

FIXED INCOME PERSPECTIVES

*A Monthly Strategy Review
of Bond Market Trends and
Economic Developments*

March 2025

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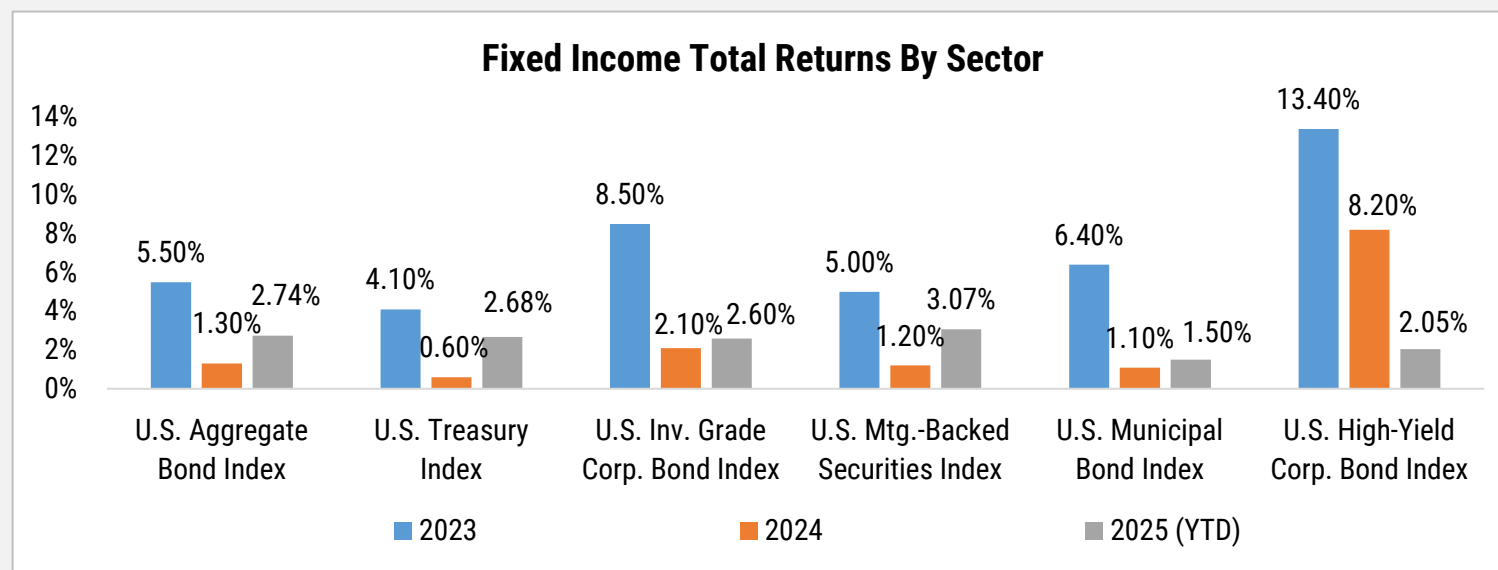
Crosscurrents



Extended periods of outperformance for fixed income relative to equities have been rare in the post-pandemic era, but that scenario unfolded over the first two months of 2025, as investors de-risked by rotating toward bonds. Building on the recovery in fixed income that started in the fourth quarter of 2023, fueled by heightened uncertainty over the U.S. economic outlook, the Bloomberg U.S. Aggregate Bond Index (AGG) generated a year-to-date total return of 2.7% through February. Over the past 16 months, the AGG has produced a cumulative total return of 12.9%. The AGG's year-to-date performance compares favorably to the S&P 500 Index, which gained 1.4%.

Prospects for a third straight year of positive returns in fixed income appear promising, given attractive yields, moderate inflation, and stable monetary policy. While macro fundamentals are currently favorable for the bond market, U.S. trade policy represents a key wildcard for future performance. The scope and timing of tariff implementation could significantly alter the outlook for economic growth, inflation, and Federal Reserve (Fed) policy as the year progresses.

