

# Fixed Income Quarterly

Market Perspectives from Fixed Income Solutions

## Yield Curves Reshape Strategies

Is the bond market predictive or reactive? Can it be both? The world around us is not always black and white, so it stands to reason that economic change and its path may not be an exact science. After all, there are thousands of variables, mostly unpredictable, that factor into world economies, including but not exclusively - employment, pricing, geopolitical events, politics, supply/demand, competition, invention, technology advancement, war/conflict, ecology, fiscal and monetary policies, natural disasters, discoveries, etc. Forecasting can be as difficult as counting the grains of sand on a beach.

So why do we work so hard to predict the future? Before participating in the financial markets, investors usually seek direction and analyze probabilities in an attempt to optimize the return on hard-earned dollars. Investing with individual bonds is a means to preserving family wealth, financial independence, and retirement. Fixed income and individual bonds are time-tested assets serving in this cause.

The Treasury yield curve has historically been one of the better financial predictors. As such, we monitor yield curve moves, not as an absolute prognosticator but as a guidance tool to aid with long-term strategy

“As the yield curve has undergone significant changes, we look to reveal what this means as a future indicator and how it may help guide long-term strategic fixed income planning.”

decisions. Equities and other growth assets may continue to help grow your wealth, while long-term fixed-income strategies work to keep that wealth intact. As the yield curve has undergone significant changes, we look to reveal what this means as a future indicator and how it may help guide your long-term strategic fixed income planning.

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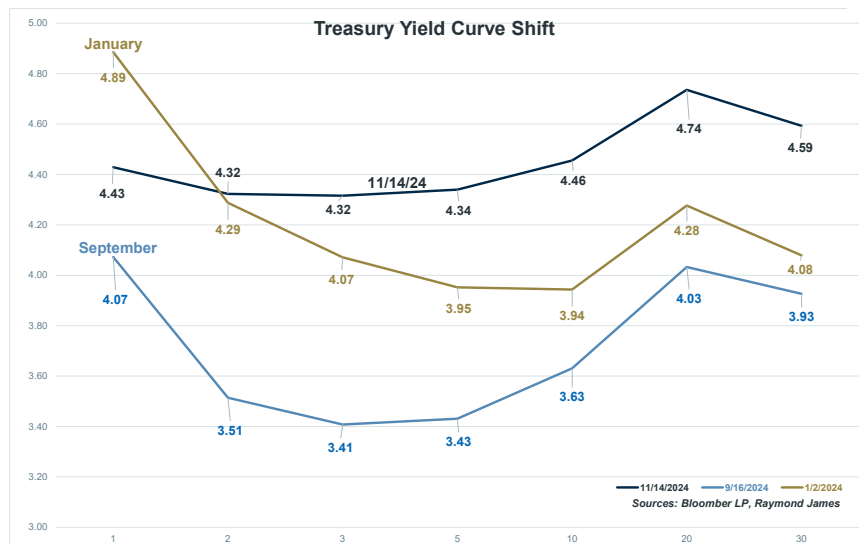
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## THE YIELD CURVE SHIFT

The Treasury yield curve has shifted appreciably all year long. In particular, the last few months have realized substantial rate changes. The shift in the Treasury curve is not isolated. The corporate curve is also changing. Once flat across all maturity points, the corporate curve boasts more of an upward-sloping shape through 10 years before flattening out. The steeper a curve gets, the greater the reward (income) for taking on risk (duration/price).

The shape of various yield curves may influence how long-term strategies are implemented. Strategic bond plan implementation can sometimes mirror tactical bond strategy implementation, which seeks to take advantage of spot market moves relative to forecasts. The graph highlights how the Treasury curve has changed shape in 2024. The gold line represents how the Treasury curve looked at the start of this year. It was extremely inverted, with short-term maturities offering higher rates of return versus longer-term maturities. The general shape in September was unchanged; however, with each maturity exhibiting a much lower rate. The most dynamic curve shape change started around September (light blue line), evolving into the present Treasury curve shape (dark blue line). Except for maturities inside two years, the Treasury curve is now flat through the 10-year note, where it begins to take on an upward slope.

