HIGH YIELD COMMENTARY

Stock market momentum continued into 4Q24, while bond investors were left out of the party, as interest rates rose across the yield curve, despite two sequential 25bp rate cuts. The Federal Open Market Committee's (FOMC) December statement highlighted, "The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. The Committee judges that the risks to achieving its employment and inflation goals are roughly in balance. The economic outlook is uncertain, and the Committee is attentive to the risks to both sides of its dual mandate. In support of its goals, the Committee decided to lower the target range for the federal funds rate by 1/4 percentage point to 4-1/4 to 4-1/2 percent. The Committee will continue reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities." U.S. Real Gross Domestic Product (GDP) increased at an annual rate of 3.1% during the third quarter. Inflation, as measured by the U.S. Consumer Price Index (CPI), rose by 2.7% for the twelve-month period ending November 2024. The Bureau of Labor Statistics (BLS) reported the unemployment rate remained stable in November at 4.2%, while the U6 measure, which includes not only the unemployed but also underemployed workers and those marginally attached to the labor force, increased slightly to 7.8%. The Conference Board Consumer Confidence Index declined to 104.7 in December, well below its 2024 high of 114.8 set back in January 2024. The Conference Board Index of Leading Economic Indicators (LEI) for the U.S. declined 1.6% over the six months ending in November 2024, slightly less than its 1.9% decline over the previous six months.

The Bloomberg U.S. High Yield Index (Index) eked out a 0.17% fourth quarter gain, bringing 2024 calendar year total returns to 8.19%. By ratings category, BB-rated and B-rated bonds recorded dispersed returns of (-0.49%) and 0.31% respectively, while the CCC-rated cohort added an impressive 2.26% in the fourth quarter. The Index option-adjusted spread (OAS) contracted by 8 bps in the fourth quarter to +287 bps, while the yield-to-worst (YTW) rose by 50 bps to 7.49%. BB-rated credits now trade at an OAS of +179 bps and offer a YTW of 6.39%, B-rated credits at an OAS of +277 bps and 7.43% YTW, and CCC-rated credits at an OAS of +558 bps and 10.16% YTW. The average dollar price of the Index declined to $95.47 by year-end. Despite three defaults in the quarter, the trailing 12-month par-weighted U.S high yield bond default/distressed exchange rate declined to 1.47%, as compared to the 25-year average default rate of 3.4%. The upgrade to downgrade ratio remains in healthy territory, although well off it's 2021 peak (JP Morgan). High Yield debt issuance in 2024 was $289 billion, up from $176 billion in 2023. Refinancings accounted for 75% of debt issuance, with $71 billion of net new supply. Stock and bond market investors had been pinning their hopes on rate cuts since the Fed began holding rates steady back in July 2023. Thus, we were curious about the muted market reaction to the oversized 50bps rate cut on September 18th, as the markets appeared unsure and seeking clarity. Did the 50bps rate cut indicate the Fed was confident they had finally gotten ahead of inflation, or did the Fed foresee increasing employment weakness that would portend an economic contraction? The market didn't need to wait long for clarity – The BLS released a very healthy jobs report on October 4th, followed by a CPI report on October 17th that exceeded expectations and confirmed the continued stickiness of U.S. inflation. As improbable as it was, the Fed appears to have successfully reduced inflation from its 9.1% peak in mid-2022 to the current 3% level, while avoiding an economic contraction. Equally remarkable, fiscal policy helped to sustain GDP growth of around 3% annually for the past two years, aided by the U.S. transition from a labor-shortage economy to a labor-balanced economy. As healthy economic data persisted through year-end, markets needed to readjust to lower recession risk and persistently sticky inflation. The Fed cut another 50bps in the fourth quarter and projects to cut another 50bps in 2025. Today, the markets appear far less confident in rate cuts due to broadening inflation concerns following the Presidential election.

President-elect Trump is preparing to start his 5th year in the White House, while his sense of conviction and urgency for policy implementation has many investors playing "wait and see." Most are optimistic about the growth prospects from reduced regulations and taxes, which require congressional approval. However, many have a more cautious attitude toward trade tariffs and deportations, which do not require congressional approval and have inflationary implications. These inflationary implications may result in higher-than-expected rates and eventually pinch consumer demand. Additionally, the uncertainty surrounding Trump's ideologies about Fed intervention, imperialism, fiscal