Fixed Income Sector Performance



Returns through 2/28/2025; Fixed income indices provided by Bloomberg; Source: Bloomberg Finance, LP

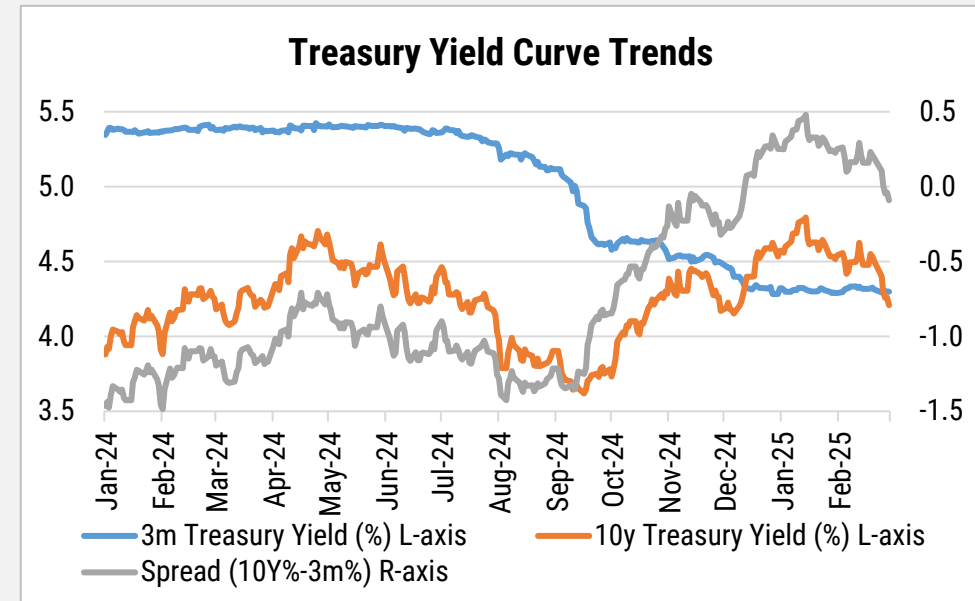


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Amid powerful crosscurrents, Treasury yields have been range-bound over the past three months. The 10-year yield has fluctuated between 4.2% and 4.8%, closing February near the bottom of that range. **A series of weaker-than-expected economic reports, along with an increasingly uncertain outlook, have put downward pressure on bond yields, while lingering concerns over inflation and federal budget deficits have limited the magnitude of the decline in rates.**

After spending 25 months in an inverted state, the yield curve regained a positive slope in December. The yield differential between the 3-month Treasury bill and the 10-year Treasury note widened by 170 basis points (bps) in 2024 to close the year at 0.30%. This measure of yield curve shape lost ground to start the year, closing at -0.09% at the end of February. Absent a sustained bout of stagflation, we expect the trend toward a steeper curve to resume in the near future, as yield differentials continue to normalize. Compared to its 30-year average of 130 bps, the 3-month to 10-year yield spread remains abnormally low.