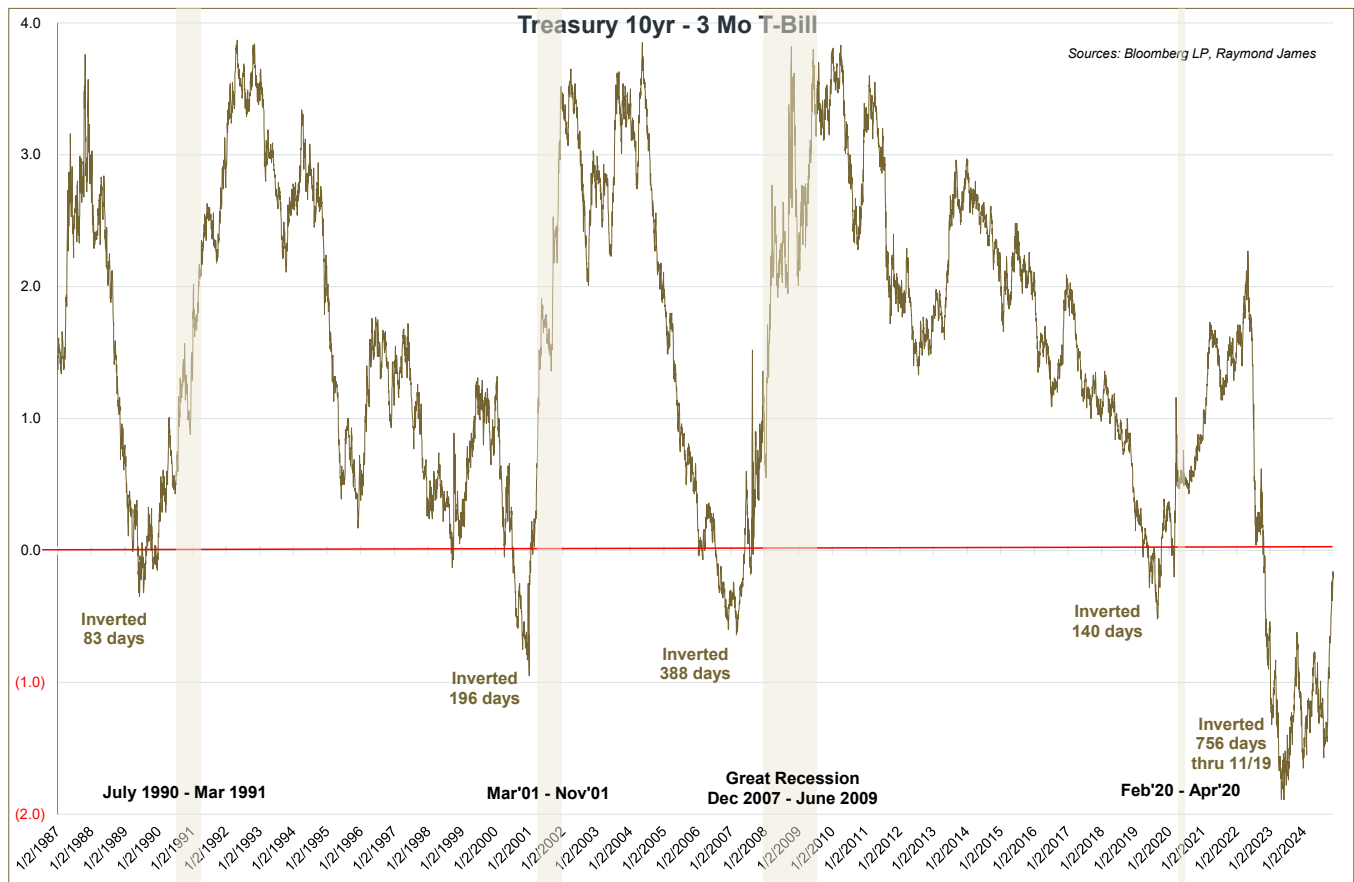


Source: Bloomberg LP

	Fed Funds			Fed Funds			
	Lower	Upper	Change	Lower	Upper	Change	
<b>2021</b>				<b>2023</b>			
Jan 27	0.00	0.25		Feb 1	4.50	4.75	0.25
Mar 17	0.00	0.25		Mar 22	4.75	5.00	0.25
28-Apr	0.00	0.25		May 3	5.00	5.25	0.25
Jun 16	0.00	0.25		Jun 14	5.00	5.25	
Jul 28	0.00	0.25		Jul 26	5.25	5.50	0.25
Sep 22	0.00	0.25		Sep 20	5.25	5.50	
Nov 3	0.00	0.25		Nov 1	5.25	5.50	
Dec 15	0.00	0.25		Dec 13	5.25	5.50	
<b>2022</b>				<b>2024</b>			
Jan 26	0.00	0.25		Jan 31	5.25	5.50	
Mar 16	0.25	0.50	0.25	Mar 20	5.25	5.50	
May 4	0.75	1.00	0.50	May 1	5.25	5.50	
Jun 15	1.50	1.75	0.75	Jun 12	5.25	5.50	
Jul 27	2.25	2.50	0.75	Jul 31	5.25	5.50	
Sep 21	3.00	3.25	0.75	Sep 18	4.75	5.00	-0.50
Nov 2	3.75	4.00	0.75	Nov 7	4.50	4.75	-0.25
Dec 14	4.25	4.50	0.50	Dec 18			

