growing pro-easing contingent within the Fed has the support of economic data.

Bond values dropped a bit in July as the 10-Year U.S. Treasury yield moved up from 4.2% to nearly 4.4% by month-end. Stock returns over the past few years make it easy to take an eye off bonds, but areas of the bond market currently look attractive. One area of unusual interest is long-term municipal bonds, which are trading with relative yields not seen in decades. Many high-rated munis are yielding close to 5%, a level that approaches similarly rated corporate bonds. For investors in higher tax brackets, the current 4-5% tax-exempt yields equate to 6-8% tax-equivalent yields.

Looking forward, we have a number of concerns hitting our radar. Market valuations remain high and will rely on steady good news on corporate earnings. Meanwhile, margins could be stressed by the overall rise in tariffs, tariff-induced inflation, and a corresponding dip in consumer sentiment and spending. Economists ballpark the inflationary impact of tariffs at .1% for each 1% rise in tariffs. With overall rates rising from 3% to around 15%, we could expect a corresponding 1.2% increase in the inflation rate, a serious bump and one that has the Fed worried.

With the increasing stress in the job market, the Fed is in a difficult position, with conflicting signals from a slowing economy and rising inflation. Fed expectations may continue to oscillate between whichever of its two mandates (full employment and price stability) is further from its goal. Right now, signs point to a September cut, but with an economic backdrop less robust than what had been driving market enthusiasm. Meanwhile, cloaked by the boost from mega-caps, the broader market already reflects some of this caution. We believe shaking out some of the excess in the stock market is overall a healthy development. From our perspective, any market dips we may see going forward are part of the natural cycle and should not deter long-term investors.

Portfolio Manager Q&A - Bill Ford

What do you make of the market movement following the July FOMC meeting and the weaker-than-expected labor market report?

At his post-meeting press conference, Chair Powell reflected a broad but not unanimous consensus at the FOMC that while policy remains mildly restrictive, the economy is holding up well as inflation risks persist. The decision to hold rates steady was met with two dissents, which is unusual, but markets were largely expecting this outcome. There is a growing contingent for easing within the Fed, and their case was strengthened by the July jobs report, which indicated that hiring has stalled and that the past couple of months were not nearly as strong as initially reported. GDP reports also came out, indicating that the economy has slowed in the first half.



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The Fed no longer has the luxury to “wait and see”, and as a result, the yield curve shifted down, with the expectation of a cut, maybe even a 50 basis points catch-up cut, in September. With concerns that the economy may be weaker than previously thought, spreads widened out, and equities sold off as well.

Within the corporate bond market, how are CFOs navigating the macro uncertainty, and what does that mean for investors?

The impact of tariffs will be different based on the industry and company, but broadly speaking, corporations are waiting to see what will happen with final tariff rates and the impact on their businesses. For now, many companies have started to take the hit to profits in the short run, indicating that they will look to raise prices where they feel they have the pricing power to do so to offset rising input costs. Investors should be cognizant of these dynamics in the companies and industries that they invest in and look for firms that have discipline around pricing and profitability. Our focus is on higher-quality, strong moat firms that have the pricing power and discipline to raise prices and protect profitability, rather than chase volume and sales.

How are you thinking about credit risk right now?

By historical standards, credit spreads are at extremely tight levels. Not only that, but lower quality credit spreads are also historically tight, and investors are not being compensated nearly as much as they used to for taking the extra risk. So, in this low-reward, high-uncertainty environment, we want to be more defensive. We are skewing higher in quality than we typically do, looking for credits that have less cyclicalities and less exposure to tariffs and trade policy. Then we’re looking for credits that we would call lower beta, which means that historically, when spreads widen out, they tend to widen out less than the market. We think this defensiveness and discipline will help to protect capital while giving us greater flexibility to take advantage of the opportunities as the market eventually adjusts.

Beyond credit risk, are there other risks that investors might be overlooking?

Beyond credit risk, one of the most underappreciated risks is the potential breakdown of the relationship between the different tenors on the yield curve. For decades, there’s been a fairly consistent pattern between the Fed Funds rate and yields across different maturities. Investors typically earn more yield as they take on longer duration, relative to the Fed Funds rate. Going forward, we may see that those term premia start to rise more than anything based on the fiscal trajectory of the U.S. Rising deficits and long-term entitlement obligations, combined with a lack of political will to address them, will have a much greater impact on the movement of longer rates than Fed policy.

This matters not just for fixed income investors, but all asset classes, because longer rates are generally more important to the real economy. They are what drive mortgage rates. They will impact equity price valuations. But specific to fixed income investors, relying on historical curve behavior to anticipate rate movements may no longer be as reliable in a world where fiscal concerns hold more weight.

