CONGRESS
ASSET MANAGEMENT COMPANY

Fixed Income Outlook

| 2Q25

KEY TAKEAWAYS:

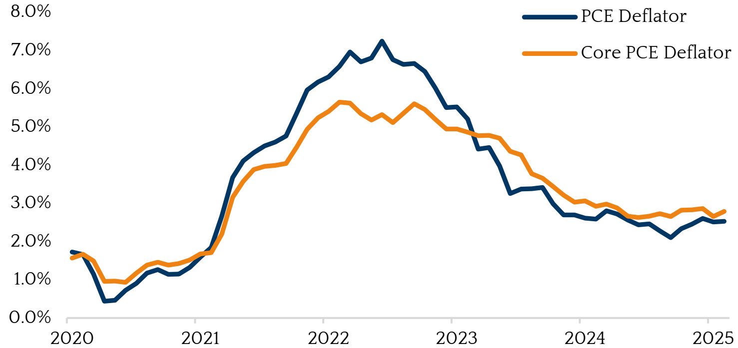
1. **Fixed income markets were aided by falling yields over the quarter, as investors flocked to bonds given the uncertain market outlook.**
2. **While credit spreads moved wider over the quarter, they remain narrow by historical standards and we do not believe this is the right time to add additional exposure.**
3. **We expect continued volatility in the bond market as the lack of fiscal policy stability may drive unpredictable moves in interest rates and corporate bond spreads**
4. **We continue to believe that our clients are best served by our focus on building high-quality portfolios that provide liquidity and strive for long-term principal protection.**

Markets were unsettled by shifts in investor expectations for the U.S. economy. The stock market saw gains into mid-February, only to reverse course in March. Bonds witnessed a decline in yields with the U.S. Government yield curve flattening over the quarter. Investors continue to grapple with rapidly evolving government policies impacting both domestic and global marketplaces. At the forefront of concerns were two key issues: GDP growth and inflation.

The economic growth picture grew cloudier during the first quarter with slowdowns in government spending and consumer activity, tempering growth forecasts. As expected, the incoming administration swiftly announced and enacted budget cuts. The speed and sweeping nature of the cuts are expected to reduce U.S. Government spending, which accounted for over 30% of domestic GDP in 2023. Consumers have also pulled back spending, as reported by several corporations across both discretionary and staples sectors. The shift has been evident for companies that provide travel, automobiles, housing, food, and clothing.

Inflation worries were ignited as the government's chaotic tariff policy dominated media headlines. Consumers are likely to bear the brunt of the tariffs as businesses typically pass them along in the form of higher prices. The incendiary rhetoric surrounding the tariff messaging has also fueled consumer anxiety. These fears are likely already influencing consumer spending patterns as they become more cautious ahead of anticipated cost increases.

Figure 1 YoY Personal Consumption Expenditures Price Indices 2020-2025

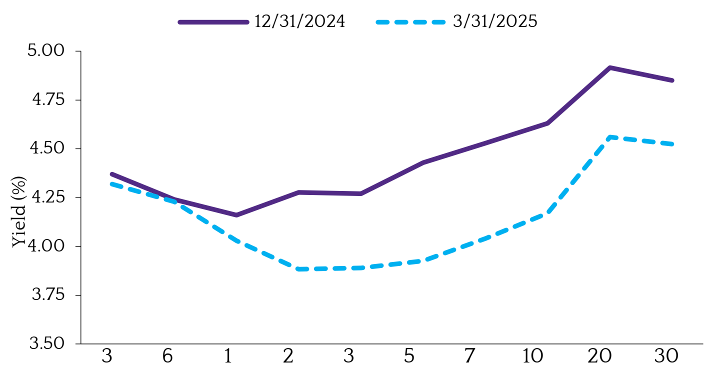


Source: Bloomberg

The Federal Reserve Open Market Committee (the Fed) has also taken notice of these trends. After their most recent meeting, they unveiled lower GDP growth expectations and higher inflation projections, corroborating recent developments. They cited that, "Uncertainty around the market outlook has increased." The bond market has been relatively steady in its own forecast of future Fed actions, which continue to stay at two 25 basis point cuts this calendar year. The Fed, for now, remains on hold and awaits further economic data alongside the rest of the market.

Longer term U.S. Treasury yields fell over the quarter, following the historical pattern of investors flocking to bonds in times of stress. The resulting shape of the curve is unusual, with short- and long-term rates offering similar yields while mid-term yields are below these levels. This somewhat flattened curve does not necessarily signal trouble, but rather reflects the ambiguous direction of the U.S. economy in the near future.

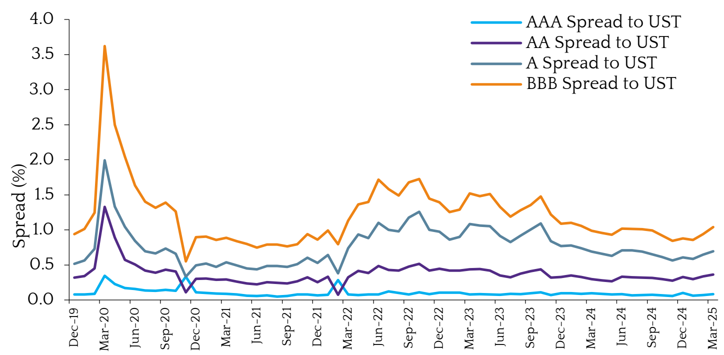
Figure 2 U.S. Treasury Yield Curve on December 31, 2024 & March 31,2025



Source: Bloomberg

Credit spreads, or the additional yield required by investors to compensate for default risk, have not shown the same volatility as seen in interest rates. Despite moving wider over the first quarter, they are still narrow by historical standards. Given the ongoing economic uncertainties, we find the persistence of these narrow spreads vexing, as investors are simply not demanding enough protection for risk.

Figure 3 Intermediate Investment Grade Credit Spreads (OAS) by Quality Rating Cohort December 2019 to March 2025



Source: Bloomberg

Corporate bonds and U.S. Government-guaranteed issues had very similar returns over the last three months. The typical benefits of Corporate bonds (e.g., higher yields, high coupons, strong demand, etc.) were dampened by the increases in spreads. Meanwhile, U.S. Treasury issues were boosted by falling long term yields. U.S. Treasuries edged out Corporate bonds by a slim margin. Overall, both cohorts delivered positive returns for the quarter, a pleasing result for investors.

Looking ahead, we expect continued volatility in the bond market. The current economic environment lacks stability and clear direction, leading to unpredictable moves in interest rates and corporate bond spreads. We are hopeful that the long running trend of low spreads will reverse. If spreads do become more attractive, we will be more inclined to increase allocations.

We best serve our clients by constructing high-quality, investment-grade bond portfolios. While credit spreads have incrementally widened, we do not believe that this is the right time to add exposure. Instead, we are maintaining our current balance between Corporate bonds and U.S. Government-guaranteed issues. Our long-term, strategic goal remains the building of portfolios that provide liquidity, carry high-quality ratings, and favor principal protection.

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