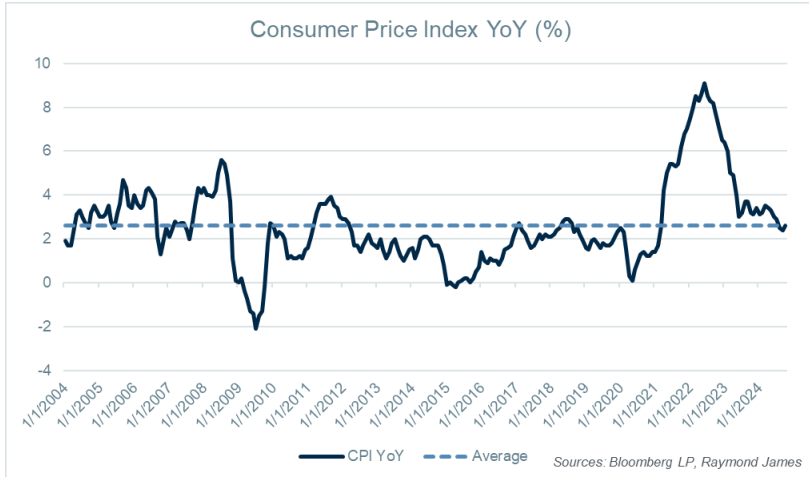
Sources: Federal Reserve, Raymond James

The timing is not coincidental. The Federal Open Market Committee, which meets eight times each calendar year, lowered the Federal Funds rate in September, the first rate cut since March 2020 when COVID pushed the Fed into a 21-month zero interest rate environment. The Fed lowered the Fed Funds rate by 50 basis points in September and 25 basis points in November. Their last meeting in 2024 is December 18. Should they follow with another 25 basis point cut, it is plausible for the Treasury yield curve to finally become “normal” or upward-sloping after two-plus years of inversion.



The graph above illustrates the historically long period of Treasury curve inversion – 756 days. Will this, at long last, correct itself in December? There are other striking patterns. The beige-shaded areas represent recessions. Each of the previous four recessions was preceded by inverted curves that moved back to a normal upward slope. If history holds, this may indicate the possibility of an official upcoming recession in 2025. We say “official” because there is an argument that many Americans believe they are already in a recession. Many people living paycheck to paycheck contend that the inflated staple goods like food and gas have already put them under financial stress.

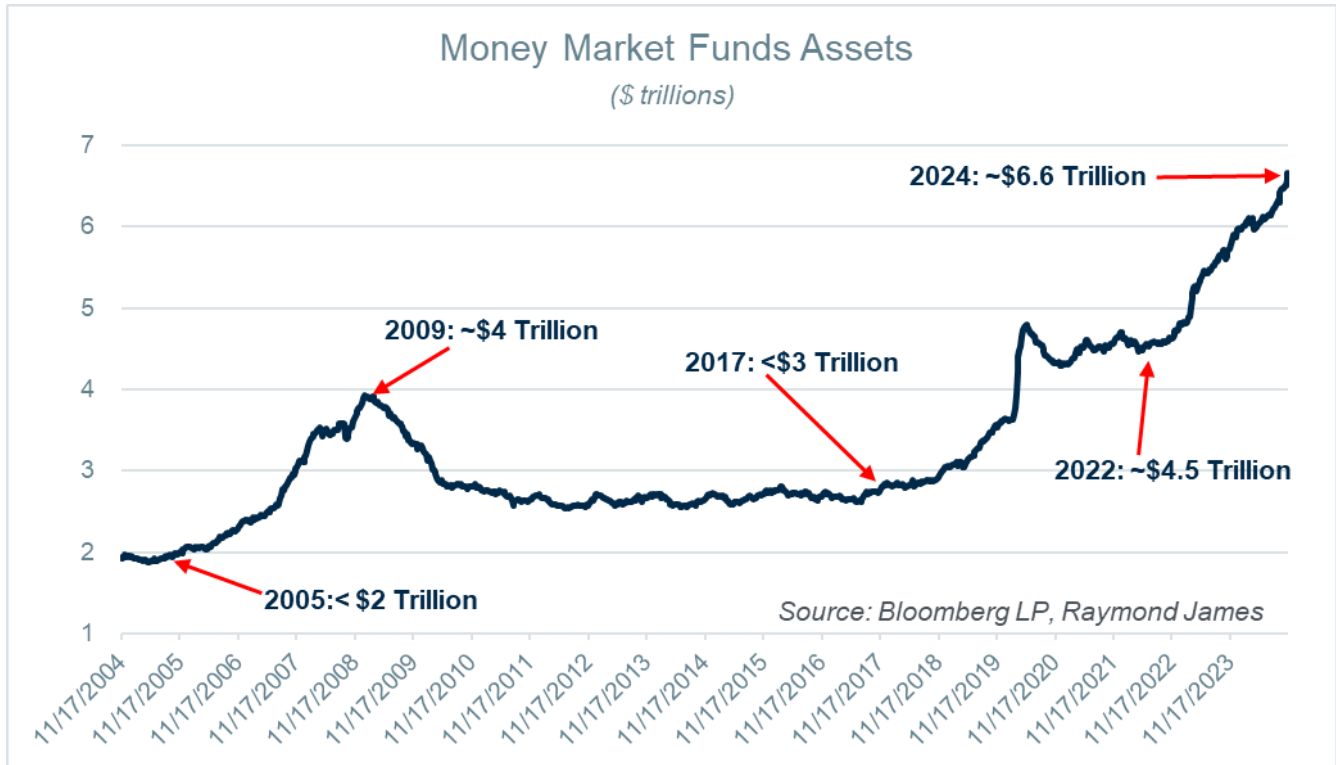
There are a lot of variables that are different this time around. The current economic environment was not shaped by a financial crisis or war but by a rare worldwide health pandemic. As highlighted above, the yield curve has recorded an unprecedented period of inversion. There has been an accumulation of more than \$6.5 trillion in money market funds, according to the ICI Money Market Fund Index. Most remarkably, the U.S. response to the pandemic included an enormous government intervention of roughly \$3.65 trillion with the Coronavirus Aid, Relief, and Economic Securities (CARES) Act which included direct cash payments to individuals. Although not many would argue with the necessity of the intervention, the most highlighted consequence has been inflation.



