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GENTER CAPITAL MANAGEMENT

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Introduction

Those who play competitive sports know that when you play "not to lose," you lose. As Red Sanders, the legendary UCLA football coach put it, "Winning is not everything, it is the only thing." Every great coach will tell you that winning requires single-minded commitment, even self-abandonment, to the cause of victory itself. When you try "not to lose," you tighten up, play scared, and, as often as not, choke it away.

But "playing to win," in this sense at least, was not in the minds of the American colonists 250 years ago. They were aiming at "not losing." The Americans knew their "Glorious Cause" could scarcely bear the full brunt of British military force, but they did hope to outlast them. At some point, they reasoned, the British authorities would calculate that the costs of staying in America were greater than the costs of leaving.

Somehow, over the eight years of the Revolutionary War, the Continental Army—plagued by short enlistments, desertions, and diseases—hung in there. Despite some close calls, it did not implode. George Washington's men would evacuate cities, and retreat from battlegrounds, because the primary goal was to keep the British from flanking and destroying our fighting force. There were notable, morale-boosting, military successes, of course, and invaluable assistance from foreign powers like France, Spain, and Holland, seeking to make mischief against their British adversaries, but for Americans, the Revolutionary War was largely a game of cat and mouse.

Ironically enough, 250 years later, we are on the other side of this equation. It has happened a few times in recent memory—Vietnam, Afghanistan, and now, apparently, Iran—where our adversary has "won" by "not losing." In one sense, it is vexing, but in another, it is instructive.

For investors, playing "not to lose" can be defined as staying measured, avoiding traps, and maintaining an open and creative mind to opportunity. This is clearly a more rational form of risk management than going for broke, and though it is an approach which does not work well in sports, it successfully taps the growth inherent to American capitalism.

Two hundred fifty years ago, the Founders of our country were less interested in "owning" the British than in being left alone by them. As it turned out, in their pursuit of self-government, the Founders laid the foundation that would reinvent the world. It is always important to revisit the principles which make our country great, but it is also helpful, occasionally, to think about the strategy which enabled our country in the first place—even when that strategy seems to contradict everything we know about "winning" and "losing."

Review and Outlook

The economy has been rolling along, with animal spirits being released through less regulation, lower taxes, and fiscal and monetary support. There have been increased capital expenditures from reshoring incentives, which appear to be playing a positive role in growth. The restrictive tariff and immigration policies have not led to any derailment, although such things, like most things, are judged in the fullness of time.

Recession indicators have eased broadly. Jobless claims are no longer flashing a warning, and the Sahm Rule, at 0.10%, is well below its 0.50% recession threshold. The Leading Economic Indicators have been below zero for 45 months, the longest ever, but these have been wrong and are now trending back toward zero. Recession expectations have fallen over the past year, as artificial intelligence, data centers, and military spending offset consumer weakness.

American consumers retain their "K" shape. The lower three quartiles have little capacity to increase spending, as credit card delinquencies keep worsening. The top quartile, in contrast, and especially the highest echelons of the top quartile, have benefited greatly from the appreciation of capital assets. It is unclear how large an equity pullback would be required to make a dent in the "wealth effect."

While the news changes from day to day, the market has been looking past the ongoing Iran crisis and is pricing its resolution. President Trump has helped contain the price of oil by jawboning the market that stabilization was around the corner, though this may have resulted in some reduction of leverage with the Iranians. The price of oil fell sharply from its Brent peak of $118.35 at the end of the first quarter to $72.92 at the end of the second. The move is reinforced by fundamentals, such as oversupply prior to the conflict, reduced macroeconomic reliance on crude generally, and the exit of the United Arab Emirates from OPEC, which undercuts the cartel's efforts to maintain production quotas.

Inflation remains well over the Fed's 2% target, but we think headline CPI should move lower in the coming months as the Iranian crisis eventually gets sorted out. Our larger worry is core PCE, which measures consumer prices (excluding food and fuel costs). Core PCE is regarded as a more reliable indicator of price stability (or instability, as the case may be), and is the bogey used by the Federal Reserve to measure the effectiveness of its inflation-fighting efforts. The measure is currently at 3.4%, its highest level in almost three years, and unlike headline CPI, core inflation has no obvious driver to lower prices.

On the employment front, continuing jobless claims, an important indicator, remain historically low and no longer flashes a warning sign. Meanwhile, the payroll jobs number bounced around, but has moved higher on a three-month annualized basis, than when entering 2026. The "slow to hire and slow to fire" dynamic remains in play, as firms are neither hiring new workers nor shedding their current workers.

