

Fixed Income Quarterly

Market Perspectives from Fixed Income Solutions

Achieving Your Income Goals

There is no shortage of debate over the economy. How many cuts will the Fed execute this year? Will there be a recession? Soft landing? We debate over job reports from their accuracy to relevance concerning underemployed or semi-forced retirements. Debates ensue regarding fiscal versus monetary policy resolve. One of the few bipartisan concerns is the recognition that government debt is too high, although we dispute solutions.

What we do know, which warrants no debate, is that this controversy has buoyed market volatility and elevated fixed income yields. Investors seeking income should benefit simply by incorporating the market's higher yields into the fixed income portion of their investment portfolios.

“Investors seeking income should benefit simply by incorporating the market's higher yields into the fixed income portion of their investment portfolios.”

concerning fixed income's ability to help preserve portfolio principal; however, allocation choices now boast improved levels of income. Understanding the process and revealing applied strategies may trigger thoughts concerning your financial situation. Personal strategies using individual bonds are tailor-built, of independent design, and created to produce unique results for every individual.

This quarterly newsletter provides individual bond portfolio construction ideas geared toward reaching long-term goals. A lot has been said about the elevated yield curve and the opportunities it presents. We will dive deeper into how to capture this income with portfolio assets dedicated to individual bonds. Nothing changes

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IN THIS REPORT

Strategic Investing (pg 2)

The Steps to Strategic Portfolio Allocation (pg 3)

Federal and State Taxes Matter in Tax-Exempt Situations (pg 7)

It's Not Only in the Name (pg 8)

Tactical Corporate Play (pg 9)

Know What You Own (pg 10)

Strategy Resources (pg 11)

STRATEGIC INVESTING

Terminology within the finance world can get complicated, especially for the passive or uninterested investor. The lack of attention or understanding could impact financial preparation and/or portfolio strategy and thus one's retirement or lifestyle. Conversely, appropriate financial preparation and strategizing can foster positive differences for your financial future.

Two distinct classifications are associated with investing objectives: tactical and strategic. Tactical investing attempts to capitalize on market inefficiencies, look for short-term opportunities, time market entry spots, and/or outdo benchmark performances with a total return focus. Tactical investing is proactive and can involve quick-changing market positioning.

Strategic investing aligns portfolio holdings based on long-term planning with no required day-to-day reallocation due to data releases or market events. Most conservative investors, including those who have a portion of funds dedicated to tactical investing, practice strategic investing on some level. These investors share the goal of long-term planning and preserving hard-earned wealth. Focus is often on income, cash flow, and principal preservation, consequently deemphasizing total return. Preserving wealth takes precedence over potential quick-hit opportunities which may bring sizeable returns although also carry additional risk.

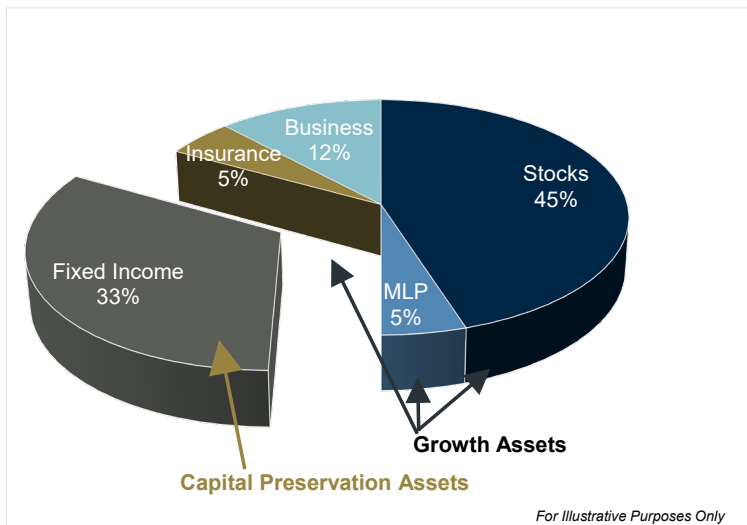
When you hear comments in the media like, "Bonds are down – they are having a terrible year." The connotation is negative and the statements can create the image of a scary path ahead for individual bondholders. The meaning of the quote reflects that Treasury bond prices have dropped precipitously since the start of the year – but what often goes unsaid is that it also means that yields have risen accordingly. So although it may be the 3rd worst yearly start for Treasury prices, at the same time it is also the 3rd best yearly start for Treasury rates. Total return or tactical investors will likely view this differently versus strategic, long-term income investors. Total return investors' short-term market plays are negatively impacted because prices have dropped. Long-term income investors, who often hold their bonds to maturity, are unaffected because they don't realize the consequences created by short-term pricing. Bonds held to maturity continue to produce the same cash flow and income as they did from the purchase date and they are not altered by pricing changes as long as the bonds remain in the portfolio.