Investors continue to sit on high levels of cash. Is there a case to be made to move into fixed income right now?

Cash yields right now are around 4.25% and the yields on high-quality intermediate fixed income are at or above that level. Why would you take extra risk to earn the same yield? Well, if you look at the past six months, rates did come down, and intermediate bonds saw price appreciation. It’s more and more likely that the Fed continues easing, so cash rates will be coming down, while you can lock in a similar or better rate further out the yield curve. If you try to wait until the cash yields come down, there’s a good chance that yields will have also come down on an intermediate portfolio, and you will have missed the opportunity for price performance. The only situation where you start to lose is that the yields on intermediate bonds go up significantly, which we view as a much lower probability scenario.



U.S. Equities (%)

	July	YTD	1 Year	3 Year	5 Year	10 Year
DJ Industrial Average	0.2	4.7	10.0	12.6	13.0	12.0
S&P 500	2.2	8.6	16.3	17.1	15.9	13.7
Russell 1000	2.2	8.5	16.5	16.9	15.5	13.4
Russell 1000 Value	0.6	6.6	8.8	10.6	13.2	9.2
Russell 1000 Growth	3.8	10.1	23.8	22.6	17.3	17.1
Russell Midcap	1.9	6.8	12.1	11.5	12.2	10.0
Russell 2000	1.7	-0.1	-0.6	7.0	9.8	7.4

U.S. Equity Characteristics - S&P 500

	July	2024
Price/Earnings Ratio (NTM)	22.3	21.6
Weighted Avg. Market Cap (\$B)	1,267.5	1,117.1
Dividend Yield (%)	1.2	1.3

International Equities (%)

	July	YTD	1 Year	3 Year	5 Year	10 Year
ACWI	1.4	11.5	15.9	15.3	12.8	10.1
ACWI ex USA	-0.3	17.6	14.7	12.6	9.1	6.1
MSCI EAFE	-1.4	17.8	12.8	13.6	10.3	6.1
Emerging Markets	2.0	17.5	17.2	10.5	5.4	5.8
China	4.8	23.0	42.1	8.2	-1.9	3.8
Japan	-1.4	10.2	6.1	12.4	8.8	5.9
Germany	-1.8	31.9	35.1	23.9	11.0	6.5
United Kingdom	0.9	20.3	16.1	14.1	13.9	5.4
India	-5.1	0.6	-8.0	10.3	14.6	8.4

Fixed Income (%)

	July	YTD	1 Year	3 Year	5 Year	10 Year
Government Bond	-0.4	3.4	2.7	0.9	-1.8	1.1
Municipal	-0.2	-0.6	0.0	1.5	0.1	2.1
U.S. Aggregate Bond	-0.3	3.8	3.4	1.6	-1.1	1.7
Investment Grade Corporate	0.1	4.3	4.4	3.2	-0.5	2.7
High Yield	0.5	5.0	8.7	8.0	5.1	5.5

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

	July	YTD	Weight
Communication Services	2.4	13.8	9.9
Consumer Discretionary	2.6	-1.3	10.4
Consumer Staples	-2.4	3.9	5.2
Energy	2.9	3.7	3.0
Financials	-0.1	9.2	13.8
Health Care	-3.3	-4.3	8.8
Industrials	3.0	16.1	8.6
Information Technology	5.2	13.7	34.0
Materials	-0.4	5.6	1.8
Real Estate	-0.1	3.4	2.0
Utilities	4.9	14.8	2.5

Key Asset Prices

	July	2024
EUR/USD	1.14	1.04
USD/CAD	1.38	1.44
USD/JPY	150.60	157.37
GBP/USD	1.32	1.25
Bitcoin (\$)	115,758.2	93,429.2
Gold (\$/oz)	3,292.0	2,608.0
Crude Oil (WTI) (\$/bbl)	70.4	72.4

U.S. Treasury Yields (%)

	July	2024
3-Month	4.4	4.4
6-Month	4.3	4.2
2-Year	3.9	4.3
5-Year	4.0	4.4
10-Year	4.4	4.6
30-Year	4.9	4.8



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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 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.

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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 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.

Municipal bond investment income may be subject to certain state and local taxes and, depending on your tax status, the federal alternative minimum tax. Capital gains are not exempt from federal income tax.

Beta: a measure of an investment's sensitivity to market movements. A portfolio with a beta greater than 1 is more volatile than the market, and a portfolio with a beta less than 1 is less volatile than the market.

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