The Equity Report below will provide further thoughts on the inflation and employment picture. On balance, this economy has proven resilient in the face of many challenges. Growth has increased confidence, and investors see it in leveraged buyouts and increased M&A activity. Conventional wisdom has been defied more than once, and with the hyper-scaling of AI, we are rushing pell-mell into a future which seems as functionally different as it is uncertain.

All that said, we do see some warning signs, which will be discussed more fully in the Equity Report. Still, and notwithstanding the histrionics which seem to accompany every national endeavor these days, we think the American economy is in decent shape. While predicting is always difficult, especially about the future, we would note that our country has a good record of landing on its feet.

Equity Report

U.S. equities advanced strongly during the quarter, supported by resilient corporate earnings, a still-expanding economy, and sustained investor enthusiasm for artificial intelligence, automation, and productivity-enhancing technologies. Although the market experienced periodic volatility tied to interest rate expectations, inflation data, and geopolitical developments, the broader trend has remained constructive.

After a slightly negative start in the first quarter, the S&P 500 produced double-digit returns in the second quarter, with a year-to-date total return close to 10%. Investors have returned to favoring growth companies tied to technology, semiconductors, cloud infrastructure, and AI-related capital spending.

The rebound has been particularly notable, given the uneven start to the year. At that point, investors worried that inflation might remain too persistent for the Federal Reserve to ease policy as quickly as hoped. Since then, investors have become more comfortable with the idea that economic growth can remain positive even as inflation gradually moderates. This narrative has helped support equity valuations, particularly for companies with durable earnings growth and strong balance sheets.

Sector performance, however, remains uneven. While Technology took a breather in the first quarter, it was the strongest performer in the second quarter—and the clear leader year-to-date. The sector remains supported by strong demand for semiconductors, data-center infrastructure, enterprise software, and AI computing capacity. The market continues to reward companies which can translate AI investment into revenue growth, margin expansion, or improved competitive positioning. While valuations in parts of the Technology sector are elevated, earnings momentum has remained strong enough to sustain investor interest.

Despite losing some momentum in the second quarter, Energy has also been among the strongest sectors year-to-date, helped by elevated commodity prices and ongoing attention to global supply risks. Energy companies have generally benefited from disciplined capital spending, strong cash generation, and shareholder-return programs. Materials and Industrials have also performed well, reflecting investor confidence that the economy remains firm enough to support demand for capital goods, infrastructure, and manufacturing-related activity.

Financials have shown improving momentum during the quarter, particularly as yield pressures have moderated and investors appear to be more comfortable with credit conditions. Banks and other financial institutions remain sensitive to interest rate expectations and the health of the consumer, but the sector has benefited from a more constructive outlook for lending, capital markets, and net interest margins. A broadening rally that includes Financials is often viewed positively because it suggests confidence in the underlying economy.

On the other side of the ledger, more defensive sectors have generally lagged. Consumer Staples and Utilities have underperformed as investors have favored growth and cyclical exposure over income-oriented, defensive businesses. Health Care has been mixed, with managed care and select healthcare service companies recovering at times. The broader Health Care sector has faced headwinds from policy uncertainty, pricing pressure, and uneven earnings trends. Communication Services has also been uneven, as investors have differentiated companies with strong advertising, subscription, and AI-related opportunities from companies facing slower growth or margin pressure.

The most important economic data released by the Bureau of Labor Statistics during the quarter centered on employment and inflation. These reports continue to shape expectations for Federal Reserve policy, bond yields and equity valuations.

The Employment Situation reports showed that non-farm payroll employment increased steadily over the past several months after an extended period where aggregate job growth appeared to stagnate, while the unemployment rate remained unchanged at 4.3%. Job gains were concentrated in areas such as health care, transportation and warehousing, and retail trade.

These more recent monthly reports reinforced the view that the labor market is cooling but not collapsing. For equity investors, that distinction matters. A labor market that is too strong can keep wage pressure and inflation elevated, delaying potential rate cuts. A labor market that weakens too quickly can raise recession risk and pressure earnings expectations. The current environment appears to fall between those extremes: slower hiring, but continued job creation.

The BLS inflation data was also highly consequential this quarter. On a year-over-year basis, headline CPI accelerated and core inflation, excluding food and energy, remained above the Federal Reserve's preferred comfort zone. The market's reaction to inflation data remains highly sensitive because even small deviations from expectations can move Treasury yields and equity valuations. Higher inflation tends to pressure price-to-earnings multiples by increasing discounts.

