FIXED INCOME PERSPECTIVES

A Monthly Strategy Review of Bond Market Trends and Economic Developments

November 2024

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Senior Portfolio Manager

A Sweeping Reset

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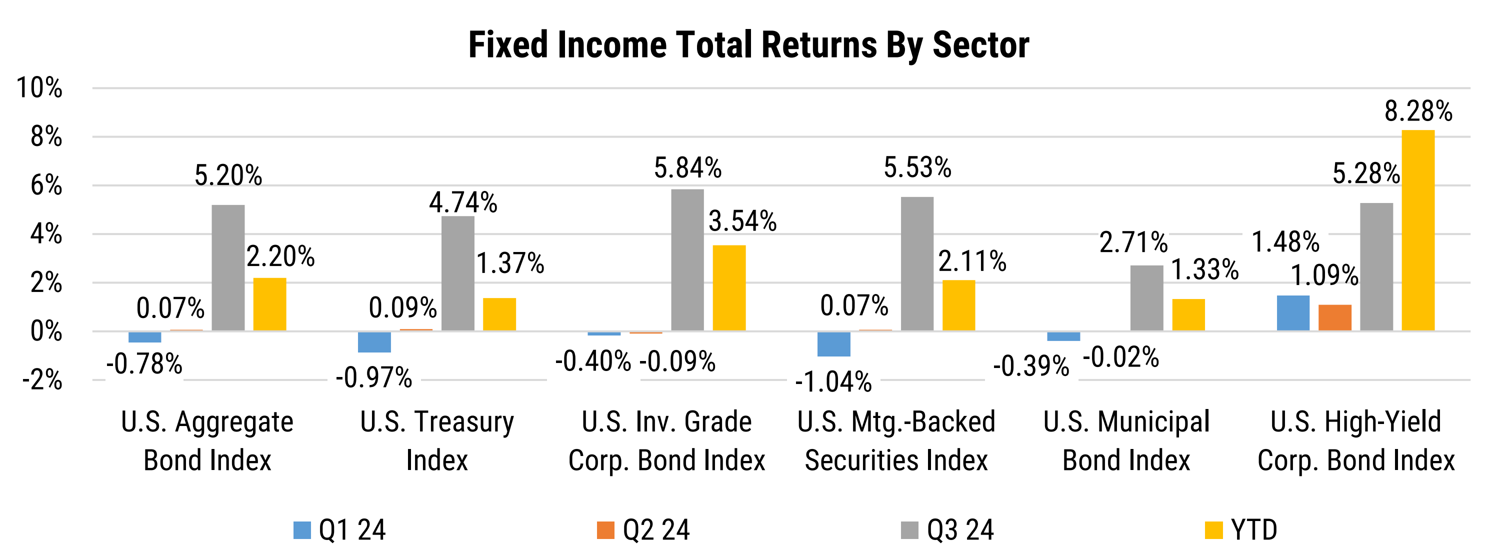
One of the more pronounced post-election trades has been the rotation out of bonds and into stocks. **The decisive shift in the U.S. political landscape has triggered a sweeping reset in expectations for economic growth (stronger), inflation (higher), and rate cuts (fewer).** These revised assumptions have sent Treasury yields higher and bond prices lower, with investors moving further out on the risk spectrum to capture potentially higher returns in other asset classes.

Bonds have given back a sizable portion of their earlier gains, with the Bloomberg U.S. Aggregate Bond Index (AGG) declining by 2.16% on a quarter-to-date basis through November 11. Despite this recent selloff, the AGG has generated a total return of 2.20% on a year-to-date basis. With bond yields climbing to their highest levels since late July, the fixed income sector should garner more investor interest through year-end.

