Eagle Monthly Commentary

EAGLE Asset Management
AN AFFILIATE OF CARILLON TOWER ADVISERS

Fixed Income

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Market Overview

The bond market, as measured by the Bloomberg U.S. Aggregate Bond Index, gained 0.61% in April, bringing the year-to-date return to 3.59%. Positive performance for the month can be attributed to slight credit spread tightening and a marginal decrease in interest rates along the belly of the yield curve. The yield on the benchmark 10-year U.S. Treasury note fell from 3.47% at the end of March to 3.42% .

Investment-grade corporate bonds, as measured by the Bloomberg U.S. Corporate Bond Index, gained 0.61% during the month. Corporate bonds stabilized in April — with marginal credit spread tightening after a tumultuous March — following the collapse of multiple banks and a spike in volatility. The average corporate credit spread tightened two basis points, from 1.38% to 1.36%.

Corporate bonds outperformed all other major fixed-income sectors on a total return basis, and they outperformed relative to U.S. Treasuries on a duration-adjusted basis. Government-related securities and securitized products (asset-backed securities, mortgage-backed securities, and commercial mortgage-backed securities) posted a positive total return during the month; government-related securities outperformed relative to Treasuries, and securitized products underperformed relative to Treasuries.

Portfolio Review[1,2]

Taxable portfolios

Our overweight to securitized products was a headwind to performance in our High-Quality Taxable portfolios: our securitized products lagged behind the benchmark index's Treasuries during the month as yields along the belly of the curve fell sharply. Positive attribution in the Taxable Managed Income Solutions strategy was generated by accretive sector allocations, duration positioning, and security selections. In the Vertical Income objective, security selection and allocations within our preferred securities and high dividend-focused equities sleeves were dilutive to performance. In our corporate bond sleeve, positive security selection was more than offset by negative broader allocation effects. Our elevated cash position detracted from performance.

Tax-sensitive portfolios

Municipal bonds were negative for April. The Bloomberg U.S. Municipal Bond Index is down 0.23%, and the year-to-date return is 2.54%. U.S. Treasuries were up 0.54% for the month, and municipal bonds underperformed the Bloomberg U.S. Treasury Index by 77 basis points. Total return performance was negative across the curve, with the long end outperforming; the 1-year and 5-year indices were down 0.29% and 0.45%, and the 20-year and 22+ year indices were down .03% and 0.19%, respectively. The selloff is the result of tapering demand driven by bank selling pressure and investor outflows from municipal bond funds, and the bonds themselves remain expensive relative to their historical levels.

Municipal AAA to Treasury yield ratios were cheaper across the curve, and short maturities cheapened the most. The 2-year, 10-year, and 30-year ratios ended April at 66%, 69%, and 95%, cheapening by 8 percentage points (pp), 3 pp, and 2 pp, respectively. These ratios are expensive relative to their five-year averages, and our approach to funding new accounts will be slow and

opportunity-specific. We are actively looking for opportunities in the market to sell credits that we believe are at peak prices and/or showing weakness in credit fundamentals. We expect May and June to be strong for municipal bonds, but we remain cautious in the face of debt ceiling uncertainty that could bring more volatility.

Net municipal bond fund outflows were elevated in April, totaling $4.2 billion. Nine of the past 11 weeks reported net municipal bond fund outflows, and April was the second consecutive month of such activity, bringing net outflows to $3.9 billion year to date. Municipal issuance in April totaled $30.6 billion, lower than April's $33.8 billion average over the past five years and down 24% year over year. Year-to-date issuance is $107.6 billion; tax-exempt issuance is down 22% to $93.2 billion; and taxable municipal issuance is down 41% to $14.4 billion. We expect supply to stay at muted levels until rate volatility diminishes.

Headlines in April focused heavily on regional bank concerns and the potential for sizeable liquidations of municipal bond positions. Although some selling did occur, the majority of bank portfolios are believed to be bond structures that our municipal programs do not buy: long-dated, low coupon, or bonds with poor credit quality. The liquidation of bonds has the potential to affect segments of the market that we do not purchase, which could put further pressure on bond prices and create buying opportunities for our programs.