Treasury Yield Curve



Source: Bloomberg Finance, LP

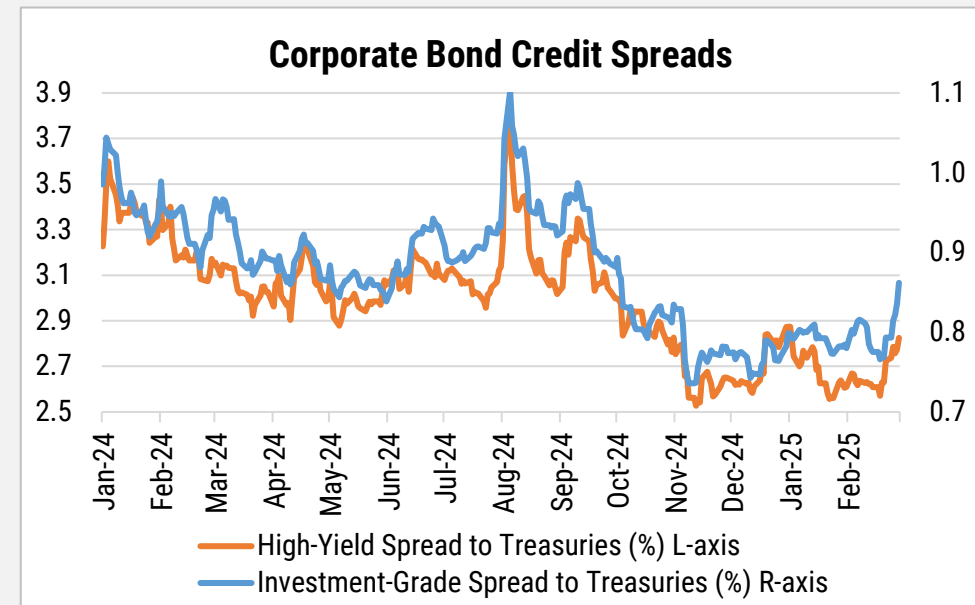


For the past several months, we have noted that corporate bond spreads appeared to be priced for perfection and were vulnerable to a correction if the economy failed to meet the credit market's optimistic assumptions.

Although investment-grade spreads remained abnormally tight at the end of February, they finished the month at their highest levels since early October.

While slightly wider spreads have resulted in modestly more attractive corporate bond valuations, this sector continues to trade at an unwarranted premium to Treasuries, in our view. The risk/reward profile of corporate bonds still appears to be skewed in favor of issuers over investors, which suggests that a larger adjustment in spreads may be needed to rationalize the relative value of company debt.

Credit Spreads

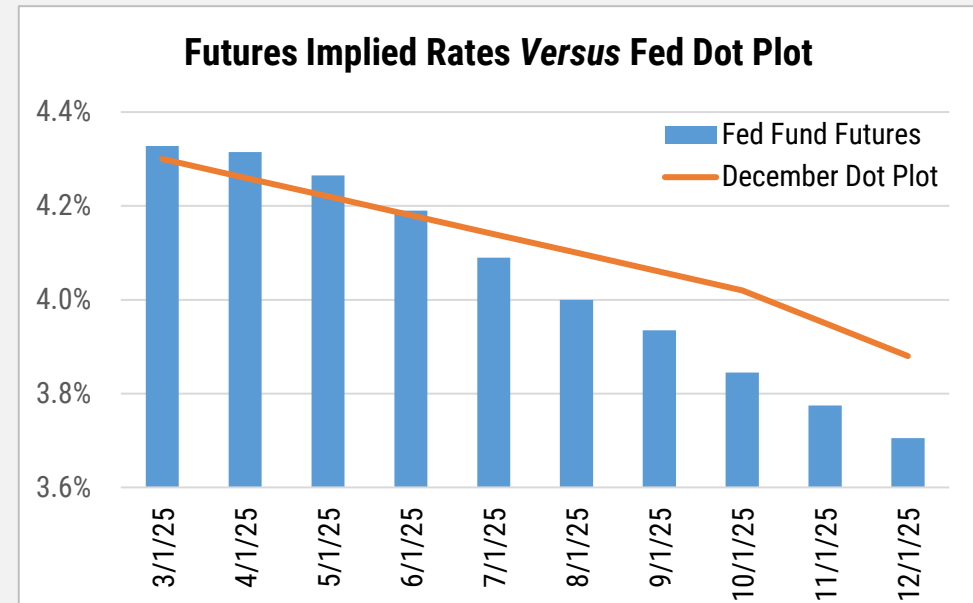


Source: Bloomberg Finance, LP



The minutes from the latest Federal Open Market Committee (FOMC) meeting reiterated the main points that Fed Chair Powell has expressed in his recent public comments. The Fed believes that the economy is close to full employment and is prepared to remain on the sidelines until there is clearer evidence that inflation is trending toward 2% on a sustained basis. The minutes foreshadowed an extended pause in the Fed's campaign to normalize short-term rates and corroborated Powell's assertion that *"we do not need to be in a hurry to adjust our policy stance."* Interest rate futures are somewhat more optimistic about rate cuts compared with the Fed's forward guidance. At month-end, futures were projecting two 25 bps rate cuts in the second half of the year and reflecting 65% odds of a third cut by December. **Assuming the Fed follows the path outlined in its latest "dot plot," the policy range for the overnight funds rate would fall to 3.75% – 4.0% by year end.**

