

## Quarter in Review and Highlights

The equity market sold off sharply after President Trump announced highly restrictive trade tariffs on April 2. The S&P 500 Index approached bear market territory by mid-April but rebounded strongly thereafter as President Trump scaled down the most extreme tariff measures. Following years of underperformance relative to U.S. equities, foreign stocks posted strong absolute and relative performance.

- **First quarter U.S. gross domestic product (GDP) contracted for the first time in three years with weaker consumer spending and trade imbalances driving the decline...**Labor market conditions remain solid, but new job creation is moderating. The unemployment rate continues to hover around 4%, near most estimates of full employment.
- **The Federal Reserve (Fed) held rates steady during its May and June meetings with Chair Powell citing new trade tariffs are likely to increase the risk of higher inflation...**Despite stable short-term rates, long-term interest rate volatility remains elevated, partly resulting from investor concerns regarding the persistently high U.S. government debt and deficits. Moody's followed the lead of S&P in 2011 and Fitch in 2023 by downgrading U.S. government debt from its AAA-rating in May.
- **The long-running trend of corporate credit spread tightening reversed course during February, March and April as bond investors turned more cautious about global economic growth prospects. However, the credit market rally resumed in May and June with spreads ending the quarter near levels seen at the beginning of the year...**Investment-grade (IG) corporate credit spreads tightened by 11 basis points (bps) during the quarter, outperforming duration-matched Treasuries by 104 bps. Agency mortgage-backed security spreads also outperformed duration-matched Treasuries.

**Our investment capabilities incorporate a unified investment philosophy and process across the risk spectrum.**

Enhanced Cash	Short Duration Bond	Strategic Income	Short Duration High Yield	Core Plus Bond	High Yield Bond	Balanced Income
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## Short Duration Bond Strategy

The Short Duration Bond Strategy outperformed its benchmark, the Bloomberg U.S. Government/Credit 1-3 Year Bond Index, during the second quarter. The 2-year Treasury note yield traded in a narrow trading range during the quarter, closing June at 3.72%.

After spreads widened substantially between February and April, corporate credit spreads tightened materially thereafter, closing June at the tightest levels since January. IG corporate bonds outperformed duration-matched Treasuries by 104 bps during the quarter while the high-yield bond market generated a total return of 3.5%.

Strategy overweights by sector include high-quality collateralized loan obligations (CLOs), student loan asset-backed securities (ABS) and IG corporate bonds. Portfolio duration is currently in line with the benchmark, but we will remain opportunistic with duration and yield curve management.

## Strategic Income Strategy

The Strategic Income Strategy outperformed its benchmark, the ICE BofA 3-Month U.S. Treasury Bill Index, during the second quarter. Long-term Treasury yields troughed in early April as investors sought safety following President Trump's proposed trade tariffs that were significantly higher than expected. Despite elevated interest rate volatility throughout the second quarter, the 10-year Treasury note yield finished two bps higher, closing June at 4.23%. The Fed held short-term interest rates steady during its May and June meetings, citing higher inflation risks from more restrictive U.S. trade policy.

Corporate credit spreads were volatile during the quarter but closed on a strong note as investor fears of a global trade war eased.

Strategy overweights include intermediate-duration corporate bonds, student loan ABS and residential mortgage-backed securities (RMBS). The Strategy remains positioned to benefit from continued yield curve steepening with duration being managed opportunistically.

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### ABOUT US

Penn Mutual Asset Management (PMAM) is an institutional asset management firm located just outside of Philadelphia, PA. Since 1989, the firm has been dedicated to creating value through a prudent, thoughtful and rigorous investment decision-making process. With over \$41 billion in assets under management, PMAM is committed to offering fixed income investment solutions and client-focused services.

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## Short Duration High Yield Strategy

The Short Duration High Yield Strategy outperformed its benchmark, the ICE BofA 0-2 Year Duration BB-B U.S. High Yield Constrained Bond Index, during the second quarter. The high-yield credit market started the quarter at the widest spreads of the year to that point, with uncertainty swirling of what “Liberation Day” would bring. Immediately following “Liberation Day” on April 2, high-yield credit spreads repriced materially higher. However, as the market became convinced that the worst-case scenario was unlikely to occur, investors began to add risk again. Over the course of May and June, high-yield spreads returned to near the tightest levels of the year.

Despite market weakness, the front end of the high-yield market performed in line with expectations as it outperformed broader high-yield market spreads during the uncertainty. Capital market access remained open during most of the quarter and default rates continue to be lower than historical average. As the quarter ended, investors seemingly chased performance as lower-rated credits started to outperform.

The Strategy maintained its overall risk profile, although a few of the potentially more volatile credits owned were swapped into more stable situations heading into “Liberation Day.” The Strategy ended the quarter with no corporate credits yielding over 10%, compared to having one credit with a yield of over 10% at the beginning of the quarter.