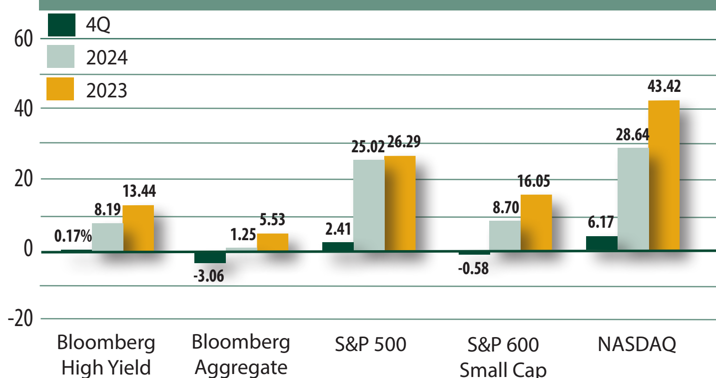
spending, abolishing the U.S. debt ceiling, and resolving the Russia-Ukraine conflict appears to be increasing the required equity and bond risk premiums. We believe the dramatic increase in interest rates following the September 18th FOMC meeting primarily reflects an increase in real yields, predominantly driven by expanded term premiums commensurate with policy and economic uncertainty. While real wage growth slowed to 0.7% by year-end, several Trump proposed policies have the potential to increase U.S. inflation. That said, Trump has proven to be a strong advocate of deregulation, which will likely attract foreign capital and free up domestic capital while loosening bank lending. Economic growth is generally a healthy catalyst for higher rates, and as previously stated, the U.S. economy had multiple pre-GFC periods of sustainable growth at/above trend with fed fund rates at/above 5%.

The PIA Investment Strategy Group (ISG) anticipates continued volatility in interest rates throughout the first quarter or at least until we have greater clarity on presidential policy, with the likelihood the yield curve may steepen further. We continue to believe the Fed's 2% inflation target will be challenging to achieve without an economic contraction. Presently, the markets are pricing in just one 25bp rate cut for the year. While we believe this rate outlook will likely change over time, we anticipate the current environment may result in another pause to determine future data paths from policy implications. The corporate bond market continues to be healthy with strong balance sheets, high cash flow, and solid fundamentals. However, credit spreads are, in our opinion, priced to perfection with their tightest spreads in over a quarter century. Therefore, if the economy begins to slow or contract, credit spreads will prove to offer inadequate compensation at current levels.

In the fourth quarter through year-end, PIA portfolio duration remained at the long end of our neutral duration range (+/- 0.25 years relative to our respective benchmark). We continue to modestly overweight corporate debt, focusing on high-quality credits with strong balance sheets. Our Industrial credits provide incremental risk-adjusted yield and our Financial credits are senior domestic debt, which we believe offer attractive compensation for their sector volatility. We maintained our modest overweight in Agency MBS during the quarter. In our Plus strategies, we maintained modest high-yield credit exposure, as current yield levels continue to offer value.

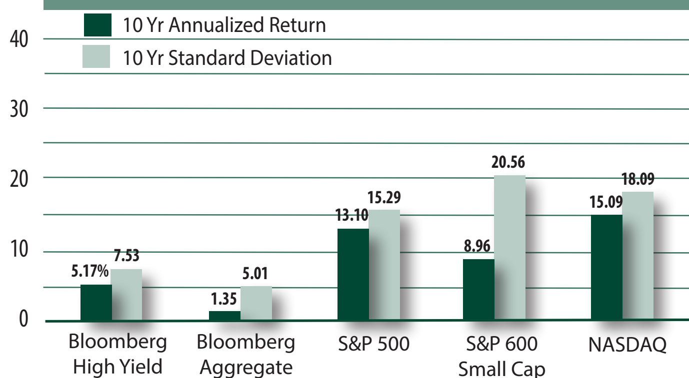
PIA Investment Strategy Group

INDEX RETURNS



Source: Bloomberg, Informais PSN
Past performance is not a guarantee of future results.

HISTORICAL PERFORMANCE



Source: Informais PSN; Annualized 10 Years
Past performance is not a guarantee of future results.

INDEX RETURNS	4Q	2024	2023
BB	-0.49%	6.30%	11.60%
B	0.31	7.38	13.78
CCC	2.26	15.09	19.84
CC - D	2.23	48.29	16.41
Basic Industry	0.29	8.18	12.18
Capital Goods	-0.68	6.38	12.82
Consumer Cyclical	0.11	8.15	16.03
Consumer Non-Cyclical	-0.56	9.92	12.93
Energy	0.34	7.40	12.81
Technology	0.07	9.19	12.64
Transportation	1.79	9.02	9.68
Communication	1.46	8.46	12.18
Other Industrials	-0.50	7.46	15.98
Utility	-1.17	5.70	10.10
Financial	0.08	8.53	14.80

Index is Bloomberg U.S. High Yield Index. Source: Bloomberg

INDEX SPREADS	12/31/24	12/31/23	12/31/22
BB	203	232	317
B	309	346	514
CCC	582	760	1,017
CC - D	1,588	785	3,148
Basic Industry	284	364	451
Capital Goods	276	284	424
Consumer Cyclical	272	283	492
Consumer Non-Cyclical	331	407	540
Energy	288	299	388
Technology	294	386	520
Transportation	319	372	433
Communication	481	529	584
Other Industrials	246	-246	468
Utility	219	272	298
Financial	269	332	528