Federal Reserve Monetary Policy



As of 2/28/2025; Source: Bloomberg Finance, LP



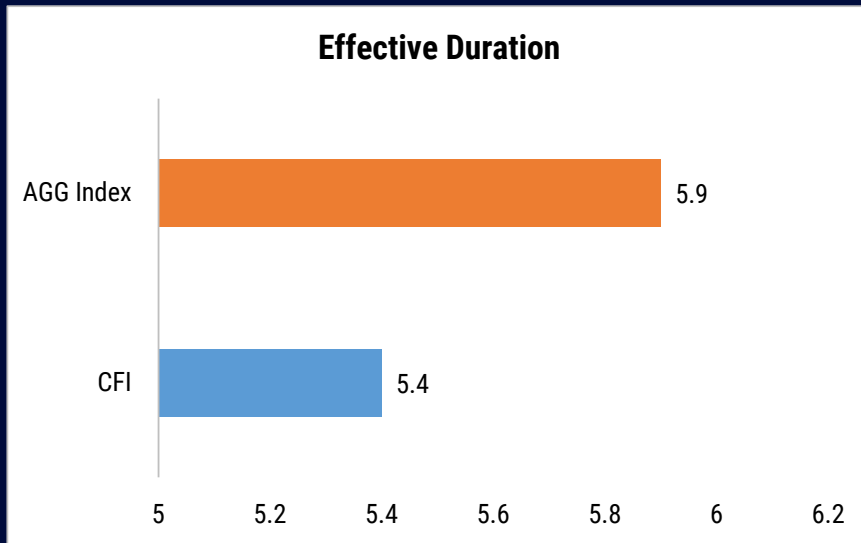
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Core Fixed Income Portfolio (CFI) Statistics

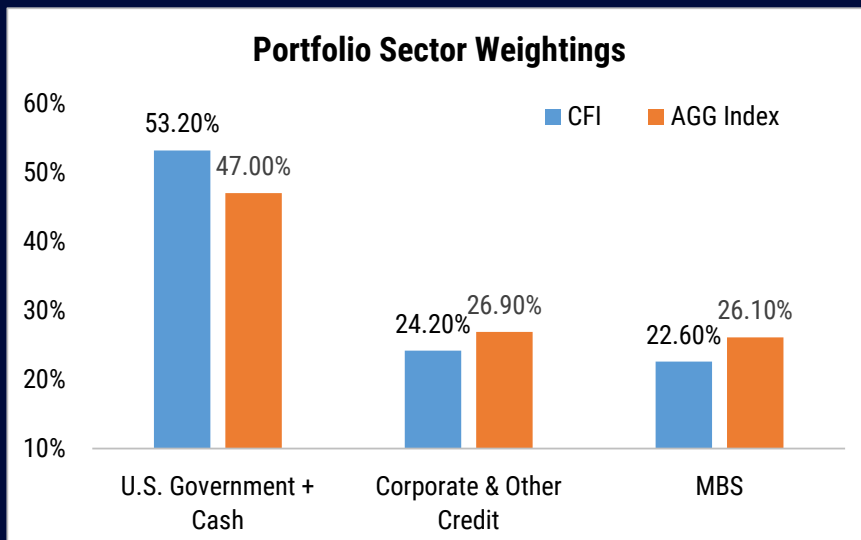
From a strategy perspective, the Core Fixed Income Portfolio (CFI) is structured to address the unique considerations of a Fed rate normalization cycle, which have historically been characterized by steeper yield curves and wider credit spreads. We expect those specific themes to drive the bond market's performance in 2025 and have tailored CFI's investment strategy to address both of those issues.

Compared to the AGG, CFI offers a similar yield, higher credit quality, and a shorter duration. For reference purposes, the yield to maturity of the AGG as of February 28 was 4.6%.

