Dodge & Cox®

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ON-DEMAND AUDIO TRANSCRIPT

2025 Semi-Annual Fixed Income Review

Ryan: Thanks for joining the Dodge & Cox Semi-Annual Fixed Income Audiocast. I'm Ryan Utsumi, Client Portfolio Manager and Head of Fixed Income Client Service at Dodge & Cox. I'm joined by Lucy Johns, our Director of Fixed Income and U.S. and Global Fixed Income Investment Committee member. Thanks for joining today, Lucy.

Lucy: Happy to be here.

Ryan: Over the next 25 minutes or so, we'll provide our thoughts on the market backdrop and share our perspective on year-to-date performance, performance attribution, and portfolio structure for the Income Fund and the Global Bond Fund. So, why don't we dive right into our first question. Lucy, how is the team approaching the uncertainty and volatility in this environment?

Lucy: Well, volatility creates opportunity for active investors, so I'd say we're embracing it. Times like April are energizing for the team. These are times we get together more often, we make more portfolio decisions for the long run, and often these are great entry points to set us up as a long-term investor.

I'd say that there's a lot of headlines these days, so it's challenging, and it can feel noisy at times, but investment focus is a key characteristic of Dodge & Cox . It's really our jobs to help filter through all that noise, to understand what's most relevant for us as investors and our clients, and to come up with a probabilistic range of scenarios.

We're not top-down macro investors that are going to come up with one scenario that we know is going to happen, but we can come up with what we think is a reasonable range and use that as a baseline to focus on what we do best, which is fundamental research, bottom-up security selection, valuation discipline, and staying focused on the long term.

Ryan: Really the hallmarks of Dodge & Cox. There's been no shortage of noise in the markets over the last six months. In fact, with tariff announcements, fiscal policy, geopolitical developments, and concerns around economic growth, there's been plenty of movement in the financial markets overall—and more specifically in the fixed income markets.

As an example, we've seen the 10-year [U.S.] Treasury in the United States trade within an 80 basis point range. From a credit perspective, we've started and ended the time period near historic tights, but you'll all recall that in April, spreads quickly widened out to more historical normal averages before retracing and again finishing June 30 near a historic tight.[1]

As we think about the U.S. dollar, we've seen weakness there as it's retraced about 7.5%, giving back some of the gains that it made over the fourth quarter of 2024. What elements of the market backdrop, Lucy, would you highlight?

Lucy: Yeah, in addition to what you provided, which was a great recap, I'd also mention within the rates market, the change in the shape of the yield curve. We've got a chart on the upper left of the page that shows the yield curve shape over time. We've seen a dramatic steepening of the yield curve over the last year and year-to-date [period ended June 30] where the long end of the curve has not moved much—it's stayed anchored—but the front end of the curve with the Fed cuts and pricing in of future rate cuts has really tightened. Even though rates have declined, it hasn't been even across the curve.

The other thing I'd mention is if we sort of zoom out and think globally—and we've got some statistics here on the bottom of the page in addition to the [U.S.] dollar moves that you've mentioned—we've continued to see real differences and activity in markets across the globe. In fixed income markets in general, rates have declined, but as you see on the bottom left of the page, there's real variation with some very large moves in places like Brazil and South Africa. [There were] also moves in some of the developed markets. So it's been an exciting time for non-U.S. investments. We'll talk more about that in the Global Bond Fund section, but overall, really a positive environment for fixed income where rates are stable to declining and, as you mentioned, credit is doing quite well.

Ryan: With that backdrop, why don't we jump into the Income Fund? Performance continues to be strong not only for the period we're discussing today, but for longer periods of time, which match our three- to five-year investment time horizon.[2]

Through the first half of 2025, the Fund returned 4.3%, driven by attractive starting yields and falling rates. On a relative basis, the Fund outperformed the Bloomberg U.S. Aggregate [Bond Index] by 30 basis points, and each leg of the attribution stool—security selection, asset allocation, and yield curve effect—contributed positively to relative returns.

Within security selection, two large and long-standing holdings—Pemex, the national oil company of Mexico, and Charter Communications, the cable company—drove outperformance.[3] Were there notable updates to these companies that led to their strong performance?