Furthermore, strategic investors may see the drop in Treasury prices as an opportunity to lock in desirable high levels of income. This window of income opportunity is one we continue to promote as we have not seen yields like the bond market currently boasts in nearly 17 years. It can be difficult to differentiate tactical and strategic messaging, particularly given that tactical or total return messaging seems to dominate the industry's communications. Focus on the purpose of investments dedicated or allocated to individual bonds. They are often dedicated to preserving wealth which implies long-term strategic planning.

Much of this quarterly newsletter is dedicated to steps in constructing a strategic portfolio allocation.

THE STEPS TO STRATEGIC PORTFOLIO ALLOCATION

One of the main advantages of constructing a portfolio of individual bonds is that it can be customized to meet the precise needs, goals, and objectives of an investor. While this approach allows for an investor's personal preferences, it requires some upfront consideration and analysis to ensure that the portfolio is in sync with an investor's goal and objectives. The following sections, which often overlap, discuss important product-choice and portfolio-building issues as they pertain to personal circumstances when constructing a customized fixed income portfolio.



OBJECTIVE

Portfolio dollars can be allocated to growth assets, such as stocks, or to conservative assets that help preserve wealth, such as individual bonds. The first step in governing the dollars dedicated to individual bonds is to identify investor intent. Is there a tax bill that needs to be paid next year due to the sale of a business? Is this money intended to be a short-term cash alternative with regulated liquidity? Is retirement dictating monthly or annual cash flow needs? How does a desired lifestyle influence the strategy? Is this a long-term buy-and-hold strategy

meant to provide stability for the portfolio as a whole?

The number of potential objectives can be infinite as they vary from investor to investor; therefore, identifying the "why" ensures that investment choice aligns with portfolio goals. It may not suffice to merely earmark a certain dollar amount or percentage of the portfolio to fixed income without understanding an investor's long-term strategic goal. Front-end planning may reveal unique bond characteristics, such as a defined redemption date or fixed cash flow streams, and thus assist with appropriate investment choices.

LIQUIDITY NEEDS

Long-term strategic planning may include near-term or long-term liquidity needs. Does a qualified account require a minimum annual distribution? Do venture considerations, such as those of a real estate investor, necessitate access to capital over the next few years? Will retirement reshape cash flow needs? Perhaps a dream boat purchase compels a specific time-horizon for available funding. Would you like to pay for your grandchild's college tuition in 15 years? Front-end discovery can help ensure that money will be available when needed.

Maturity		
Average Maturity 7.8 yrs		
Year	Curr Face	%
2024	250,000	27.2%
2025	125,000	13.6%
2026		
2027		
2028		
2029		
2030		
2031		
2032		
2033		
2034	100,000	10.9%
2035	80,000	8.7%
2036	95,000	10.3%
2037	80,000	8.7%
2038	90,000	9.8%
2039	100,000	10.9%
2040		

Liquidity (2024-2033)
Core (2034-2039)

For illustrative purposes only. Example 10-15yr core ladder for investors also needing short-term liquidity.