To prepare for a continued steepening of the Treasury curve (lower short-term yields coupled with flat to higher long-term yields), we have set the portfolio's duration at 5.4 years, which is approximately 92% of the AGG's duration. To address the potential risks associated with wider credit spreads, CFI maintains a significantly higher credit quality posture relative to the AGG. Compared to the benchmark, CFI holds an overweight of 620 bps to the combination of Treasuries and cash, with a commensurate underweight to corporate bonds and other sectors with higher risk exposures.



As of 2/28/2025; Source: FactSet Data Systems, Inc. and Bloomberg Finance, LP



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Fixed Income Market Review

- With heightened economic uncertainty permeating the broader financial markets, investors rotated toward bonds over the first two months of the year.
- Guided by strong crosscurrents, the 10-year U.S. Treasury yield dipped to the lower end of its recent trading range, while the yield curve flattened.
- Credit spreads remained low by historical standards but widened slightly during the second half of February on concerns over a potential economic slowdown.
- The Fed signaled an extended pause in its campaign to normalize short-term rates but continued to guide toward 50 bps of additional cuts by year end.
- Amid rich corporate bond valuations and economic ambiguity, the Core Fixed Income Portfolio remained defensively positioned from a credit risk perspective.

The potential for an aggressive U.S. tariff regime to spark a broader and prolonged trade war has complicated an already challenging economic outlook. The incoming data through February has produced conflicting results and failed to provide a great deal of clarity. The monthly reports for January were generally disappointing. In addition, the latest reading on the Conference Board's Leading Index (LI) warns of a potential broader economic slowdown in the first quarter.

Despite those areas of concern, the high-frequency indicators in our Economic Monitor have shown steady improvement in February. In the three-week lookback horizon, the majority of the high-frequency variables have trended in a favorable direction throughout the past month. **Taken as a whole, the preponderance of evidence suggests that the U.S. economy remains generally healthy, though the downside risks are mounting.**

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	488	481	480	479	1.5%	1.7%	1.9%
Raw Steel Production	1,659	1,670	1,675	1,656	-0.7%	-1.0%	0.2%
MBA US Purchase Index	144.3	144.0	153.1	156.7	0.2%	-5.7%	-7.9%
JRI Same Store Sales Monthly (YoY)	5.9%	5.8%	5.3%	4.8%	0.1%	0.6%	1.1%
Department Store YOY % Change (MTD)	2.2%	2.4%	1.5%	0.4%	-0.2%	0.7%	1.8%
Initial Jobless Claims	242	220	214	220	10.0%	13.1%	10.0%
Continuing Jobless Claims	1,862	1,867	1,845	1,886	-0.3%	0.9%	-1.3%
N.Y. Fed Weekly Economic Index (WEI)	2.4	2.5	2.5	2.4	-5.2%	-6.3%	-0.4%
U.S. TSA Checkpoint Numbers	2,593,719	2,394,833	2,186,009	2,331,307	8.3%	18.7%	11.3%
Chicago Board Options Exchange (VIX)	20.1	18.2	14.8	16.5	10.4%	36.1%	21.5%
IG Corp. Credit Default Spread (CDX)	49.6	48.5	46.7	48.5	2.4%	6.1%	2.3%

Data as of 2/28/2025. Green denotes positive trend; red denotes negative trend.
Source: Bloomberg Finance, LP



