MONTHLY FIXED INCOME MARKET UPDATE

VICTORY income investors®
A VICTORY CAPITAL® INVESTMENT FRANCHISE

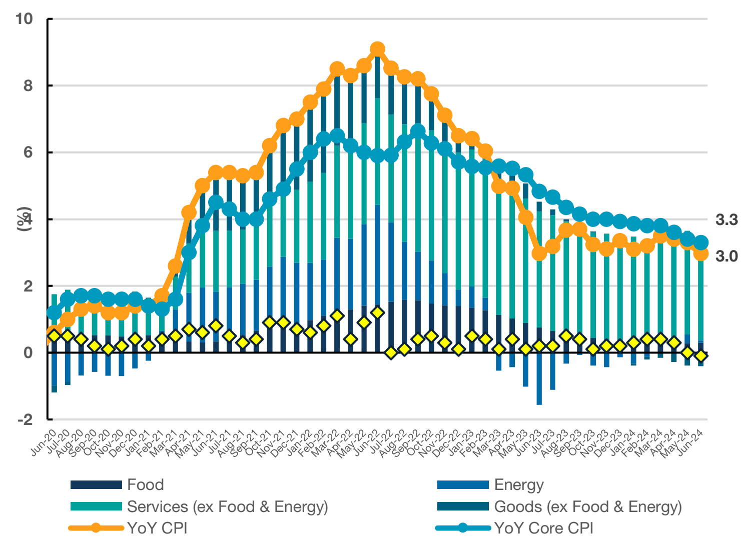
As of July 31, 2024

Key Takeaways

1. Treasury yields decreased across the curve in July as inflation continued to trend downward and market participants grew more confident in future rate cuts, driving positive performance.
2. The Consumer Price Index and Personal Consumption Expenditure Index figures for June came in at or below 3%, a win for investors eager to see rate cuts and progress for the Federal Reserve (the Fed).
3. After the Fed kept rates unchanged at the July Federal Open Market Committee meeting, market participants are pricing in a nearly 100% chance for a rate cut in September, as well as raising their expectations for additional cuts in 2024.

The Month in Charts

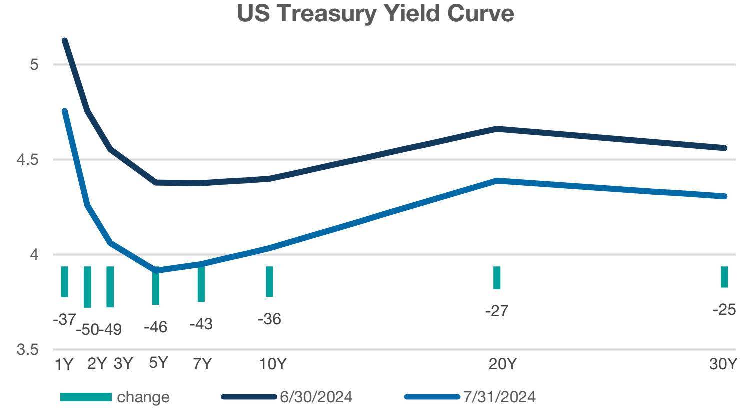
Year-over-year CPI for June came in at 3.0% driven by services inflation. While we aren't quite out of the woods yet in terms of inflation, July's FOMC meeting indicated to markets that, barring any shocking developments, a September rate cut is possible. While no official confirmation on timing was made in the following press conference, the tone was more confident that the economy is slowing at an appropriate pace. Policy easing seems more likely than it has in the past few months amidst some weaker labor market data.



Source: Bloomberg

The Treasury yield curve moved down across all tenors as markets quickly reacted to comments from policymakers that seemingly align with market pricing for a September rate cut.

