August 2025

osaic

MARKET VIEW MONTHLY

Philip Blancato, Chief Market Strategist, Osaic

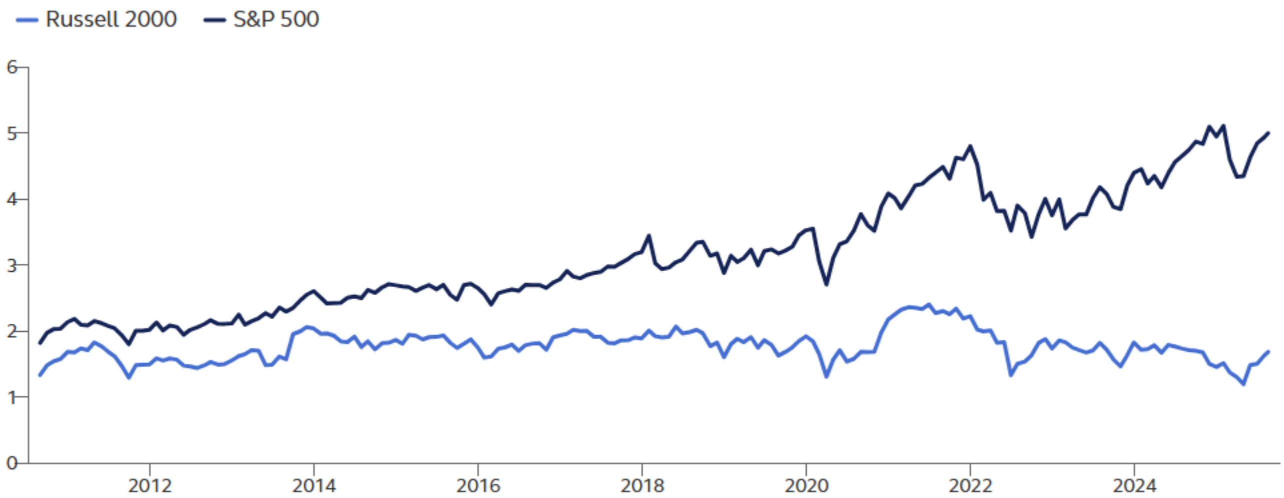
ECONOMIC REVIEW[1]

- U.S. nonfarm payrolls rose by just 73,000 in July, well below expectations of 106,000, with major downward revisions to May and June totaling -258,000, resulting in a net loss, including revisions, of 185,000 jobs.
  - The unemployment rate ticked up to 4.2% from 4.1% in line with expectations as both labor demand and supply have contracted in recent months. The rate itself remains unchanged from a year ago.
- ISM Manufacturing PMI declined to 48.0 in July from 49.0 the month prior, missing expectations, marking a fifth straight month of contraction, and representing the lowest reading since October 2024.
- The Consumer Price Index (CPI), a broad measure of inflation, rose roughly in line with expectations.
  - Headline CPI rose 0.2% in July, less than June's increase of 0.3%, but the annual rate held steady at 2.7%.
  - Core CPI, which excludes the volatile food and energy categories, came in slightly hotter than expected at 0.3% for the month, and is up 3.1% from a year ago. Both remain elevated relative to the 2% target.
- The Producer Price Index (PPI), a measure of inflation that pertains to price pressures affecting businesses, rose substantially and unexpectedly.
  - In rebounding from a flat reading in June, PPI rose 0.9% in July, significantly outpacing expectations of 0.2%, and raised concerns around the impact of tariffs and how producers are handling rising input costs.
- Retail sales, which provide a glimpse into the spending of American consumers, rose 0.5%, showing a continuation of the strong spending that has bolstered the economy in recent years.
  - The only measure of services spending, food and drink services, declined in the most recent report, but spending growth was broad elsewhere.
- The number of housing starts in July beat expectations and increased 5.2% month-over-month (MoM) to an annualized rate of 1.428 million, which marked the highest reading in five months.
- Existing home sales increased by 2.0% in July, rising above expectations to an annualized rate of 4.010 million.
  - The median price of an existing home fell MoM to $422,400 and is roughly unchanged over the last year.
- U.S. Gross Domestic Product (GDP) expanded at an annualized rate of 3.3% in Q2 2025, revised up from the initial 3.0% estimate. This marks a strong rebound from the -0.5% contraction recorded in Q1.
  - The upgrade was driven by stronger business investment and a record contribution from net exports.
- Headline Personal Consumption Expenditures (PCE) rose 0.2% in July and held steady at a 2.6% year-over-year (YoY), both matching estimates as softer goods prices offset higher services costs.
  - Core PCE, the Federal Reserve's (Fed) preferred inflation gauge, increased 0.3%, month-over-month, and accelerated to 2.9% YoY, the highest in five months and a sign of persistent underlying inflation pressures.