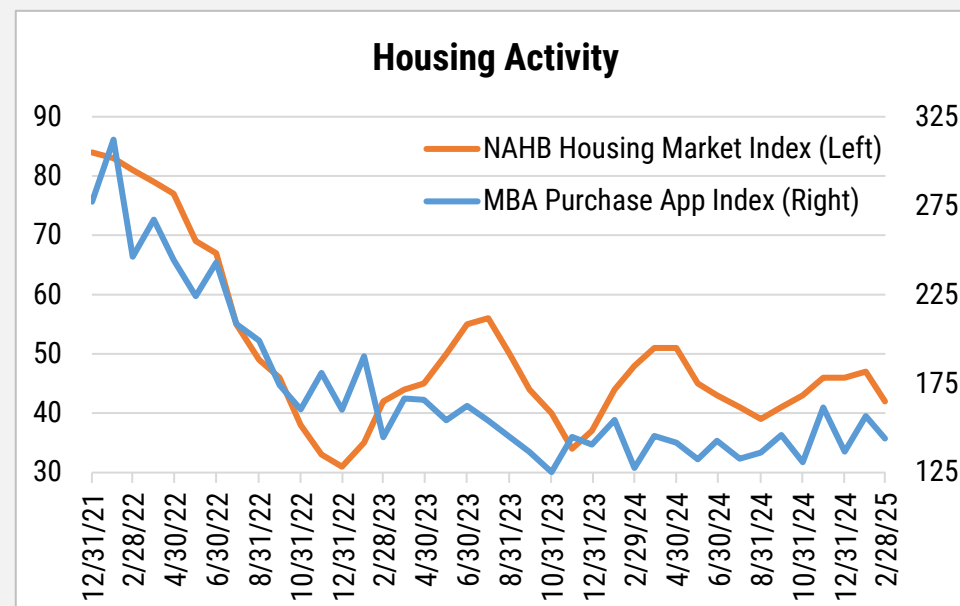
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The latest round of reports on the U.S. housing market reflected the ongoing challenges facing this key economic sector.

The NAHB Housing Market Index for February dropped by 11% month-over-month (m/m) to 42—its lowest level since September. According to the latest survey, two issues topped the list of homebuilders' concerns in the current environment: (1) high mortgage rates and (2) potential tariffs on building materials.

Mortgage applications for home purchases have declined by 11% m/m and remained near 30-year lows. According to Bankrate.com, the average 30-year fixed mortgage rate dipped slightly below 7% this week for the first time in four months. If sustained, lower rates should help to improve affordability and increase turnover rates, but it will take some time before this is evident in the data.

Mortgage Applications



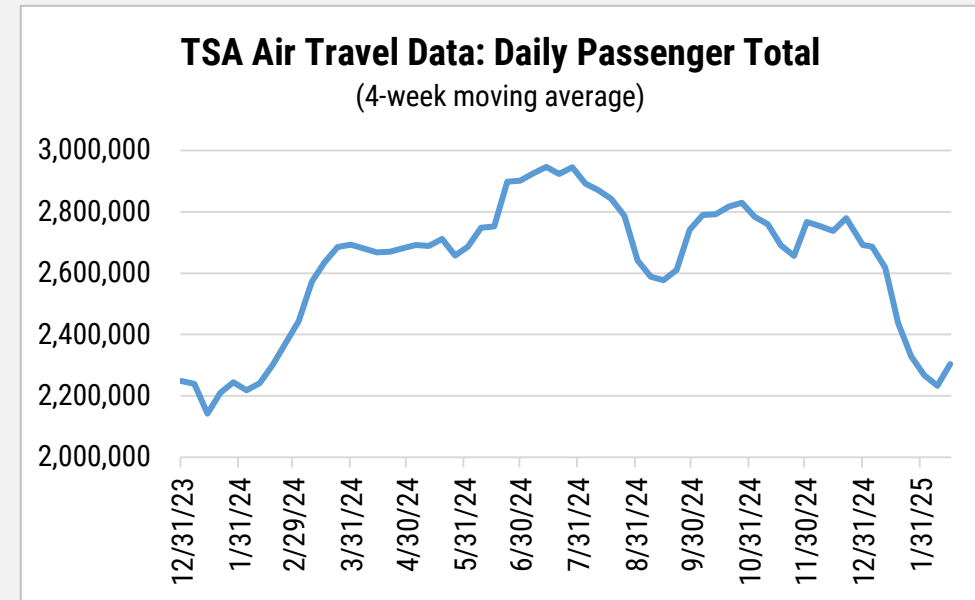
Source: Bloomberg Finance, LP



Air Travel By Total Passengers

Since the pandemic subsided, upper income households have ramped up their spending on services and experiences. Air travel has been a primary beneficiary of this trend, setting a record for total passengers last year. According to the TSA, the daily passenger count for air travelers averaged 2.5 million in 2024, surpassing the previous high set in 2019 by 9%. Through the first two months of the year, air travel volume has been running at a similar pace compared to the same time period last year.

