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Market Update

Volatility was the defining theme of the fixed income markets in the second quarter. Investors were forced to navigate a whirlwind of shifting headlines, including tariff policy reversals, escalating tensions in the Middle East, political posturing around a “Big Beautiful Bill,” and a growing narrative questioning the continuation of U.S. exceptionalism. These factors created significant volatility for bond yields. The 10-year U.S. Treasury yield fell below 4.0% in early April, surged to 4.6% in May, and ultimately settled at 4.23% by quarter-end—relatively unchanged, but with considerable turbulence along the way.

The underlying cause of this volatility has been the market’s ongoing attempt to interpret and respond to a complex mix of domestic, geopolitical, and economic signals. Shifting expectations around inflation, monetary policy, and global growth have led to frequent reassessments of risk and opportunity.

Despite these challenges, the first half of the year has generally been constructive for fixed income assets. Inflation has continued to trend lower, moving closer to the Federal Reserve’s 2% target. Economic data has remained decent, though recent indicators point to a deterioration. One notable development is the pullback in discretionary consumer spending—even as the labor market remains resilient on the surface. This dynamic will be closely monitored by the Fed in the months ahead.

Should the labor market begin to weaken or further signs of consumer strain emerge, the Fed may respond with interest rate cuts. As of now, market expectations suggest two rate cuts by year-end, which would bring the Federal Funds rate down to 3.75% - 4.00%.

At AMI, we expect continued volatility in the bond market during the second half of the year as investors digest ongoing trade developments and signs of economic deceleration. In response, we’ve adopted a more defensive positioning. Our approach is designed to preserve capital while maintaining flexibility to adapt as the landscape evolves.

Core Taxable Fixed Income

Core taxable accounts posted positive returns in the second quarter, closely mirroring the index’s 1.66%¹ gain. Taxable municipal bonds, corporate bonds, and Treasuries, all had positive returns in the quarter, with corporate bonds rising the most. Given the increased market volatility, we will maintain a more cautious allocation in Core portfolios, favoring intermediate Treasuries over corporate bonds, which currently offer historically low additional compensation.



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Municipal Bonds

Municipal accounts were flat in the second quarter, underperforming the benchmark, which gained 1.38%². The California municipal market lagged the national market due to factors such as the Los Angeles fires, increased municipal issuance, a high budget deficit, and increased negative headlines between California and the Federal Government. These factors are expected to be temporary, with a reversal of trends anticipated throughout the year. At AMI, our focus remains on essential service sectors, such as water, sewer, and electric utilities, as well as Mello-Roos bonds backed by stable property tax revenues and minimal pension liabilities.

High Yield Fixed Income

High Yield accounts posted positive returns in the second quarter but underperforming the index, which rose by 3.49%³. This was primarily driven by an overweight position in higher-rated corporate bonds, reflecting our cautious stance on the economy. With the additional compensation for lower rated corporate bonds at an all-time low, our focus remains on higher-quality bonds, which we believe will be more resilient to economic pressures.



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Disclosures

AMI Asset Management (AMI) is an independent investment management firm registered with the Securities and Exchange Commission since 1994. Registration does not imply a certain level of skill or training. AMI provides discretionary asset management services to institutional and individual clients through separately managed accounts using six equity and fixed income strategies.

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To receive a complete list of composite descriptions, GIPS® Reports, or the latest copy of our ADV Part 2 contact Katharine Kim at (424) 320-4003 or write AMI Asset Management Corporation, 10866 Wilshire Boulevard Suite 770, Los Angeles, California 90024, or Katharine@amiassetmanagement.com.

1. Figures presented on page one are from the ICE BofAML 1-10 Year US Corp and Government Index as of 6/30/25.
2. Figures presented on page one are from the ICE BofAML 3-7 Year US Municipal Securities Index as of 6/30/25.
3. Figures presented on page two are from the ICE BofAML 1-10 Year US High Yield BB-B Index as of 6/30/25.

