4Q 2024

QUARTERLY COMMENTARY

Penn Mutual Asset Management

QUARTER IN REVIEW AND HIGHLIGHTS

U.S. economic growth continues to show no signs of slowing despite weaker growth elsewhere across the global economy. U.S. consumer spending remains on solid footing supported by strong labor market conditions and record-high household wealth. Fourth quarter gross domestic product (GDP) is expected to increase by approximately 3%, which would mark the third consecutive quarter with growth rates near 3%.

- **Following the Federal Reserve's (Fed) 50-basis-point rate cut in September, monetary policymakers lowered interest rates by 25 basis points (bps) during the November and December Fed meetings...** Despite the Fed's pivot to easier monetary policy, longer-term Treasury yields moved steadily higher during the quarter. The 10-year Treasury note closed December at 4.57%, up approximately 80 bps during the quarter. The Treasury yield curve (as measured between the 2-year and 10-year Treasury) continued to steepen after the record-long inversion came to an end in early September.
- **Investment-grade (IG) and high yield credit spreads tightened steadily during the year as strong investor demand absorbed near-record volumes of new issuance...** IG credit spreads tightened by nine bps during the quarter, outperforming duration-matched Treasuries by 82 bps. The high-yield market registered a quarterly total return of 0.17% with lower-quality bonds performing the best.
- **The rapid increase in long-term Treasury yields since the Fed's first rate cut in September started to weigh on equity valuations as 2024 came to a close...** Despite ending on a weaker tone, the S&P 500 Index notched 57 record high closes and generated a total return above 25% for the year. The Magnificent Seven led the way again, representing more than 60% of the S&P 500's annual gain.
- **The increase in long-term interest rates during the quarter more than offset any benefit from Fed rate cuts for homebuyers...** Mortgage rates moved back above the 7% level, leaving housing affordability measures near the lowest in decades.

Our investment capabilities incorporate a unified investment philosophy and process across the risk spectrum

Enhanced Cash	Short Duration Bond	Strategic Income	Short Duration High Yield	Core Plus Bond	High Yield Bond	Balanced Income

SHORT DURATION BOND STRATEGY

The Short Duration Bond Strategy outperformed its benchmark, the Bloomberg U.S. Government/Credit 1-3 Year Bond Index, during the fourth quarter and year-to-date. The 2-year Treasury note yield unexpectedly moved in the opposite direction increasing by 60 bps during the quarter, closing December at 4.24%. Fixed-income investors scaled back expectations for rate cuts during 2025 after Fed policymakers expressed a more cautious approach for easing policy during its December meeting.

Credit markets posted strong performance throughout the year as fixed-income investors continued to take advantage of attractive all-in yield levels. Rapidly changing expectations for Fed monetary policy and elevated interest rate volatility failed to dent the favorable environment for credit markets.

Corporate and securitized credit sector outperformance contributed to the positive results during the fourth quarter and year-to-date. Strategy overweights by sector include collateralized loan obligations (CLOs) and student loan asset-backed securities (ABS). Portfolio duration will be managed in-line to modestly long with the benchmark following the increase in Treasury yields during the fourth quarter.

STRATEGIC INCOME STRATEGY

The Strategic Income Strategy underperformed its benchmark, the ICE BofA 3-Month U.S. Treasury Bill Index, during the quarter but outperformed year-to-date. Long-term interest rates moved materially higher during the quarter even as Fed policymakers continued to lower short-term rates. Fixed-income investors turned more cautious about the inflation outlook after the Republican sweep on Election Day.

Corporate credit spreads continued to grind tighter with investor demand easily absorbing near record-high volume of corporate bond issuance. Agency residential mortgage-backed securities (RMBS) performance modestly trailed duration-matched Treasuries strength during the quarter and year-to-date with elevated interest rate volatility weighing on valuations.

