FIXED INCOME PERSPECTIVES

A Monthly Strategy Review of Bond Market Trends and Economic Developments

April 2024

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Senior Portfolio Manager

Holding Pattern

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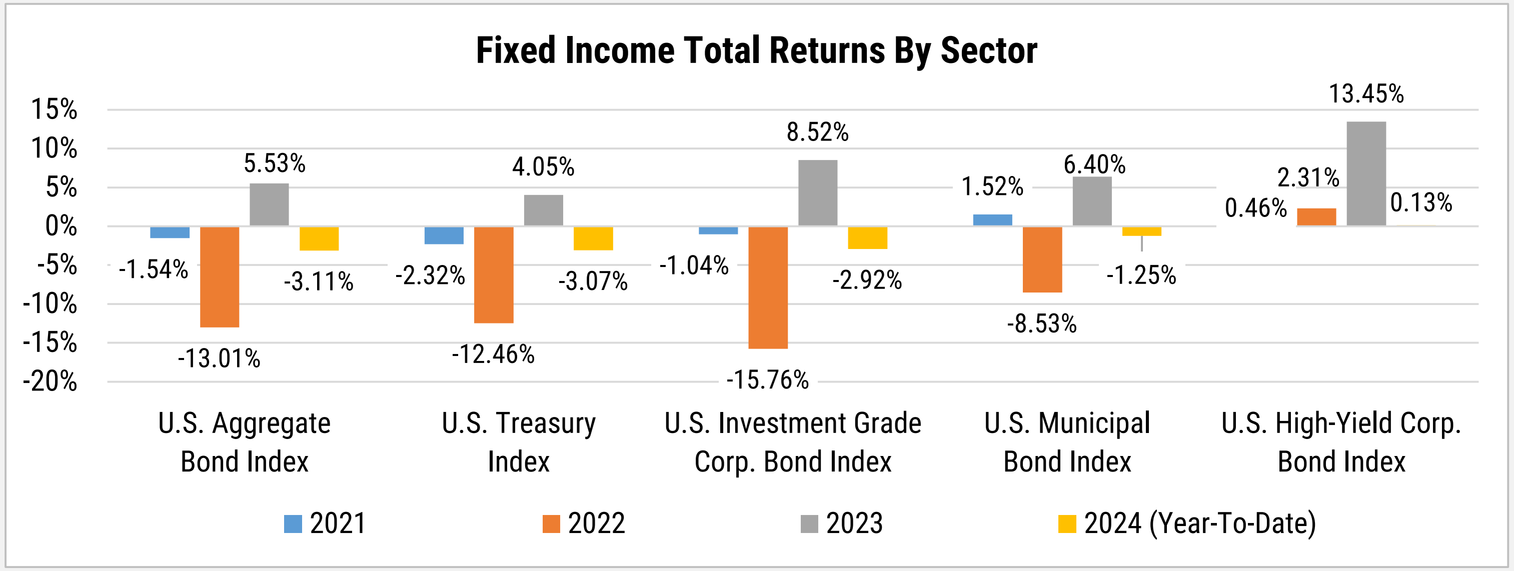
After posting a stellar 7.5% gain in the fourth quarter, the Bloomberg U.S. Aggregate Bond Index (AGG) declined by 3.1% on a year-to-date basis through April 15. The bond market's initial overreaction to the Federal Reserve's (Fed) pivot in December has been tempered in recent weeks. Since the beginning of the year, the 10-year U.S. Treasury yield has risen by 70 basis points (bps) to 4.6%, as traders have downshifted their expectations for the timing and magnitude of rate cuts in 2024, amid signs of sticky inflation and tight labor market conditions. **In our view, this warranted correction has placed the bond market on stronger footing and created a more favorable risk/reward profile for investors.**