## Core Plus Bond Strategy

The Core Plus Bond Strategy outperformed its benchmark, the Bloomberg U.S. Aggregate Bond Index, during the second quarter. Treasury yields moved lower in April as investors sought safety in response to risks of a global trade war. The 10-year Treasury note yield moved lower, touching 4.0% in early April, but quickly reversed course after President Trump scaled down the most severe tariff measures. Inflation declined during the quarter; however, the Fed is remaining patient with additional rate cuts.

Strategy overweights remain focused on securitized spread sector investments including agency guaranteed RMBS and student loan ABS. We are maintaining Strategy duration, or interest rate risk, in line with the benchmark and positioned to benefit from yield curve steepening.

## High Yield Bond Strategy

The High Yield Bond Strategy outperformed its benchmark, the Bloomberg U.S. High Yield BA/B 2% Issuer Capped Index, during the second quarter. The high-yield credit market started the quarter at the widest spreads of the year to that point, with uncertainty swirling of what “Liberation Day” would bring. Immediately following “Liberation Day” on April 2, high-yield credit spreads repriced materially higher by approximately 200 bps from the tightness of the year. However, as the market became convinced that the worst-case scenario was unlikely to occur, investors began to add risk again. Over the course of May and June, high-yield spreads returned to near the tightest levels of the year and inside of 300 bps again.

The Strategy was well positioned heading into “Liberation Day” as it had limited exposure to the retail and auto sectors, two of the sectors most directly impacted by broad-based tariffs. Throughout the quarter, the Strategy stayed the course and continued to invest in what we believed to be the best relative value and total return opportunities. Specifically, the Strategy put more cash to work in attractive opportunities across the risk spectrum as volatility created opportunities. The Strategy finished the quarter with less cash and net added higher-yielding securities.

## Balanced Income Strategy

The Balanced Income Strategy underperformed its benchmark, the Morningstar Moderately Conservative Target Risk Total Return USD Index, during the second quarter. Both stocks and bonds rose modestly on an absolute basis. The strategy’s fixed-income portfolio lagged on a relative basis during the quarter, but equity performance rebounded on an absolute and relative basis.

The second quarter witnessed significant swings in risk market valuations as investor fears of a global trade war gradually eased after President Trump rolled back the most severe trade tariffs. The S&P 500 Index moved into record-high territory by quarter-end and corporate credit spreads moved back to the tightest levels since January.

The Strategy’s positioning should provide the potential for higher portfolio yields with the goal of also achieving a favorable total return. We will continue to monitor our investable universe for any opportunity to add value. We believe this focus on individual security selection will help to see us through this period of elevated uncertainty.

## Outlook

Despite the uncertainty created by U.S. trade policy, inflation continues to trend lower, which should allow the Fed to resume interest rate cuts during the third quarter. The biggest risk to financial assets is a “crack in the bond market” leading to a surge in long-term bond yields.

## Index Definitions

**Bloomberg U.S. Aggregate Bond Index** – An index that is a broad-based flagship benchmark that measures the investment grade, US dollar denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate securities, MBS (agency fixed-rate and hybrid ARM pass-throughs), ABS and CMBS (agency and non-agency).

**Bloomberg U.S. Government/Credit 1-3 year Bond Index** – The Bloomberg U.S. Government/Credit Bond Index is a broad-based benchmark that measures the non-securitized component of the US Aggregate Index. It includes investment grade, US dollar-denominated, fixed-rate Treasuries, government-related and corporate securities.

**Bloomberg U.S. High Yield Ba/B 2% Issuer Capped Index** – This index measures the performance of fixed-rate dollar-denominated debt securities with rating Ba/B. The securities instruments are non-investment grade. There is a limit of 2% maximum exposure to any one issuer.

**ICE BofA 0-2 Year Duration BB-B U.S. High Yield Constrained Index** – This index measures the performance of ICE BofAML 0-2 years Duration BB-B U.S. High Yield Bond. It's all securities in the ICE BofAML U.S. High Yield Index rated BB1 through B3 and with a duration-to-worst less than two years, but caps issuer exposure at 2%.

**ICE BofA 3-Month U.S. Treasury Bill Index** – This index measures the performance of a single issue of an outstanding treasury bill which matures closest to, but not beyond, three months from the rebalancing date. The issue is purchased at the beginning of the month and held for a full month; at the end of the month that issue is sold and rolled into a newly selected issue.

**Morningstar Moderately Conservative Target Risk Total Return USD Index** – The Morningstar Target Risk Index family is designed to meet the needs of investors who would like to maintain a target level of equity exposure through a portfolio diversified across equities, bonds and inflation-hedged instruments. The Morningstar Moderately Conservative Target Risk Index seeks approximately 40% exposure to global equity markets.\*

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