Fixed Income Sector Performance



Returns through 11/11/2024; Fixed income indices provided by Bloomberg; Source: Bloomberg Finance, LP

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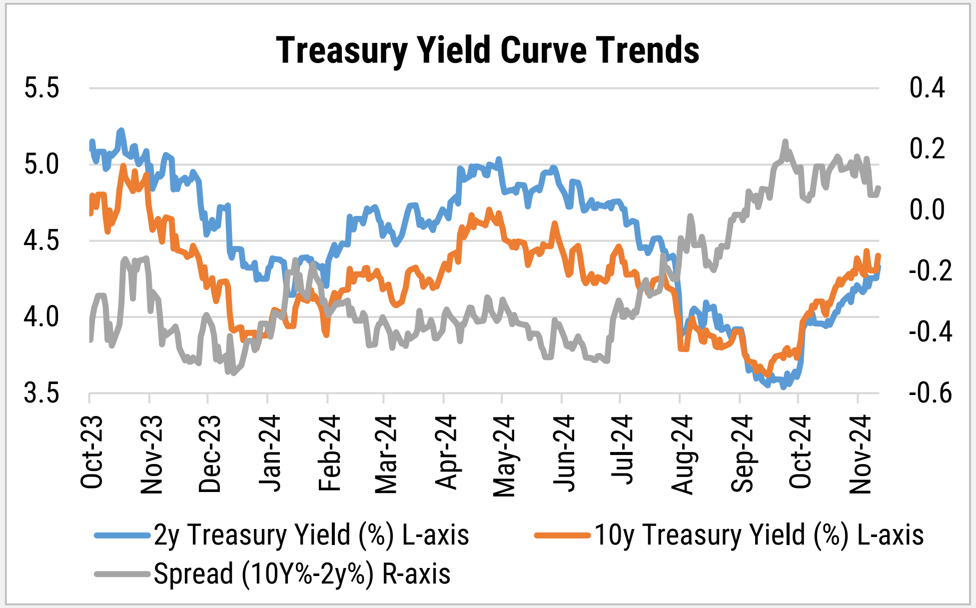
Indices are unmanaged, do not reflect fees and expenses, and are not available for direct investment.
Past performance cannot and should not be viewed as an indicator of future performance.

Treasury yields can be decomposed into two parts: (1) real yield and (2) inflation compensation. Both components were trending higher in advance of the election and have continued to ascend since November 5 given favorable prospects for a Republican sweep. **After dipping to 3.6% in mid-September, the 10-year U.S. Treasury yield has climbed by 80 basis points (bps) to 4.4%, with the real yield gaining 52 bps and the inflation component adding 38 bps.**

Expectations for stronger economic growth have lifted real yields, while uncertainty surrounding the implementation of tariffs and deportations has raised inflation estimates. The upward adjustment in the Treasury curve has been largely parallel in nature, with the 2-year to 10-year yield spread trading in a narrow range centered around 10 bps over the past two months.

Treasury Yield Curve



Source: Bloomberg Finance, LP

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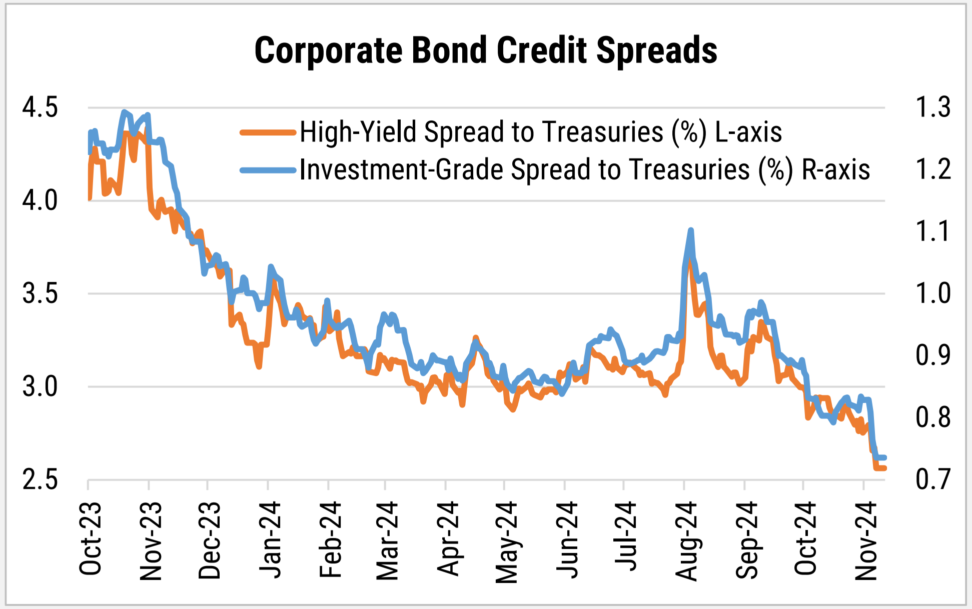
Credit Spreads