On the policy front, debt ceiling negotiations are front and center; state and local governments are bracing for a halt to federal funding if Congress and the White House fail to reach an agreement. According to the National Association of State Budget Officers, federal funds accounted for 38% of state budgets in fiscal year 2022. Without federal funding, it is difficult for states to make funding decisions and run essential programs.

Congress raised the debt ceiling in December 2021, and the United States is expected to hit its $31.4 trillion debt limit sometime in June. If congressional grandstanding increases market volatility, municipal issuers could delay issuances and contribute to further imbalances in supply and demand. Eagle structures its municipal programs to withstand market volatility, and we expect the high-quality nature of the securities we own to have less price sensitivity. We recommend dollar-cost averaging into municipals for portfolios that are underweight fixed income.

Outlook[1]

Our near-term outlook remains cautiously constrained. The unknown extremities of ongoing headwinds continue to muddy the future economic landscape, and the headline-driven nature of the market has sparked bearish sentiment and rash reactions as investors speculate about the next shoe to drop. As we position portfolios for the future, prominent concerns include — but are certainly not limited to — continued stresses within the banking sector, debt ceiling negotiations, and the impact that those events will have on the economy and future monetary policy.

The accelerating timeline for a potential U.S. debt default has rapidly increased investor angst. Treasury Secretary Janet Yellen has warned government leaders and the public that the Treasury could run short of cash to fund its obligations by June 1. An event of this nature would not only force a sharp rise in volatility, it would also be unequivocally bad for risk assets. We've seen a drastic repricing at the front end of the yield curve as investors brace for the worst, demanding heightened compensation for the underlying risks. Yields on two- and three-month U.S. Treasury bills spiked by more than 30 basis points in April, closing the month near a 5% yield.

Although past negotiations involving the debt ceiling were typically resolved at the last minute — which remains the highest-probability outcome in the present — current discussions are marked by an elevated likelihood of miscalculation or failed negotiations. In the past, members of Congress have pitched the idea of debt-limit prioritization, having the Treasury divert funds from other government entities to make debt interest payments and avoid default. This sort of prioritization is likely to be unfeasible, and it risks a multitude of legal headaches.

The impact of an actual debt ceiling event would likely be short-lived; market reactions should impose pressure for a swift resolution. However, the negative trends already in place suggest that even a brief hiccup could have severe economic repercussions.

The U.S. Federal Reserve (Fed) has reached a tough inflection point: its resolve to maintain a "higher for longer" interest rate environment is being tested by multiple bank failures, the possibility of a U.S. debt default, and an economy that is slowing, yet resilient. The initial first quarter real gross domestic product (GDP) print was 1.56% year over `year, or a 1.06% quarter-over-quarter seasonally adjusted annualized rate (headline), which was well below consensus estimates of 1.9% headline growth. In the fourth quarter of 2022, growth accelerated from 0.88% on a year-over-year basis, driven by upside to consumer spending. To a lesser extent, growth was also assisted by government

spending while business investment, home building, and inventories decreased.

This reacceleration is important; we're big believers in monitoring rates of change and not "levels." However, this acceleration in GDP growth does not look especially relevant from our perspective. It was largely on the back of robust January data, and we are now in May. For more context, February and March data shows that monthly growth for headline retail sales, retail control group sales, and real personal consumption expenditures averaged -0.69%, -0.19%, and -0.14%, respectively. They have reverted to decelerating each month on a year-over-year basis.

One of the next hurdles on the horizon — which will only add to an already complicated outlook for the Fed — is how upcoming inflation measures stack up against easier base effects in the summer months. We expect the Federal Open Market Committee to hike another 25 basis points in the upcoming May meeting, marking its 10th consecutive hike this cycle. Although markets are not pricing in a hike in June, we do not believe that the possibility should be taken completely off the table; the impact of previously mentioned events remains unknown. It will be worth watching to see whether the Federal Reserve reacts to a broader selloff triggered by the debt-ceiling issue and/or a deeper banking crisis. Any sort of pivot to Fed policy would be decidedly bearish for risk assets, considering the aforementioned crises.