Producer-price data adds another layer of complexity. The April Producer Price Index for final demand increased 1.4% on a seasonally adjusted basis, the largest monthly increase since March 2022. Over the prior 12 months, final demand prices rose 6.0%. The increase was driven by both services and goods, including a notable contribution from energy. This matters because producer prices can feed into corporate margins and consumer prices. If companies are unable to pass higher input costs through to customers, margins may compress. If they can pass costs through, inflation may remain stickier than the Federal Reserve would prefer.

Taken together, the BLS data points to an economy that is still expanding but facing crosscurrents. Employment remains healthy enough to support household income and consumer spending, but the pace of job creation is slowing. Inflation has improved from prior extremes, but the latest CPI and PPI figures show that price pressure has not fully disappeared. This combination has created a market environment in which equity investors are trying to balance optimism about growth with caution about monetary policy and the prospect of higher rates.

Interest rates remain a central variable. When inflation data is hotter than expected, Treasury yields tend to rise, which can pressure both rate-sensitive sectors and long-duration growth stocks. When labor data show moderation, yields may decline, supporting equities by improving the outlook for future monetary policy. This push-and-pull has defined much of the quarter's market action. Investors are not simply asking whether the economy is strong or weak; they are asking whether the economy is strong enough to sustain earnings but cool enough to allow inflation to decline.

Equity markets have responded by rewarding companies with visible earnings growth, pricing power, and strong balance sheets. Businesses that can grow revenue without relying heavily on cheap financing have been favored. Companies with high debt levels, weak margins, or limited pricing power have faced more scrutiny. This is a healthy form of market discipline and underscores the importance of selectivity.

From a portfolio perspective, the current environment favors balance. Growth companies remain attractive where earnings are durable and valuations are supported by real cash flow. At the same time, the broadening of market leadership creates opportunities in Financials, Industrials, Energy, and select areas of Health Care. Defensive sectors may also regain appeal if economic data weakens more meaningfully or if investors begin to prioritize dividend stability and lower volatility.

We continue to believe that quality remains the most important investment attribute. Companies with strong balance sheets, recurring revenue, disciplined capital allocation, and sustainable competitive advantages are best positioned to navigate a market shaped by changing interest-rate expectations and uneven economic data. While short-term volatility is inevitable, especially around inflation and employment releases, long-term equity returns are ultimately driven by earnings growth, cash flow generation, and valuation discipline.

Looking ahead, investors will remain focused on three questions. First, will inflation continue to trend lower, or will recent price pressure prove more persistent? Second, will the labor market continue to cool gradually, or will slowing job growth become a more serious concern? Third, can corporate earnings continue to expand enough to justify current valuations? The answers to these questions will likely determine whether the market rally continues to broaden or becomes more volatile.

Despite these uncertainties, the backdrop remains constructive. Corporate America continues to adapt, innovate, and invest. Artificial intelligence and automation are creating new opportunities across industries, not just within technology. The consumer remains resilient, albeit more selective. Businesses are still hiring, though at a slower pace. Inflation remains the primary challenge, but the economy has absorbed higher rates better than many expected.

At the same time, we caution that investors should recognize that optimism has become increasingly widespread. One area receiving our close attention is the growing use of leverage throughout the financial markets. Margin borrowing has increased, alongside rising equity prices, while options activity—particularly among retail investors—has reached historically elevated levels. Short-dated options leveraged exchange-traded products and concentrated positioning in momentum-driven themes have contributed to increasingly speculative market behavior.

Periods of abundant liquidity and rising investor confidence often encourage greater risk-taking. While leverage can amplify returns during advancing markets, it can also accelerate volatility should sentiment suddenly reverse.

Valuations also deserve continued attention. Although earnings expectations have improved, many of the market's highest-growth companies already discount considerable future success. Any disappointment in earnings growth, inflation progress, or monetary policy would produce heightened volatility, particularly among stocks with elevated expectations.

As always, our approach remains grounded in disciplined long-term investing. We seek to own high-quality businesses that can compound value in different market environments. Periods of volatility can create opportunities, but they also reinforce the importance of patience, diversification, and a focus on fundamentals. While markets will continue to react to each new economic release, we believe investors are best served by playing the long-game, retaining perspective, and emphasizing companies with the financial strength and competitive positioning to succeed over full market cycles.

Fixed Income Report

The second quarter was characterized by economic resiliency, some labor market strength, and a notable shift in monetary landscape as Kevin Warsh was installed as Fed Chair. Markets repriced interest rate expectations while Warsh asserted his independence from the Trump administration and set a "hawkish tone"—or at least a "price stability" tone, which is not necessarily the same thing.