Extending the 2017 corporate tax cuts is expected to be one of the key initial priorities of the Trump administration. Status quo tax policy, or perhaps even lower marginal rates, would be a positive factor for corporate credit quality. Along with expectations for stronger economic growth in the coming years, a more hospitable tax regime has driven corporate bond spreads to 20-year lows. **At these historically tight levels, corporate spreads appear to be largely "priced for perfection" and could widen significantly if the economy fails to meet the credit market's optimistic assumptions.**

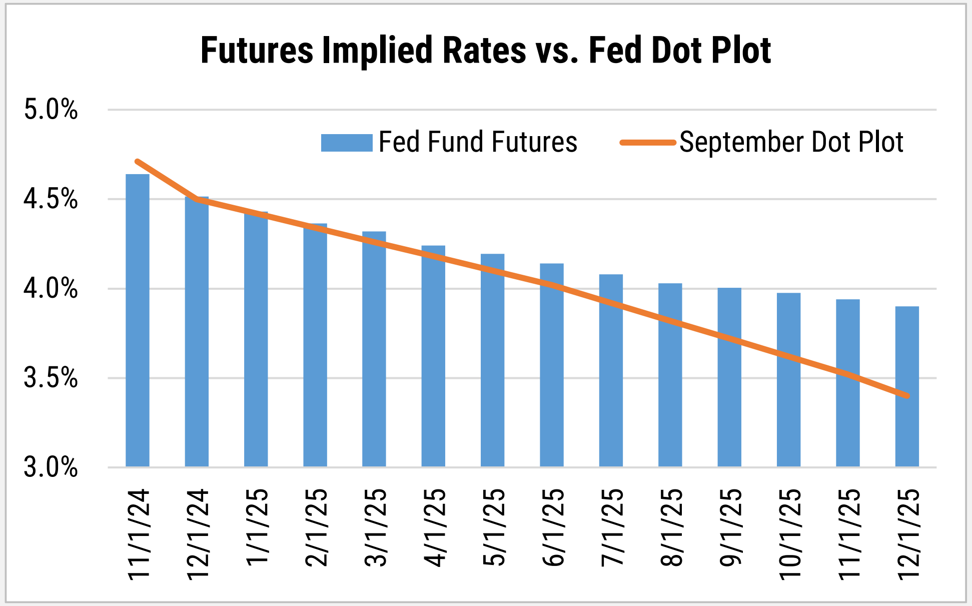


Source: Bloomberg Finance, LP

Federal Reserve Monetary Policy

With the labor market cooling and inflation subsiding, the Federal Reserve (Fed) delivered another 25 bps rate cut in November, lowering the policy range for the fed funds rate to 4.50%–4.75%. **While short-term rates are expected to take a further step downward at the December 18 meeting of the Federal Open Market Committee (FOMC), a pause in the easing cycle may occur in the first quarter of 2025 as policymakers await more details surrounding the incoming administration's economic policies.**

The Fed will provide updated forward guidance and revised economic projections at the December FOMC meeting. According to interest rate futures, this upcoming information refresh from the Fed will likely reflect fewer rate cuts and a more methodical approach to normalizing policy compared to the September data. Prior to the election, interest rate futures were pricing in a fed funds rate of 3.75% by the end of next year. As of November 11, this year-end 2025 estimate had been upwardly revised to 4.0%.