Prior to the pandemic, the Consumer Price Index (CPI), which measures inflation, had a 20-year average of 2.2%. The pandemic peaked CPI at 9.1% and although it has radically dropped, it sits at 2.6%. Falling inflation does not mean falling prices but rather prices that are not increasing at quite the same pace. A 30% decrease from the current level is required to reach the FOMC's desired 2% level.

## SHORT-TERM MONEY

Yields on the short end of the curve have appealed to many investors for the past few years. As the FOMC waged its fight against inflation, it raised the Fed Funds rate by 525 basis points between early 2022 and mid-2023. As the Fed Funds rate goes, short-term yields follow. This pushed yields on many money market



assets well north of 5%, which attracted investors to put money into these funds. Since mid-2022, the total holdings in money market funds (per ICI data) have risen from ~\$4.5 trillion to over \$6.6 trillion, an increase of over \$2 trillion or ~45% in a little over 2 years. The chart provides a longer-term view of the increase in money market assets over the past 20 years.

Money market funds can be a great investment vehicle for an alternative cash allocation, but they may have some pitfalls as a substitute for a longer-term fixed income allocation. Most notably, the yield that they earn is constantly changing. When short-term yields are high, as has been the case for the past few years, they can provide attractive returns relative to other short or even long-term options; however, when short-term yields fall, it is likely that money market fund yields will follow suit. Money market funds typically maintain very short-term maturing securities, and their rates are typically correlated with the Fed Funds rate.

Money market yields have fallen recently, in line with the FOMC lowering the Fed Funds rate by 75 basis points over their last two meetings. Market expectations for future FOMC action (per Bloomberg) are currently for another 75 basis points in cuts over the next ~12 months. Given this outlook, expectations are for money market yields to continue to fall over the next year.

Individual bonds do not subject the investor to this same market risk. When held to maturity, the yield earned on a bond does not change when yields change. The yield, cash flow, redemption date, and redemption price are locked in at the time of purchase, barring a default. This means that even if yields fall, a bond yielding 5% will earn 5% annually until the bond matures.

The illustration below shows a hypothetical 5-year time horizon with investments in different products and puts the effect of owning a money market fund versus an individual bond in context. Using the FOMC's most recent projections for the Fed Funds rate (based on their September Summary of Economic Projections) as a proxy for money market yields, the chart below compares a money market investment over the next five years to purchasing a 5-year Treasury or a 5-year BBB rated corporate bond (note that this is a simplistic comparison looking at average yields and does not take into account reinvestment of income). The yield earned on the money market falls over time, while the Treasury and corporate bond yield remain constant over the five-year timespan.

	<b>Money Market Yield*</b>	<b>5yr Treasury Yield</b>	<b>5yr BBB Corporate Yield</b>
2025	4.375%	4.45%	5.11%
2026	3.375%	4.45%	5.11%
2027	2.875%	4.45%	5.11%
2028	2.875%	4.45%	5.11%
2029	2.875%	4.45%	5.11%
<b>Avg</b>	<b>3.275%</b>	<b>4.45%</b>	<b>5.11%</b>

\*hypothetical yield based on FOMC Dot Plot on 9/18/24. Sources: Bloomberg LP, Raymond James