INSIGHT: In August, the U.S. economy continued a rebound from a negative Q1 GDP print and the market turmoil that ensued following initial 'Liberation Day' tariff announcements. Second-quarter GDP was revised higher to 3.3%, consumers continued to spend in excess of forecasts, and a number of trade deals were reached with key partners like the European Union, South Korea, and Japan, somewhat clarifying the new international trade environment (critical deals with China, Mexico, and Canada have yet to be settled). Financial markets moved higher across sectors, styles, regions, and asset classes as investors cheered the positive developments, but debate focused on stubborn inflation and a softening labor market. Chairman Powell's comments at the Fed's annual Jackson Hole Economic Symposium highlighted the crucial considerations and a potential policy shift: "the baseline outlook and shifting balance of risks may warrant adjusting our policy stance," in an effort to meet the central bank's dual mandate of balancing maximum employment and stable prices. Market participants took the comments as a near guarantee of an interest rate cut at the impending September FOMC meeting, pushing both stocks and bonds higher.

CHART OF THE MONTH: Large-cap and Small-cap Valuations[2]

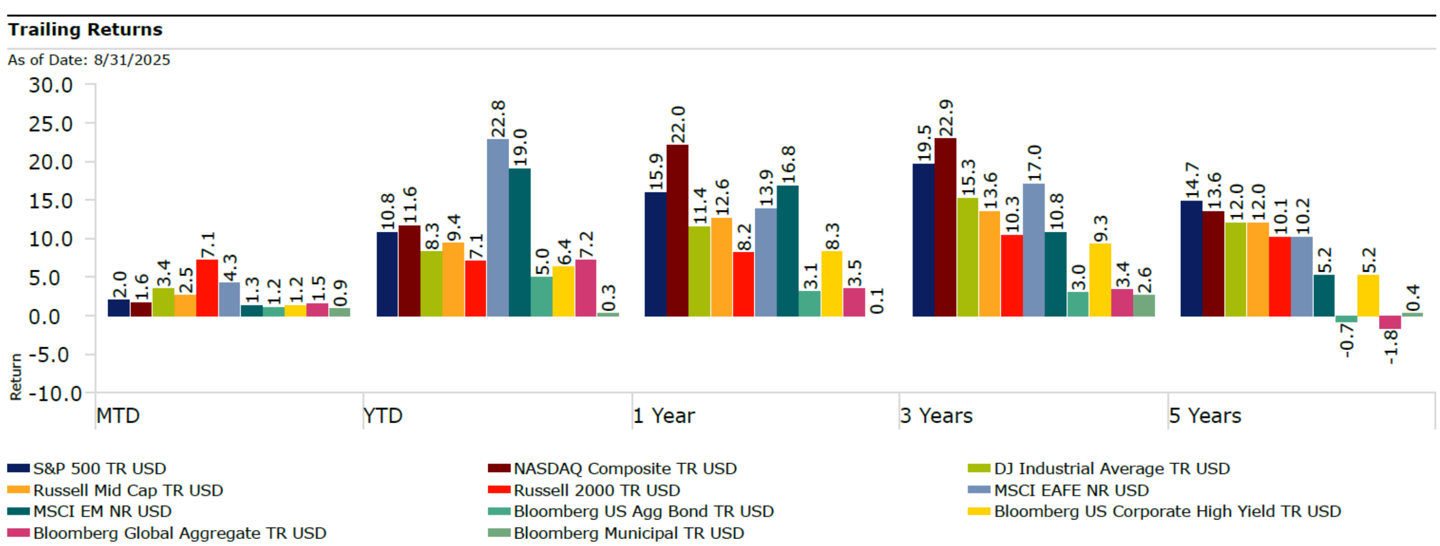
Price-to-book, August 2010–present



Source: Bloomberg, Principal Asset Management. Data as of August 18, 2025.