The end of the current rate hike regime may be approaching, but yields continue to present income-oriented investors with attractive opportunities that have not been attainable in either the fixed-income market or other income-producing assets for more than a decade. The enhanced yield landscape and turbulence in the regional banking sector have supercharged flows into money market assets, adding more than $650 billion year-to-date.

It is worth noting that in each of the past five interest-rate tightening cycles — dating back to the late 1980s — the bond market has outperformed relative to money market assets in all subsequent 1-, 3-, and 5-year periods following the end of the interest-rate hike cycle. Investors need to remain nimble, applying a tactical approach to adjust portfolio exposures on the margin and deploying sidelined cash for long-term income-generating opportunities. An active risk management approach, and a focus on selecting securities that boast strong credit metrics and ample liquidity, will be necessary to ride out the elevated stochasticity present in the markets.

1. References to specific securities are intended to illustrate the types of securities Eagle may hold in this portfolio. They are not intended as representations of specific investment recommendations that would have been profitable to an investor. Past performance is not a guarantee of future results. Opinions and estimates offered constitute Eagle's judgment and are subject to change without notice as are statements of financial-market trends, which are based on current market conditions. Investing involves risk, including the possible loss of principal.

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2. Sources: Investor Tools Perform and Yield Book

Investing in bonds involves risks that may adversely affect the value of your investment such as inflation risk, credit risk, call risk, interest rate risk, and liquidity risk, among others. The two most prominent factors are interest rate movements and the credit worthiness of the bond issuer. Investors should pay careful attention to the types of fixed income securities that comprise their portfolios and remember that, as with all investments, there is the risk of loss of capital. A Real Estate Mortgage Investment Conduit (REMIC) is a type of multiclass mortgage-related security in which interest and principal payments from mortgages are structured into separately traded securities. These classes are distinguished by their sensitivity to the prepayment risk of the underlying mortgage-related collateral. Therefore, they may be more or less sensitive to prepayment risk, bear different interest rates, and have various average lives and final maturities.

Asset-backed securities (ABS) and mortgage-backed securities (MBS) are created by pooling loans from a variety of sources and issuing bonds that are backed by these loans. Creditworthiness stems from the credit quality of the underlying loans, as opposed to corporate bonds in which creditworthiness is derived from the earning power of the issuing company. The primary risk of these securities is interest-rate risk. Rising interest rates might cause loan principal prepayments to slow, resulting in less available principal to invest at prevailing higher rates. Conversely, rate decreases might accelerate prepayments, leaving more dollars to invest at lower rates.

Investment-grade refers to fixed-income securities rated BBB or better by Standard & Poor's or Baa or better by Moody's.

Convertible securities and preferred stock combine the fixed income characteristics of bonds with some of the potential

for capital appreciation of equities and, thus, may be subject to greater risk than pure fixed-income instruments. Unlike bonds, preferred stock and some convertible securities do not have a fixed par value at maturity, and in this respect may be considered riskier than bonds. Convertible securities may include convertible bonds, convertible preferred stocks and other fixed-income instruments that have conversion features.

Investments in high-yield bonds and convertible securities are subject to the client's authorization, as set forth in the Investment Management Agreement. Such investments may be subject to greater risks than other fixed-income investments. The lower rating of high-yield bonds (less than investment grade) reflects a greater possibility that the financial condition of the issuer or adverse changes in general economic conditions may impair the ability of the issuer to pay income and principal. Periods of rising interest rates or economic downturns may cause highly leveraged issuers to experience financial stress, and thus markets for their securities may become more volatile. Moreover, to the extent that no established secondary market exists, there may be thin trading of high-yield bonds, which increases the potential for volatility.