An individual bond's defined maturity date is unique versus other investment vehicles. It provides a specific date when its face value will be returned to the investor. This allows precise planning to match liquidity needs with maturing bonds. Other "fixed income" packaged products do not provide this level of transparency into the future. Products without maturity dates rely upon market pricing at the time of a sale or liquidation, and therefore the amount of money available on a specific future date is unknown. Liquidity needs may fluctuate making the adaptability of individual bonds a solid choice.

TAX BRACKET

Knowledge of federal and state tax brackets supports a well-intentioned tax-efficient investment approach.

High-earning top-tax bracket investors nearing retirement may be approaching a tax-changing event affecting long-term planning. Investors moving to a different state may encounter changing tax consequences. Optimizing take-home earnings involves investment choices evaluated on an after-tax basis. After all, it isn't how much you make, it is how much you get to keep.

Various fixed income products have a range of tax considerations to consider

in tandem with personal tax situations. Most municipal bonds are exempt from federal taxes, which can lift after-tax income levels especially for high-tax bracket investors. Moreover, municipal bonds issued from an investor's tax-filing state are often exempt from state taxes as well (there are some exceptions to this).

U.S. Treasury bonds possess an often-overlooked tax-exempt feature asserting not being subject to state income taxes. Investors residing in states with a high state income tax may have a considerable advantage in buying Treasuries versus fully taxable products. This potential benefit is highlighted in the chart, which

	Yield	After-Tax Yld*
Brokered CD	5.00%	2.49%
Treasury	5.00%	3.15%

**37% Federal Tax Bracket + 13.3% State Tax Rate;
For Illustrative Purposes Only*

compares a brokered CD and a Treasury with identical nominal yields. Assuming an investor is in the top federal tax bracket (37%) and the top California state income tax bracket (13.3%), the after-tax yield for the Treasury is ~65 basis points higher than that of the brokered CD due to the Treasury avoiding the California state income tax.

While this is an extreme example by using the state with

the highest income tax rate, it emphasizes the importance of considering taxes for even the least complicated investments.

To reemphasize, take-home (after-tax) earnings are what matters. Avoiding taxes with in-state municipal bonds might not get the best after-tax return for an investor if the state tax rate is low or availability is limited. Investors in low federal tax brackets often do not markedly benefit from tax-exempt products which may offer minimal "tax savings". It often is the case that a taxable alternative, even after paying taxes, will optimize a low federal tax bracket investor's return. This means that earning \$1,000,000 and paying \$200,000 in taxes is better than making \$700,000 and paying no taxes.

Municipal 3-10yr Laddered Portfolio						
	Cpn	Avg Price	Avg Maturity	YTW	Tax-Equivalent YTW	
NY taxpayer; Fed tax=37%, NY tax=10.90%	4.56%	105.13	6.89yrs	3.20%	6.140%	
FL taxpayer; Fed tax=37%, FLtax=0%	4.56%	105.13	6.89yrs	3.20%	5.080%	

Sources: Tradeweb Portfolio Solutions portfolio - for illustrative purposes; Raymond James; as of 5/14/24

The same portfolio composed of New York-issued tax-exempt bonds benefits the New York resident more than the Florida resident since New York has a high state tax but the New York investor will not pay it due to a residence's in-state exemption.

CASH FLOW

Another unique characteristic of individual bonds is their known stream of cash flows. Will cash flow needs remain static? A \$100,000 face value bond with a 5% coupon returns \$5,000 in cash flow every year until the bond matures (barring a default). A defined cash flow stream can be influenced by purchasing smaller or larger coupon bonds, thus matching an investor's specific cash flow needs. For example, a retiree may be planning to replace their salary with a steady cash flow stream obtained by choosing bonds with specific coupons.

Cash flow needs may also influence the maturity structure of a portfolio. The maturity of a specific bond may coincide with a desired cash demand on that date. Alternatively, a portfolio may be designed to generate a certain amount of cash flow through interest payments combined with maturities. There is no right or wrong methodology as different strategies will work for various investors with dissimilar needs.