In terms of headwinds, fiscal deficits remain elevated (~5% of GDP), while federal borrowing needs are likely to stay high over the medium-term. Additionally, the $10 trillion in Treasury debt maturing in 2026 will require significant refinancing operations. If investor demand softens, these supply conditions could place upward pressure on long-term yields.

Still, we think higher Treasury yields present a good investment opportunity, since headline inflation, dependent upon energy costs, should fall, even as other categories maintain a disinflationary trend. We would also note that although employment growth has been decent, it is probably not enough to stoke wage inflation.

On the credit side, private credit concerns linger, though not "front and center" like last quarter. Business development companies were able to raise debt in the primary market without large new issue concessions, and that helped ease investor fears about the solvency of private credit.

New issuance in the investment grade market this year has been approximately $1.2 trillion, putting it on track to be the busiest issuance year since 2020. New issue concessions have remained tight, underscoring the strong demand for investment grade credit.

Meanwhile, corporate balance sheets are broadly healthy. Taken as an aggregate, the trimmed mean investment-grade Net Debt/EBITDA ratio has held steady in the range of 2.4x to 2.6x over the past twelve quarters. Interest coverage is also steady at around 6.4x. Corporate profitability remains stable, and credit rating upgrades, at least for investment grade credit, have far outpaced downgrades.

While fundamentals support current spread levels, valuations are still rich historically, leaving limited room for additional spread compression. The key risks we are monitoring are any deterioration in corporate fundamentals, continued geopolitical tensions, and inflation trending higher.

On the tax-exempt side, you may recall from our last market letter that March was an especially poor-performing month. Like the stock market, "buying the dip" also applies to the municipal bond market. In April we saw investor flows "lock in" the yield after March's weakness, and with our active management approach, we did much the same.

A bull flattener was in full swing for the muni market, with strong quarterly returns coming in the 15 to 30-year range. The long end of our modified barbell approach helped provide excess returns for our flagship intermediate product. In terms of future yield and relative value opportunities, the new issue market continues to be a major thrust for all our tax-exempt strategies.

Taking both tailwinds and headwinds into account, we have moved our strategies to a moderately long duration orientation relative to their specific benchmarks, especially on the taxable side. This positioning reflects our thinking that inflation has peaked for this cycle and that growth is unlikely to push meaningfully higher in the short term. As a rule, these two variables, growth and inflation, steer interest rates directionally. While we are alert to the prospect that growth and inflation can rekindle in a manner that ignites rates higher, we think the current likelihood is inflation curtailing and growth muting a bit.

Federal Reserve Report

These have been busy months at the Fed, from Jerome Powell's nearly unprecedented decision to remain on the Board, to Kevin Warsh's ascent to the chair, to his first FOMC meeting and its aftermath, to the Supreme Court's resolution of the Lisa Cook case. If we were to summarize the current landscape in a sentence: "There is a new sheriff in town and change is in the air."

In the Trump v. Cook case, the Supreme Court prevented President Trump's "for cause" dismissal of Federal Reserve Governor Cook. While the Court voted in her favor, by a surprisingly narrow margin (5-4, rather than the expected 6-3 or even 7-2), the decision points to a path that the Trump administration can take to adjudicate their allegations that Cook engaged in fraud while filing a mortgage application in 2021. In other words, Governor Cook is not out of the woods yet.

As for Jerome Powell, the former chair, he broke 79 years of precedent by remaining on the Federal Reserve Board after being replaced as its chair. Powell has argued that the criminal investigation into cost overruns at the Fed's headquarters building is politically motivated—and said that he would not leave until the Department of Justice probe is "well and truly over, with transparency and finality." The DOJ has dropped its investigation, and an inspector general has picked it up, as Powell requested. The results should be known by the end of the summer. To be determined is whether Powell will leave at that time.

But the biggest news at the Federal Reserve this past quarter has been the rise of Kevin Warsh to its chair. Warsh, who served as a governor for five years, has sharply criticized the Fed since he resigned in 2011. He has proposed substantial reforms, even to the extent of "regime change." One can only imagine the heated conversations behind closed doors as Warsh makes his pitch to his new colleagues.

The themes of the Warsh proposals seem to converge around taking the Fed back to where it was under Alan Greenspan, who passed away in June. Warsh wants reduced guidance, formalized by Benjamin Bernanke in the aftermath of the Global Financial Crisis, and reduced data dependency, which was the chief characteristic of the Powell tenure. He prefers policy derived from forward projections, basically using supply-side precepts. His singular focus will be "price stability," which should not be confused with inflation-fighting zeal. Rather, and like Greenspan, Warsh thinks that if prices remain stable, then the market itself will optimally handle growth and employment.