Fixed Income Sector Performance

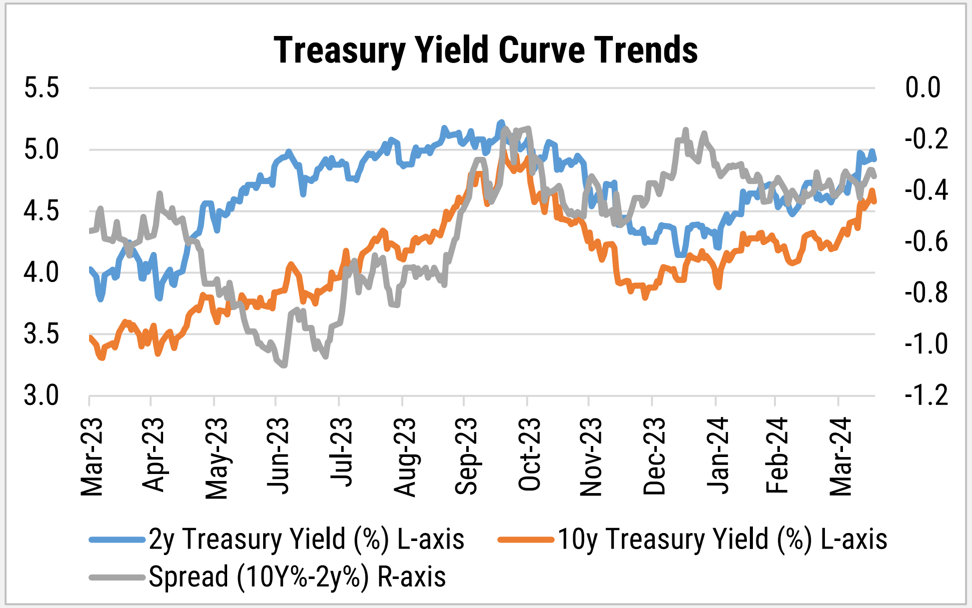


Returns through 4/15/2024; Fixed income indices provided by Bloomberg; Source: Bloomberg Finance, LP

Indices are unmanaged, do not reflect fees and expenses, and are not available for direct investment.
Past performance cannot and should not be viewed as an indicator of future performance.

Since dropping to a low of 3.8% in the fourth quarter, the 10-year U.S. Treasury yield has ascended to a five-month high, with Fed policy seemingly stuck in an indefinite holding pattern. While the upward shift in the Treasury yield curve has largely been justified by the incoming data, there are two important points to keep in mind regarding the bond market's recent selloff. First, our assessment of the fair value range for the 10-year yield is 4.3% to 4.8%. This latest increase in rates has simply returned the 10-year yield to slightly above the mid-point of our fair value range. Second, bond yields now look increasingly attractive relative to their longer-term averages. Compared to the 20-year average of 2.9% and 30-year average of 3.8%, the 10-year Treasury yield is trading well above those levels. **Historically, bonds have provided attractive forward total returns when their starting yields were significantly above their longer-term averages.**

Treasury Yield Curve



Source: Bloomberg Finance, LP

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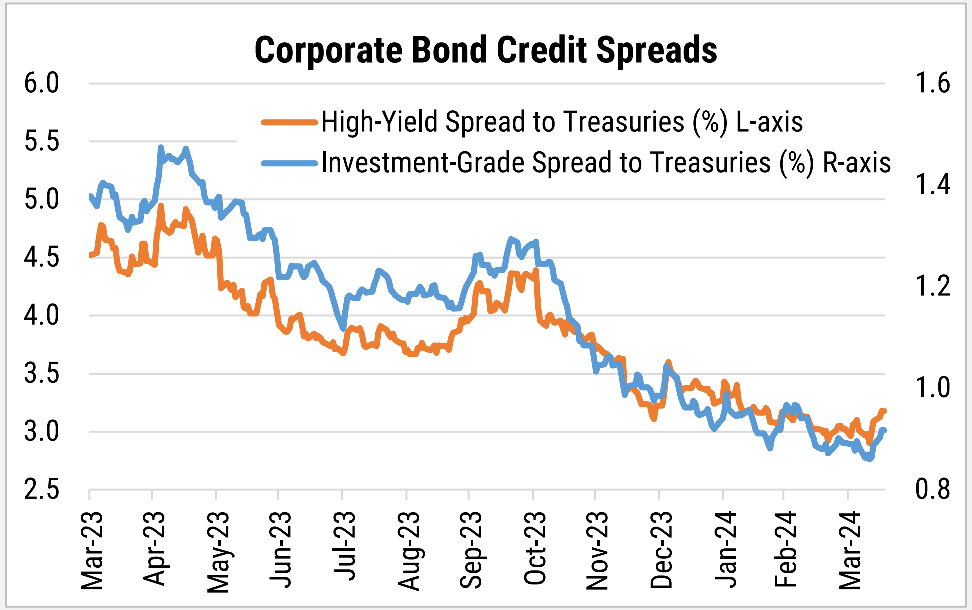
Credit Spreads

Corporate bond spreads are hovering near their tightest levels over the past 20 years, despite mixed signals from high-frequency economic data, consensus projections for slower gross domestic product (GDP) growth, and warning signs from leading economic indicators. **Given the notable disconnect between credit spreads and economic fundamentals, the corporate bond sector appears overvalued, and spreads are at risk of significantly widening in an environment of slower economic growth and higher than expected inflation.** During periods of material spread widening, Treasuries typically outperform the more credit-sensitive fixed income sectors, as cash rotates to the perceived safety of U.S. government debt.