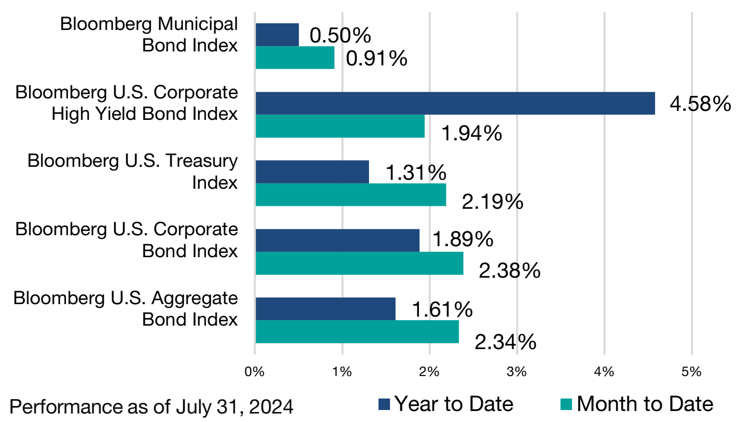
US Treasury Yield Curve



Source: Bloomberg

Bonds rallied toward the end of July after some weaker economic reports and concern that the Fed is not moving fast enough to keep up with labor market softening. Yields dropped, driving positive performance across indices.

Returns (%) for Fixed Income Indices



Performance as of July 31, 2024

Past performance is no guarantee of future results. *Source: Bloomberg*

Credit spreads were mixed across fixed income classes throughout July, investment grade and high yield corporate credit concluded near their three-month wides.

				Quarter		Change		
Asset Class	Yield	Spread	Trend	Tight	Wide	MoM	QoQ	YoY
U.S. Treasury	4.19							
U.S. MBS	4.88	44		42	53	-4	-12	44
U.S. Corporate	5.14	93		84	94	0	7	93
U.S. Corporate High Yield	7.79	314		288	321	3	14	314
CMBS	5.07	99		94	100	2	0	99
ABS	4.91	57		51	58	1	7	57
A	5.02	82		73	83	0	7	82
BBB	5.36	116		105	116	0	7	116
BB	6.41	188		168	191	12	9	188

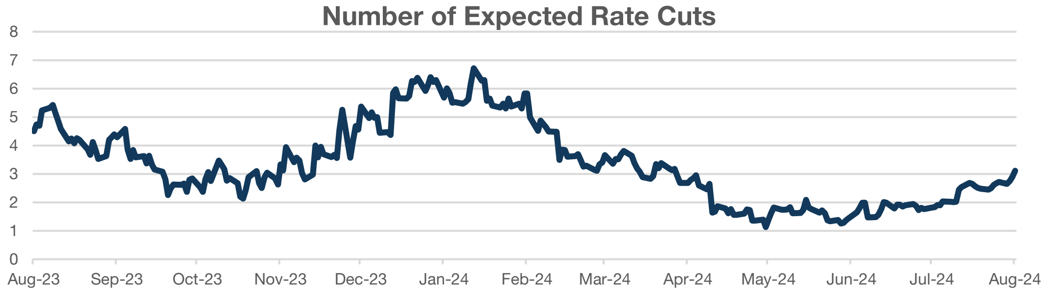
Source: Bloomberg; Asset Classes represented by: ICE BofA US Treasury & Agency Index, Bloomberg US MBS Index, Bloomberg US Agg Total Return Value Unhedged USD, ICE BofA US High Yield Index, ICE BofA US Fixed Rate CMBS Index, ICE BofA US Fixed Rate Asset Backed Securities Index, Bloomberg US Agg A Total Ret Index, Bloomberg US Agg Baa Total Ret Index, Bloomberg Ba US High Yield TR Index. MoM/QoQ/YoY as of 07/31/2024

Bonding over Bonds

Our video series on the fixed income markets

In our #BondingOverBonds video series, experts discuss notable activity in the fixed income markets: Watch Now

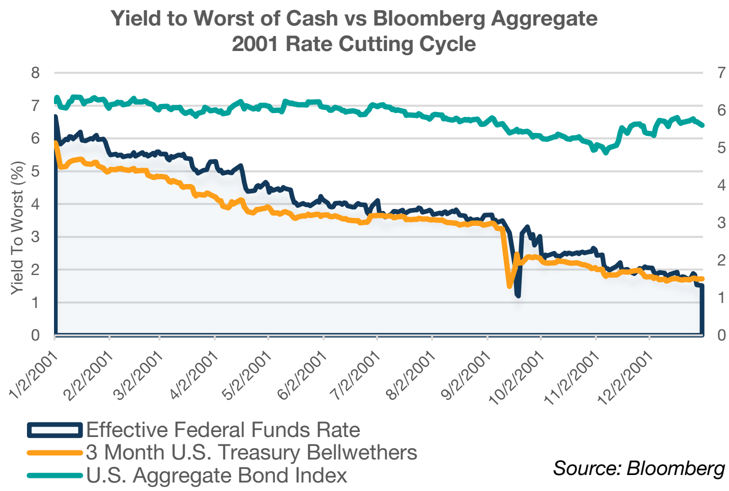
The July FOMC meeting confirmed the expectations of many market participants–rates were held steady, and Chairman Powell used more dovish language, stating that a rate cut could come as soon as September. While not a complete shock to those paying attention, policymakers continue to hedge on the timing of a rate cut and have indicated that they still require more confidence in the data prior to lowering borrowing costs. Market expectation for rate cuts in 2024 increased following the meeting from two to three cuts in 2024.



