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## MARKET REVIEW

- In December, global sovereign yield curves steepened markedly despite hawkish rhetoric from major central banks as term premium rose in response to deteriorating fiscal trajectory. Credit spreads widened and fixed income sectors posted mixed excess return results.
- Most global sovereign bond yields moved upward with yield curves steepening across major developed economies. US Treasury yields rose, particularly in the latter part of the month following the Fed's hawkish tilt. European yields also moved higher despite European Central Bank's fourth rate cut this year as President Christine Lagarde stated the euro zone was getting very close to reaching the central bank's medium-term inflation goal. US Federal Reserve delivered a rate cut of 25 basis points but signaled a hawkish stance. The European Central Bank cut rates by 25 basis points but stressed vigilance on service inflation.
- Global credit markets outperformed duration-equivalent government bonds over the month. The industrials and utilities sectors performed in line with duration-equivalent Treasuries, whereas the financials sector underperformed relative to duration-equivalent Treasuries. Broadly, municipal bonds underperformed duration-equivalent Treasuries. Within the securitized sectors, agency mortgage-backed securities, commercial mortgage-backed securities, and asset-backed securities each outperformed duration-equivalent government bonds.

## FUND PERFORMANCE AND ATTRIBUTION

- The portfolio generated a negative total return during the month, but it outperformed the Bloomberg Global Aggregate hedged to USD index.
- The portfolio's corporate credit positioning had a small positive impact on performance overall. At the broad sector level high yield credit underperformed while US investment grade corporates performed in line duration-equivalent government bonds, respectively. Positioning within high yield credit had a small positive impact on performance. An underweight to US investment grade corporates, mainly industrials, detracted from results. This negative impact was offset by positive results from an overweight to financial institution issuers within developed non-US IG credit. An allocation to emerging markets high yield corporates was neutral for relative results.
- Within securitized sectors, an overweight to agency mortgage back securities (MBS) in support of the Affordable Housing theme had a neutral impact on performance, while an allocation to commercial mortgage-backed securities (CMBS) helped results as spreads tightened amid the Fed's third rate cut of the cycle and a decline in short-term rates.
- An allocation to taxable municipals, primarily allotted to Education & Training and Health themes, had a small positive impact on results.
- Overall duration and yield curve positioning benefited performance the most over the month. The portfolio held an underweight duration position.

## FUND POSITIONING AND OUTLOOK

- We believe a "no landing" scenario is likely in 2025, in which a strong consumer, low employment, and loose fiscal policy support economic growth while sticky inflation keeps rates "higher for longer" and restrains the pace of global central bank cutting. We believe that the current credit cycle remains robust, supported by strong fundamentals, technicals, and attractive all-in yields. As a result, we think investors can benefit from a pro-credit tilt while exploiting potentially compelling bottom-up sector and security selection opportunities.
- Although major global central banks have continued to cut short-term interest rates throughout 2024, we expect rates to remain higher for longer. Uncertainty around central banks' reaction functions, the pace of balance sheet reductions, and the magnitude of government debt issuance could contribute to greater credit spread volatility and increased dispersion in the credit spreads of individual issuers.
- In terms of positioning, the portfolio has a close to neutral credit risk profile, while preserving high-quality liquid instruments to take advantage of future market dislocations.
- From a sector perspective, the portfolio maintains an off-benchmark allocation to select taxable municipals, emphasizing healthcare and education issuers. The portfolio holds select below investment-grade corporates and bank loan issuers that in our view carry attractive credit spreads.
- The portfolio maintains positioning in agency MBS issuers with a focus on supporting housing affordability for low-income borrowers. We continue to hold select single-asset single borrower CMBS backed by LEED certified buildings.
- The portfolio maintains exposure to labelled use-of-proceeds government and agency bonds intended to fund green, social, and sustainability-related projects.

## PAST PERFORMANCE DOES NOT PREDICT FUTURE RETURNS. AN INVESTMENT CAN LOSE VALUE.

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