Corporate 6-10yr Laddered Portfolio							
	Cpn	Avg Price	Avg Maturity	YTW	Annual Cash Flow	Market Value	Face Value
High Coupon Investment-grade Corporate Portfolio	6.89%	108.45	8.06	5.46%	17,225	275,410	250,000
Low Coupon Investment-grade Corporate Portfolio	2.60%	80.96	8.11	5.55%	8,703	273,906	335,000
<i>Sources: Tradeweb Portfolio Solutions portfolio - for illustrative purposes; Raymond James; as of 5/14/24</i>							

Both portfolios have similar maturities and yields with roughly the same amount initially invested; however, the low coupon discount portfolio has a much greater face value. If all things remain equal, both portfolios invest the same amount and will ultimately receive close to the same (slight yield difference) amount of cash flow + principal return as they mature. The low coupon portfolio will receive less cash flow during the holding period and a greater chunk at maturity while the higher coupon portfolio will produce a higher cash flow with less principal at maturity.

RISK TOLERANCE

There is a range of considerations in determining an investor's appropriate risk level. While not all-inclusive, here are a few of the more significant fixed income risks:

- **Credit risk** is usually recognizable and likely to be one of the first risks that come to an investor's mind. This risk measures an entity's ability to meet its financial obligations such as paying interest or returning borrowed funds. An inability to meet financial obligations corresponds to a company's *default risk*. Credit risk is personal and important towards identifying product choice. Fixed income options span a wide range of credit risks, including products with little credit risk (Treasuries or FDIC insured-brokered CDs), minimal credit risk (investment-grade corporate or municipal bonds), or higher levels of credit risk (junk bonds). There is likely an investment vehicle that meets nearly every investor's need.

Moody's S&P	Issuer	Coupon	Maturity	Yield
5-Year Maturities				
Aa2/AA-	Chevron USA Inc	3.250%	10/15/2029	4.798%
Baa2/BBB+	Ryder Sys Inc.	5.500%	6/1/2029	5.384%
10-Year Maturities				
Aa3/AA-	Proctor & Gamble Inc.	5.800%	8/15/2034	4.751%
Baa2/BBB	Marriott Intl Inc.	4.500%	10/1/2034	5.671%
<i>Sources: TradeWeb Portfolio Solutions, Raymond James; as of 5/14/24</i>				

For illustrative purposes only.

There is a 59-basis point pick up between the AA-rated and BBB-rated five-year offerings. The pickup in yield jumps to 92 basis points on the 10-year offerings. The five-year default rate (according to Moody's Investors Service) for Aa corporate issuers is 0.01% and 1.88% for BBB-rated issuers. Another way to view is that 99.99% of Aa and 98.12% of BBB issuers do not default. Individual investors can assess whether that risk is worth the additional yield pickup.

- **Reinvestment risk** is often overlooked but may significantly affect long-term portfolio returns. When interest rates drop during an investment's holding period, coupon payments and eventually returned principal must be reinvested into a lower-yielding rate environment. While this risk can never be eliminated, a portfolio can be structured to align reinvestment risk with current market outlooks. Many investors in today's environment are opting to extend maturities to reduce reinvestment in the short term since there is a consensus that interest rates may go lower. Theoretically, investors benefit from higher yields associated with longer maturities, avoid short-term reinvestment into a likely lower rate environment, and eventually benefit when securities mature later by having an open choice dependent upon the future interest rate environment.
- **Interest rate risk** happens when interest rates rise in the future, and the value of current bond holdings falls. Conversely, if future rates fall, current bond-holding values will rise. When investors desire or need to sell a bond prior to its maturity, a bond's market value is dependent upon the market price at that point in time. Interest rate risk is not germane when investors plan to hold bonds to maturity. Market prices are irrelevant (never realized). As a bond approaches its maturity, its price gravitates to par.

An investor's control over a portfolio of individual bonds compared with that of a packaged product can be a significant advantage in ensuring that the portfolio meets a specific set of needs while staying within desired risk parameters.



