

City of Scottsdale

Innovest Executive Summary

For the Quarter Ending June 30, 2025

1. Review Items

- Fee Review update scheduled for the second quarter review.
- Share Class Review update scheduled for the second quarter review.

2. Upcoming Items

- Investment Policy Statement review scheduled for the third quarter review.
- Fiduciary Education scheduled for the third quarter review.

3. Market Update and Outlook (through June 30, 2025)

- After a tumultuous start to the quarter following President Trump's tariff announcements, domestic equities rebounded strongly, ending the quarter with a gain of nearly 11% for the S&P 500. Mid-caps and small-caps behaved similarly, both gaining approximately 8.5% as measured by the Russell Mid-Cap and Russell 2000 Indices. International equities performed best of all, with the MSCI EAFE Index adding 11.8% to its strong first quarter performance to reach nearly a 20% gain for the first half of 2025. It is important to note that the majority of this performance can be attributed to the weakened dollar. In local currency, returns were only 4.8% for the quarter and 7.8% for the first half of the year. Nevertheless, U.S. investors profited from global diversification, and valuations outside of the U.S. remain attractive on a relative basis. The Eurozone's price-to-earnings ratio remains close to its 20-year average at 14.3x. In contrast, U.S. equities trade at over 21x earnings, which is significantly above their 20-year average.
- U.S. tariff policy was arguably the most prominent catalyst for equity returns this quarter. As of the end of June, tariffs on foreign goods had settled at an average effective rate of about 15%. Although amounting to much less than the nearly 30% effective tariff rate announced in early April, the current rate still far outstrips the sub 5% levels that the U.S. has employed since the 1970s. The excess inflation that tariffs were expected to produce has yet to fully materialize in the Consumer Price Index, which rose only 0.3% in the month of June, putting annual inflation at 2.7%. Although this is lower than many economists expected, it may reflect only a temporary reprieve as inventory stock piling and paused manufacturing likely dampened the initial impact of tariffs. Much depends on the outcome of ongoing trade negotiations, but most economists consider it unlikely that the mammoth tariffs currently on "pause" will become permanent policy.
- In the second quarter, the Federal Reserve continued to hold interest rates steady, citing a foggy outlook for inflation and the as-yet unrealized impacts of tariffs. The nineteen members of the committee were nearly evenly split on their expectations for rate cuts this year: nine members expected one or zero rate cuts, while the remaining ten predicted two or three. Adding to the complexity, inflation and foreign policy have weighed on the dollar. The dollar has suffered its worst start to the year since 1973, losing 10.7% of its value relative to foreign currencies in the last six months. Despite currency volatility, core fixed income posted a modest gain of 1.2% in the second quarter, as measured by the Bloomberg U.S. Aggregate Bond Index, bringing year-to-date performance to just over 4%. The U.S. Federal Reserve has followed a more conservative rate cutting cycle than other central banks, which has helped to limit the decline of the dollar and may bolster fixed income returns in the near term.
- The second half of the year promises to be eventful. More trade agreements will be finalized, the impact of tariffs on inflation will be more fully understood, and the implications of President Trump's One Big Beautiful Bill will be further analyzed. Before such an uncertain horizon, disciplined investing—anchored in diversification and a commitment to one's time horizon—will be key to weathering future volatility.



4. Investment Results

- Total Plan Assets for the quarter ending June 30, 2025:
 - City of Scottsdale 457(b) Plan: *\$237,494,794*
 - City of Scottsdale PEHP Plan: *\$15,031,729*
- Quarterly Strongest Performers by Individual Strategy:
 - Emerald Small Cap Growth Fund: *20.28%*
 - Harbor Capital Appreciation Fund: *19.59%*
- Quarterly Weakest Performers by Individual Strategy:
 - Nuveen Real Estate Securities: *-1.31%*
 - Scottsdale NW Fixed Account: *0.53%*

5. Manager Updates

- JP Morgan Mid-Cap Growth Fund has a new minor concern in the people category. Daniel Bloomgarden no longer serves as comanager and analyst on this strategy effective May 2025, as he transitions to a new role at JPM. He is succeeded by Michael Stein, a seasoned analyst who has been with the small- and mid-cap growth team since 2014. Stein has worked closely with lead manager Felise Agranoff throughout his tenure and now steps into the comanager role alongside her. Innovest will continue to monitor this team transition.
- Harbor Capital Small-Cap Growth Fund has a new minor concern in the people category. Westfield Capital, the sub-advisor on this strategy, has experienced recent turnover with the exits of Ethan Meyers and analyst Kevin Shin. Despite this, the 16-member team remains deep and collaborative. Lead manager Will Muggia continues to steer the strategy with a consistent, valuation-conscious growth approach. Innovest will continue to monitor this team transition.