Index is Bloomberg U.S. High Yield Index. Source: Bloomberg

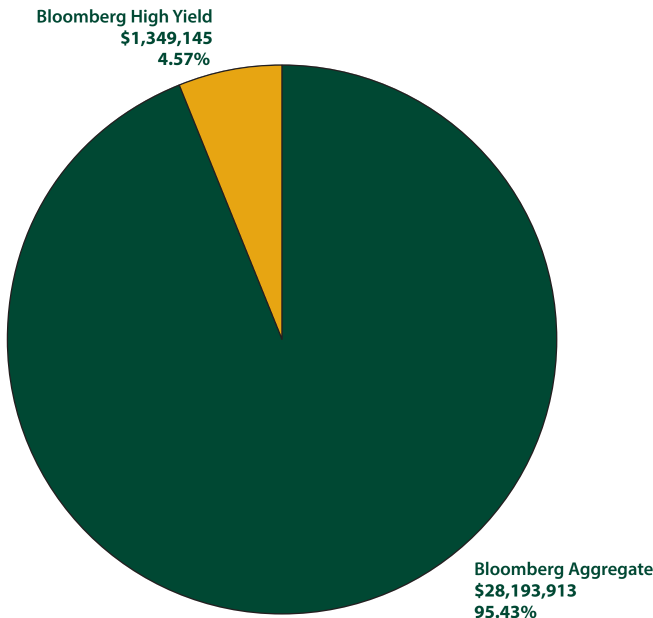
KEY CHARACTERISTICS	12/31/24	12/31/23
Duration	3.1	3.2
Yield To Maturity	7.6	7.8
Current Yield	6.7	6.5
Yield To Worst	7.5	7.6
Weighted Average Maturity	4.7	4.9
% $500mm and under	24.5	26.5
% $501mm and over	75.5	73.5

Index is Bloomberg U.S. High Yield Index. Source: Bloomberg, Yield Book

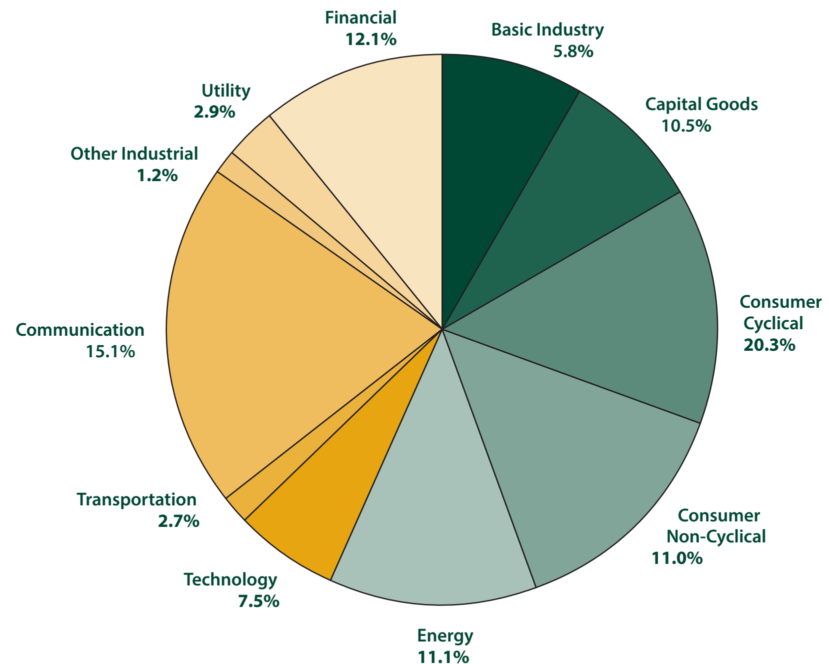
KEY CHARACTERISTICS	12/31/24	12/31/23
% BB or >	50.8	46.1
% B	35.2	41.1
% CCC	12.0	11.7
% CC and below	2.0	1.1
% Debt Maturing in < 3 Years	19.6	20.7
% Debt Maturing in 3 - 5 Years	42.1	33.8
% Debt Maturing in > 5 Years	38.3	45.5

Index is Bloomberg U.S. High Yield Index. Source: Bloomberg

US DEBT MARKET ($MM)



BLOOMBERG HIGH YIELD



Source: Bloomberg

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Bloomberg U.S. High Yield Index covers the universe of fixed rate, non-investment grade debt. Eurobonds and debt issues from countries designated as emerging markets (e.g., Argentina, Brazil, Venezuela, etc.) are excluded, but Canadian and global bonds (SEC registered) of issuers in non-EMG countries are included. Original issue zeroes, step-up coupon structures, 144-As and pay-in-kind bonds (PIKs, as of October 1, 2009) are also included. The index includes both corporate and non-corporate sectors. The corporate sectors are Industrial, Utility, and Finance, which include both U.S. and non-U.S. corporations. The Yankee sector has been discontinued as of 7/1/00. The bonds in the former Yankee sector have not been removed from the index, but have been reclassified into other sectors.