Strategy overweights include intermediate-duration corporate bonds, student loan ABS and RMBS. We are positioning for continued yield curve steepening while remaining opportunistic with duration management.

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ABOUT US

Penn Mutual Asset Management (PMAM) is an insitutional asset management firm located just outside of Philadelphia, PA. Since 1989, the firm has been dedicated to creating value through a prudent, thoughtful and rigorous investment decision-making process. With over $39 billion in assets under management, PMAM is committed to offering fixed income investment solutions and client-focused services.

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SHORT DURATION HIGH YIELD STRATEGY

The Short Duration High Yield Strategy underperformed its benchmark, the ICE BofA 0-2 Year Duration BB-B U.S. High Yield Constrained Bond Index, during the fourth quarter but outperformed year-to-date.

High yield credit spreads continued to tighten during the fourth quarter as the market rallied post-presidential election. This occurred despite the 10-year Treasury rising approximately 80 bps, largely in anticipation of higher inflation and additional Treasury supply. Spreads ended the year at close to 15-year tights with the growth outlook solid and default projections for 2025 benign. The front end of the high-yield market was strong, supported by tender/call activity as issuers looked to term out maturities. New issue supply was robust and met with strong demand.

The Strategy maintained its overall risk profile, adding selectively to a few bonds with more spread duration. The Strategy ended the year with a portfolio duration of just under two years, approximately half of year longer than the benchmark. Average portfolio credit quality was in the BB category while the average position size was approximately 1%.

CORE PLUS BOND STRATEGY

The Core Plus Bond Strategy outperformed its benchmark, the Bloomberg U.S. Aggregate Bond Index, during the fourth quarter and year-to-date. Corporate credit spreads tightened steadily throughout the year as strong investor demand easily absorbed near-record new issue volume. IG and high-yield corporate credit spreads finished the year near the tightest levels in two decades. IG corporate bonds tightened by 19 bps during 2024, outperforming duration-matched Treasuries by 246 bps. The high yield corporate bond market generated returns above 8% during the year with lower-quality credits outperforming.

New purchase activity during the quarter remains focused on securitized spread sector investments including agency guaranteed RMBS, which offer attractive value relative to corporate bonds. We are moving Strategy duration, or interest rate risk, in line with the benchmark and positioned to benefit from yield curve steepening.

HIGH YIELD BOND STRATEGY

The High Yield Bond Strategy outperformed its benchmark, the Bloomberg U.S. High Yield BA/B 2% Issuer Capped Index, during the fourth quarter and year-to-date.

The high yield credit market was solid during the quarter with spreads tighter and volatility muted. This occurred despite an approximately 80-basis-point rise in the 10-year Treasury rate. The rise in rates was attributable to the stronger growth outlook, the anticipated tariff and immigration policies of the new administration which could lead to stickier inflation as well as a slower trajectory for future Fed rate cuts. Down in quality credit continued its strong performance due to the benign default environment and solid fundamental outlook. New issue supply remained robust, largely to support refinancing activity, which further served to chip away at the high yield maturity wall.

The Strategy maintained its overall risk profile, balancing select exposure to low-quality credit that has a solid fundamental outlook and/or positive catalysts/event risk, with core BB-rated bonds. Energy exposure was reduced in response to the decline in oil prices — the latter being a function of adequate supply in the market and concerns regarding reduced Chinese demand.

BALANCED INCOME STRATEGY

The Balanced Income Strategy outperformed its benchmark, the Morningstar Moderately Conservative Target Risk Total Return USD Index, during the fourth quarter and year-to-date. Both stocks and bonds fell modestly on an absolute basis. The Strategy's equity portfolio performed well on a relative basis as both its stock and bond portfolios declined less than their respective benchmarks.

