

Market Commentary

September 30, 2025



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INVESTMENT ADVISORS

U.S. Equities Market

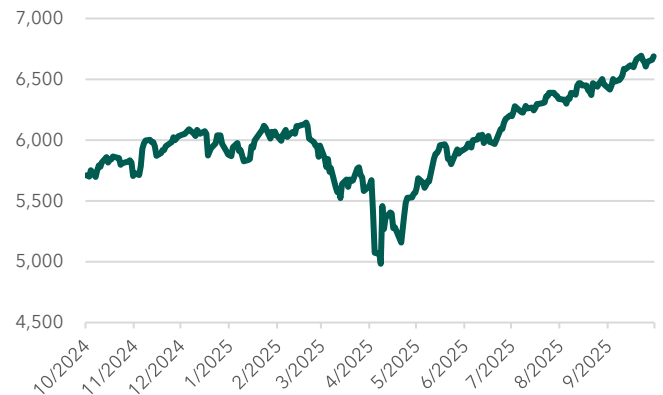
All About AI

U.S. equities performed strongly in the third quarter with the S&P 500® Index gaining 8.1% in the quarter. Information Technology and Communication Services stocks led the market as Artificial Intelligence companies continue to rally on strong momentum and guidance regarding spending and demand. Stocks in the Financials sector also did well in response to the first rate cut from the Federal Reserve ("Fed") and a benign credit market. Consumer Staples was the only sector to post negative returns as investors continued to rotate away from defensive into riskier assets. As with the first two quarters, Growth indices outperformed Value, and large-cap dominance remained intact. Not only did the market finish at near record levels, but market concentration is also at record levels. At quarter end, the largest 10 companies in the S&P 500® Index together account for approximately 40% of the index's market capitalization, with the top five representing about 27%, above the peaks reached in 2000.

As mentioned above, the excitement of Artificial Intelligence was a main driver of stock market performance, but the expectation and commencement of the Fed's cut in short-term interest rates was a significant tailwind. It is often stated, "Don't fight the Fed," but with the dual mandate of price stability and full employment, the Fed is in a somewhat difficult position. The labor market, though resilient, is weakening and consumer sentiment is moving lower; further, inflation remains well above the Fed's target of 2%. If inflation picks up, the Fed will be limited in its ability to support the labor market. Additionally, with budget deficits and partisan conflict in Washington DC at high levels, there is little the federal government may be able to do to stimulate a weaker economy. However, despite tariff uncertainties and a lack of trade agreements with large markets, the economy is growing, corporate profitability is high, and consumers continue to spend at a solid pace though a significant bifurcation is emerging between high-income and low-income earners.

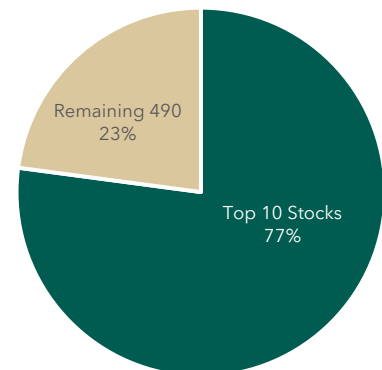
Lastly, it bears mentioning the lofty valuations we are seeing in the financial markets. Corporate bond spreads are so low that Microsoft recently was paying a lower rate on its debt than the U.S. government. Most valuation ratios in the stock market are near highs, and the equity risk premium is closer to zero than any other time since (again) 2000. Leverage ratios are still fine, household and corporate balance sheets are solid, and incomes are rising albeit at slower levels. It's simply prudent to set investor expectations accordingly and monitor how much risk one is taking for an acceptable level of return.