Lucy: Yes, in both cases there were idiosyncratic events over recent time periods that led to strong performance within them.

For the case of Pemex, it continues to have a challenging credit profile with very high debt levels, questionable governance, and [a] challenging operating environment. But the valuation has continued to stay high—the yield approaches 10%, which there's not a lot of things available at that yield these days. But it's continued to be a very strategic asset for the government of Mexico. It's 100% owned, the government has repeatedly in the past stepped forward to support Pemex and its debt load and financial profile, and more recently, the President [of Mexico] announced that perhaps a more comprehensive or larger plan would be forthcoming. Bonds traded well in expectation of that news.

Moving on to Charter—Charter is in the competitive cable sector. We've liked it for a long time given its stable cash flows [and] given its scale. It has had a higher debt level than some of its peers, which is why it's tended to trade a little bit more cheaply, which we like. But one thing that happened recently is that they made an announcement that they would be acquiring Cox, another smaller cable provider—actually another holding of ours, so impacts that as well. But alongside this deal, the management of Charter indicated that they would be reducing their leverage target—so managing the company with a lower debt level. As a credit holder, that's great news for us and did result in a decline in those spreads as well.

Both of these are great examples of security selection and [our] fundamental, deep-research approach and how that can play out over our long-time horizon.

Ryan: That's right. In terms of the Fund's sector exposure—now turning to how we're positioned—I think if we think about the most notable changes over the year-to-date time period, listeners will see that Credit has increased over the course of the last six months and correspondingly, we've seen a reduction to U.S. Treasuries. To put some numbers behind that, the Credit [sector] exposure has increased by 3.4%, with additions following the general themes of higher-quality issuers and shorter-dated bonds.

That said, the exposure to [the] Credit [sector] continues to be at the lower end of the range that we've seen historically within the Income Fund: 34% as of June 30. That makes sense given the historically tight credit spread environment that we find ourselves in.

So, thinking about that credit spread environment, how would you frame our approach to credit given the paltry spread levels?

Lucy: In this environment, we're doing what we always do, which is focus on bottom-up security selection and maintaining our valuation discipline.

Given that spread levels are priced for perfection, there's not a lot of bargain shopping available, and so there's not a lot of big exciting opportunistic things that we're doing. That being said, we're happy to focus on high-quality staples in this market, and we found some of those year to date [as of June 30], as you mentioned—enough to move the credit weight up a few percent. Some of those adds occurred in that volatile April timeframe.

If you look at the page here on the right-hand side, you see that there's about nine credits that we've added to in a material way. Six of them are new names so that reflects that we're finding new ideas. Many of these issues we bought through a primary or new issue process. The bond market has been plenty busy this year. Some of those names include Mars, Synopsys, and Japan Tobacco—so different types of industries and each of these investments has its own sort of unique investment thesis.

As you indicated, we're focusing on short and intermediate holdings—often three, five, [and] seven years is the type of tenor that we've been buying recently. That's because when you invest there, you have less price risk. If we do see a broad widening of spreads in a risk-off environment, we'll have more price protection in this part of the credit curve.

Ryan: I think it's really interesting. We take a look at what you've mentioned about Pemex and Charter, then we talk about the new-to-the-portfolio issuers that we've added over the course of the last six months. It really emphasizes the security-by-security approach and individual bond-by-bond selection, and that's reflected in the security selection component of the attribution that we've looked at previously.

If we pull up a level, the aggregation of our security-by-security selection has left us with a unique positioning versus the Index. Can you walk us through some of those differentiations?

Lucy: Absolutely. The chart on this page on the right-hand side does a good job of framing up some of these dimensions of how we look versus the broader credit markets. It is quite unique.

Notably, security selection really highlights itself in just the fact that we own 63 names—individually picked and vetted very carefully through our process—versus over 1,000 in the benchmark. So, we really are picking our spots.

Then, in terms of some of the characteristics of what we hold, as I just mentioned, to reflect that we're buying and focusing and finding more value in shorter-duration credit, if you look at the third row—duration—you see that our average is about four years versus close to seven for the benchmark. So, a different amount of price risk.

