Fixed Income Quarterly Commentary

Growth Through Stability

Q1 ▪ 2024

Market Update

The fixed income market spent the first quarter of 2024 stuck between strong economic data and the prospect of the Federal Reserve cutting interest rates later in the year. At the beginning of the quarter, the market was pricing in six interest rate cuts for 2024. After strong economic data and stickier inflation reports, that number is now down to three cuts. The persistent inflation data also moved intermediate and longer treasury yields higher during the quarter, with the 10-year treasury yield finishing at 4.20% compared to 3.93% to start the quarter. This increase in yield weighed on higher rated bonds that are more interest rate sensitive. Lower rated bonds, which are more economically sensitive, outperformed on the strong economic data. The bond market is also wrestling with a supply and demand mismatch in Treasuries, driven by Federal Government issuance to fund deficit spending and weaker demand due to the Fed tapering off the massive bond purchases (QE) from prior years. These two cross currents will likely make Treasury yields more volatile going forward. At AMI, we are somewhat skeptical of the "soft landing" scenario where the economy avoids a recession and inflation falls as consumer spending is showing signs of stress. This has us positioned defensively to avoid the more cyclical parts of the market.

Core Taxable Fixed Income

Core Taxable accounts finished with positive returns in the first quarter and generally outperformed the index that returned -0.06%[1]. The outperformance was primarily driven by taxable municipal bonds, which outperformed other government bonds during the quarter. Portfolios also benefited from outperformance in corporate bonds, which were buoyed by some of the stronger economic data points in the first quarter.

Municipal Bonds

Municipal accounts were relatively flat in the first quarter, generally outperforming the index that was down -0.31%[2]. The increase in Treasury yields hurt most municipal bonds, with the longer maturity bonds underperforming shorter bonds, a reversal of last quarter. Callable bonds drove the outperformance relative to the index due to their higher yield. At AMI, we continue to focus on essential services (water, sewer, and electric) and Mello-Roos bonds (backed by property taxes) with clear cash flows and low pension liabilities.

High Yield Fixed Income

High Yield accounts posted positive returns during the first quarter and outperformed the index that was up 1.26%[3]. The primary driver of the outperformance was due to being overweight floating rate bonds and financials. We remain cautious on the economy and are positioned for an economic slowdown with a focus on higher quality bonds that should be less sensitive to a recession.

<u>Disclosures</u>

AMI Asset Management (AMI) is an independent investment management firm registered with the Securities and Exchange Commission since 1994. Registration does not imply a certain level of skill or training. AMI provides discretionary asset management services to institutional and individual clients through separately managed accounts using seven equity and fixed income strategies.

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1. Figures presented on page one are from the ICE BofAML 1-10 Year US Corp and Government Index as of 3/31/24

2. Figures presented on page one are from the ICE BofAML 3-7 Year US Municipal Securities Index as of 3/31/24

3. Figures presented on page one are from the ICE BofAML 1-10 Year US High Yield BB-B Index as of 3/31/24