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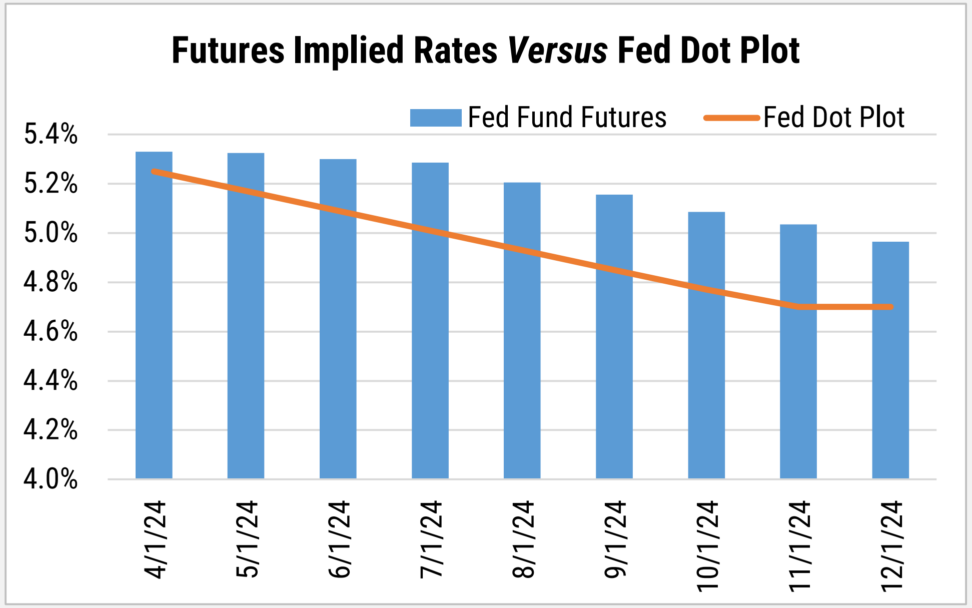
Federal Reserve Monetary Policy

The Fed's March Summary of Economic Projections envisions a sustained series of rate cuts over the next three years, at a pace of 75 bps per annum. **Assuming the Fed's projections come to fruition, an extended easing campaign of that magnitude would serve as a positive performance catalyst for the bond market.** During similar easing cycles over the past 40 years, bonds have enjoyed a multi-year bull market in every instance. Implied forward interest rates derived from fed funds futures are now well aligned with the dot-plot through the end of the year.



As of 4/15/2024; Source: Bloomberg Finance, LP

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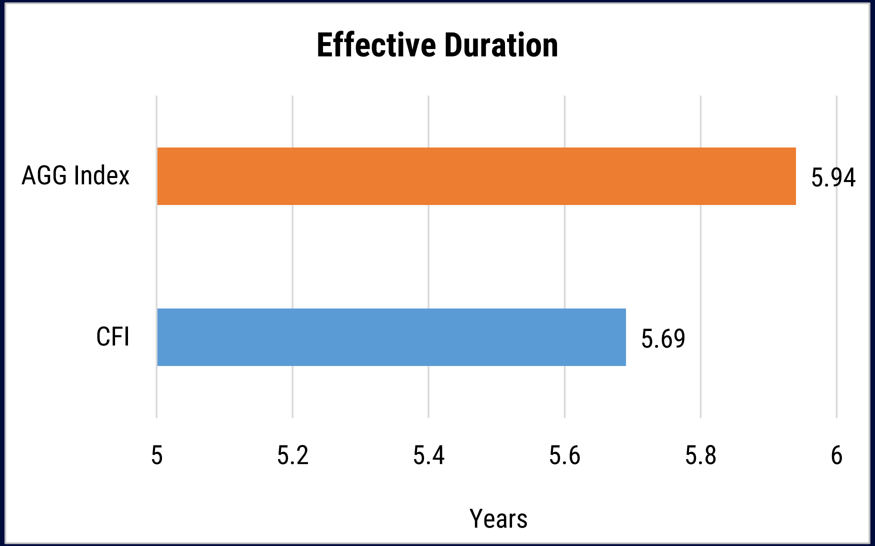
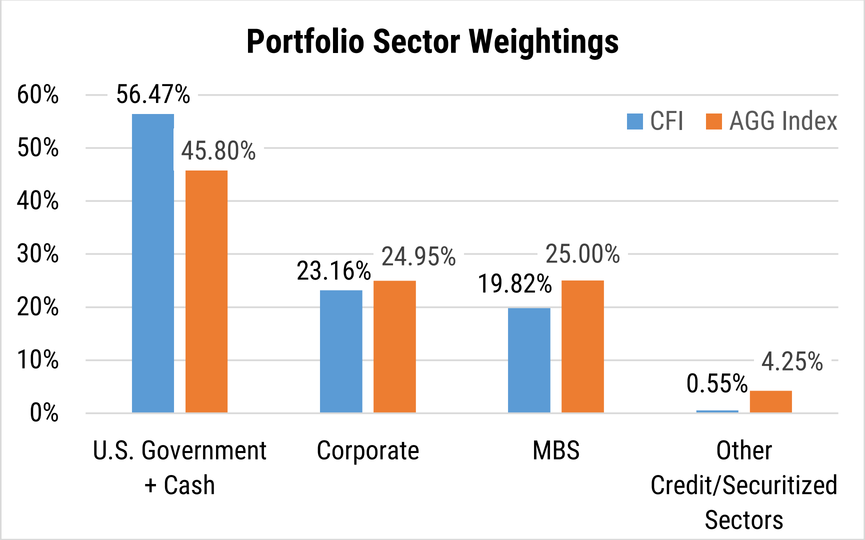
Core Fixed Income Portfolio (CFI) Statistics