As of 11/11/2024; Source: Bloomberg Finance, LP

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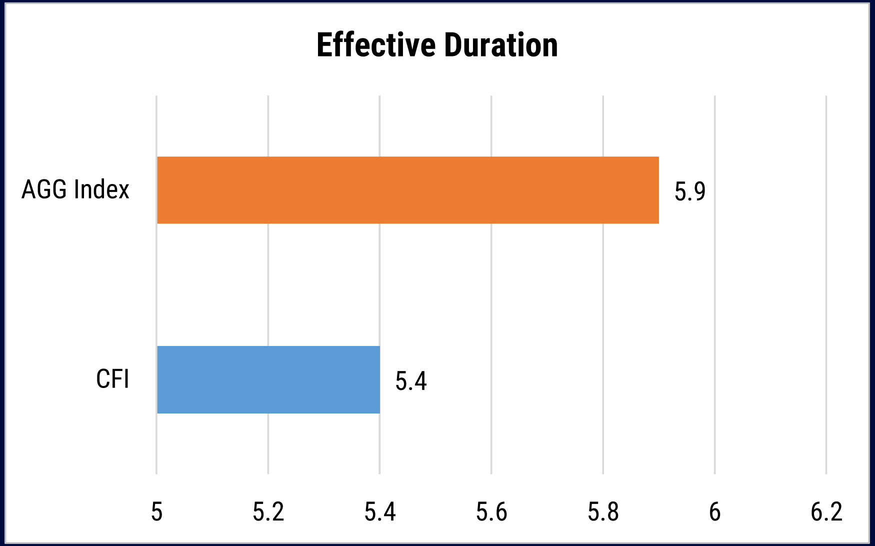
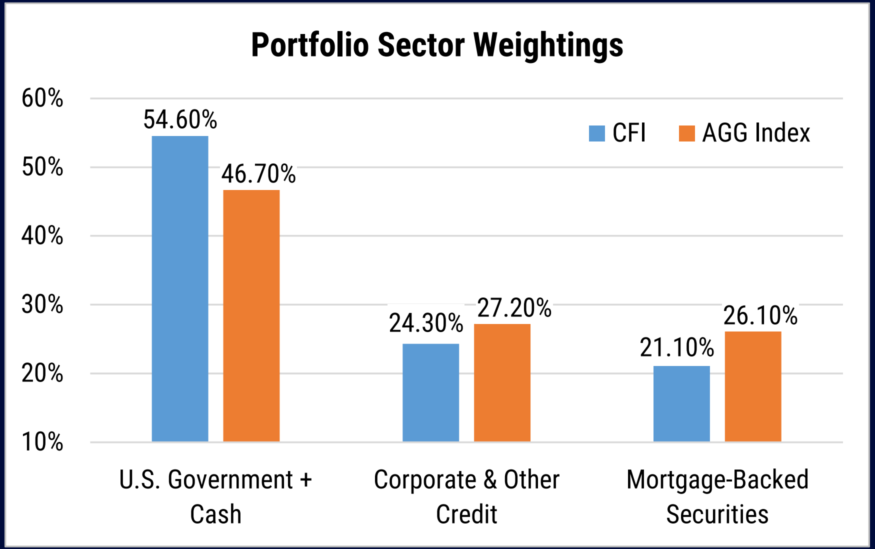


As of 10/31/2024; Source: FactSet Data Systems, Inc. and Bloomberg Finance, LP



As of 10/31/2024; Source: FactSet Data Systems, Inc. and Bloomberg Finance, LP

Core Fixed Income Portfolio (CFI) Statistics

The election results reinforced our expectations for a steeper yield curve over the next few years. In anticipation of further yield curve steepening (lower short-term yields coupled with flat to higher long-term yields), we continue to target the portfolio's duration at 5.5 years, which is approximately 92% of the AGG's duration. To address the potential risk of wider credit spreads, CFI maintains significantly higher credit quality relative to the AGG. Compared to the benchmark, CFI holds an overweight to Treasuries (including cash) of 790 bps, with a commensurate and combined underweight to corporate bonds and other credit-sensitive sectors.

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Fixed Income Market Review

- The election results have dramatically altered the U.S. political landscape and triggered a sweeping reset in the bond market.
- Treasury yields have steadily ascended over the past eight weeks to their highest levels since late July.
- Corporate credit spreads have collapsed to 20-year lows, with traders upgrading their projections for economic growth.
- While another 25 bps rate cut seems likely in December, a pause in the easing cycle may occur early next year as the Fed awaits more clarity on the incoming administration's economic agenda.
- Compared to its benchmark, the Core Fixed Income Portfolio offers a similar yield with higher credit quality and a shorter duration.

In stark contrast to the euphoria permeating the risk asset complex, current economic conditions remain sluggish and highlight potential downside risks to lofty market valuations. For the past five consecutive weeks, the majority of the high-frequency indicators that we track on a weekly basis have been moving in the wrong direction.