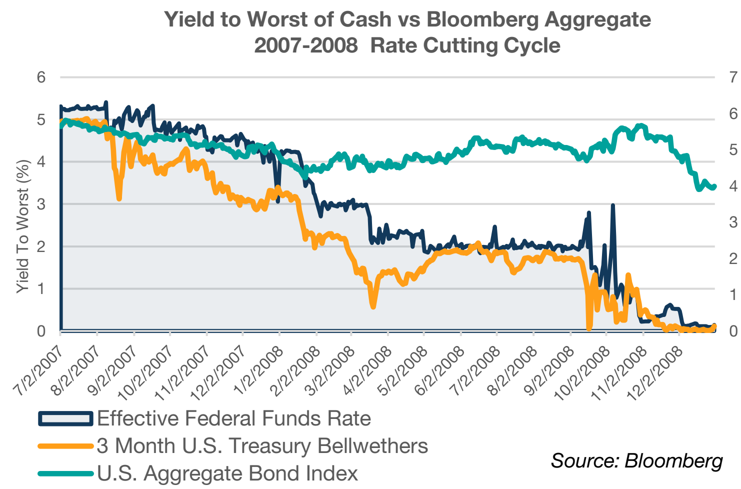
Source: Bloomberg

Our Current Thinking

As fixed income investors closely watch for the next move in monetary policy, we suggest considering some of the historical implications rate cutting cycles had for cash and money markets, particularly when the yield curve was inverted. In the most recent rate cutting cycles, 2001 and 2007-2008, we saw money market yields drop dramatically once the Fed began easing monetary policy. Because the yield curve was inverted, like the current state, the yields on the shorter end of the curve had the most room to fall. See below two examples of historical changes in money market yields as rates were lowered. Historically, money market yields have tracked the effective federal funds rate closely.



Source: Bloomberg



Source: Bloomberg

It's our view that fixed income investors looking to lock in the attractive yields intermediate term bonds currently offer, which are still elevated by historical standards, could benefit by extending duration and making a shift from cash or money markets into risk assets. In the two charts, we show that intermediate term fixed income, represented by the Bloomberg Aggregate Index, declines but not to the same magnitude as money markets.

What We'll Be Watching in the Month Ahead

We will be watching the economic health indicators, inflation, and the following in the month to come:

- **August 2nd,** the next Nonfarm Payrolls and Unemployment Rate: These reports will be important data points for the market and Fed, as they provide further insight into the labor market and future monetary policy.
- **August 14th,** the next CPI will be released: This report will offer insight into whether inflation is continuing to moderate and moving towards the Fed's 2% target.
- **August 27th,** the next Conference Board Consumer Confidence report: This report is a leading indicator of economic conditions and will offer insight into how consumers view the economy, including labor market conditions, business conditions, and future spending plans amongst other points.

Basis point "bps" is 1/100th of a percentage point. **Credit spread** is the difference in yield between a U.S. Treasury bond and another debt security of the same maturity but different credit quality. Credit spreads are the additional compensation that investors require to hold securities that are not as safe and liquid as those issued by the US Treasury. **The Treasury Yield Curve** shows the relationship between the US bond yield and the time to maturity. Yield and price have an inverse relationship. As the yield curve lowers, the price of bonds increase. **Tenor:** the length of time until a debt is due. **Core CPI:** CPI excluding food and energy. **Consumer Price Index (CPI),** a popular measure of inflation and deflation calculated by the Bureau of Labor Statistics, measures the monthly change in prices paid by U.S. consumers. **Personal Consumption Expenditure Price Index** is a measure of the prices that people living in the United States, or those buying on their behalf, pay for goods and services and is known for capturing inflation (or deflation) across a wide range of consumer expenses and reflecting changes in consumer behavior.

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