Dana Fixed Income Strategies

Quarterly Review

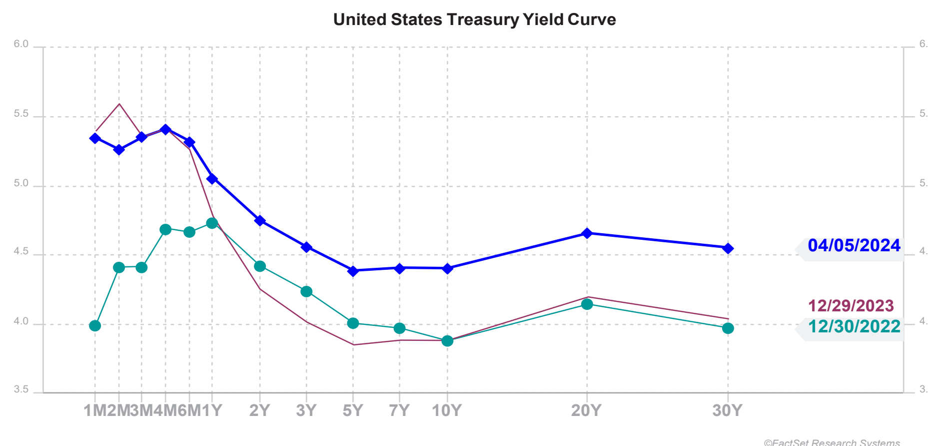
As of March 31, 2024

Strong Economic Data Continues to Keep the Fed at Bay

Over the first quarter, the U.S. economy delivered very solid GDP growth along with surprisingly strong job growth. However, interest rates drifted higher as sticky inflation prints have limited the market's expectations for the number of interest rate cuts in 2024. To illustrate, labor market strength continued to spill over into 2024 as January payrolls reported gains of 229,000 new jobs while February payrolls showed gains of 275,000 new jobs. The unemployment rate continued to stay low at 3.9% but inflation, the primary focus of the Federal Reserve, has remained sticky as measured by both the CPI and Core CPI with recent readings at 3.15% and 3.75%, respectively. By quarter end, the market's expectation for the total number of Fed rate cuts this year had declined from six at the start of the year to just three, with the first move now expected in June rather than March. Given the continued strength of the economic data, investors should expect the Fed to move cautiously in an effort to avoid doing more harm than good to the economy as it "gains a little more confidence that inflation is coming down in a sustainable way."

While the economy is proving stronger than originally expected, and inflation remaining stickier, the Fed will remain cautious in cutting rates in order to prevent a reignition of higher inflation. However, this doesn't override two very important key points to come out of the latest FOMC meeting in March. First, the Fed raised its long-run expectations for the future Fed Funds Rate from 2.5% to 3%. The higher 3% terminal rate implies that the Fed has increased its projection for the potential growth rate of the U.S. economy which allows for interest rates to remain higher for longer. Second, the Fed has not changed its message to the markets, namely that the Fed is expecting to cut interest rates beginning in 2024; it has only delayed the start of the interest rate cuts. Pulling the pieces together, a healthy economy coupled with a gradual removal of restrictive monetary policy allows for the yield curve to steepen and drift downwards. This could create an investment environment that provides an opportunity to both extend duration to capture higher yields and improve total returns at the same time.

Today's volatile fixed income market provides ample reason for active bond management. It is important for investors to remain focused on high-quality factors during periods of transition or market volatility. A portfolio of high-quality bonds consisting of U.S. Treasuries, U.S. Agencies, and investment-grade corporate bonds can offer attractive yields without high interest-rate risk. Tax-exempt yields in municipal bonds are also attractive for investors in higher tax brackets. In these uncertain and transition periods, investors should consider maintaining a well-diversified core fixed income portfolio managed in an active manner to continue compounding interest no matter what path interest rates may follow in the future. Fixed income investments provide important benefits, including diversification from equities, lower return volatility, and the added predictability of a recurring income stream.



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DANA FIXED INCOME STRATEGIES

As of March 31, 2024

FIXED INCOME PORTFOLIO MANAGEMENT TEAM

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Director of Fixed Income

BRIAN LEHKY
Lead Municipal Bond Portfolio Manager

NOAMAN SHARIEF
Lead Intermediate Bond Portfolio Manager

MATTHEW SLOWINSKI, CFA
Lead Limited Volatility Bond Portfolio Manager

DANA LIMITED VOLATILITY BOND STRATEGY

Dana's Limited Volatility Bond Strategy performed well in Q1 as income from higher portfolio coupons drove performance. Agency adjustable rate mortgage pools were especially accretive as spread tightening in the sector provided a boost to performance beyond interest income. The Strategy is well positioned for 2024 as prepayment speeds on callable and paydown securities should remain low due to moderate refinance activity. While we continued to add some short fixed agency securities to lock-in higher yields, the Strategy's attractive 5.79% yield with an average duration of 0.88, provides exceptional value with minimal credit and duration risk.

DANA INTERMEDIATE BOND AND SOCIAL ESG BOND STRATEGIES

The Dana Intermediate Bond and Social ESG Bond Strategies performed relatively well in Q1, posting positive returns while the benchmark return was negative. Each Strategy's broad diversification and risk controls provided stability as the yields rose during the quarter. Moreover, their corporate bond overweight provided additional yield and better relative performance as their spreads tightened during the quarter. Total returns in Q1 2024 were driven by each Strategy's slightly longer Treasury exposure and overall corporate spread tightening. The Strategies are well positioned for the remaining three quarters of 2024 with attractive above benchmark yields and neutral to slightly defensive durations.

DANA MUNICIPAL BOND STRATEGY

Municipal yields moved higher over the quarter but were contained due to heightened demand and manageable supply. Municipal bonds offer very attractive, tax adjusted yields and are very healthy from a credit perspective. Given the current interest rate uncertainty, municipal investors should look to the active, high-quality portfolios Dana manages which have navigated through difficult market environments. While we anticipate markets to remain volatile in the short term, we feel it is important to have an allocation to high-quality municipal securities that offer diversification and low correlations to other asset classes.

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Strategy characteristics, allocation, contributors, detractors, top 10 holdings, style, activity, returns, and risk are based on actual composite holdings.

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