As of 4/15/2024; Source: Bloomberg Finance, LP



As of 4/15/2024; Source: Bloomberg Finance, LP

To prepare for a steeper curve (lower short-term yields coupled with flat to higher long-term yields), we are targeting the portfolio's duration at 5.7 years, which is approximately 96% of the AGG's duration. **Concentrating principal cash flows in the intermediate-term segment of the curve should assist performance and help mitigate risks in several ways, including maximizing potential roll down benefits, reducing front-end reinvestment risk, and lowering the inflation risk associated with longer duration instruments.**

To protect against wider corporate bond spreads, CFI maintains a significantly higher credit quality posture relative to the AGG. Compared to the benchmark, CFI holds a 10.7% overweight to Treasuries, with a commensurate and combined underweight to mortgage-backed securities, corporate bonds, and other credit-sensitive sectors.

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Fixed Income Market Review

- Following a stellar fourth quarter, bonds have returned a portion of their previous gains, amid signs of sticky inflation and a reset in Fed expectations.
- Treasury yields have ascended to their highest levels in five months, with Fed policy seemingly stuck in an indefinite holding pattern.
- Corporate credit spreads have continued to tighten on strong demand for higher yielding bonds, despite mixed economic signals.
- After pricing in 150 bps in rate cuts for 2024 at the beginning of the year, interest rate futures are now much more closely aligned with the Fed's dot plot.
- Amid heightened bond market volatility and elevated economic uncertainty, the Core Fixed Income Portfolio maintains a significant underweight to corporate bonds and is positioned to benefit from a steeper yield curve and a mean reversion in credit spreads.

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After a sustained run of generally healthy economic reports during the fourth quarter, the past 15 weeks have brought mixed results in the high-frequency data, with eight positive weeks and seven negative weeks. **Beyond these inconclusive signals, key leading indicators warn of a looming economic slowdown.** The Conference Board's Leading Economic Index (LEI) has declined 23 of the past 24 months, falling by 13% from its December 2021 peak. Declines of that magnitude have historically preceded recessions. The latest Bloomberg economic survey also reflects an outlook for slower growth in 2024. After expanding by 3.2% last year, GDP growth is expected to moderate to 2.2% in 2024.

High-Frequency Economic Data Monitor

High-Frequency Indicators	Current Reading	-1 Week	-2 Weeks	-3 Weeks	1 Week Pct	2 Week Pct	3 Week Pct
U.S. Crude Rotary Rig Count	508	506	509	510	0.4%	-0.2%	-0.4%
Raw Steel Production	1,745	1,722	1,703	1,714	1.3%	2.5%	1.8%
MBA U.S. Purchase Index	138.7	145.6	145.7	146.0	-4.7%	-4.8%	-5.0%
JRI Same Store Sales Monthly (YoY)	4.2%	3.9%	3.4%	3.2%	0.3%	0.8%	1.0%
Department Store YOY % Change (MTD)	-0.1%	0.0%	-0.3%	-0.4%	-0.1%	0.2%	0.3%
Initial Jobless Claims	211	222	212	212	-5.0%	-0.5%	-0.5%
Continuing Jobless Claims	1,817	1,789	1,810	1,795	1.6%	0.4%	1.2%
NY Fed Weekly Economic Index (WEI)	1.9	1.7	1.7	1.5	11.1%	15.2%	28.4%
U.S. TSA Checkpoint Numbers	2,663,438	2,586,606	2,744,927	2,728,408	3.0%	-3.0%	-2.4%
Chicago Board Options Exchange (VIX)	17.3	16.0	13.0	13.1	8.0%	33.1%	32.5%
IG Corp. Credit Default Spread (CDX)	54.6	52.5	51.5	52.3	3.9%	6.0%	4.2%

