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Domestic Investment Grade Fixed Income Market Summary

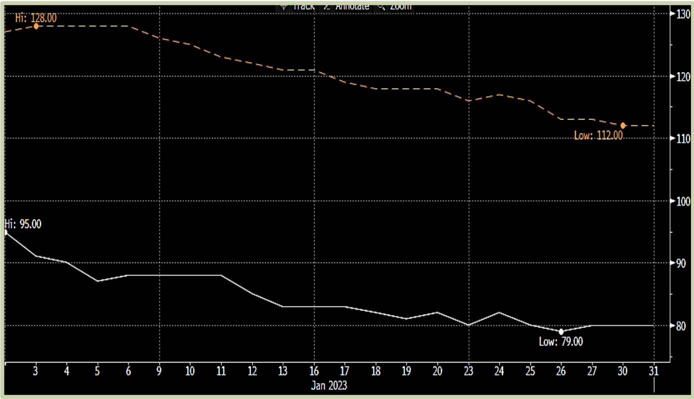
January 2023

Treasuries Reversed December Weakness, Rallied to Start Year

- Treasury bonds rallied strongly in January as signs of decelerating inflation boosted confidence in the Fed, reduced market volatility and pulled benchmark rates lower to start the year.
  - 5+ year Treasury yields declined 34-40 basis points (bps) with the 10-year rate at 3.51% to close January compared to a recent high of 4.34% in October.
  - The 2-year Treasury rate fell 23 bps, widening the curve inversion; the 2-10 year Treasury spread ended the month at -69 bps.
- The December Fed meeting minutes released in January had a relatively hawkish tone, expressing some concern over tight labor market conditions and the downward shift in the market-implied path of the Fed funds rate for the second half of 2023.
  - Despite commenting that no Committee participant anticipated reducing the Fed funds rate target in 2023, the minutes did not cause investors to reduce expectations for near-term rate cuts.
- The U.S. labor market added 223,000 nonfarm jobs in December, the fewest in two years but above the 203,000 projection. Meanwhile, average hourly earnings growth decelerated to +0.3% (expected: +0.4%), and the unemployment rate moved lower to 3.5% (expected: 3.7%).
- Led by falling energy prices, the Consumer Price Index (CPI) declined -0.1% in December, the first post-pandemic negative print.
  - The core CPI index matched expectations at +0.3%, largely due to a +0.8% increase in the shelter component despite private sector indications that rental costs have already peaked.

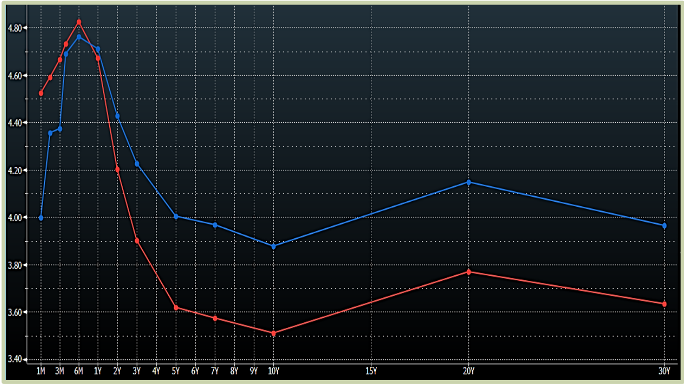
Segment0	January Return	2023 Return
Bloomberg Barclays Intermediate Government Credit Index	1.87%	1.87%
ICE BofA 1-10 Year US Treasury Index	1.56%	1.56%
ICE BofA 1-10 Year US Inflation-Linked Treasury Index	1.36%	1.36%
ICE BofA 1-10 Year Corporate Index	2.51%	2.51%
ICE BofA 1-10 Year Taxable Municipal Index	2.55%	2.55%

1-10 Year IG Credit Spreads: Corporate (orange) and Taxable Municipal (white): January 2023



Maturity	12/31/22 Treasury	1/31/23 Treasury	Change
2-Year	4.43%	4.20%	-0.23%
5-Year	4.01%	3.62%	-0.39%
7-Year	3.97%	3.57%	-0.40%
10-Year	3.88%	3.51%	-0.37%
30-Year	3.97%	3.63%	-0.34%

Treasury Yield Curve: 12/31/22 (blue) vs. 1/31/23 (red)



