

Core Plus Fixed Income Managed Account

MARKETING COMMUNICATION

Quarterly Review

- Within corporate credit, selections in technology, basic industry, and consumer non-cyclical, added value. Within agency mortgage-backed securities (MBS) pass-throughs, the strategy benefitted from being underweight to underperforming Ginnie Maes, and overweight to outperforming lower coupon Fannie Maes.
- Duration positioning was a positive contributor, as the strategy was roughly 1/3rd of a year long versus its benchmark, the Bloomberg US Aggregate Index, giving it more interest rate sensitivity and positive excess returns from the decline in interest rates over the quarter.
- Sector allocation was modestly additive overall. The 9% out-of-benchmark allocation to high yield was a positive contributor to performance over the quarter, as the sector outperformed the benchmark and investment grade credit. However, the decision to underweight agency MBS pass-throughs, the top-performing asset class in the universe, detracted.
- Security selection within securitized credit detracted from overall performance, as holdings in non-agency commercial mortgage-backed securities (CMBS) underperformed.
- Cash and equivalents were a drag on performance over the three-month period.

Outlook

- Fixed income markets delivered a solid positive total return during the fourth quarter as yields declined and the curve bull-steepened, while credit spreads drifted slightly higher but remained near historic tights. The Federal Reserve (Fed) grappled with a break in official data due to the extended government shutdown, as well as risks to both sides of its dual mandate with inflation remaining above target and labor market conditions deteriorating. Monetary policy was eased another 50 bps in the fourth quarter, following the 25 bp rate cut in September, although voting member dissents among Federal Open Market Committee (FOMC) members increased. The Fed Funds Rate target now stands at 3.75%. Markets are currently pricing in only a 50% probability of another cut in the first quarter of 2026, although just over 2 more cuts are priced by year end, 2026. Spread sectors (primarily corporate bonds, mortgage-backed securities, asset-backed securities and commercial mortgage-backed securities) remained well supported with new supply easily absorbed.
- We are monitoring corporate fundamentals, which remain at a healthy level by historical standards. Growth in the first quarter of 2026 may be flattered by higher tax refunds and a reversal of the negative impacts from the shutdown. However, weak corporate pricing power and rising debt service costs suggest margin compression going forward. On the consumer front, we believe that moderating demand for labor, the continued decline in excess savings, and increasing impatience with higher prices are potential catalysts for weaker spending, which may be further exacerbated by higher prices for goods.
- We continue to believe that we are in the late expansion phase of the credit cycle, with growth slowing to below trend, while inflation - which is still above target, should moderate as the effects of tariffs dissipate. While we do not anticipate that the US will enter a recession, we continue to see elevated risk of a downturn scenario. We are concerned that slowing rates of hiring and reduced affordability may weigh more heavily on incomes and consumption. Additionally, the risk of additional Federal Government stimulus leading up to mid-term elections may also add to the growing fiscal burden. This concern has been evident in the still elevated level of term premium in the longer end of the yield curve. Market volatility may remain elevated due to ongoing geopolitical



tensions and interventionism.

- We continue to maintain an “up in quality and price transparency” bias in the portfolio, given our base case view that the economy is more likely to slow than to re-accelerate from current elevated levels. We currently hold roughly 1/3 of the portfolio in US Treasurys. Looking ahead, we expect Treasurys to be supported by slowing economic activity and continued disinflation. Importantly, we have significant liquidity for re-entering spread markets should valuations cheapen meaningfully from current levels.
- During the quarter we reduced overall duration as rates rallied, though we continue to believe that the balance of risks seems to favor lower rates. We are currently roughly 3/10th of a year long on a nominal basis. We continue to favor the belly (5-10 year) of the yield curve, which we believe currently offers a better relative risk/reward in alternative scenarios including a sharper than anticipated economic slowdown.
- We continue to have a modest underweight agency mortgage-backed securities, in favor of more liquid and higher quality US Treasurys, and continue to emphasize favorable convexity and structure through coupon and specified pool selection.
- Within investment grade corporate credit, we remain underweight on both market value and contribution-to-duration measures. However, we do have a bias towards BBB-rated securities, as we believe they offer attractive valuations within a sector where spreads are close to historical tights. We tend to favor industries that have benefitted from higher rates, such as banks and business development companies, and those with favorable demand dynamics such as aircraft leasing companies.
- We have a large overweight to high quality investment grade securitized credit, primarily in the front end of the yield curve, for more defensive, non-corporate carry. We continue to favor higher-rated asset-backed securities (ABS) related to consumer receivables, as well as aircraft-related, automotive rental fleet, infrastructure, and whole loan ABS. We have minimal exposure to commercial real estate.
- Within the plus sectors our allocation to high yield remains at around 10% in total, including roughly 1% in bank loans. We remain at the low end of our historical allocation range in high yield given stretched valuations, and continue to favor front-end, lower spread duration yield.



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