Then, at the same time that we're reducing risk there, we're maintaining yield or spread in the portfolio. If you look at the row above that—OAS (option-adjusted spread) or spread—we have a significant advantage over that of the broader Index.

So, these are some different characteristics that highlight how unique we are and in a way that we think sets us up well for the future.

Ryan: Turning from Credit to other sectors within the Income Fund—those who are looking at the chart on the top left will notice that securitized products are the largest holding from a sector weighting within the Income Fund and an overweight versus the Index.

This is the highest we've seen the securitized products portion of the portfolio since the Global Financial Crisis in 2008–2009. What's driving the high weighting, and what specific investments would you highlight within the Securitized [sector] bucket?

Lucy: Yeah, the fact that over half the portfolio is in securitized products clearly indicates that it's an area that we're finding value. I'd say that's on both an absolute basis as we look at the return outlook for these securities, and certainly on a relative basis.

We've been talking about credit, how we pulled back there, and partly because of that, we have more cash to deploy in other parts of the portfolio. Relative to [U.S.] Treasuries, we think securitized products is quite attractive. That really has underpinned us continuing to find value there.

Now, typically for us in securitized products, we tend to focus on very high-quality holdings—largely agency MBS (mortgage-backed-securities) or high-quality asset-backed securities (ABS). These are very liquid securities. To the extent that we find more opportunities in [the] Credit [sector] going forward, it's very easy for us to adjust this positioning.

But for now, what we like is the combination of valuation and security-specific features. From a valuation standpoint, mortgage-backed securities are trading at spread levels that are fairly average. Unlike credit, where you're seeing these really low historical percentiles, you're not seeing that here. You're still getting typical compensation.

At the same time, you're getting lower-than-average prepayment risk, which is the primary risk for these securities. We're generally focused on lower-coupon Agency[4] mortgage-backed securities. These are securities that trade at a discount to par. The borrowers are very out of the money—meaning they have no incentive to refinance financially—and so there's just very low cash flow variability.

So, we think, overall, this part of the market has a really attractive risk/return characteristic. Within ABS, we're finding value in places like prime auto ABS and student loans. Again, mostly AAA—not a lot of credit risk —just a way to pick up some incremental yield.

Ryan: That's the work that we do—is to find those opportunities. So maybe, finally, we can talk about duration within the Income Fund. The Income Fund ended the second quarter at 6.3 years of duration, which is two-tenths of a year longer than the Index. The position, as we think of it, is partially driven by our view on the attractiveness of real and nominal yields.

With that as a lead-in, Lucy, how are you and the Committee thinking about duration positioning going forward, particularly given the rate environment that is unclear and could be a little volatile?

Lucy: Yeah, as we talked about at the onset of this, the rate markets have been plenty exciting over the course of this year, and that has kept the Committee active in having conversations. And while the headline duration you mentioned—6.3 [years]—hasn't changed over the course of the year, we have made tactical adjustments in the interim to take advantage of that volatility.

As we sit today, we think interest rate risk—and being a bit longer than the benchmark, being 6.3 [years], which is as high from a long-term perspective as we've been in some time—makes sense because as we look at our outlook for the economy, for inflation, and for what's likely to transpire for rates, we think that it's asymmetric to the downside. In other words, that rates are more likely to fall than rise, and we get paid at this point—given the shape of the curve I mentioned earlier—for going somewhat out the curve. We think that growth will continue to fall. We think inflation—even though the ride is likely to be bumpy with the tariff noise and there are ranges of what could happen—is likely to subside.

All this should lead to declines both in the federal funds rate but also somewhat in longer-term rates. This is what really drives our comfort with holding this longer position and really gives us a fairly positive view of returns for fixed income going forward.