Reinvestment risk and interest rate risk are a tradeoff. When investing short, reinvestment risk increases as reinvestment occurs quickly or more frequently. Thus, investors are subject to brief market moves and the possibility that reinvestment won't match holding yields. Conversely, when investing for longer periods (longer maturities), investor holdings are subject to a longer period of which the value of that holding can fluctuate.

** The authors are not tax experts and do not intend to provide any tax advice. All strategies should be reviewed with a tax professional prior to making investment decisions.*

FEDERAL AND STATE TAXES MATTER IN TAX-EXEMPT SITUATIONS (An excerpt from the May 8 Municipal Bond Investor Weekly - authored by Ted Ruddock, Managing Director, Head of Fixed Income Private Wealth)

Although certain states are popular moving destinations, particularly those with low or no-income tax, nearly 80% of the estimated 39 million Americans relocated within their current state of residence, according to the Census Bureau. (2022 American Community Survey, <https://www.census.gov/programs-surveys/acs/>)

More people are moving within their home states or to a neighboring state versus “region hopping.” Take New York, for example, a state often cited for losing population. It’s true: more people are moving out (~545k) versus those moving in (~301k) with a net negative migration of approximately 244k, or ~1.1% of the state’s population. However, more New Yorkers moved to the neighboring states of Pennsylvania (~45k), Connecticut (51k), Massachusetts (21k), and New Jersey (75K). The total of ~192,000 movers is more than two times the number of New Yorkers who moved to Florida (~91k). Here’s something else not frequently reported: over 30k New Yorkers left the state and moved to California enduring potentially higher taxes!

“...moving can have financial implications for clients, particularly to their municipal bond portfolios.”

The takeaway is that moving can have financial implications for clients, particularly to their municipal bond portfolios.

Take the example of a client moving from New York City to neighboring New Jersey. The client was in the top federal bracket and subject to New York state and city taxes. Their existing municipal portfolio was a 1 – 10-year ladder, comprised entirely of tax-exempt New York bonds with a yield-to-call of 3.67% and yield-to-maturity of 3.92%. The taxable equivalent yields to the call and maturity are 8.26% and 8.82%. If the client moved to New Jersey, the New York bond issues no longer benefit from in-state tax exemption lowering the taxable-equivalent YTC/YTM to 6.25%/6.69% - a significant 200+ basis point reduction.

		Taxable-Equivalent			
		YTC	YTM	YTC	YTM
Pre-Move	NY bonds in NY	3.67	3.92	8.26	8.82
Post NJ Move	NY bonds in NJ			6.25	6.69
State Tax-Rebalancing in NJ Bonds		3.67	3.92	7.57	8.09
<small>Sources: Tradeweb, Raymond James; Federal 37%, State NY10.9% - NJ 10.75%, NIIT 3.8%</small>					

For Illustrative Purposes Only

Selling the existing New York portfolio and repositioning into New Jersey bonds is a more tax-efficient solution and more closely replicates the taxable-equivalent yield of the original portfolio. With all the bonds now exempt from state and local taxes the taxable-equivalent YTC/YTM is 7.57%/8.09%, more than 150 basis points higher than the New York portfolio subject to New Jersey taxes.

Life changes, such as moving, can affect certain bonds within the portfolio. Consult with your financial advisor to review holdings whenever your circumstances change.

IT'S NOT ONLY IN THE NAME

Fixed income is an instrument suited to preserving wealth while providing cash flow and income. A strategic long-term investing approach can be instrumental in achieving these objectives. This strategic foundation lends itself to prioritizing the preservation of capital through high-quality investment-grade credits. This may be especially essential for those in the retirement phase of their life.

Household Names

The corporate bond sector has benefitted from the recent high-interest rate environment boasting yields not obtainable for nearly 17 years. Many investors gravitate towards names/brands that they are familiar with and the ability to custom design a portfolio based on an individual's specifications is one of the features of an individual bond portfolio. Whether those specifications require specific names, desired durations, or certain cash flow provisions – it is likely achievable. Although familiarity with a name may be comforting, there is a possibility that similar unfamiliar issuer names may offer higher yields.