Data as of 4/15/2024. Green denotes positive trend; red denotes negative trend.
Source: Bloomberg Finance, LP

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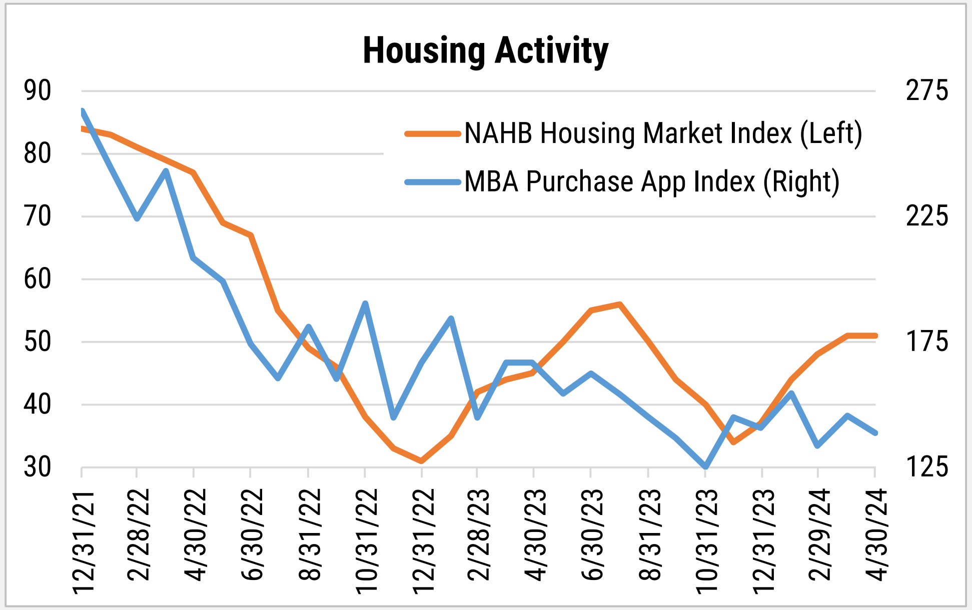
Mortgage Applications

After declining sharply over the past two years due to rising mortgage rates and poor affordability, housing turnover appears to be stabilizing, as the market adjusts to higher borrowing costs and elevated price levels.

- Compared to the fourth quarter, mortgage applications have been running 6% higher on a year-to-date basis, with an average weekly reading on the Mortgage Purchase Index of 147.2.
- The National Association of Home Builders (NAHB) Market Index has shown signs of stabilizing around 50, but it remains lower by 35% compared to its March 2022 level.



Source: Bloomberg Finance, LP

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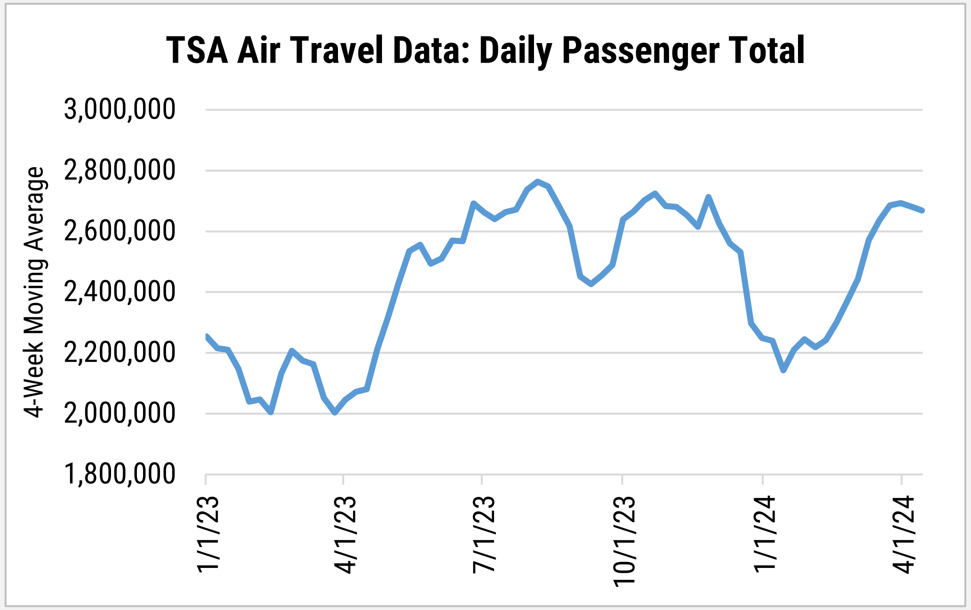
Air Travel By Total Passengers

The daily passenger count for air travelers averaged 2.3 million over the first three months of the year, a 10% increase compared to the first quarter of 2023 and the strongest start to the year since 2019. **Lingering pent-up demand, coupled with persistently low unemployment, have provided a tailwind to air travel despite higher interest rates and greater economic uncertainty.** Over the past two years, the travel and leisure sector has provided a helpful boost to the economy and helped to mitigate some of the softness in the housing and manufacturing sectors.