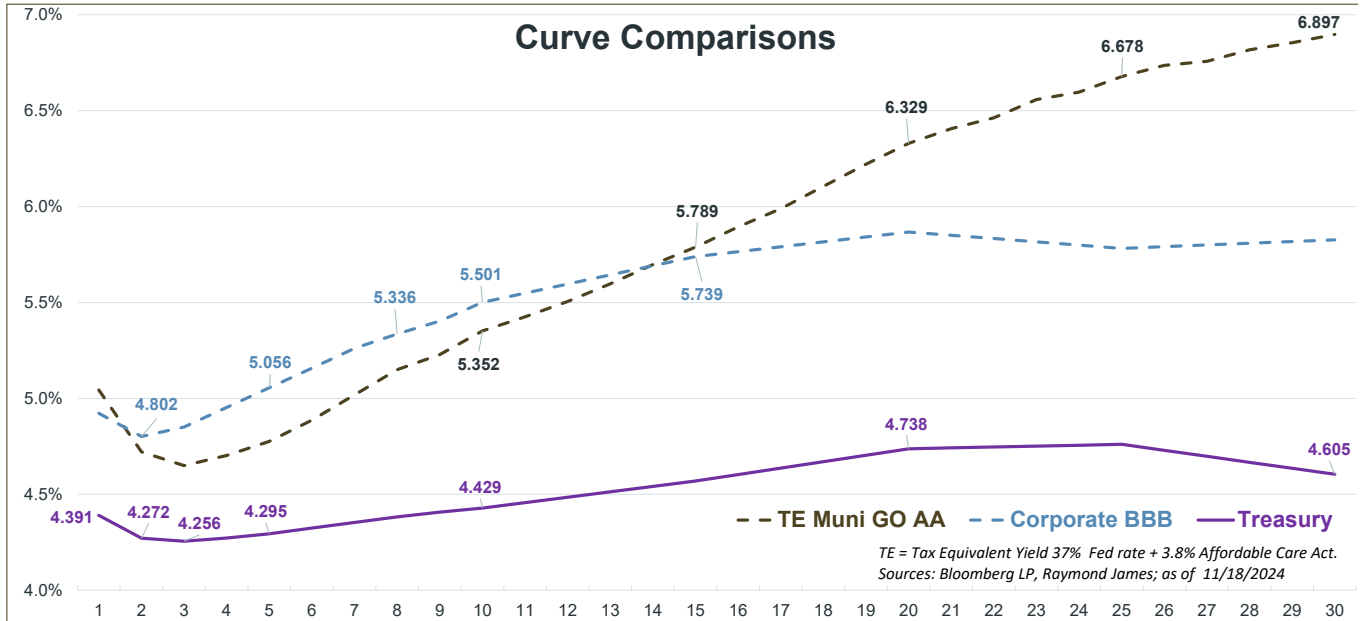
Actual investor results may vary.

The initial yield on the money market versus the Treasury is similar. This is why some investors, when considering the option of putting their fixed income allocation into a money market or purchasing a longer-term Treasury have chosen to go with a money market. Over

much of the past two years, the money market yield was higher than the 5-year Treasury and even now, with the yields as close as they are, investors might not see the benefit of moving from a cash alternative product like a money market out into a longer-term investment. A consideration might be the longer holding period and potential effects on return. The chart illustrates the effects of a potential five-year timespan. Over this hypothetical five-year scenario, the investor would earn an average yield of 3.275% if they chose to invest in a money market versus an average yield of 4.45% if they chose the 5-year Treasury. The difference of ~120 basis points compounded over 5 years can be significant. Purchasing a 5-year BBB rate corporate bond could increase the annual yield by 180 basis points. This 180 basis point benefit on a \$1 million investment is an additional \$18,000 annually. Over 5 years, that is \$90,000. While the yield differences might not seem significant today, it pays to consider the longer-term implications of your investment decisions.

## USING CALL RISK TO BOOST YIELD

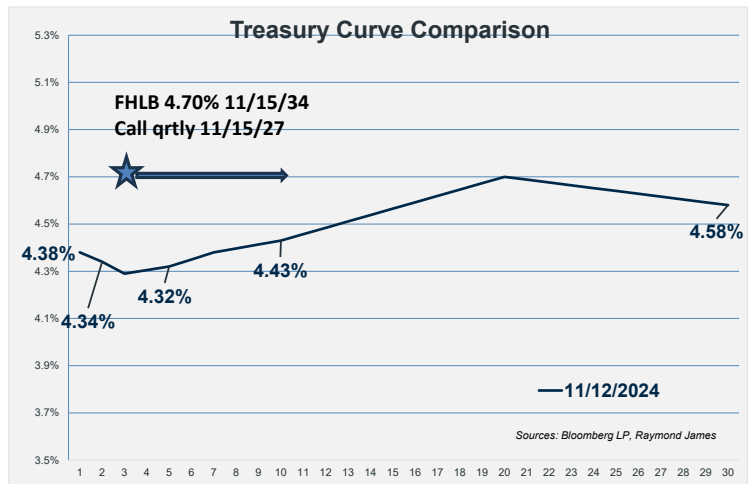
When comparing the Treasury yield curve to alternative product curves, it is easier to pinpoint areas of interest. The purple line below is the Treasury curve and it is notably flat. The light blue dashed line represents the S&P BBB rated corporate curve. This curve has distinctly steepened from roughly 2 to 12



years in maturity before flattening out. A steep curve gives an investor more reward (income) when taking on more risk (price/duration). The dark gray dashed line is the tax-equivalent AA municipal curve. An investor's tax bracket will alter this tax benefit. The higher the tax bracket, the more significant the tax-equivalent impact, and conversely, the lower the tax bracket, the lesser the tax-equivalent yield. This municipal curve has remained upward-sloping for roughly 3 to 30 years.

## AGENCY CALLABLE BONDS

Government agency bonds offer an alternative to investors who understand and are willing to carry call risk. An investor can purchase a 3-year Treasury note at ~4.32% and a 10-year Treasury note at ~4.43%. The illustration depicts a 10-year maturity, 3-year non-call Federal Home Loan agency bond with a 4.7% coupon and yield. The investor is declared 3 years, earning 4.7%, with the possibility that it is not called for up to 10 years. This is a 38 basis point pick up to a 3-year Treasury and a 27 basis point pick up to a 10-year Treasury in an implied government-backed federal agency credit. This may appeal to an investor seeking a little extra yield, willing to accept call risk, but wanting to remain in a very high-quality credit.