Grading Bonds

The school grading system inflicts familiarity as it is ingrained throughout our education during our formative years. It may imply that a "B" grade signifies a satisfactory performance but with room for improvement. This stance does not necessarily translate accurately with financial credit ratings and avoidance of BBB credits can constrain diversification and reduce yields. Approximately 52% of investment-grade issuers are rated in the "BBB-category". This represents roughly 28% of all corporate issues (per Moody's 2023 data). BBB companies have demonstrated resilience over time boasting relatively low default rates. Although (according to Moody's Investor Service data) one-year cumulative BBB-rated issuers possess three times the default rate of A-rated issues (0.15% vs. 0.05%) this is statistically insignificant. Another way to look at this is to say that over roughly the past 50 years, 99.95% of A-rated issuers and 99.85% of BBB-rated issuers did not default. It should be noted that the default percentages become more meaningful when credit ratings dip below investment grade.

Corporate Bonds

Corporations often raise capital through the bond market to sustain operations, promote research, and grow. Choosing companies based solely on one criterion, such as familiarity or credit rating can impact portfolio returns. BBB-rated bonds are regarded as high-quality credits and typically provide improved returns versus A-rated bonds. The avoidance of BBB bonds could potentially hinder the construction of an optimal, long-term strategic bond portfolio. Therefore, it may be impactful to reassess preconceived notions about credit ratings and their implications for investment decisions with a more balanced and diversified portfolio that better aligns with strategic long-term investing.

TACTICAL CORPORATE PLAY

Instinctively, investors may strive to receive a “good deal” but this encompasses subjectivity. “Good” can refer to price, quality, quantity, creditworthiness, etc. Whether an investor’s goal is strategic or tactical may also slant sentiments. Turning the page on the previous articles focused on long-term strategy, let’s examine a potential tactical (short-term/total return) situation embedded in the current interest rate curves. The graph



Source: Bloomberg LP

tracks BBB-rated (white line) and A-rated (orange line) corporate bond yields over the past four years. Bond yields are higher than at any other time over the past two decades, except for two brief periods in the fourth quarters of 2022 and 2024.

The pandemic created disorder and unpredictability among various markets, including the corporate sector. Investment-grade corporate bond yields hit lows in 2020 – 10-year BBB-rated yields were ~1.92% and A-rated yields were ~1.43%. Amazingly, yields are almost 400 basis points higher now. BBB-rated 10-year corporate bonds have averaged a 4.10% yield over the past four years. During that same period, A-rated corporate bonds averaged a 3.60% yield. Today, A and BBB corporate yields are 150 basis points higher than the four-year average yield. Albeit the current yield is not at the peak of this yield range, it remains a favorable time to buy bonds.

The recent move in spreads (the margin between a corporate bond and a corresponding Treasury bond) has sparked a potential tactical play for investors. The relationship between A-rated and BBB-rated corporate spreads has narrowed. The spread was as wide as 76 basis points in July, 2022. While the average spread between the two ratings over the last four years has been around 50 basis points, the current spread is roughly 37 basis points. Historical patterns suggest that there could be a regression to the mean and A-rated bonds will eventually outperform BBB-rated bonds. Although buy-and-hold investors should maximize yields with credit-appropriate yields, there may be increased confidence in the additional measured creditworthiness of an A-rated versus BBB-rated holding.

For example, take a 10-year BBB-rated bond and a 10-year A-rated bond with the same maturity. The yield is 5.71% for the BBB-rated bond and 5.34% for the A-rated bond for a spread of 37 basis points between the two. If the spread regresses to the mean (50 basis points) and the BBB-rated bond remains the same, the yield on the A-rated bond will move to 5.21%. This would equate to a 1-point gain in price (1%) or a \$100 increase in value for every \$10,000 of face value.