Source: Bloomberg Finance, LP

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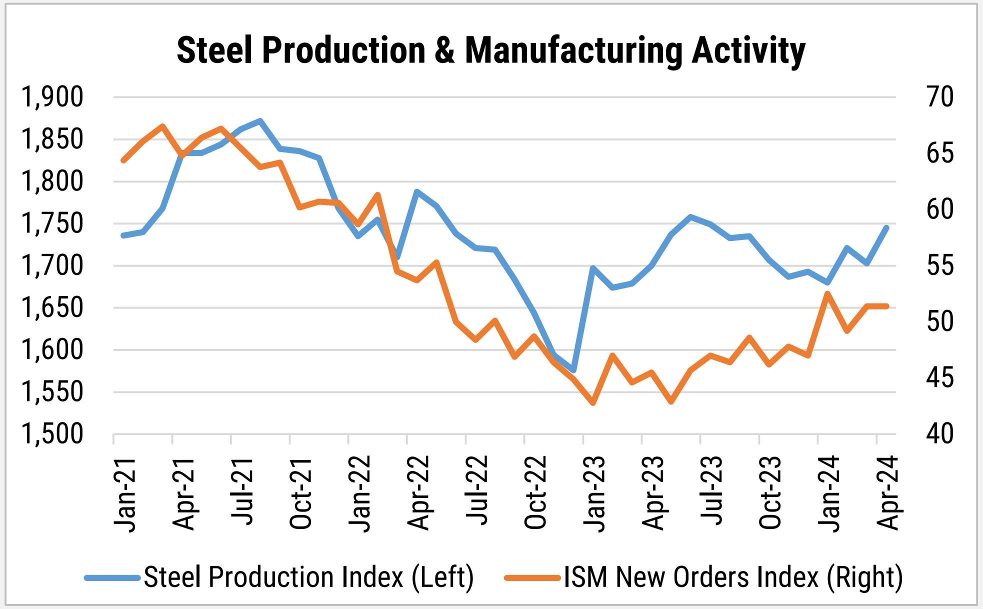
Outside of technology spending, higher interest rates have curtailed business investment, to the detriment of the production side of the economy. The ISM Manufacturing New Orders Index, a key leading indicator of manufacturing activity, held below 50 for 16 consecutive months through the end of last year. **On a positive note, new orders may have bottomed, with the index posting a 51.3 average monthly reading over the past three months, its best showing since the second quarter of 2022.** In anticipation of stronger order flow for durable equipment, steel production has recently been on the upswing, climbing to an 8-month high in early April.

Steel Production



Source: Bloomberg Finance, LP

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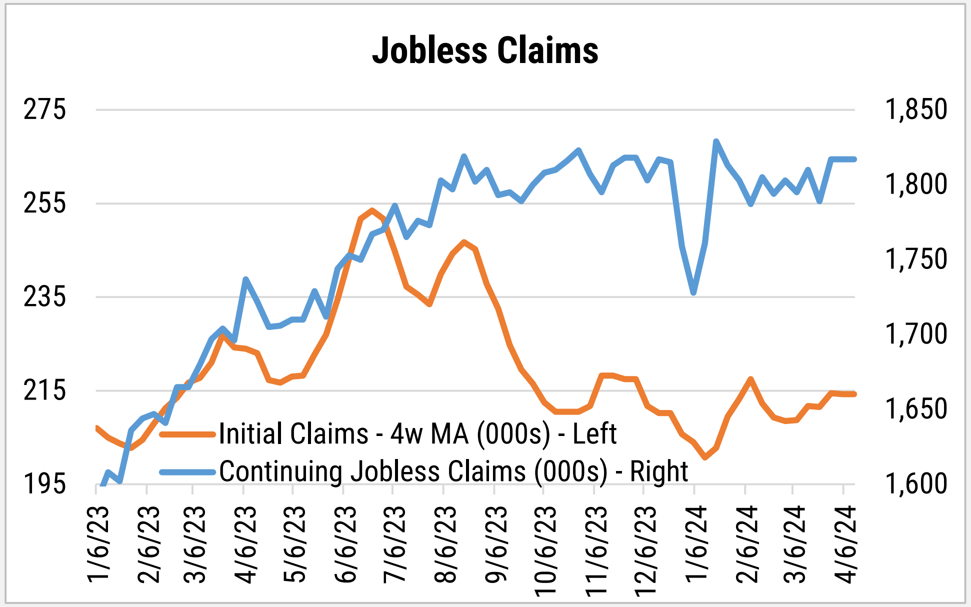
Building on a stronger than expected gain in nonfarm payrolls for March, the latest jobless claims data reinforced the labor market's persistent strength. The four-week moving average for initial jobless claims has been range bound between 200,000 and 220,000 for the past six months. The most recent reading was 214,000 for the week of April 5, a slight decrease from the previous week. With the exception of the sharp swings that occurred around the year-end holidays, continuing claims have been hovering around 1.8 million since last August. A low and relative stable pace of layoffs is consistent with a robust labor market and high employment, factors which should continue to support a healthy level of consumer spending.