In August, the most notable outperformance came from a recently unloved segment of the market: small-cap stocks. The Russell 2000 index of small company stocks improved 7.14% last month alone, outpacing the next best performing asset class by nearly 3%. Despite the recent rally, valuations are still substantially cheaper for small-cap equities than for domestic large-cap stocks. As the chart above shows, the S&P 500 currently trades near 5x price-to-book while the Russell 2000 trades well below 2x. A healthy and growing economy is crucial for small-cap outperformance, and macroeconomic headwinds have held the asset class back of late. However, uncertainty around economic activity, tariff policy, and interest rates may soon shift from headwinds to tailwinds. Q2 GDP was recently revised higher to 3.3%, several important trade deals were settled with lower tariff rates than initially expected, and a preemptive rate cut aimed at stimulating growth is on the table for September with nearly 90% probability implied by futures markets. The time may be right to add small caps to client portfolios.

MARKET UPDATE[3]



Investments as of 8.31.2025	Trailing Returns MTD	YTD	1 YR	3 YR	5 YR	Equity Evaluations P/E Ratio	P/B Ratio
S&P 500	2.03%	10.79%	15.88%	19.54%	14.74%	26.84	4.89
NASDAQ	1.65%	11.60%	21.95%	22.94%	13.60%	31.56	6.88
Dow Jones Industrial Average	3.42%	8.30%	11.45%	15.27%	12.04%	22.40	4.77
Russell Mid-Cap	2.50%	9.45%	12.58%	13.60%	12.02%	22.04	2.84
Russell 2000 (Small Cap)	7.14%	7.06%	8.17%	10.28%	10.13%	17.51	1.85
MSCI EAFE (International)	4.26%	22.79%	13.87%	17.04%	10.15%	17.31	1.96
MSCI Emerging Markets	1.28%	19.02%	16.80%	10.82%	5.21%	14.69	1.90
Bloomberg Barclays US Agg Bond	1.20%	4.99%	3.14%	3.02%	-0.68%	—	—
Bloomberg Barclays High Yield Corp.	1.25%	6.35%	8.26%	9.30%	5.16%	—	—
Bloomberg Barclays Global Agg	1.45%	7.21%	3.47%	3.39%	-1.76%	—	—
Bloomberg Barclays Municipal	0.87%	0.32%	0.08%	2.59%	0.40%	—	—

MARKET REVIEW

Equities

- Domestic equity markets continued to climb higher in August as economic data remained resilient and a surprisingly strong earnings season powered stocks higher. The Dow Jones Industrial Average had a particularly strong month among the major large-cap indices, returning 3.42%. The S&P 500 and Nasdaq were also positive, gaining 2.03% and 1.65%, respectively, but trailed other segments of the market as investors faded some of the market-leading, mega-cap tech stocks, semiconductors, and growth stocks, generally. Marginally disappointing guidance from Nvidia, elevated valuations, and extreme concentration contributed to weaker performance from these typically high-flying sectors and stocks, limiting overall index performance. Instead, investors focused on some of the recently forgotten areas of the market, like small- and mid-caps. The Russell Mid-Cap index returned a respectable 2.50% in August, and small-caps led all major indices with a very robust 7.14% monthly return. Developed international markets resumed their march higher with a strong 4.26% return in August after a bit of a reprieve from the dramatic outperformance earlier this year.

Fixed Income

- Fixed income markets were also solidly positive in August. The Bloomberg Barclays Global Aggregate Index led major benchmarks with a 1.45% return on the month, but bonds were also positive domestically (1.20%) and across the credit spectrum (1.25%). Credit spreads remain extremely tight, well below long-term averages for both investment-grade and high-yield bonds, but largely due to solid credit fundamentals, strong corporate earnings, and resilient economic data. Municipal bonds finally registered a strongly positive month (0.87%), although this fixed income segment remains plagued by elevated issuance earlier this year and a steepening municipal yield curve that contributed to rising long rates. Chair Powell’s comments at the Federal Reserve’s annual Jackson Hole Economic Symposium, indicating a greater emphasis on the maximum employment element of its dual mandate, spiked expectations of an interest rate cut at the impending September FOMC meeting, supporting bonds across the fixed income landscape.

Economic Definitions

CPI (headline and core): Consumer prices (CPI) are a measure of prices paid by consumers for a market basket of consumer goods and services. The yearly (or monthly) growth rates represent the inflation rate.