KNOW WHAT YOU CAN OWN

Most individual bonds provide investors with a few prominent features that are difficult to find in other product types, most notably: known cash flow for the life of the security, known income (yield) at the time of purchase, and a known date when the principal will be returned. While most individual bonds provide these benefits to investors, there are many types of individual bonds, each having different features and applications within a portfolio. As an investor, sometimes it's difficult to know which product is most appropriate for a particular situation. Below are listed attributes that may illustrate how various products

might work within a portfolio. Identify acceptable risk factors.

- ✓ Define desired income.
- ✓ Create required cash flow.
- ✓ Identify the requisite redemption period.
- ✓ Create needed liquidity.
- ✓ Isolate personal biases.
- ✓ Use appropriate asset mix.
- ✓ Diversify.
- ✓ Rebalance when applicable.

	PRODUCT ATTRIBUTES	HOW DOES THIS FIT?	ADDITIONAL CONSIDERATIONS
TREASURY	Minimal credit risk. State and local tax exempt.	Can I benefit from the state tax exemption? Am I seeking safety and liquidity over maximizing yield?	Although credit risk is minimal, market risk increases with lengthening maturity.
CERTIFICATES OF DEPOSIT BROKERED	FDIC insured. Ability to diversify with multiple issuers.	Do I need higher safety of principal? Typically more attractive yield versus Treasuries.	\$250,000 per issuer per tax ID maximum size for insurance. Sales prior to maturity subject to interest rate risk and liquidity risk.
MUNICIPAL TAX-EXEMPT	Tax exempt income with favorable long-term credit standing.	The higher the tax bracket, the greater the tax benefit. The high credit quality is often viewed favorably.	Diversification can be attainable yet the liquidity is lesser versus other alternatives due to limited issue sizes. Subject to credit and interest rate risk.
MUNICIPAL TAXABLE	High quality, taxable alternative.	High credit quality alternative taxable investment. Investors in a lower tax bracket not benefitting from tax-exemption but still seeking the high quality and diversification offered by municipal bonds.	Diversification can be attainable yet the liquidity is lesser versus other alternatives due to limited issue sizes. Subject to credit and interest rate risk.
INVESTMENT GRADE CORPORATES	High quality, relatively good liquidity and competitive yields.	The breadth of the corporate market can allow for extensive diversification from credit ratings to multiple sectors. Generally liquid. Flexibility to create desired cash flow and income levels.	Wide range of issuers with various degrees of credit risk. Credit risks can fluctuate during holding period although this will not alter designated cash flow, income or redemption periods.
PREFERRED SECURITIES	Appeal to investors seeking higher yields and/or high cash flow	This may benefit the portfolio as a higher yielding component with more risk versus true fixed income alternatives.	Preferred's are subordinate to debt securities but placed ahead of common stock in the corporate structure. Being perpetual or very long dated exposes them to increased price volatility. Not a hold-to-maturity alternative.

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The Fixed Income Strategy Group provides market commentary, portfolio analysis, and strategy to Raymond James financial advisors for the benefit of their clients and prospects. We are part of the larger 14-person Fixed Income Solutions group within the Raymond James' Fixed Income Capital Markets Group's 38 fixed income locations with more than 480 fixed income professionals including trading and public finance specialists nationwide. This publication does not constitute Fixed Income research, but rather it represents commentary from a trading perspective.

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- [Weekly Bond Market Commentary](#)
- [Fixed Income Weekly Primer \(PDF\)](#)
- [Municipal Bond Investor Weekly \(PDF\)](#)
- [Weekly Interest Rate Monitor \(PDF\)](#)

Investment Types/Expertise Include

- Treasuries/Agencies
- Brokered CDs
- Corporate bonds
- MBS/CMOs
- Tax-exempt municipals
- Taxable municipal bonds
- Preferred securities

RAYMOND JAMES

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Bond Market Commentary

Fixed Income Solutions

Don't Fear the Language – Understand It



DOUG DRABIK
Managing Director,
Fixed Income Strategist

The finance world can get complicated, especially for the passive or uninterested investor. Let's face it, some of us are not curious about sports, movies, exercise, reading, or other things while others of us carry a passion for them. Interest levels also differ in the finance world although the lack of attention here could inflict severe consequences to one's retirement or lifestyle. Financial preparation and strategizing can foster positive differences in our lives and future.