Ryan: I think that's a great summary of the Income Fund. Thank you, Lucy, for that perspective. Summarizing the highlights that we've talked about:

- First, performance over both short- and long-term time horizons has been strong.
- Second, from a sector exposure perspective, Credit—as we've discussed—has incrementally increased over the first six months of the year, though we remain at historical low levels of market value exposure, based on an environment where credit spreads are historically tight. On the Securitized [sector] side, we're finding opportunities based on valuations that we find more attractive than the credit space, and we have high-quality and highly-liquid securities that we're investing in, that can be used to fund opportunities in [the] Credit [sector] if and when we find them occurring.
- Third, duration ended the quarter slightly longer than the Index at 6.3 years. As Lucy mentioned, part of this is driven off of our perspective, as we think of a variety or a range of outcomes, that rates may fall from where we are today—benefiting not only the Income Fund but fixed income investments more broadly.

Why don't we turn to the Global Bond Fund? Before we get into the specifics of the strategy, Lucy, maybe you can tee up how the strategy is differentiated from the Income Fund.

Lucy: Happy to do that. In many ways, it's similar. The key pillars of Dodge & Cox carry over—we have the same investment process, many of the same team members on the Investment Committee and broader investment team. We have the same long-term time horizon, focus on security selection, and valuation discipline.

There are some important differences. I think top of mind is the larger opportunity set that the Global Bond Fund has. Notably, in the Income Fund, we don't invest in non-U.S. dollar-denominated securities. In the Global Bond Fund, we do. So, we have a bigger opportunity set across sectors and geographies.

When we talk about the Fund, we really talk about three main levers, which are credit, currency, and rates. We manage the Fund with a total-return mindset, and that sort of results in a higher return objective than the Income Fund, but also that comes with somewhat higher risk.

We believe it's attractive for long-term investors seeking global diversification without taking excessive credit or currency risk. At this point, it's more than a decade old, and we're really excited in the current environment.

You mentioned the [U.S.] dollar earlier, but it's been on a very strong trend for over a decade, and now we're seeing some weakness. As I mentioned earlier, there's also a lot of different things happening outside the United States and more interest in that globally. And so we think it's an exciting time for the Global Bond Fund.

Ryan: Yes, certainly lots of opportunities that we'll walk through. But maybe we can start with performance, which has been quite impressive—both on an absolute and a relative basis.

You can see in the year-to-date period [as of June 30], returns on an absolute basis of 7.8%. As we think about performance versus the hedged Bloomberg Global Aggregate [Bond Index]—the benchmark for the strategy—there was nearly 5% of outperformance over the same period.

So, strong performance on both an absolute and relative basis. Importantly, supporting this performance was strong positive contributions from the three elements, Lucy, that you had mentioned—so credit, currency, and rates. Each of those were really contributive in a positive manner to returns over the first half of the year. What areas of performance would you emphasize?

Lucy: Well, I think the Credit [sector] returns that you mentioned—which were strong—really have parallels to what we talked about in the Income Fund. It's sort of remarkable how well Credit has done through this period, but it's certainly been additive to the Fund.

But perhaps it's worth spending a little more time on the non-[U.S.] dollar holdings, which are unique to the Fund and did do particularly well in recent history due to a combination of currency appreciation and also stable-to-declining rates in many of the markets in which the Fund invests.

If you think about the Fund holistically, it owns a collection of government, government-related, and corporate bonds across these different markets. Some of these holdings—particularly some of our government bond holdings—did well in both developed markets (places like Japan and Norway) and also within emerging markets (places like Brazil and Mexico).

Ryan: Yeah, and as we're talking about non-U.S. holdings, why don't we shift the conversation to currency. Those familiar with the Global Bond Fund strategy will know that over the past several years we've held roughly 20 to 25% in non-U.S. dollar holdings.

What changes have been made recently, and what's our outlook for the dollar?

Lucy: Yeah, before answering your question, I think it's worth taking a moment just about how we approach currency in the Fund. It's a question we get a lot because there's really a lot of ways different managers approach currency.

I would say that we come at management of the Fund through a hedged mindset. In other words, we only add currency exposure when we're really excited about those investments. We don't like the idea of passive currency exposure, and we believe the bar is high when it comes to the returns we should expect from this part of the portfolio.

In terms of where we are today, we've been fairly high conviction, to your point. Twenty to 25% is a pretty full position we think for currency, and that has been a reflection for the last few years of our view that the [U.S.] dollar appears fairly overvalued.