S&P 500® Index



Source: Bloomberg

Q3 2025 S&P 500 Contribution-to-Return



Source: Bloomberg

Equity Risk Premium



Source: Bloomberg

U.S. Taxable Fixed Income Market

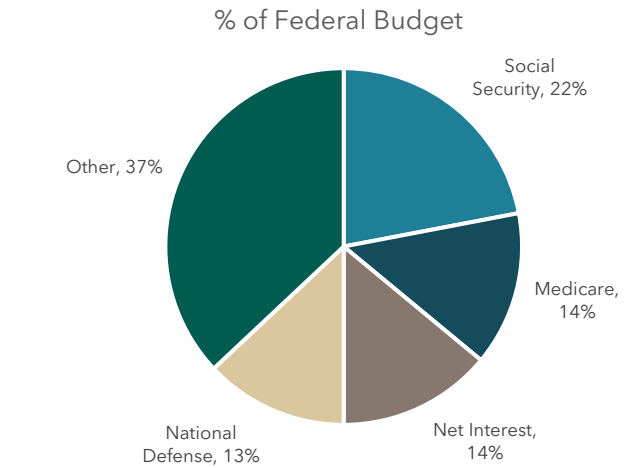
Secular vs. Cyclical Dynamics

For much of the first half of 2025, the story in fixed income was both secular and fiscal policy driven, as the potential for inflation with high, persistent deficits and tariffs dictated much of the market narrative. That slowly changed over the course of the third quarter as the cyclical dynamic came into fuller view and the potential for the Fed to cut interest rates more aggressively began to drive market decision making. This helped propel the Bloomberg Intermediate U.S. Government/Credit Bond Index to return 1.5% in the quarter and post a gain of 5.7% year-to-date.

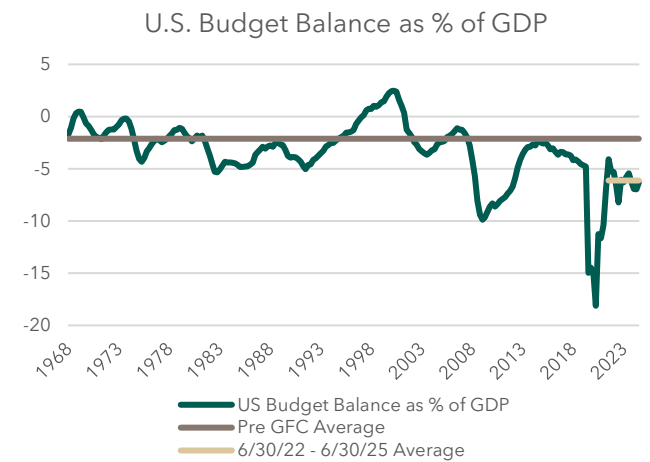
After hitting 4.79% in January, the yield on the 10-year U.S. Treasury note fell all the way to 3.99% before finishing the third quarter at 4.15%. Similarly, investment grade credit spreads hit their widest levels of the year in April before steadily tightening more than 50 basis points to finish the quarter. Spreads have tightened as investors expect more Fed cuts than they did at the beginning of the year, while still avoiding a recession. Given that these easing expectations emanated from a view that the economy was weakening, longer maturity yields also moved lower through the quarter.

While cyclical employment and inflation dynamic dominated investor mindsets in the third quarter, the secular forces that prevailed earlier in the year have yet to show strong signs of materializing. Tariffs have been implemented and are working their way through the economy, causing slight upward pressure to prices as many economists expected, though they have failed to match consumer expectations. Federal deficit spending persists and, likely, will remain well above its long run average. From 6/30/22 to 6/30/25, the federal deficit has averaged 6.12% of GDP, nearly three times the pre-financial crisis average, dating back to 1969, of 2.12%. According to the U.S. Treasury Department, 14% of federal spending this year has been consumed by net interest payments, while roughly another 59% went to transfer payments, with the largest being Social Security. This dynamic is unlikely to change any time soon, so with U.S. debt-to-GDP already around 120% and deficits necessitating further borrowing, a convincing argument for structurally higher long-term interest rates can still be made.