Jobless Claims



Source: Bloomberg Finance, LP

Economic Data Review

- Economic growth has exceeded consensus expectations, though the most recent high-frequency data has been mixed, and key leading indicators warn of a potential slowdown later this year.
- High mortgage rates and record home prices have restrained housing turnover rates over the past two years, though activity levels have recently shown tentative signs of stabilization.
- In a sign of persistent strength in the consumer services sector, air travel passenger count reached its highest level since 2019 in the first quarter.
- The production side of the economy has languished due to higher borrowing costs and a shift in consumer spending preferences but may be poised for a meaningful rebound as demand patterns normalize.
- Labor market conditions remain healthy, given the low unemployment rate, solid wage growth, steady monthly payroll gains, and modest layoffs.

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About the Author

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Senior Portfolio Manager

Jim joined EquityCompass in July 2019. He is a Senior Portfolio Manager for the Core Fixed Income Portfolio, Municipal Income Enhanced Portfolio, and co-manager of the High-Dividend Portfolio. Prior to joining the portfolio management team, Jim served as the Chief Fixed Income Strategist at Stifel, Nicolaus & Company, Incorporated for 12 years. At Stifel, Jim created investment portfolio and risk management strategies for the firm's institutional fixed income clients. He also managed a $3 billion bond portfolio for Stifel Bank. Previously, he spent five years at Legg Mason as a fixed income strategist and 13 years at the Federal Deposit Insurance Corporation (FDIC) in bank supervision. His FDIC career focused on the credit analysis of bank balance sheets and the risk profile of innovative credit market instruments, including corporate bonds, mortgage-backed securities, and derivatives.

Jim has a B.S.B.A. in Finance from West Virginia University. He is also a CFA charter holder and member of the CFA Society Baltimore.

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About EquityCompass

EquityCompass Investment Management, LLC ("EquityCompass") is a Baltimore-based equity investment management team that provides portfolio strategies with respect to assets of approximately $5.0 billion.[1]

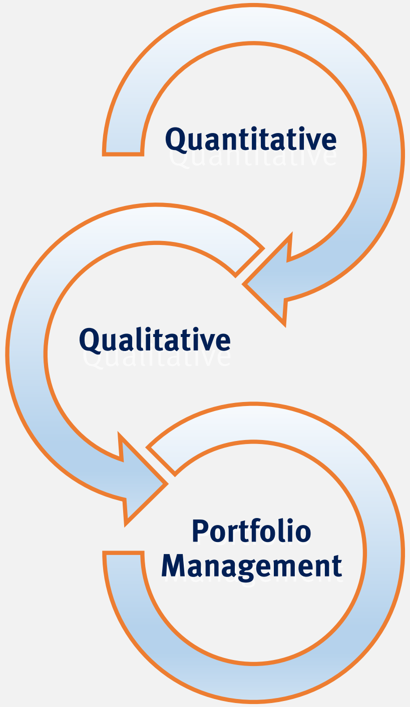
At EquityCompass, our mission as an asset management company is to provide investment solutions that address the needs of clients accumulating, mitigating risk to, and decumulating wealth. We aim to accomplish these goals with an organization culture that prizes intellectual honesty, open dialogue among colleagues, and a commitment to continually improve ourselves and the investment process.

Extensive Investment Experience

- Investment team led by Richard Cripps, CFA – former Managing Director of Portfolio Strategy at Stifel and former Chief Market Strategist and Co-Chairman of the investment committee at Legg Mason Wood Walker
- Senior members include Robert Hagstrom, CFA, as Chief Investment Officer and Chris Mutascio as Senior Managing Director – both with 20+ years of investment experience
- Publishing investment research since 2001
- Offering investment portfolios on the Stifel platform since 2006

Research-Driven, Risk-Managed Portfolio Strategies

- Incorporates fundamental, technical, and behavioral insights evolving from original research by EquityCompass professionals
- Portfolios are designed to maximize expected returns by focusing on stock selection while incorporating rigorous risk management strategies
- The investment team collaborates to leverage ideas, research, and expertise in making investment decisions on all strategies



Rigorous empirical testing to identify favorable risk-adjusted investment insights

Experienced qualitative analysis for final investment selection

Focused and disciplined portfolio decision-making

(1) Total assets combines both Assets Under Management and Assets Under Advisement as of March 31, 2024. Assets Under Management represents the aggregate fair value of all discretionary and non-discretionary assets, including fee paying and non-fee paying portfolios. Assets Under Advisement represent advisory-only assets where the firm provides a model portfolio and does not have trading authority over the assets.