Source: Raymond James; For illustrative purposes only.



## MORTGAGE-BACKED SECURITIES

Mortgage-backed securities (MBS) are often, but not always, government agency-backed. Agency-backed MBS have a strong credit backing. These securities are comprised of a pool of underlying mortgages with a myriad of underlying characteristics. Depository institutions sell their loans to lock in a specified spread, free capital to make more loans, and take prepayment and default risk off their books. Investors seek MBS pools to provide both strong yields and strong credit quality. There is risk of return of principal at an undefined pace which is dictated by the prepayment or default of the mortgages that are pooled and are the collateral for the security, known as prepayment risk.

Fannie Mae Pools			
i-rate Δ (bps)	0	+300	-300
<b>4% Coupon [underlying 4.937%]</b>			
Yield	4.90%	4.77%	6.15%
PSA	115	72	552
Avg. Life	10.3	12.6	3.5
Mod. Duration	7.3	8.6	3.0
<b>4.5% Coupon [underlying 5.543%]</b>			
Yield	5.08%	5.00%	6.12%
PSA	129	79	762
Avg. Life	9.8	12.3	2.7
Mod. Duration	6.9	8.3	2.4
<b>5.5% Coupon [underlying 6.524%]</b>			
Yield	5.42%	5.45%	5.12%
PSA	174	87	1012
Avg. Life	8.4	12.1	2.2
Mod. Duration	6.0	7.8	2.0

*Source: Raymond James; Bloomberg (for illustrative purposes only)*

The hypothetical examples depict Fannie Mae (FNMA) pools with a 4%, 4.5% and 5.5% coupon. Note that this is the coupon passed along to the investor. The underlying loans average 4.937%, 5.543%, and 6.524% respectively. This is an important characteristic because the higher the underlying mortgage rate, the higher the likelihood that it prepays. Think of your personal mortgage. If you hold a 7% mortgage and interest rates fall, it may provide an opportunity to refinance (prepay) your mortgage at a lower rate.

The first two pools are priced at a discount and expect to produce ~4.9% and ~5.08% yields. The third pool is priced at a slight premium of \$100.5 with an expected yield of ~5.4%. The speed at which the underlying mortgages pay off ultimately dictates the

realized yield and time when an investor's principal is returned. Unlike many bonds, the principal is not returned in a lump sum at maturity. It is paid back over a time range as the underlying mortgages pay. An investor receives interest and any pro-rata share of principal that pays off early. Therefore, as time passes, an investor risks a decreasing principal amount and receives interest on whatever portion of the principal remains.

The model runs the expected prepayment speed (PSA = the speed at which underlying mortgages pay down) and corresponding yield as well as the expected results should interest rates go up 300 basis points or fall 300 basis points. Since the behavior of the underlying collateral is unknown, looking at extreme possibilities reveals that if an investor finds the range of results attractive, it may be a good investment for the portfolio.



## MUNICIPAL BONDS ~PAR

The municipal curve remains upward sloping providing more yield the further out on the curve invested. With the latest boost in the overall rate environment, 4% coupon bonds near a par dollar price have been available as soon as 15 years in maturity and through 30 years in maturity. This strategy fits well with an overall desire to increase duration and lock into higher yields for longer. The 4% tax-free coupon provides good cash flow with a lower risk of being called than coupons greater than 4%. Most municipal issues are structured with calls inside of 10 years and shorter. The lower the coupon, the more price volatility: 4% coupons provide attractive cash flow while maintaining a lower likelihood of being called.

					37% Fed Tax Rate	32% Fed Tax Rate	22% Fed Tax Rate
Coupon	Maturity	Next Call	Price	Yield-to-Call	TEY-to-Call	TEY-to-Call	TEY-to-Call
				Yield-to-Maturity	TEY-to-Maturity	TEY-to-Maturity	TEY-to-Maturity
4.00%	12/1/2040	12/1/2032	100.26	3.96%	6.29%	5.83%	5.08%
				3.98%	6.31%	5.85%	5.10%
4.00%	4/1/2045	4/1/2034	99.00	4.13%	6.55%	6.07%	5.29%
				4.07%	6.46%	5.99%	5.22%
4.00%	5/15/2050	5/15/2031	97.93	4.37%	6.94%	6.43%	5.60%
				4.13%	6.56%	6.08%	5.30%

Sources: Tradeweb Direct, Raymond James. For illustrative purposes only. Yields and prices are subject to change.

The illustration highlights 2040, 2045, and 2050 maturities with call options in 8, 10, and 7 years respectively. For investors in higher federal tax brackets, tax equivalent yields are greater than 6% and closer to 6.5%. This rate goes up in states with high state taxes for investors holding in-state issues. It should also be noted that the tax-exempt benefit decreases for investors in lower federal tax brackets. The last two columns compare the 32% and 22% tax bracket yields with those of a 37% tax bracket. Municipals tend to be highly rated with very low default rates, and they appeal to wealthy individuals in higher tax brackets seeking to optimize income for extended periods.

