Government Only Managed Account

Quarterly Review

- Most segments of the US bond market lost ground in the fourth quarter, dampening returns for the full year. Although the US Federal Reserve (Fed) reduced interest rates by a quarter-point at its meetings in November and December, which followed a half-point cut in September, investors appeared to focus on Fed Chair Jerome Powell's indication that the central bank may slow its pace of rate cuts in the year ahead. With inflation not yet at the Fed's target and and the potential for the anticipated policies to be pursued under the incoming administration to be inflationary, the number of rate cuts expected to occur in 2025 declined. Whereas the Fed projected as many as four quarter-point rate cuts in 2025 at its September meeting, that number fell to two in December. This shift in expectations weighed heavily on market performance in the quarter, with longer-dated issues experiencing some of the largest losses.
- We believe the combination of an improving growth outlook, together with indications that the Fed would take a less accommodative policy path than investors had previously anticipated, pressured the performance of US Treasurys and other rate-sensitive assets in the fourth quarter. The yield on the two-year note rose from 3.66% to 4.25% (as its price fell), while the 10-year yield climbed from 3.81% to 4.58%. These price moves led to negative total returns across the maturity spectrum, with longer-term issues generally suffering the weakest performance. The Treasury yield curve continued to steepen (meaning the gap between longer- and shorter-dated issues widened), continuing a trend that began in the third quarter.
- Over the quarter we maintained a slight overweight to US Agency. Selection and allocation effects were positive while yield curve effects detracted.

Outlook

- We believe we are currently in the mid-expansion phase of the credit cycle. Our macroeconomic base case is that of a "Soft Landing". Risk assets continued to be well supported by yield-based buyers, with robust demand for new issues, helping to hold credit spreads near historic tights and provide healthy liquidity. Tight credit spreads, strong equity performance, recent Fed rate cuts, with nominal GDP remaining around 5.0% has been supportive of Corporate and Consumer health. However, we have seen some weakness in lower-income consumers, which has led the team to remain in higher quality names that we believe can weather potential economic and policy turbulence. We continued to seek and invest in fixed income asset classes, sectors and names that exhibit potential upside.
- The Federal Reserve (Fed) delivered the expected 25 bps cut in December but policy guidance was hawkish. The Fed focus had shifted from inflation to supporting a cooling labor market. This most recent cut reduced the risk to further labor market cooling, however, inflation risk is now more skewed to the upside. If inflation continues to trend lower we expect there to be 3 additional 25 bps rate cuts in 2025

Important Disclosure

Key Risks: Credit Risk, Issuer Risk, Interest Rate Risk, Liquidity Risk, Prepayment Risk and Extension Risk.

Past performance is no guarantee of future results.

There is no guarantee that the investment objective will be realized or that the strategy will generate positive or excess return.

Commodity, interest, and derivative trading involves substantial risk of loss.
Diversification does not ensure a profit or guarantee against a loss.
Any investment that has the possibility for profits also has the possibility of losses, including the loss of principal.

Market conditions are extremely fluid and change frequently.

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