The vibrant travel and leisure sector has provided a helpful boost to the broader economy, offsetting at least a portion of the weakness in housing.

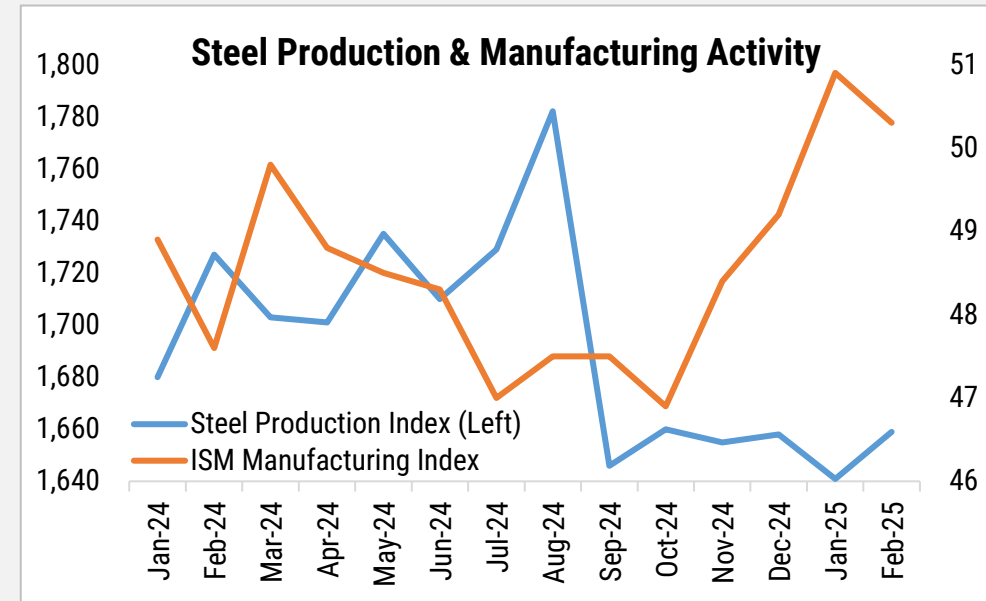


Source: Bloomberg Finance, LP



Over the past two years, 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. **While manufacturing activity remains weak, the latest ISM reports included some constructive data.** For the second consecutive month, the ISM Manufacturing Index showed expansion with a reading above 50. Following January's level of 50.9, the index stood at 50.3 in February. This represents the first two consecutive months above 50 for this key production gauge since September/October 2022. If sustained, this apparent upturn in manufacturing activity should result in stronger steel production over the coming months.