When you look at metrics like purchasing power parity, when you think about the fundamentals of the United States., when you look outside the United States at individual currency pairs—many of which are in double-digit undervaluations—that has gotten us excited about having a large, at least in our minds, up to 25% of the portfolio in foreign currency.

Now, more recently, as you talked about, we've seen a reversal in the [U.S.] dollar. We've seen it decline, and some of our positions go up. You saw us reduce non-[U.S.] dollar exposure by about 3% year to date [as of June 30]—so from about 24% to 21%.

That's really a reflection of the valuation discipline of trimming on strength in some of these currencies that have done really well. Also, reflecting fundamentals. One area we've trimmed back, for example, is a few of our Asian currency holdings, such as Malaysia and Korea.

We've gotten a little bit more—or a little less constructive, I should say—about the outlook given what's happening with tariffs, what's happening potentially with China. Again, valuation and fundamentals have driven us to shift somewhat, but we still have 21%. We still think the trend could continue. Again, it's an area that we're excited about within the portfolio.

Ryan: Yeah, it's really a great illustration of the levers we have to pull within the Global Bond Fund. So thank you for that example.

As we turn to credit, thematically, things are quite similar to the Income Fund. Credit spreads on a global basis are also historically tight, and with that we're roughly at our historical low in terms of [the] Credit [sector] exposure—39% for the Fund.

As you look at the additions over the first half of the year, many of the issuers—particularly those that are in the United States—mirror what we've done in the Income Fund. There are some unique stories within the Global Bond Fund where we've added to issuer names that are not in the Income Fund. Can you speak to some of these changes?

Lucy: Absolutely. The two that are on the page here on the left side that I'd highlight are Romania and Queensland, and they really both highlight some of the unique things we can do in the Global Bond Fund.

In the case of Romania, it's got some economic and political challenges, but we think that the bonds are attractively priced relative to other countries with similar fundamentals. Also, there is a recent presidential election there, a newly announced fiscal plan, and we think that those things have taken off some of the tail risks in Romania. So we think it's a fairly stable credit.

And one interesting thing is that we bought euro-denominated bonds in this Fund rather than [U.S.] dollar, because there actually is a difference in the pricing between those two markets. So it's a very specific type of security selection that we can use in this Fund.

In a somewhat similar vein, I'll pivot to Queensland. Queensland was a way for us to take advantage of—or basically find what we think is an attractive way to invest in Australian-denominated bonds. We could have bought the government bonds, and that would've been fine, but we instead decided to buy the State of Queensland bond because you can get an additional premium for them with, we think, minimal credit risk. Like Australia, Queensland's got incredibly strong and stable fundamentals and really has essentially implicit guarantee of the Australian government. So this is just, again, a way for us to find a very specific security within the landscape of Australian [dollar]-denominated holdings and express a view through that.

Ryan: Returning to the Fund's overall duration—it remains unchanged over the course of the last six months. It's 6.3 years, which I'll note is the same as the Income Fund. That's not a mistake, as we're talking through that. Of course, the team is remaining vigilant as we're looking at the Fund's headline duration, and there were some moves underneath the surface that didn't impact the overall headline duration exposure.

How are we thinking about the global rates environment in today's world?

Lucy: Yeah, I think I'd first expand a little on what you said about the magical 6.3 number between the two Funds. It is really quite different when you think about the 6.3 years here versus the Income Fund, because in this case—in the Income Fund's case—that's all sensitivity to U.S. interest rates.

In this case, it's really the aggregation of exposure to more than 15 markets. We've got exposure to a whole variety of places, each with a unique reason we like those areas.

Right now, we see really an array of opportunities that offer return and diversification. I shared the constructive view we have of U.S. rates, but there's other places that I'd highlight, including in developed markets, the United Kingdom, Australia, New Zealand. Those are places we've extended further out the curve, and we like the mix of our growth and inflation outlook. They have strong central banks. There's also places in EM (emerging markets) like Mexico, where they have a steep curve, very high real rates relative to a lot of developed markets, and their nominal rates are in the high single digits. So, lots of opportunities in this space.