In addition to the lackluster real-time data, the Conference Board's Leading Index declined in September, dropping for the 31st time in the past 33 months, with one unchanged reading over that time span. On a month-over-month basis, the Leading Index fell by 0.5%. On a six-month annualized basis, the Leading Index has declined by 5.2%, its worst showing since February.

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	479	480	482	481	-0.2%	-0.6%	-0.4%
Raw Steel Production	1,629	1,660	1,631	1,620	-1.9%	-0.1%	0.6%
MBA U.S. Purchase Index	130.8	137.8	131.3	138.4	-5.1%	-0.4%	-5.5%
JRI Same Store Sales Monthly (YoY)	5.5%	5.3%	5.1%	5.6%	0.2%	0.4%	-0.1%
Department Store YOY % Change (MTD)	-0.2%	0.0%	0.0%	0.2%	-0.2%	-0.2%	-0.4%
Initial Jobless Claims	221	218	228	242	1.4%	-3.1%	-8.7%
Continuing Jobless Claims	1,892	1,853	1,888	1,869	2.1%	0.2%	1.2%
N.Y. Fed Weekly Economic Index (WEI)	1.7	2.1	1.7	1.9	-21.8%	-3.5%	-14.9%
U.S. TSA Checkpoint Numbers	2,646,740	2,796,574	2,933,132	2,759,142	-5.4%	-9.8%	-4.1%
Chicago Board Options Exchange (VIX)	14.9	21.9	20.3	18.0	-31.7%	-26.5%	-17.1%
IG Corp. Credit Default Spread (CDX)	47.2	53.0	52.9	51.2	-10.9%	-10.7%	-7.8%

Data as of 11/8/2024. Green denotes positive trend; red denotes negative trend.
Source: Bloomberg Finance, LP

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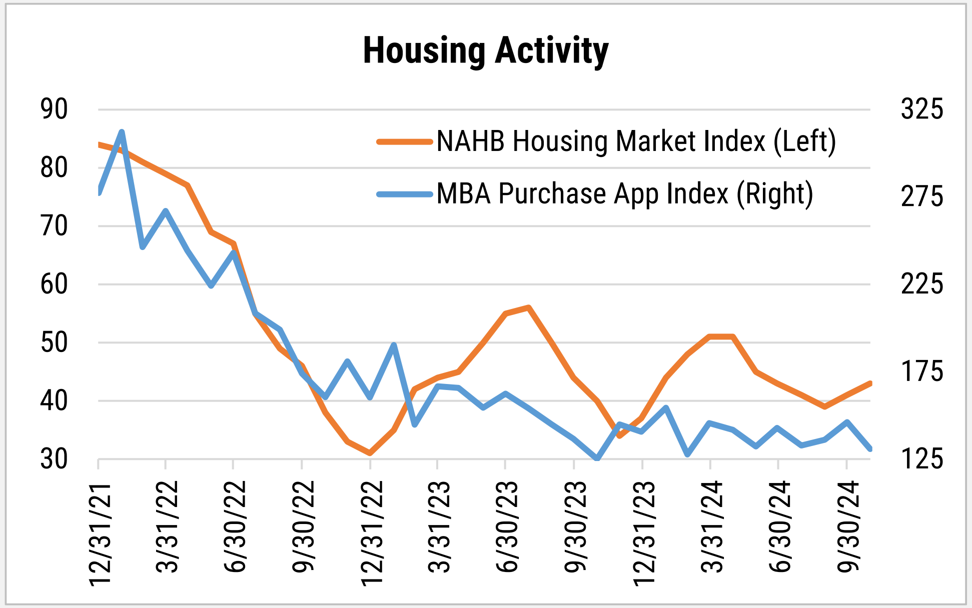
Housing has been the most negatively impacted sector from higher interest rates, and it is unlikely to show lasting improvement without significantly lower mortgage rates. The latest round of housing data confirmed the ongoing stress in turnover rates for residential real estate.

- Existing home sales have fared poorly this year, falling by another 1% in September to a 14-year low of 3.8 million units on an annualized basis.
- The National Association of Home Builders Market Index has languished below the 45 level for the past six months and posted a lackluster 43 reading in September.
- Mortgage purchase applications have taken another turn lower, with mortgage rates climbing above 7.2%. The Mortgage Bankers Association's Mortgage Purchase Index dropped by 5% week-over-week through November 1 to a nine-month low.