TIPS Trailed Nominal Treasuries Slightly While Credit Strongly Outperformed

- Treasury Inflation Protected Securities (TIPS) held up well despite a negative month-over-month headline CPI print, which was heavily influenced by volatile energy prices; inflation expectations moved only marginally lower for the month.
  - 1-10 year TIPS lagged nominal Treasuries by 25 bps in January on a duration-adjusted basis, as the 10-year break-even inflation rate declined 5 bps to 2.25%.
  - The 5-year TIPS inflation expectation fell 7 bps during the month to 2.28%, approaching the Fed's 2% inflation target and indicating market confidence that pricing pressures are well-anchored.
- As market volatility fell in January, risk assets performed well, including credit markets with longer-dated benefiting the most from both spread tightening and lower benchmark rates.
- For the fourth consecutive month, intermediate investment grade corporate bonds outperformed Treasuries, outpacing government bonds by an impressive 85 bps in January when adjusted for duration.
  - Credit spreads in the 1-10 year maturity range generally tightened around 15 bps during the month and have now compressed nearly 50 bps from the recent wide in late October.
  - Intermediate BBB rated issuers continued to outpace higher quality issuers, providing 103 bps of alpha over Treasuries in January compared to 68 bps for A and better.
- 1-10 year taxable municipal bonds essentially matched performance of comparable maturity corporate debt in January, providing 83 bps of excess return over Treasuries on a duration-adjusted basis.
  - After lagging the credit rally to close 2022, taxable municipal spreads tightened 15 bps in January.

Source: Bloomberg; Bureau of Economic Analysis; Federal Reserve; ICE BofA; Veritable, L.P. All numbers are estimates. See Disclosures for index descriptions and additional information.

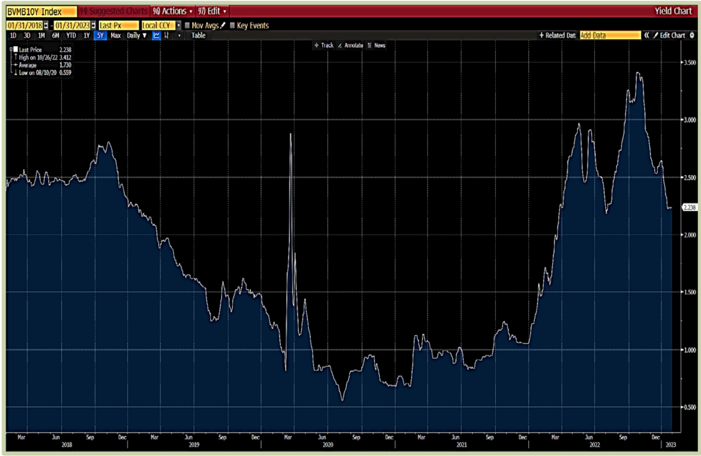
Municipals Posted Strong Rally, Outperformed Treasuries

- Municipal yields followed Treasury rates lower with the annual January Effect causing a supply-demand imbalance, resulting in 2-30 year tax-exempt rates dropping by 33-47 bps for the month.
  - Demand remained strongest in short and intermediate maturities as 1-10 year municipal yields declined 43-58 bps.
  - 15+ year rates fell by 33-38 bps, as demand for longer-dated municipals gained momentum throughout the month from value-hunting investors in a declining rate environment.
  - After rising 37 bps in December due in part to typical year-end selling pressure, the 1-year AAA municipal yield experienced a snapback rally in January, plummeting 58 bps to 2.28%.
- Municipals outperformed their taxable counterparts thanks to a combination of strong demand bolstered by retail investors and a lack of sufficient bond supply.
  - As a result, the 10-year AAA municipal-to-Treasury yield ratio fell to just 62% by January month-end, well-below the 5-year average of 88% breached as recently as the fourth quarter 2022.
- For the month, the 10-year AAA municipal yield declined 44 bps to 2.19%, 46 bps above the 5-year historical average of 1.73% but well below the October peak of 3.41%.
- The yield spread between 2-year and 10-year AAA municipal rates declined 1 bp to 2 bps, a new multi-year low and about 55 bps below the 5-year average.
  - Although the municipal curve could compress further to catch-up to the Treasury counterpart at -69 bps, tax-exempts likely will not deeply invert, as less-sophisticated retail investors typically balk at the idea of locking-in longer-term bonds at lower yields.

Maturity	12/31/22 Muni	1/31/23 Muni	Change	% of U.S. Govt 1/31/23
2-Year	2.60%	2.17%	-0.43%	51.67%
5-Year	2.52%	2.05%	-0.47%	56.63%
7-Year	2.54%	2.09%	-0.45%	58.54%
10-Year	2.63%	2.19%	-0.44%	62.39%
15-Year	3.15%	2.82%	-0.33%	79.89%
20-Year	3.37%	2.99%	-0.38%	79.31%
30-Year	3.58%	3.20%	-0.38%	88.15%

- After a record $121 billion of net outflows in 2022, retail investors returned in force in January.
  - Following a $2.5 billion net outflow for the week ended January 4, weekly-reporting municipal bond funds experienced inflows of $4.4 billion through February 1 according to Refinitiv Lipper data, as retail investors chased yields lower.
  - While January inflows could represent an end to the durable year-long outflow cycle with attractive nominals luring income-focused investors, retail demand for municipal debt remains vulnerable to periods of Treasury market volatility.