When hearing terminology associated with other industries, it can easily be ignored, or worse, misinterpreted. "Going into the kitchen" in pickleball has nothing to do with the food industry. Cleaning up the deck will likely elicit a different action plan for a ship's deckhand versus a businessperson preparing for a presentation.

The finance world is laden with complicated phrases and financial terms. For example, two distinct classifications are associated with investing objectives: tactical and strategic. Tactical investing attempts to capitalize on market inefficiencies, look for short-term opportunities, time market entry spots, and/or outdo benchmark performances with a total return focus. Tactical investing is proactive and can involve quick-changing market positioning.

Strategic investing aligns portfolio holdings based on long-term planning with no required day-to-day reallocation due to data releases or market events. Most conservative investors, including those who have a portion of funds dedicated to tactical investing, practice strategic investing on some level. These investors share the goal of long-term planning and safeguarding hard-earned wealth. Focus is often on income and cash flow consequently deemphasizing total return. Safeguarding wealth takes precedence over potential quick-hit opportunities which may bring sizeable returns although also carry substantial risk.

When you hear comments in the media like, "Bonds are down – they are having a terrible year." The connotation is negative and the statements can create the image of a scary path ahead for individual bondholders. The meaning of the quote reflects that Treasury bond prices have dropped precipitously since the start of the year – but what often goes unsaid is that it also means that yields have risen accordingly. So, although it may be the 3rd worst yearly start for Treasury prices, at the same time it is also the 3rd best yearly start for Treasury rates. Total return or tactical investors will likely view this differently versus strategic, long-term income investors. Total return investors short-term market plays are negatively impacted because prices have dropped. Long-term income investors, who often hold their bonds to maturity, are unaffected because they don't realize the consequences created by short-term pricing. Bonds held to maturity continue to produce the same cash flow and income as they did from the purchase date and they are not altered by pricing changes as long as the bonds remain in the portfolio.

Furthermore, strategic investors may see the drop in Treasury prices as an opportunity to lock in desirable high levels of income. This window of income opportunity is one we continue to promote as we have not seen yields like the bond market currently boasts in nearly 17 years. It is difficult to differentiate tactical and strategic messaging, particularly given that tactical or total return messaging dominates the industry's communication. Focus on the purpose of investments dedicated or allocated to individual bonds. They are often dedicated to safeguarding wealth which implies long-term strategic planning.

A credit rating of a security is not a recommendation to buy, sell or hold the security and may be subject to review, revision, suspension, reduction or withdrawal at any time by the assigning Rating Agency. Ratings and insurance do not remove market risk since they do not guarantee the market value of the bond.

VIX Index: financial benchmark designed to be an up-to-the-minute index estimate of the expected volatility of the S&P 500 Index, and is calculated by using the midpoint of real-time S&P Index (SPX) option bid/ask quotes.

MOVE Index: this is a yield curve weighted index of the normalized implied volatility on 1-month Treasury options. It is the weighted average volatilities on the CT2, CT5, CT10 and CT30. (weighted average of 1m2y, 1m5y, 1m10y and 1m30y Treasury implied vols with weights 0.2/0.2/0.4/0.2, respectively).

S&P Index: is widely regarded as the best single gauge of large-cap U.S. equities and serves as the foundation for a wide range of investment products. The index includes 500 leading companies and captures approximately 80% coverage of available market capitalization.

U.S. Bloomberg Aggregate Bond Index (U.S. Corporate Investment Grade/LUACTRUU): Measures the investment grade, taxable corporate bond market. It includes USD denominated securities publicly issued by US and non-US industrial, utility and financial issuers.

Duration is the measure of a bond's price sensitivity relative to interest rate fluctuations.

Diversification and strategic asset allocation do not ensure a profit or protect against a loss. Investments are subject to market risk, including possible loss of principal. The process of rebalancing may carry tax consequences.

Rebalancing a non-retirement account could be a taxable event that may increase your tax liability.

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