Ryan: That's great, [a] really nice summary of what has happened in the Global Bond Fund over the last six months. Maybe to summarize the highlights:

- From a performance perspective, returns have been strong over short- and long-term time horizons.
- For currency, we've trimmed some of our non-U.S. dollar exposure based on strong performance, and we believe the dollar could fall versus select currencies going forward.
- On the Credit [sector] side, valuations remain tight, but we've found some idiosyncratic opportunities to add both to U.S. and global issuers. But our sector exposure remains near its historical lows at 39%.
- From a global rates perspective, we're finding opportunities in a variety of global rates markets, as evidenced by the 15 plus markets that we're investing in currently within the Fund.

Thanks, Lucy, for sharing your perspectives, and thank you to those listening, for your interest in this investment review and your continued confidence in Dodge & Cox.

Lucy, with our final minute, maybe I'll ask you: What would you encourage our listeners to keep top of mind as they enter the second half of the year?

Lucy: Lots of good options there, but I'd probably highlight that it feels that we're early days in this new administration and understanding what policies will be enacted and what the long-term impact of those policies will be.

We would expect more volatility—marking back to your first questions. We hope for more volatility, and we're ready for that given the liquidity in the portfolio, given we de-risked to a great degree. So, we look forward to seeing what pans out.

Ryan: That's terrific. Sounds like a great place to end. Thank you again.

The Income Fund — Class I SEC yield calculated for June 30, 2025 was 4.48%. This material must be accompanied or preceded by the Fund's prospectus.

Dodge & Cox Income Fund — Class I SEC Standardized Average Annual Total Returns as of June 30, 2025: 1 Year 6.49%, 5 Years 1.08%, 10 Years 2.89%. Fund and Index standardized performance is available on our website.

Income Fund's Ten Largest Positions (as of June 30, 2025): Fannie Mae (21.9% of the Fund), Freddie Mac (17.6%), U.S. Treasury Note/Bond (14.9%), Ginnie Mae (3.9%), Navient Student Loan Trust (2.3%), Petroleos Mexicanos (2.1%), Charter Communications, Inc. (1.7%), Prosus NV (1.4%), HSBC Holdings PLC (1.3%), and Imperial Brands PLC (1.3%).

The Global Bond Fund — Class I SEC yield calculated for June 30, 2025 was 4.99% using net expenses and 4.94% using gross expenses. This material must be accompanied or preceded by the Fund's prospectus.

Dodge & Cox Global Bond Fund — Class I SEC Standardized Average Annual Total Returns as of June 30, 2025: 1 Year 9.13%, 5 Years 3.80%, 10 Years 4.45%. Fund and Index standardized performance is available on our website.

Global Bond Fund's Ten Largest Positions (as of June 30, 2025): Fannie Mae (12.5% of the Fund), Freddie Mac (8.7%), U.S. Treasury Note/Bond (8.7%), Brazil Government (3.8%), Japan Government (3.7%), Norway Government (3.2%), Colombia Government (2.8%), Mexico Government (2.6%), TC Energy Corp. (2.2%), and SMB Private Education Loan Trust (2.2%).

1 Unless otherwise specified, all weightings and characteristics are as of June 30, 2025.

2 All Fund performance results discussed are for the Class I shares of the Income Fund and Global Bond Fund.

3 The use of specific examples does not imply that they are more or less attractive investments than the Fund's other holdings.

4 The U.S. Government does not guarantee the Fund's shares, yield, or net asset value. The agency guarantee (by, for example, Ginnie Mae, Fannie Mae, or Freddie Mac) does not eliminate market risk.

The Fund invests in securities and other instruments whose market values fluctuate within a wide range so your investment may be worth more or less than its original cost. International investing involves more risk than investing in the U.S. alone, including currency risk and a greater risk of political and/or economic instability; these risks are heightened in emerging markets. The Fund may use derivatives to create or hedge investment exposure, which may involve additional and/or greater risks than investing in securities, including more liquidity risk and the risk of a counterparty default. Some derivatives create leverage.

Returns represent past performance and do not guarantee future results. Investment return and share price will fluctuate with market conditions, and investors may have a gain or loss when shares are sold. Fund performance changes over time and currently may be significantly lower than stated above. Performance is updated and published monthly.

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