## UNCERTAINTY

While history is not guaranteed to repeat itself, the shape of the yield curve has been a very good predictor of a coming recession. Specifically, when the 10-year/3-month Treasury yield spread goes from negative to positive (disinverts), a recession usually follows within a year. The curve has been inverted for over two years, but it is getting very close to disinverting. The 10-year/3-month spread inversion peaked at ~190 basis points in May 2023 and as recently as this September it was over 130 basis points. The inversion is currently less than 10 basis points, so it won't take much of a move to disinvert.

There are a wide range of variables that could have a detrimental effect on the global economy – however, there are also impacts that could provide economic benefits. In reality, things will likely play out somewhere in the middle, as the extreme fear and/or euphoria trumpeted across the market is generally more of a bid for attention and readership/viewership by media outlets than being grounded in a plausible reality. With uncertainty on the horizon, it is a good time to look at the credit risk associated with corporate and municipal investments.

The chart below shows Moody's default statistics over the past 10 years for municipal and corporate bonds. Portfolios with investment-grade bonds benefit from these low default percentages. Over a 5-year period, investment-grade municipals had a 0.01% default rate while investment-grade corporates had a 0.59% default rate. Flipped around, if you owned an investment-grade bond since 2014, there is a 99.4% that the bond did not default over that five-year holding period.

<u>Municipals</u>					
	Year 1	Year 2	Year 3	Year 4	Year 5
<b>Aaa</b>	0.00%	0.00%	0.00%	0.00%	0.00%
<b>Aa</b>	0.00%	0.00%	0.00%	0.00%	0.00%
<b>A</b>	0.00%	0.00%	0.00%	0.01%	0.01%
<b>Baa</b>	0.03%	0.06%	0.10%	0.15%	0.16%
<b>Investment-grade</b>	0.00%	0.01%	0.01%	0.01%	0.01%
<b>Speculative-grade</b>	1.03%	2.21%	3.24%	3.69%	3.97%
<u>Global Corporates</u>					
	Year 1	Year 2	Year 3	Year 4	Year 5
<b>Aaa</b>	0.00%	0.00%	0.00%	0.00%	0.00%
<b>Aa</b>	0.00%	0.00%	0.00%	0.00%	0.00%
<b>A</b>	0.03%	0.06%	0.09%	0.13%	0.19%
<b>Baa</b>	0.11%	0.28%	0.52%	0.77%	1.02%
<b>Investment-grade</b>	0.07%	0.16%	0.30%	0.44%	0.59%
<b>Speculative-grade</b>	3.80%	7.70%	11.42%	14.95%	18.32%

*Source: Moody's Ratings, Raymond James. Cumulative default rates, average over the period 2014-23, municipal vs. global corporate issuers*

Another point to note, specifically in the corporate bond landscape, is the dramatic difference between investment-grade and speculative-grade default rates. While speculative-grade covers a wide range of credit qualities, the numbers shown in the chart are a good reminder as to why speculative-grade bonds (or “junk bonds”) are generally not an appropriate product for the wealth preservation portion of a portfolio. Furthermore, spreads on junk bonds are near their lowest levels of the past 20 years. This means that investors are being compensated relatively little, from a historical perspective, for the additional credit risk that is being taken by purchasing a junk bond.

Investment-grade municipal and corporate bonds provide relatively conservative investment choices with good income opportunities, reliable cash flows, and wealth preservation qualities for many investors.

## MANAGING INTEREST RATES

Interest rates have been a hot topic this year, specifically since the election. The Treasury curve (2yr vs 10yr) was inverted for 793 days making it the longest inversion ever and eclipsing the 624-day inversion which began in 1978. Although the 10-year to 3-month Treasuries are still inverted, the 10 to 2-year inversion ended Friday, September 6, 2024. The Treasury yield curve is currently flat with general sentiment anticipating that it will steepen going into the new year. Given the shifting yield curve, where to position on the yield curve may be in question. It can be good practice to spread out maturities, thus mitigating reinvestment risk. Two different strategies provide a means to mitigate interest rate risk: ladder and barbell structures.

### What is a Laddered Portfolio?

A laddered portfolio allows for an equally weighted capital cash flow distribution for a predetermined time range. It mitigates the effects of falling interest rates since much of the portfolio remains intact and income streams are locked in. If interest rates rise, the shorter-term investments can provide reinvestment opportunities into the higher rate environment. In this way, laddered strategies provide a hedge against changing interest rates. The laddered strategy is flexible and can be customized to meet each client's individual financial goals.

### Benefits of Laddering

A diversified ladder is created by layering a range of maturities and thus reduces overall sensitivity to interest rates. Investing solely in short-term maturities minimizes interest rate risk and provides a higher degree of price stability, yet likely sacrifices income or higher yields. Conversely, investing only in long-term securities may result in greater returns, but increases price volatility and exposes potential losses if early redemption is required.