Steel Production

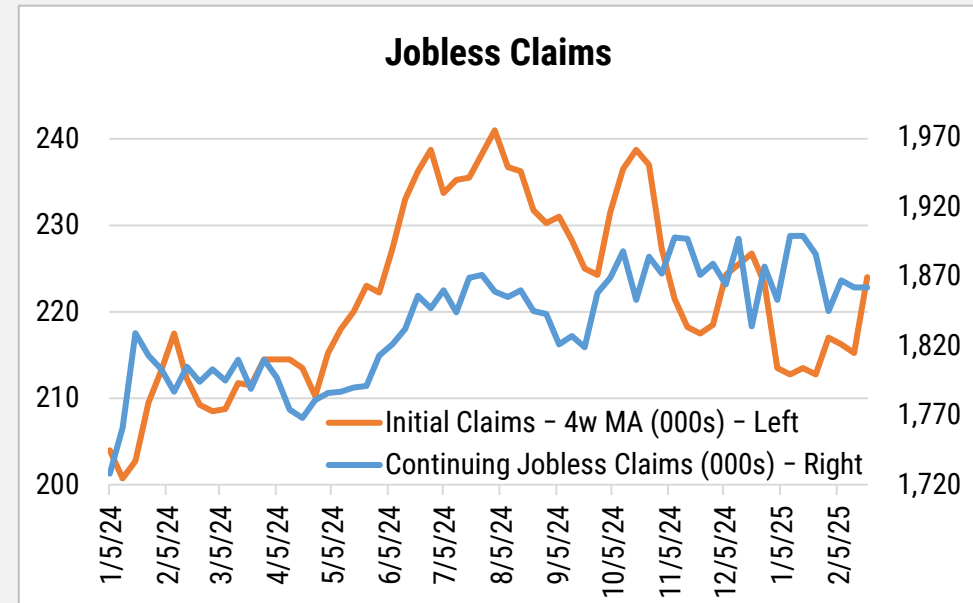


Source: Bloomberg Finance, LP



The unexpected tightening in labor market conditions in the fourth quarter was an important factor in the Fed's decision to pause its rate normalization campaign at the January FOMC meeting. **With the latest round of employment data showing a slight cooling trend on the labor front, the door remains open for further rate cuts later this year, assuming inflation continues to gradually moderate.** While jobless claims have dropped from their recent peaks, both initial and continuing claims have turned slightly higher since the end of January. The combination of rising layoffs, weaker job growth, and slower advances in real wages may curtail household consumption over the next few quarters.

Jobless Claims



Source: Bloomberg Finance, LP



Economic Data Review

- Incoming data for the first quarter has provided mixed results, and uncertainty over U.S. trade policy has clouded the economic outlook.
- Housing remained a weak link in the economic chain, though lower mortgage rates may help to revive this languishing sector as the year progresses.
- Air passenger volume reached a record high in 2024 and maintained a similar pace to last year through the first two months of 2025.
- The production side of the economy underperformed the services sector by a wide margin last year, but manufacturing has shown tentative signs of improvement over the past two months.
- Labor market conditions remained healthy overall, but rising federal layoffs, slower job growth, and softer advances in real wages may restrain household consumption.

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.

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 \$5.4 billion.¹

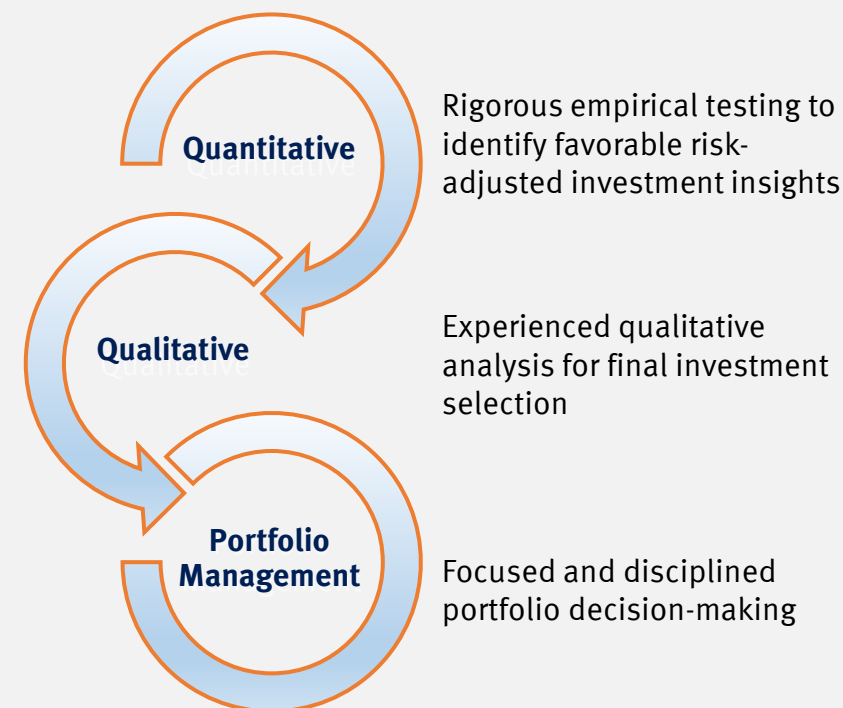
At EquityCompass, our mission as an asset management company is to provide investment solutions that address the needs of clients accumulating, mitigating risk to, and decumulating wealth. We aim to accomplish these goals with an organization culture that prizes intellectual honesty, open dialogue among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



(1) Total assets combines both Assets Under Management and Assets Under Advisement as of February 28, 2025. 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.

Disclosures

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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