Core Fixed Income Managed Account

Quarterly Review

- Fixed income markets changed course during the fourth quarter as economic indicators led market participants to believe monetary policy may be easing in the future. Yields changed course and fell through the period. The US 2-Year note yield declined from 5.04% to 4.25%, which was lower than the 4.43% yield observed at the start of 2023. The US 10-Year note yield declined from 4.57% to 3.88%, which was close to the same yield on the 10-Year at the beginning of the year. As economic and corporate data improved during the quarter, risk assets fared well and spreads declined. Asset backed securities did not participate in a risk rally during the quarter as the Bloomberg ABS index showed spreads increased very slightly from 67 to 68 bps. However, other high quality markets experienced tighter spreads. The Bloomberg CMBS index indicated spreads improved 4 bps during the period and closed out the year at 126 bps. Agency mortgages, as measured by the Bloomberg MBS index, declined from 66 bps to 47 bps by the end of the quarter. Corporate bond spreads, as measured by the Bloomberg Corporate index, declined from 121 bps to 99 bps by year-end.
- The strategy remained overweight corporate bonds on a market value basis, which positively impacted performance via allocation effect as spreads contracted during the period. However, negative issue selection more than offset the allocation benefit.
- The strategy remained underweight agency mortgages and this negatively impacted performance as mortgage spreads narrowed during the period. Issue selection was negative in the sector for the quarter.
- Duration continued to be managed in line with the benchmark but duration differences along the yield curve resulted in a positive performance contribution during the period.

Outlook

- The Federal Reserve elected to hold the fed funds rates steady at 5.25% throughout the fourth quarter, although forward guidance shifted from a hawkish to a dovish tone, as inflation surprised to the downside and softer economic data increased the odds of achieving the elusive "soft landing". In our view, the shift in tone caused market sentiment to dramatically reverse course; yields fell sharply while spreads tightened. Yields on the 10-year Treasury peaked at just over 5% in late-October before falling over 110 bps to 3.88% by year-end. Market expectations for any additional hikes seemingly disappeared, while expectations for easing monetary policy rose and were pulled forward into early 2024. Current pricing reflects 150 bps of anticipated cuts in the next 12 months, equivalent to three additional hikes on top of what is reflected in the Fed's Summary of Economic Projections. The yield curve steepened but remained inverted during the quarter, with higher yields on shorter maturity Treasurys relative to longer-dated notes and bonds.
- We continue to hold the view that we are in the late expansion phase of the credit cycle, with a significant probability of either a softer landing or more meaningful slowdown (i.e. downturn) sometime over the next 6-9 months. Corporate balance sheets have deteriorated, but from a very strong starting point; profit margins could continue to be pressured amid higher input costs, tighter credit conditions, and a slowdown in de-leveraging trends. We believe a relatively healthy middle class consumer and resilient labor market should prevent the economy from entering into a severe recession in this cycle.
- We remain concerned about the lagged effects of significant monetary tightening, globally. This has come

through traditional monetary policy tightening, including some central bank asset sales and/or balance sheet run-off, and covers many developed and emerging economies across the globe. Notable exceptions include the Bank of Japan, where policy remains very accommodative, and the Bank of China, where weakness in the Chinese property sector in particular remains a concern, in our view. We also remain concerned about potential exogenous shocks to growth, possibly emanating from the ongoing conflict in the Middle East.

- The strategy's corporate bond risk is currently at the low end of our risk budget, which we believe can provide room to increase risk if valuations and bid-ask spreads improve.

- For strategies that use securitized assets, we continue to favor non-agency spread products such as commercial mortgage-backed securities and asset-backed securities.

- For strategies that use high yield corporate bonds, we continue to have exposure to the asset class with room to add in the event valuations materially improve.

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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