Building a laddered portfolio requires buying an assortment of bonds with maturities distributed over time. For example, invest equal amounts in securities maturing in two, four, six, eight and ten years. In two years, when the first bonds in the ladder mature, it is reinvested in a 10-year maturity, therefore maintaining the ladder. The goal is to receive the highest return and minimize interest rate and reinvestment risks.

### What is a Barbell Portfolio?

A barbell portfolio is taking a portion of the funds and investing on the front end of the curve and taking another portion of the funds and investing on the intermediate or long end of the curve. This is another way to spread out maturities and may be appropriate for investors who want to keep a greater portion of their maturities on the front end with the expectation that rates could increase in the near term.

### Conclusion

Whether using a ladder or barbell, it can be beneficial to spread out reinvestment risk by using one of these strategies as opposed to putting all your fixed income dollars to work in one spot on the yield curve. This can help provide stability as interest rates move. Regardless of interest rate biases, this year's rate volatility serves as an example of how quickly rates can change. Ladders and barbells are tested strategies that help mitigate reinvestment and interest rate risks.

## 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 more principal assurance? 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 14-person Fixed Income Solutions group within the Raymond James' Fixed Income Capital Markets Group's 43 fixed income locations with more than 500 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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- [Fixed Income Weekly Primer](#)
- [Municipal Bond Investor Weekly](#)
- [Weekly Interest Rate Monitor](#)

## INVESTMENT TYPES/EXPERTISE INCLUDE

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

## Bond Market Commentary

Fixed Income Solutions

### Yield Curve Shift

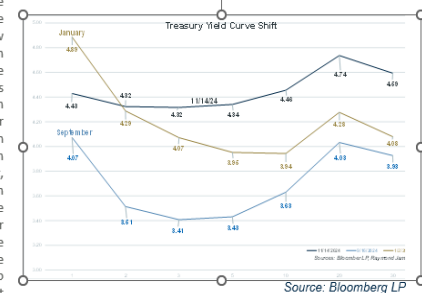


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The Treasury yield curve has shifted appreciably all year long. In particular, the last few months have realized substantial rate changes. The shift in the Treasury curve is not isolated. The corporate curve is also changing. Once flat across all maturity points, the corporate curve boasts more of an upward-sloping shape through 10 years before flattening out. The steeper a curve gets, the greater the balance of reward (income) versus risk (duration/price) for investments that stretch further in maturity.

The shape of fixed income product curves may influence how long-term strategies are implemented. Strategic bond plan implementation can sometimes mirror tactical bond strategy

implementation, which seeks to take advantage of spot market moves relative to forecasts. The graph highlights how the Treasury curve has changed shape in 2024. The gold line represents how the Treasury curve looked at the start of this year. It was extremely inverted, with short-term maturities offering higher rates of return versus longer-term maturities. The general shape in September was unchanged; however, with each maturity exhibiting a much lower rate. The most dynamic curve shape change started around September (light blue line), evolving into the present Treasury curve shape (dark blue line). Except for maturities inside two years, the Treasury curve is now flat through the 10-year note, where it begins to take on an upward slope.



The timing is not coincidental. The Federal Open Market Committee, which meets eight times each calendar year, lowered the Federal Funds rate in September, the first rate cut since March 2020 when COVID pushed the Fed into a 21-month zero interest rate environment. The Fed lowered the Fed Funds rate by 50 basis points in September and 25 basis points in November. Their last meeting in 2024 is December 18. Should they follow with another 25 basis point cut, it is plausible for the Treasury yield curve to finally become "normal" or upward-sloping after two-plus years of inversion.

The markets are fluid, and so are fixed income strategic planning and implementation. Two evolving rate

U.S. Treasury securities are guaranteed by the U.S. government and, if held to maturity, generally offer a fixed rate of return and guaranteed principal value. Fixed-income securities (or "bonds") are exposed to various risks including but not limited to credit (risk of default or principal and interest payments), market and liquidity, interest rate, reinvestment, legislative (changes to the tax code), and call risks. There is an inverse relationship between interest rate movements and fixed income prices. Generally, when interest rates rise, fixed income prices fall and when interest rates fall, fixed income prices generally rise. Short-term bonds with maturities of three years or less will generally have lower yields than long term bonds which are more susceptible to interest rate risk. Credit risk includes the creditworthiness of the issuer or insurer, and possible prepayments of principal and interest. Bonds may receive credit ratings from a number of agencies however, Standard & Poor's ratings range from AAA to D, with any bond with a rating BBB or higher considered to be investment grade. Individual investor's results will vary. Moody's rates more than 10,000 investment-grade municipal issuers, has tracked rating changes over the past 50 years and looked at rating changes (transitions, both year-over-year and multi-year). Each year, Moody's summarizes the number of rating changes, up and down, along with the number of notches in movement.

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The Consumer Price Index (CPI) is a price index representing a weighted average market basket of consumer goods and services purchased by households. Changes in measured CPI track changes in prices over time.

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.

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