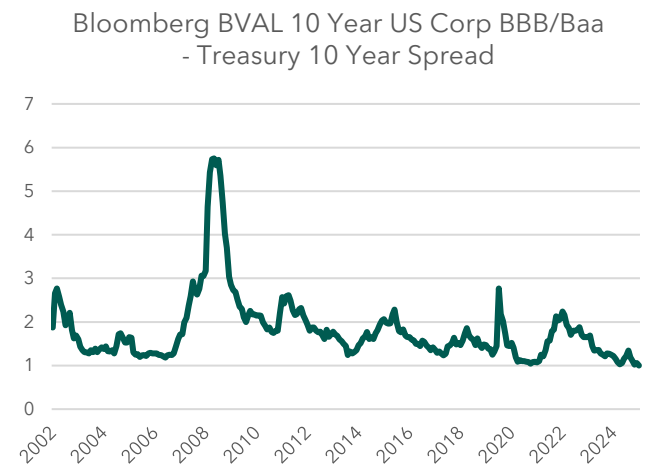
While consumer spending remains robust, higher-income consumers account for a significant portion of it. The unemployment rate has risen steadily over the last two years from a low of 3.4% to 4.3%, and were this weakness to continue, more Fed rate cuts would be in the offing. This is the case for yields to fall across the curve in the more immediate future, but a significant decline from here would likely necessitate a recession, which given corporate and consumer balance sheets might be a step too far. That is a dynamic currently reflected by 10-year BBB-rated corporate spreads sitting at 100 basis points. In fact, those spreads fell below 100 for seven days in September, the only seven days they have been below 100 in 5,970 trading days of data.



Source: fiscaldata.treasury.gov



Source: Bloomberg



Source: Bloomberg; Federal Reserve

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U.S. Municipal Fixed Income Market

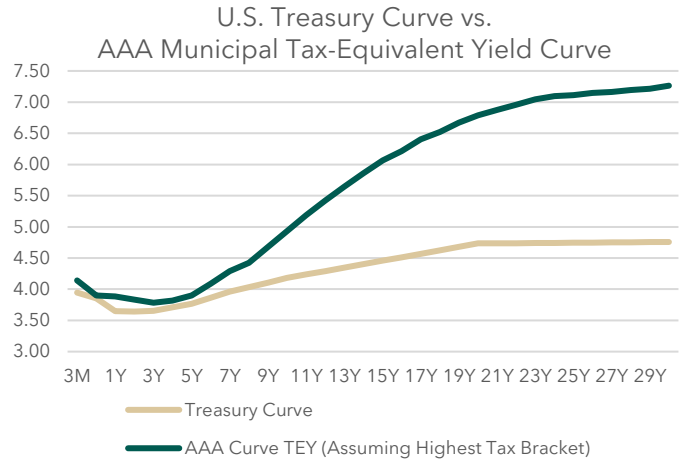
A Steep Climb Up a Mountain of Supply

The third quarter of 2025 saw rates for which markets began to price in a weaker labor outlook and corresponding Fed cuts, which provided relief to most fixed income assets by the end of the period. While municipal bond yields fell over the quarter, the largest decline was for bonds maturing within the next ten years. This created a steeper yield curve, where investors receive more income for each year of maturity, especially between the ten- and twenty-year part of the curve. At the beginning of 2025, a twenty-year AAA muni yielded roughly 75% of the twenty-year U.S. Treasury; at the end of the third quarter, that stood at roughly 85% of the corresponding U.S. Treasury yield.

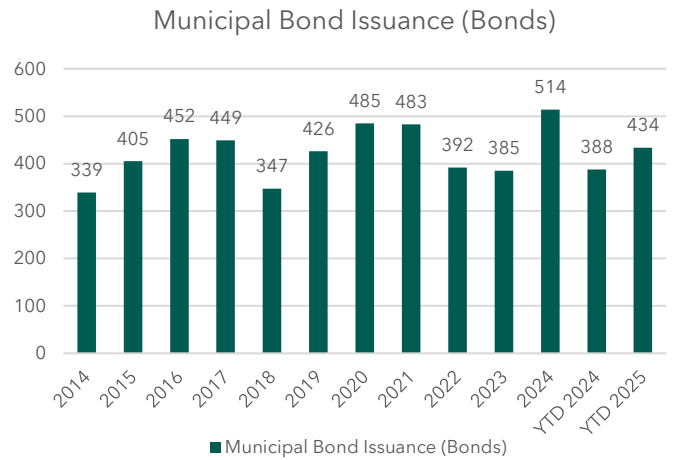
Despite record tax-exempt supply this year, the Bloomberg 1-15 Year Municipal Index was up 3.71% year-to-date as of September 30th. To put that in perspective, the annualized return for the index from 12/31/2014 to 12/31/2024 was just 2.04%. Even as longer maturity municipal yields have moved higher this year, the index has been able to post above-average returns compared to the last decade. Were the economy to weaken or even hit stall speed and longer rates were to fall, it is likely that portfolios positioned in this steeper portion of the curve would perform well. Additionally, this could drive demand out of the short end of the yield curve, where tax-equivalent yields are not nearly as robust compared to taxable options.