Mortgage Applications



Source: Bloomberg Finance, LP

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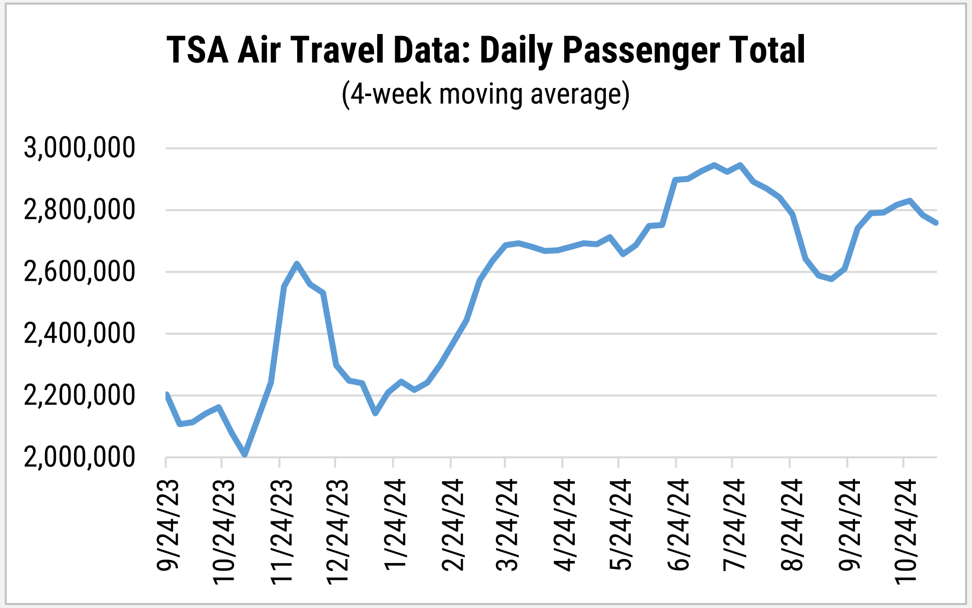
Air Travel By Total Passengers

The daily passenger count for air travelers has averaged 2.7 million in 2024—an 8% increase compared to the same period in 2023 and the strongest ten-month stretch since 2019. Lingering pent-up demand, coupled with low unemployment, has created a tailwind for air travel despite reduced cash reserves and significant economic uncertainty. **Over the past two years, the travel and leisure sector has provided a beneficial boost to the economy and helped to mitigate some of the weakness in the housing and manufacturing sectors.**



Source: Bloomberg Finance, LP

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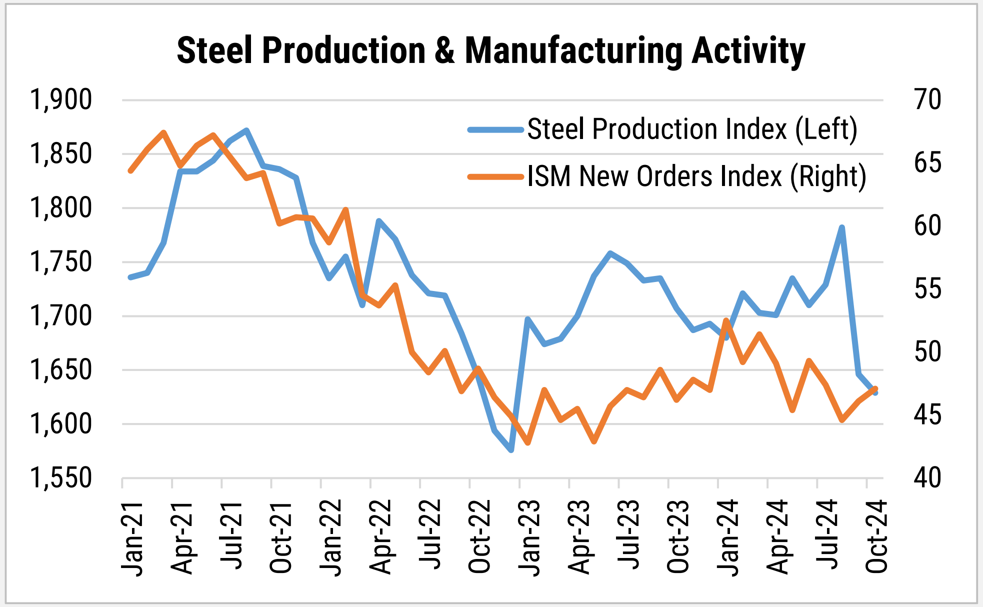
Steel Production

