Intermediate Duration Fixed Income 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 the 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.
- The strategy remained overweight corporate bonds which generated positive allocation effects due to spreads contracting. However, adverse issue selection overshadowed the positive allocation effect.
- Duration continued to be managed in line with the benchmark but the strategy experienced a positive performance contribution during the period.

Outlook

- We continue to believe that we are in the late expansion phase of the credit cycle. Our base case scenario remains for a softer economic landing, under which we would expect growth and inflation to normalize toward trend-like rates, allowing the Federal Reserve to proceed at a steady pace towards a long-run neutral rate in the low to mid-3% range. We anticipate that the incoming Trump administration will aggressively pursue its expansionary agenda, and we are watching for changes in trade and immigration policies and their potential impacts on the labor market, growth, and inflation.
- Currently we are constructive on the macro and fundamental backdrop for credit health and corporate fundamentals. Profits remain elevated, and a potential reduction in the corporate tax rate, as well as de-regulation, may provide another boost. Risk assets continue to be well supported, helping to hold credit spreads near historic tights and provide healthy liquidity. However, debt service costs have been rising, despite rate cuts and narrow spreads, and consumer demand could stumble due to a combination of weakness in labor markets, lagged effects of tighter credit conditions, and depleted excess savings. We believe this scenario would negatively impact near term growth expectations, and precipitate a more dovish monetary policy than the approximately 30 bps in rate cuts currently priced in for 2025.
- We are concerned about the growing fiscal burden in the US, potential for retaliatory tariffs, and a significant slowdown in China impacting global growth. We also remain concerned about potential exogenous shocks, possibly emanating out of the ongoing conflicts in the Middle East and Ukraine.
- While the strategy's corporate bond exposure remains overweight on a market value basis, risk relative to benchmark is currently underweight risk largely due to a higher quality bias and shorter maturities than the benchmark. We believe this allows the strategy 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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