Federal Reserve (Fed): The Federal Reserve System is the central banking system of the United States of America.

GDP: Gross domestic product (GDP) measures the final market value of all goods and services produced within a country. It is the most frequently used indicator of economic activity. The GDP by expenditure approach measures total final expenditures (at purchasers' prices), including exports less imports. This concept is adjusted for inflation.

ISM Manufacturing Index: PMI Surveys track sentiment among purchasing managers at manufacturing, construction and/or services firms. An overall sentiment index is generally calculated from the results of queries on production, orders, inventories, employment, prices, etc.

ISM Services Index: PMI Surveys track sentiment among purchasing managers at manufacturing, construction and/or services firms. An overall sentiment index is generally calculated from the results of queries on production, orders, inventories, employment, prices, etc. Target Audience: supply management professionals Sample Size: 300 individuals Date of Survey: through the month The Services Index is a composite index of four indicators with equal weights: Business Activity, New Orders, Employment and Supplier Deliveries. An index reading above 50% indicates an expansion and below 50% indicates a decline in the non-manufacturing economy. Whereas per Supplier Deliveries Index, above 50% indicates slower deliveries and below 50% indicates faster deliveries.

Nonfarm Payrolls: This indicator measures the number of employees on business payrolls. It is also sometimes referred to as establishment survey employment to distinguish it from the household survey measure of employment.

PCE (headline and core): PCE deflators (or personal consumption expenditure deflators) track overall price changes for goods and services purchased by consumers. Deflators are calculated by dividing the appropriate nominal series by the corresponding real series and multiplying by 100.

Producer Prices – PPI (headline and core): Producer prices (output) are a measure of the change in the price of goods as they leave their place of production (i.e., prices received by domestic producers for their outputs either on the domestic or foreign market).

Retail Sales: Retail sales (also referred to as retail trade) tracks the resale of new and used goods to the general public, for personal or household consumption. This concept is based on the value of goods sold.

Unemployment Rate: The unemployment rate tracks the number of unemployed persons as a percentage of the labor force (the total number of employed plus unemployed). These figures generally come from a household labor force survey.

Index Definitions

S&P 500: The S&P 500® is widely regarded as the best single 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.

NASDAQ: The NASDAQ Composite Index is a broad-based capitalization-weighted index of stocks in all three NASDAQ tiers: Global Select, Global Market and Capital Market. The index was developed with a base level of 100 as of February 5, 1971.

Dow Jones Industrial Average: The Dow Jones Industrial Average is a price-weighted average of 30 blue-chip stocks that are generally the leaders in their industry. It has been a widely followed indicator of the stock market since October 1, 1928.

Russell Mid-Cap: Russell Midcap Index measures the performance of the 800 smallest companies in the Russell 1000 Index, which represents approximately 25% of the total market capitalization of the Russell 1000 Index.

Russell 2000: The Russell 2000 Index is comprised of the smallest 2000 companies in the Russell 3000 Index, representing approximately 8% of the Russell 3000 total market capitalization. The real-time value is calculated with a base value of 135.00 as of December 31, 1986. The end-of-day value is calculated with a base value of 100.00 as of December 29, 1978.

MSCI EAFE: The MSCI EAFE Index is a free-float weighted equity index. The index was developed with a base value of 100 as of December 31, 1969. The MSCI EAFE region covers DM countries in Europe, Australasia, Israel, and the Far East.

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

Bloomberg Barclays US Agg Bond: The Bloomberg Barclays US Aggregate Bond Index 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 pass-throughs), ABS and CMBS (agency and non-agency).

Bloomberg Barclays High Yield Corp: The Bloomberg Barclays 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 Barclays EM country definition, are excluded.

Bloomberg Barclays Global Agg: The Bloomberg Barclays Global Aggregate Index is a flagship measure of global investment grade debt from twenty-four local currency markets. This multi-currency benchmark includes treasury, government-related, corporate and securitized fixed-rate bonds from both developed and emerging markets issuers.

Bloomberg Barclays Municipal Bond Index: The Bloomberg Barclays U.S. 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.

Disclosures

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[1] Data from Bloomberg as of 8.31.2025

[2] Small cap equities: What could fuel a sustainable rally? | Principal Asset Management

[3] Data from Morningstar as of 8.31.2025