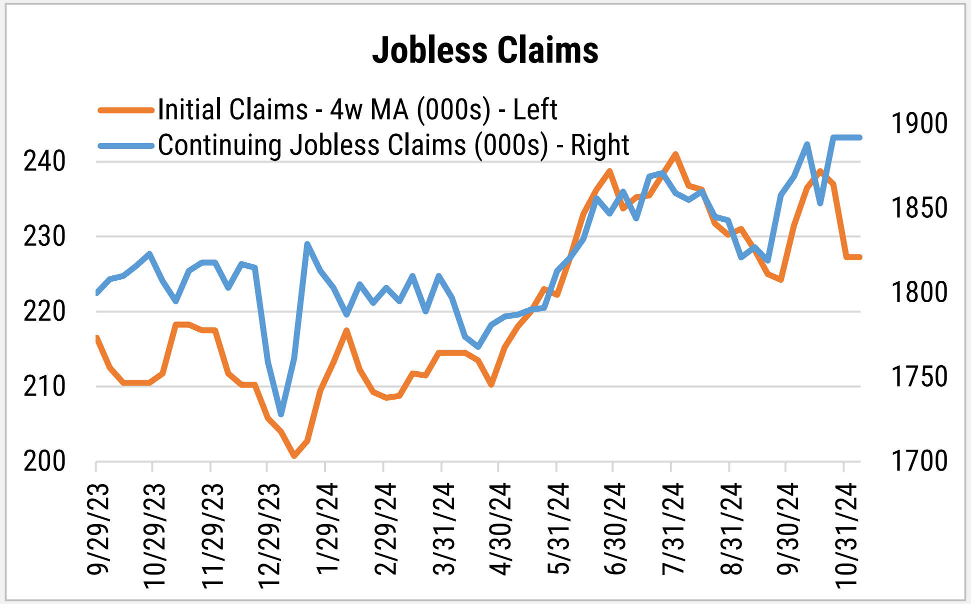
Through the first ten months of the year, the production side of the economy has lagged the services sector by a wide margin, primarily due to elevated borrowing costs and a shift in consumer spending preferences. **The ISM New Orders Index, a key leading indicator of manufacturing activity, has held below 50 for the past seven months, with an October reading of 47.1.** Steel production has dropped sharply given the persistent sluggishness of new orders and tepid end-user demand.



Source: Bloomberg Finance, LP

Jobless Claims

The October Employment Report showed a sharp drop in monthly job creation, with nonfarm payrolls increasing by only 12,000 (consensus 100,000). While this was the lowest monthly gain in nonfarm payrolls since the height of the pandemic shutdown in April 2020, the total was likely suppressed by the two major hurricanes that hit the southeast U.S. in October, as well as the Boeing strike. Compared to the noisy employment report, the weekly jobless claims data may provide a more reliable assessment of current labor market conditions. **Continuing claims have risen by 8% year to date and finished October at their highest level in two years.**



Source: Bloomberg Finance, LP

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Economic Data Review

- Key economic indicators have remained sluggish since the end of the third quarter.
- Housing turnover rates have shown little improvement, given record high prices, locked-in mortgage rates, and limited supply.
- In a sign of persistent strength in consumer services, air passenger volume is running well ahead of last year's pace.
- The production side of the economy has underperformed the services sector by a wide margin, due primarily to elevated borrowing costs and a sustained shift in consumer spending preferences.
- Higher continuing claims, fewer open positions, and slower job creation highlight the recent cooling in labor market conditions.