Bloomberg U.S. Aggregate Bond Index is an unmanaged index that covers the investment grade fixed rate bond market with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities. The issues must be rated investment grade, be publicly traded, and meet certain maturity and issue size requirements.

S&P 500 Index – The S&P 500 index includes 500 leading companies in leading industries of the U.S. economy. The S&P 500 is designed to be a leading indicator of U.S. equities and is meant to reflect the risk/return characteristics of the large cap universe.

S&P SmallCap 600 covers approximately 3% of the domestic equities market. Measuring the small cap segment of the market that is typically renowned for poor trading liquidity and financial instability, the index is designed to be an efficient portfolio of companies that meet specific inclusion criteria to ensure that they are investable and financially viable.

Nasdaq Composite is a stock market index of the common stocks and similar securities (e.g. ADRs, tracking stocks, limited partnership interests) listed on the NASDAQ stock market, meaning that it has over 3,000 components. It is highly followed in the U.S. as an indicator of the performance of stocks of technology companies and growth companies. Since both U.S. and non-U.S. companies are listed on the NASDAQ stock market, the index is not exclusively a U.S. index.

Bond ratings provide the probability of an issuer defaulting based on the analysis of the issuer's financial condition and profit potential. Bond rating services are provided by credit rating agencies currently registered as Nationally Recognized Statistical Rating Organizations ("NRSROs"). Bond ratings start at AAA (denoting the highest investment quality) and usually end at D (meaning payment is in default). Securities not covered by any agency will receive a non-rated (NR) rating.

Standard Deviation - is applied to the annual rate of return of an investment to measure the investment's volatility.

Yield to Maturity - The rate of return anticipated on a bond if held until the end of its lifetime.

Weighted Average Maturity - Tells how many years it will take to pay half of the outstanding principal.

Current Yield - Annual income (interest or dividends) divided by the current price of the security.

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 the country's economic health.

Consumer Price Index (CPI) is a measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food, and medical care. It is calculated by taking price changes for each item in the predetermined basket of goods and averaging them.

Consumer Confidence Index (CCI) is a survey, administered by The Conference Board, that measures how optimistic or pessimistic consumers are regarding their expected financial situation.

The Bureau of Labor Statistics (BLS) is a federal agency that collects and disseminates various data about the U.S. economy and labor market.

The Conference Board (CB) is a not-for-profit research organization that distributes vital economic information to its peer-to-peer business members.

The Federal Open Market Committee (FOMC) is the branch of the Federal Reserve System (FRS) that determines the direction of monetary policy specifically by directing open market operations (OMOs).

Basis point (bp)- A unit that is equal to 1/100th of 1%, and is used to denote the change in a financial instrument.

Yield - The income return on an investment. This refers to the interest or dividends received from a security and is usually expressed annually as a percentage based on the investment's cost.

Duration - A commonly used measure of the potential volatility of the price of a debt security, or the aggregate market value of a portfolio of debt securities, prior to maturity. Securities with a longer duration generally have more volatile prices than securities of comparable quality with a shorter duration.

Spread - The difference in yields between two fixed-income securities with the same maturity, but originating from different investment sectors.

The U-6 (Unemployment) rate measures the percentage of the U.S. labor force that is unemployed, plus those who are underemployed, marginally attached to the workforce, and have given up looking for work.

Option-adjusted spread (OAS) is the measurement of the spread of a fixed-income security rate and the risk-free rate of return, which is adjusted to take into account an embedded option. Typically, an analyst uses the Treasury securities yield for the risk-free rate.

Yield to worst - the lowest potential yield that can be received on a bond without the issuer actually defaulting.

The Leading Economic Index (LEI) provides an early indication of significant turning points in the business cycle and where the economy is heading in the near term.

An "upgrade to downgrade ratio" refers to the proportion of credit rating upgrades compared to downgrades, essentially indicating how many times a company's credit rating is positively adjusted compared to when it is negatively adjusted by a rating agency

A yield curve is a line that plots the yields or interest rates of bonds that have equal credit quality but different maturity dates.

Opinions expressed are subject to change, are not intended to be a forecast of future events, a guarantee of future results, nor investment advice.

A distressed exchange is a technical default that occurs when a company negotiates a new debt agreement with its creditors.

Past performance does not guarantee future results.

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