10-Year AAA Municipal Yie ld: 2018-2023



- Despite expensive relative valuations in the 1-10 year range, buyers remained undeterred.
  - Taxable crossover opportunities remained, as AAA municipal-to-Treasury yield ratios ended January below 60% out to 7-year maturities.
  - Municipal-to-Treasury yield ratios could normalize higher over the next few months as supply-demand moves toward equilibrium after the annual January Effect concludes.
- The seasonal surge in demand for short-term municipal investment vehicles, particularly variable rate demand notes (VRDNs), due to high levels of reinvestment cash, pulled the SIFMA weekly floating rate well below historical norms relative to its taxable counterpart.
  - After rising to as high as 3.8% in mid-December, the SIFMA rate ended January at just 1.66%, well below the long-run trend of around 80% of the Fed funds rate although signs of normalization emerged near month-end.
- Investors can generate incremental yield through callable bonds and less favorable structures like municipals with coupons below the standard 5% rate.
- The January Effect resulted in a supply-demand imbalance with reinvestment demand from bond redemptions exceeding new municipal issuance by $4.3 billion, according to Bloomberg data.
  - According to JP Morgan estimates, net supply is expected to remain in negative territory in February, potentially generating a continued short-term outperformance tailwind
  - However, with net supply expected to rise to equilibrium levels in March through May, municipals may come under pressure given rich relative valuations and the flat yield curve.
- A barbell structure combining short-term and long-term maturities allows investors to take advantage of the more attractive back-end of the curve while maintaining a more neutral blended duration to reduce overall portfolio interest rate risk.
- Strength in the Treasury market along with a strong technical environment in tax-exempts resulted in the ICE BofA 1-12 Year Municipal Securities Index producing a +2.01% return for the month, the best January performance since 2009.

Source: Bloomberg; ICE; JP Morgan; MRSB; Refinitiv; SIFMA; Veritable, L.P.
All numbers are estimates. See Disclosures for index descriptions and additional information.

Disclosures

This Summary reflects the views of Veritable's Fixed Income Desk and is for your general information. It is not intended to provide personal investment advice and does not take into account the unique investment objectives and financial situation of the reader. Investors should only seek investment advice from their individual financial adviser. Investments in fixed income securities involve the risk of loss that investors should be prepared to bear. Forecasts may not be realized due to a variety of factors, including changes in economic growth, corporate profitability, geopolitical conditions, and inflation.

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Index Descriptions *(Investors cannot invest directly in an index)*

Bloomberg Barclays Intermediate Government Credit Index is a total returns index of U.S. dollar denominated U.S. Treasuries, government-related securities, and investment grade U.S. corporate securities that have a remaining maturity of greater than or equal to 1 year and less than 10 years. Securities must have $250 million or more of outstanding face value and must be fixed rate and non-convertible.

Consumer Price Index (CPI) is a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services. The yearly (or monthly) growth rates represent the inflation rate. The CPI is published by the US Bureau of Labor Statistics on a monthly basis.

ICE BofA 1-10 Year US Treasury Index is a subset of ICE BofA Treasury Index including all securities with a remaining term to final maturity greater than or equal to 1 year and less than 10 years.

ICE BofA 1-10 Year US Inflation-Linked Treasury Index is a subset of ICE BofA US Inflation-Linked Treasury Index including all securities with a remaining term to final maturity greater than or equal to 1 year and less than 10 years.

ICE BofA 1-10 Year Corporate Index measures the performance of investment grade corporate bonds of both U.S. and non-U.S. issuers that are U.S. dollar-denominated and publicly issued in the U.S. domestic market with a remaining term to final maturity greater than or equal to 1 year and less than 10 years.

ICE BofA 1-10 Year Taxable Municipal Index is designed to track the performance of U.S. dollar-denominated taxable municipal debt publicly issued by U.S. states and territories, and their political subdivisions, in the U.S. market with a remaining term to final maturity greater than or equal to 1 year and less than 10 years.

ICE BofA 1-12 Year Municipal Securities Index is a subset of ICE BofA Municipal Securities Index including all securities with a remaining term to final maturity less than 12 years. The ICE BofA Municipal Securities Index is market capitalization weighted and tracks the performance of U.S. dollar denominated investment grade tax-exempt debt publicly issued by U.S. states and territories, and their political subdivisions, in the U.S. domestic market. Qualifying securities must have at least one-year remaining term to final maturity, at least 18 months to final maturity at the time of issuance, a fixed coupon schedule and an investment grade rating (based on an average of Moody's, S&P and Fitch).

The Securities Industry and Financial Markets Association (SIFMA) Municipal Swap Index is a 7-day high-grade market index comprised of tax-exempt Variable Rate Demand Notes (VRDNs) with certain characteristics. The Index is calculated and published by Bloomberg. The Index is overseen by SIFMA's Municipal Swap Index Committee.