Definitions

A credit spread is the difference in yield between a U.S. Treasury bond and another debt security with the same maturity but different credit quality. Also referred to as "bond spreads" or "default spreads," credit spreads are measured in basis points, with a 1% difference in yield equaling a spread of 100 basis points. Credit spreads reflect the risk of the debt security relative to the Treasury bond, which is considered to be risk-free. Higher quality securities have a lower chance of the issuer defaulting. Lower quality securities have a higher chance of the issuer defaulting.

A yield curve is a line that plots yields (interest rates) of bonds having equal credit quality but differing maturity dates. The slope of the yield curve gives an idea of future interest rate changes and economic activity.

Basis points (bps) are measurements used in discussions of interest rates and other percentages in finance. One basis point is equal to 1/100th of 1%, or 0.01%.

Total return, when measuring performance, is the actual rate of return of an investment or a pool of investments over a given period of time. Total return includes interest, capital gains, dividends, and distributions realized over the specified period. Total return accounts for two categories of return: income including interest paid by fixed-income investments, distributions, or dividends and capital appreciation, representing the change in the market price of an asset.

Duration incorporates a bond's yield, coupon, final maturity and call features into one number, expressed in years, that indicates how price-sensitive a bond or portfolio is to changes in interest rates. Bonds with higher durations carry more risk and have higher price volatility than bonds with lower durations.

Levels and rates of change are used in economic analysis: A level identifies the value of a specific indicator at a given point in time, and a rate of change is used to determine how fast an indicator has risen (or declined) over a specific period.

Headline measures of economic activity, such as retail sales, include all economic activity and are often referred to as nominal measures. Real measures of economic activity are adjusted for inflation, in some cases by excluding more volatile prices for things like food and fuel.

The retail control group represents the total industry sales that are used to prepare the estimates of the Personal Consumption Expenditures Price Index for most goods. Those sales include total retail trade, less automobile dealers, building material and garden equipment and supplies dealers, gasoline stations, office supply and stationery stores, mobile home dealers, tobacco stores, and gasoline sales at warehouse clubs, supercenters, and grocery stores, except for convenience stores.

Real personal consumption expenditures (PCE) is the primary measure of consumer spending on goods and services in the U.S. economy.

The AAA Municipal to Treasury yield ratio is a comparison of the yield of AAA municipal bonds to U.S. Treasuries. It aims to ascertain whether AAA municipal bonds are an attractive buy in comparison.

Credits are a generic term for fixed-income securities such as corporate bonds, mortgage- or asset-backed securities, municipal bonds, or emerging market bonds.

Fund flow is the net of all cash inflows and outflows into and out of a particular financial asset, sector, or index. It typically is measured on a quarterly or monthly basis. Investors and others look at the direction of fund flows for indications about the health of specific securities and sectors or the overall market.

Indices

The Bloomberg U.S. Aggregate Bond Index is composed of the total U.S. investment-grade bond market. The market-weighted index includes Treasuries, agencies, commercial mortgage-backed securities (CMBS), asset-backed securities (ABS) and investment-grade corporates.

The Bloomberg U.S. Corporate Bond Index measures the investment grade, fixed-rate, taxable corporate bond market.

The Bloomberg Municipal Bond Index is a rules-based, market-value-weighted index engineered for the long-term tax-exempt bond market.

The Bloomberg U.S. Treasury Index measures U.S. dollar-denominated, fixed-rate, nominal debt issued by the U.S. Treasury. Treasury bills are excluded by the maturity constraint, but are part of a separate Short Treasury Index.

The Bloomberg 1-Year Municipal Bond Index is an unmanaged index comprised of investment-grade municipal bonds with maturities of one to two years.

The Bloomberg 5-Year Municipal Bond Index is a capitalization-weighted bond index intended to be representative of major municipal bonds of all quality ratings with an average maturity of approximately five years.

The Bloomberg 20-Year Municipal Bond Index is a capitalization-weighted bond index intended to be representative of major municipal bonds of all quality ratings with an average maturity of approximately 20 years.

The Bloomberg 22+ Year Municipal Bond Index is an unmanaged index comprised of investment grade municipal bonds with an average maturity of more than 22 years.

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