Aside from potential macroeconomic weakness, any slowing of the municipal supply tsunami that hit this year would add further technical strength to longer maturity munis by bringing a more balanced supply and demand dynamic. In 2024, total muni supply reached its highest level this century, hitting \$514 billion. Through September 2025, issuance has totaled \$434 billion, \$46 billion more than was seen through September of 2024. As previously mentioned, much of the demand this year has focused on the 1 to 10-year part of the curve, as investors worried about tariffs and the potential knock-on effects they might have on inflation. As 2025 draws closer to its end, labor market concerns are starting to overtake inflation worries, leaving room for the Fed to potentially continue its rate cut path and potentially leading to more demand in the longer end of the curve.

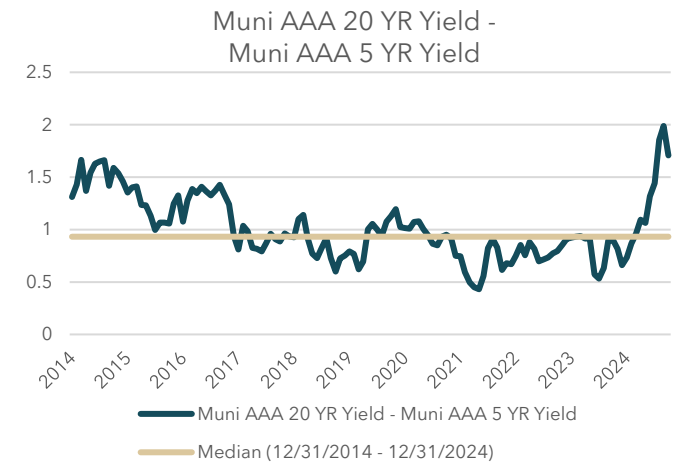
Finally, the yield difference between a five-year AAA muni and a twenty-year AAA muni now sits at 1.71%, almost double its decade-long median of 0.93%. In fact, except for the last two months, it has not been higher going back to 2014. As such, having exposure to this longer portion of the municipal curve might prove advantageous to investors over the coming months, quarters, and years.



Source: Bloomberg



Source: Bloomberg



Source: Bloomberg



International Equities Market

Trade Agreements Drive Risk-On

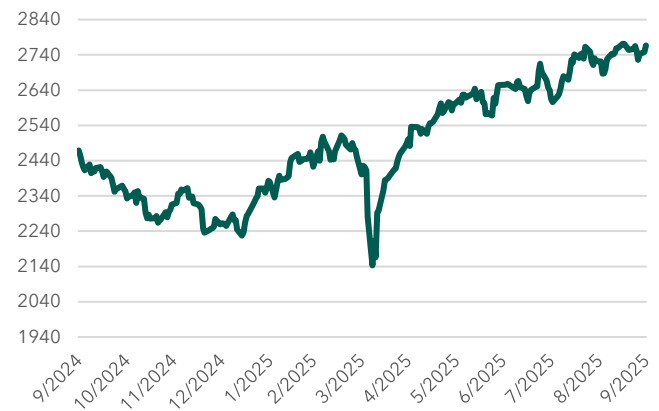
Equity performance was strong across markets during the third quarter. The MSCI Emerging Markets® Index performed best, returning 10.6% for the quarter. Domestic equities, represented by the Russell 3000® Index, returned 8.2% for the quarter whereas the MSCI EAFE® Index, our proxy for developed international equities, generated a return of 4.8%. International equities continue to outperform domestic equities on a year-to-date basis with the Emerging Markets Index up 27.5% and the MSCI EAFE Index up 25.1% versus the Russell 3000® Index up 14.4%. The dollar strengthened modestly, with the Bloomberg U.S. Dollar Spot Index up 86 basis points and was a moderate headwind to international equity performance.