The market rallied broadly following the initial reaction to the U.S. presidential election results. However, as the markets digested the potential impacts of future policy changes, the stock market reversed course and interest rates climbed higher. One big factor in this reversal, especially for U.S. Treasury bonds and interest rates, was Fed rate cut expectations declining sharply after the December meeting. Risk assets, which were eagerly anticipating an extended easing cycle, were disappointed. The result was an increase in interest rates for longer maturities that offset most of, if not all, of the Fed's rate cuts to date. For the Strategy, non-interest-rate sensitive positions, namely convertible bonds and preferred stock holdings, provided positive absolute returns which also led to relative gains.

In terms of overall allocation (stock, bond and cash weightings), the allocation successfully reinvested much of the inflow received at the end of the third quarter. By year end, the Strategy finished with 39% in common stock, 47% in fixed income and 14% in cash and equivalents. The intention now is to manage its positions actively while maintaining as much flexibility as possible given the potential for headwinds due to political policy changes, rising interest rates and future market volatility.

The Strategy's positioning should provide the potential for higher portfolio yields and favorable total return. We will continue to monitor our investable universe for any opportunity to add value. We believe this focus on individual security selection will help to decrease the portfolio's exposure to market beta while allowing for positive alpha generation.

OUTLOOK

The rapid rise in Treasury yields since the Fed started to lower interest rates marks a significant shift in the balance of power for setting monetary policy. Fed policymakers will likely be forced to follow the lead of bond investors who are now saying the Fed needs to be patient with additional rate cuts.

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INDEX DEFINITIONS:

Bloomberg U.S. Aggregate Bond Index – An index that is a broad-based flagship benchmark that measures the investment grade, US dollar denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate securities, MBS (agency fixed-rate and hybrid ARM pass-throughs), ABS and CMBS (agency and non-agency).

Bloomberg U.S. Government/Credit 1-3 year Bond Index- The Bloomberg U.S. Government/Credit Bond Index is a broad-based benchmark that measures the non-securitized component of the US Aggregate Index. It includes investment grade, US dollar-denominated, fixed-rate Treasuries, government-related and corporate securities.

Bloomberg U.S. High Yield Ba/B 2% Issuer Capped Index – This index measures the performance of fixed-rate dollar-denominated debt securities with rating Ba/B. The securities instruments are non-investment grade. There is a limit of 2% maximum exposure to any one issuer.

ICE BofA 0-2 Year Duration BB-B U.S. High Yield Constrained Index – This index measures the performance of ICE BofAML 0-2 years Duration BB-B U.S. High Yield Bond. It's all securities in the ICE BofAML U.S. High Yield Index rated BB1 through B3 and with a duration-to-worst less than two years, but caps issuer exposure at 2%.

ICE BofA 3-Month U.S. Treasury Bill Index – This index measures the performance of a single issue of an outstanding treasury bill which matures closest to, but not beyond, three months from the rebalancing date. The issue is purchased at the beginning of the month and held for a full month; at the end of the month that issue is sold and rolled into a newly selected issue.

Morningstar Moderately Conservative Target Risk Total Return USD Index – The Morningstar Target Risk Index family is designed to meet the needs of investors who would like to maintain a target level of equity exposure through a portfolio diversified across equities, bonds and inflation-hedged instruments. The Morningstar Moderately Conservative Target Risk Index seeks approximately 40% exposure to global equity markets.[*]

[*]The Morningstar Indexes are the exclusive property of Morningstar, Inc. Morningstar, Inc., its affiliates and subsidiaries, its direct and indirect information providers and any other third party involved in, or related to, compiling, computing or creating any Morningstar Index (collectively, "Morningstar Parties") do not guarantee the accuracy, completeness and/or timeliness of the Morningstar Indexes or any data included therein and shall have no liability for any errors, omissions, or interruptions therein. None of the Morningstar Parties make any representation or warranty, express or implied, as to the results to be obtained from the use of the Morningstar Indexes or any data included therein.

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Offering a wide range of tailored investment strategies and solutions to help meet the investment goals of our clients, while focusing on our mission to provide exceptional experience and service.

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