While Kevin Warsh has a large "wish list," we note with particular interest his formation of five task forces. These reflect his areas of focus and where he needs to build consensus. The task forces are expected to report back by year end and will presumably anchor Warsh's internal reform discussions within the Fed.

Chairman Warsh's Five Task Forces

Task Force	Purpose
Communication	Examine the ways that the Fed communicates. Define the hidden costs of guidance. Warsh wants a more circumspect Fed.
Balance Sheet Operations	Understand the consequences of balance sheet operations. Warsh has called the large balance sheet "fiscal policy by other means."
Data Sources	Evaluate the merit of various data metrics. Warsh wants to revisit data gathering methodologies, as well as consider new datasets, where "actionable" data is better than "echoes of history."
Productivity	Does AI point to a new wave in productivity and employment? Warsh thinks it does, and that it may enable lower rates despite high growth. Other Fed officials see AI as inflationary.
Inflation Fighting Framework	Warsh regards price stability as the primary duty of central banks. Look for renewed focus on inflation expectations. The 2% target will remain intact, but does he intend to replace Core PCE (now at 3.4%) with the Dallas Trimmed Mean (2.4%)? That would be a major reset!

In terms of the current policy situation, if inflation crests and exhibits signs of receding, then that will make a big difference to policymakers. Most Fed officials would agree that raising rates into declining inflation is risky policymaking. At the same time, higher inflation prints create pressure within the Fed among already-antsy officials. The June core PCE number will be released just before the next FOMC meeting later this month and will likely play a big role in determining the cadence and tone coming out of that meeting.

At a recent symposium in Europe, Kevin Warsh argued that inflation expectations have come down since he began as chair, as indeed they have. Whether measured as the difference between the Ten Year Note and the Ten Year TIPS rate, or as the 5-10 year University of Michigan index, the reduction of long-term inflation expectations over the past month or two has been impressive.

Warsh is probably hoping that the balance of the year will be quiet in terms of policy, which makes it easier to be loud in terms of managing reform. But that will depend on the data. And in this sense, even if he looks at different data elements, and analyzes those elements in a different manner, he will be stuck, like Powell, Yellen, Bernanke, and every Fed Chair prior to him, with what the data is telling him—and the rest of us.

Conclusion

Coach Sanders, referring to his cross-town rival, said that "Beating USC is not life and death—it is more than that." Competition has "the thrill of victory and the agony of defeat," and to such an extent that we forget about competition in its extended, more open-ended form. In that version of competition—the real-world version—opponents are always "voting," glory is fleeting, and yesterday's "winners" can become today's "losers."

For the early Americans, securing the Revolution did not mean that threats subsided. Quite the opposite, the young republic was besieged on all sides. Our former occupiers, the British, continued to make trouble at the frontiers of our new country: inhibiting our western expansion, blockading our coastline, seizing our sailors, and undermining our diplomatic efforts.

Finally, fed up, and surmising that Great Britain was bogged down fighting Napoleon, the United States invaded British Canada. The War of 1812 created some more harrowing moments for the young republic, including the sacking of our new capital, Washington City. After the successful resolution of this "Second War of Independence," in 1815, Americans grew euphoric and entered what is now called "the Era of Good Feelings." This was a period marked by a lack of partisanship, widespread pride in our democratic republic, and a high level of trust between Americans.

Two hundred years ago, in 1826, as the 50th celebration of our country's Founding approached, Thomas Jefferson was invited to Washington to celebrate the occasion. Jefferson, who was ailing, declined, but in sending his regrets, noted with satisfaction that the younger generation continued "to approve the choice we made," and, looking to the wider world, that "all eyes are opened, or opening, to the rights of man."

It was a gratifying time for Americans, arguably one of the two or three high marks of our civic heritage. Our young country was vigorous and dynamic. We were masters of our own house. And the people of the world were looking to the United States as a living alternative to the despotic realities they were enduring. But all this was achieved, we should remember, because we lived to fight another day. We managed to win, decisively, by not losing.

Playing "not to lose" may not work well on athletic fields of competition, but it is often the best strategy in real life. At Genter Capital, we think it is usually the best approach for managing financial investments. We may live in an "all or nothing" era, where gambling is ubiquitous and actively encouraged, but we also have the freedom to find other, more rational, ways to advance and maximize our interests.