Disclosures

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Description of Benchmark(s): **The MBA (Mortgage Bankers Association) Purchase Index** is a weekly report of mortgage loan applications based on a sample of 75% of U.S. mortgage activity. Analysts consider the report to be a leading indicator of housing market activity. The **Bloomberg U.S. Aggregate Bond Index** is a broad-based flagship benchmark that measures the investment grade, U.S. 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). The **Bloomberg U.S. Treasury Index** measures U.S. dollar-denominated, fixed-rate, nominal debt issued by the U.S. Treasury. Treasury bills are excluded by the maturity constraint, but are part of a separate Short Treasury Index. STRIPS are excluded from the index because their inclusion would result in double-counting. The **Bloomberg U.S. Mortgage Backed Securities (MBS) Index** tracks fixed-rate agency mortgage backed pass-through securities guaranteed by Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC). The index is constructed by grouping individual TBA-deliverable MBS pools into aggregates or generics based on program, coupon and vintage. The **Bloomberg U.S. Corporate Bond Index** measures the investment grade, fixed-rate, taxable corporate bond market. It includes USD-denominated securities publicly issued by U.S. and non-U.S. industrial, utility and financial issuers. The **Bloomberg U.S. 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 EM country definition are excluded. The **Bloomberg U.S. Municipal Bond Index** is considered representative of the broad market for investment grade, tax-exempt bonds with a maturity of at least one year.

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Disclosures

The **Chicago Board Options Exchange (CBOE)** created the VIX (**CBOE Volatility Index**) to measure the 30-day expected volatility of the U.S. stock market, sometimes called the "fear index." The VIX is based on the prices of options on the S&P 500 Index and is calculated by aggregating weighted prices of the index's call and put options over a wide range of strike prices. **The Institute of Supply Management (ISM) Manufacturing Purchasing Managers Index (PMI)** is based on data compiled from monthly replies to questions asked of purchasing and supply executives in over 400 industrial companies. For each of the indicators measured, this report shows the percentage reporting each response, the net difference between the number of responses in the positive economic direction and the negative economic direction and the diffusion index. **The Raw Steel Production Index** measures the real output of all relevant establishments located in the United States, regardless of their ownership, but not those located in U.S. territories. The **Weekly Economic Index (WEI)** provides a signal of the state of the U.S. economy based on data available at a daily or weekly frequency. The WEI is an index of ten indicators of real economic activity, scaled to align with the four-quarter GDP growth rate. It represents the common component of series covering consumer behavior, the labor market, and production. The **Manufacturing ISM Report** is based on data compiled from monthly replies to questions asked of purchasing and supply executives in over 400 industrial companies for each of the indicators measured: New Orders, Backlog of Orders, New Export Orders, Imports, Production, Supplier Deliveries, Inventories, Customers Inventories, Employment, and Prices. The **Conference Board Leading Economic Index** is an American economic leading indicator intended to forecast future economic activity. It is calculated by The Conference Board, a non-governmental organization, which determines the value of the index from the values of ten key variables. The **NAHB/Wells Fargo Housing Market Index (HMI)** is based on a monthly survey of NAHB members designed to take the pulse of the single-family housing market. The survey asks respondents to rate market conditions for the sale of new homes at the present time and in the next six months as well as the traffic of prospective buyers of new homes. The **credit default swap index (CDX)** is a benchmark financial instrument made up of credit default swaps that have been issued by North American or emerging market companies. A credit default swap is an over-the-counter derivative contract that offers one counterparty protection against a credit event, such as the default or bankruptcy of an issuer. It can be thought of as insurance in the financial world. The credit default swap index tracks and measures total returns for the various segments of the bond issuer market so that the overall return of the index can be benchmarked against funds that invest in similar products. **Gross domestic product (GDP)** is the total monetary or market value of all the finished goods and services produced within a country's borders in a specific time period. As a broad measure of overall domestic production, it functions as a comprehensive scorecard of a given country's economic health. All benchmark returns are shown on a total return basis and assume that all cash distributions, such as dividends, are reinvested. The volatility of the indices identified in this report may be materially different from the volatility of the model portfolios presented by EquityCompass. Indices are unmanaged, do not reflect fees and expenses, and are not available for direct investment.

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