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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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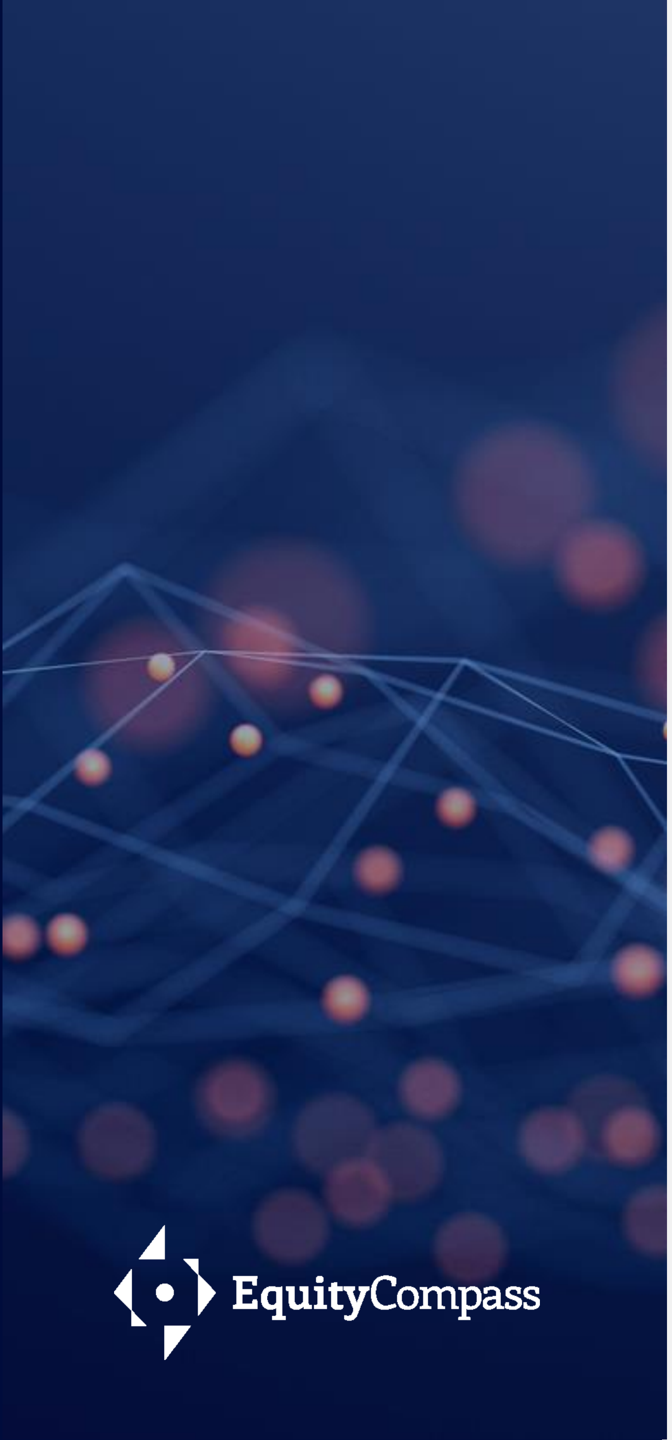


About EquityCompass

EquityCompass Investment Management, LLC ("EquityCompass") is a Baltimore-based equity investment management team that provides portfolio strategies with respect to assets of approximately $5.2 billion.[1]

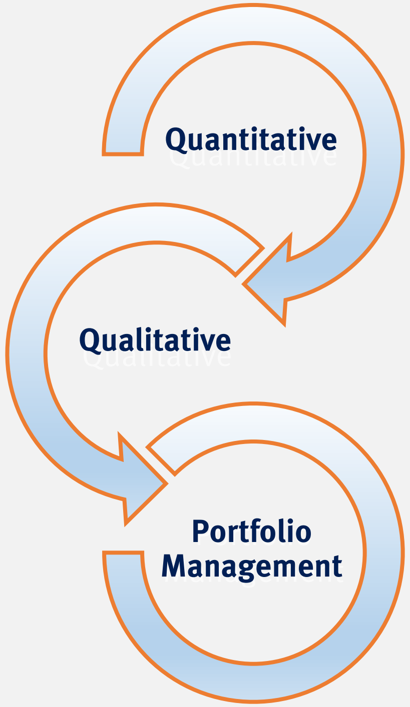
At EquityCompass, our mission as an asset management company is to provide investment solutions that address the needs of clients accumulating, mitigating risk to, and decumulating wealth. We aim to accomplish these goals with an organization culture that prizes intellectual honesty, open dialogue among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