The tariff picture is slowly beginning to come into focus with a number of preliminary agreements announced during the quarter. One thing that is very clear is the Trump Administration is set on changing global trade. Several country representatives remarked that once they accepted this point of view, progress on negotiations improved. Hence, their focus shifted to mitigating the damage from tariffs rather than attempting to avoid them altogether. As such, the situation remains fluid. Most tariff-related announcements were of preliminary agreements and not final. In addition, the administration continues to announce new tariffs, such as with steel and copper, which can make getting to a final agreement more chaotic. Nevertheless, it is encouraging to see progress because markets favor certainty even if the consequences are somewhat negative.

The U.S. International Trade Commission issues a statistic of the approximate effective tariff rate, which as of the end of July was 9.75%. That rate is up from 2.31% reported for November 2024. There are estimates from other sources that estimate a higher effective rate in the upper teens. Regardless of which figure is correct, it is the amount of increase in the effective rate that concerns investors. Interestingly, one of the biggest surprises to the markets this year is that the negative effect from those higher rates has not yet impacted the global economy to the degree expected earlier. For example, in September, the Organization for Economic Co-operation and Development increased its global GDP forecast for 2025, stating that the full effects of higher tariffs have yet to be felt. They stated that tariffs are rolling out more gradually than expected, and that firms are choosing to give up some margin by absorbing the tariffs rather than passing them onto consumers. Their outlook for 2026 did not change, up 2.9%, but they now assume the growth rate will decelerate year-over-year.

It will be interesting to see if this year's momentum continues into the fourth quarter. There are still a number of very important deals yet to be determined – agreements with China, Mexico and Canada come to mind. Clarity on these three is paramount given they are the U.S.'s largest trading partners.

MSCI EAFE® Index



Source: Bloomberg

MSCI Emerging Markets® Index



Source: Bloomberg

Bloomberg Dollar Spot® Index



Source: Bloomberg

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The S&P 500® Index is a gauge of large-cap U.S. equities and serves as the foundation for a wide range of investment products. The index includes 500 leading companies and captures approximately 80% coverage of available market capitalization.

The equity risk premium is defined as the excess return that investing in the equities over the risk-free rate. This index is calculated by Morgan Stanley. The risk premium is measured as the spread (in basis points) between the index's next twelve-month consensus earnings yield and the 10Y treasury yield.

The Bloomberg Intermediate U.S. Government/Credit Bond Index is a broad-based flagship benchmark that measures the non-securitized component of the U.S. Aggregate Index with less than 10 years to maturity. The index includes investment grade, U.S. dollar-denominated, fixed-rate treasuries, government-related and corporate securities.

The Russell 3000® Index is a capitalization-weighted stock market index that seeks to be a benchmark of the entire U.S. stock market.

The MSCI Emerging Markets® Index is a free-float weighted equity index that captures large and mid-cap representation across Emerging Market countries. The index covers approximately 85% of the free float-adjusted market capitalization in each country.

The MSCI EAFE® Index is broadly recognized as the pre-eminent benchmark for U.S. investors to measure international equity performance. It comprises the MSCI country indexes capturing large and mid-cap equities across developed markets in Europe, Australasia and the Far East, excluding the U.S. and Canada. Numerous exchange-traded funds are based on the MSCI EAFE® Index, and the Chicago Mercantile Exchange, NYSE Liffe U.S. and the Bclear platform of Liffe are licensed to list futures contracts on this index as well.

The Bloomberg Dollar Spot Index tracks the performance of a basket of 10 leading global currencies versus the U.S. Dollar. It has a dynamically updated composition and represents a diverse set of currencies that are important from trade and liquidity perspectives.