TRENDS IN FIXED INCOME

Fed Policy and Long-Duration Investing

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EAGLE | Asset Management

Annualized Returns Post Fed Rate Hike Pause

	1-Year Return			3-Year Return			5-Year Return		
Federal Funds Rate Hike Cycle Ended	S&P U.S. Treasury Bill 0-3 Month Index	Bloomberg Municipal Bond Index	Bloomberg Aggregate Bond Index	S&P U.S. Treasury Bill 0-3 Month Index	Bloomberg Municipal Bond Index	Bloomberg Aggregate Bond Index	S&P U.S. Treasury Bill 0-3 Month Index	Bloomberg Municipal Bond Index	Bloomberg Aggregate Bond Index
2/24/1989	N/A	10.3%[1]	12.7%[1]	N/A	9.8%[1]	12.6%[1]	N/A	9.7%[1]	11.0%[1]
2/1/1995	5.6%	15.1%	17.1%	5.3%	9.6%	10.2%	5.2%	6.2%	7.3%
5/6/2000	6.0%	12.8%	13.7%	3.4%	9.8%	11.1%	2.6%	7.4%	7.8%
6/29/2006	5.1%	4.9%	6.5%	3.0%	3.9%	6.6%	1.8%	5.0%	6.6%
12/19/2018	2.2%	7.9%	8.8%	1.0%	4.8%	4.9%	1.9%	2.3%	1.0%
Average	**4.7%**	**10.2%**	**11.8%**	**3.2%**	**7.6%**	**9.1%**	**2.9%**	**6.1%**	**6.7%**

[1]Based on monthly returns rounded to the nearest month-end.
N/A represents no data available for the period.
Source: Bloomberg, as of 12/19/23

Our View

With many market participants speculating the U.S. Federal Reserve (Fed) has reached the end of the fastest rate-hiking cycle in history, many investors are looking to take advantage of the fact that fixed income is finally again providing income. The Fixed Income team at Eagle Asset Management has been examining many alternatives available in environments where the Fed has ended a hiking cycle. We conclude it is best to invest in assets that have longer duration (maturities) than money market funds, despite these funds currently offering higher yields in the short run.

Why not invest in higher-yielding money markets?

With current money market yields being advertised above 4%, it is important to note that these yields are not fixed rates but rates that can change daily. This introduces reinvestment risk, where you are at the risk of receiving lower rates in the future. When these bonds mature, the principal needs to be reinvested. In a falling rate environment, this would result in lower rates. In contrast, investing in longer-duration assets allows you to lock in higher rates of return for years to come, resulting in a higher total return over a longer period.

Why does this make sense?

Duration is a bond's sensitivity to interest rate changes. The more duration a bond has, the more sensitive it is to changes in interest rates. Since bonds generate positive returns when interest rates fall (with the reverse also applying, as noted in 2022), holding longer-duration instruments when rates begin to fall would be the most profitable way to invest in this asset class.

How to invest after a Fed hiking cycle?

The chart above shows three separate return streams in order of duration held. The S&P U.S. Treasury Bill 0-3 Month Index is the shortest (under one year of duration), with the Bloomberg Municipal Bond Index and the Bloomberg U.S. Aggregate Bond Index, each with about six years of duration, being the longest. You can see that in periods immediately following the pause of Fed hiking cycles, in almost all 3- and 5-year periods longer-duration assets generated the highest total return, supporting our belief that long duration is the best way to move forward given the markets' views that the Fed cycle has reached a pause.

About Eagle Asset Management

Eagle Asset Management provides a broad array of fundamental equity and fixed-income strategies designed to meet the long-term goals of institutional and individual investors. Eagle's multiple independent investment teams have the autonomy to pursue investment decisions guided by their individual philosophies and strategies.

Risks associated with Fixed Income investing:

Many investors consider bonds to be "risk free" investment vehicles. Historically, bonds have indeed provided less volatility and less risk of loss of capital than has equity investing. However, there are many factors that may affect the risk and return profile of a fixed-income portfolio. The two most prominent factors are interest-rate movements and the creditworthiness of the bond issuer. Bonds issued by the U.S. government have significantly less risk of default than those issued by corporations and municipalities. However, the overall return on government bonds tends to be less than these other types of fixed-income securities. Investors should pay careful attention to the types of fixed-income securities that comprise their portfolio and remember that, as with all investments, there is the risk of the loss of capital.

This material may include forward-looking statements. These statements are not historical facts, but instead represent only beliefs regarding future events, many of which, by their nature, are inherently uncertain. You should not place undue reliance on forward-looking statements as it is possible that actual results and financial conditions may differ, possibly materially, from the anticipated results and financial conditions indicated in these forward-looking statements. There are uncertainties, unknown risks, and other factors that may cause actual results, levels of activity, performance, or achievements to be materially different from any future results, levels of activity, performance, or achievements expressed or implied by these statements.

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Definitions

The federal funds rate, known as the fed funds rate, is the target interest rate set by the Federal Open Market Committee of the U.S. Federal Reserve. The target is the Fed's suggested rate for commercial banks to borrow and lend their excess reserves to each other overnight.

Duration incorporates a bond's yield, coupon, final maturity, and call features into one number, expressed in years, that indicates how price-sensitive a bond or portfolio is to changes in interest rates. Bonds with higher durations carry more risk and have higher price volatility than bonds with lower durations.

Reinvestment risk is the possibility that an investor will not be able to reinvest cash received from an investment, such as interest earned or coupon payments received, at a rate of return that is equal to or better than the original investment's current rate of return.

Total return, when measuring performance, is the actual rate of return of an investment or a pool of investments over a given period of time. Total return includes interest, capital gains, dividends, and distributions realized over the specified period. Total return accounts for two categories of return: income including interest paid by fixed-income investments, distributions, or dividends and capital appreciation, representing the change in the market price of an asset.

Indices

The S&P U.S. Treasury Bill 0-3 Month Index measures the performance of U.S. Treasury bills maturing in 0 to 3 months.

The Bloomberg U.S. Aggregate Bond Index is composed of the total U.S. investment-grade bond market. The market-weighted index includes Treasuries, agencies, commercial mortgage-backed securities (CMBS), asset-backed securities (ABS) and investment-grade corporates.

The Bloomberg Municipal Bond Index is a rules-based, market-value-weighted index engineered for the long-term tax exempt bond market.

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Indices are unmanaged and one cannot invest directly in the index.