Brandes Investment Partners
Core Plus Fixed Income Strategy Notes
Fourth Quarter 2024 (October 1 – December 31, 2024)

The Brandes Core Plus Strategy declined 2.55% net of fees and 2.55% gross of fees, but outperformed its benchmark, the Bloomberg U.S. Aggregate Bond Index, which fell 3.06% in the fourth quarter.

Annualized total return as of December 31, 2024	1-year	5-year	10-year
Brandes Core Plus Fixed Income Composite (net)	2.19%	0.85%	1.83%
Brandes Core Plus Fixed Income Composite (gross)	2.46%	1.10%	2.10%
Bloomberg U.S. Aggregate Bond Index	1.25%	-0.33%	1.35%

Past performance is not a guarantee of future results. One cannot invest directly in an index. Returns include reinvestment of all dividends and are reduced by any applicable foreign withholding taxes, without provisions for income taxes, if any.

Treasury yields made a rather abrupt turn upwards towards the end of the year after the Fed (Federal Reserve Bank) delivered what many pundits described as a "hawkish cut" of 25 basis points at their December 18th meeting. Fed Chair Jerome Powell threw the market a curveball with his post-meeting comments, toning down the number of projected rate cuts for 2025. In doing so, he was perhaps tacitly admitting that the Fed continues to underestimate the staying power of inflation and made a mistake by cutting the fed funds rate by 50 basis points in September.

One of the hallmarks of the Fed under Chair Powell's leadership is the effective adoption of a policy that every rate move should be fully expected and discounted by the market in advance. The market was expecting a 25 basis point cut in the fed funds rate. Therefore, the Fed delivered this, even if the fundamental data and their own forward economic projections might have suggested no cut at all.

Fundamental data suggest that heading into the most recent Fed meeting that the feds funds rate was at best minimally restrictive. Equity markets are hovering near all-time highs, credit spreads are near three-decade lows, economic data has moderated but remains strong, inflation ticked higher in the fourth quarter, and my wife keeps asking me how we can buy bitcoin.

After the December meeting, the Fed released their Summary of Economic Projections (SEP). This revised estimates for 2024 economic growth upward, and unemployment rate downward. These projections also revised their estimate of inflation for 2025 upward and pushed out their expected time horizon for inflation to hit their 2% target until 2027. Finally, the Fed adjusted the amount of expected rate cuts for 2025 down from 100 to 50 basis points.

Other than hewing to an ingrained *habit* of not surprising the markets, the question is whether a 25 basis point rate cut was the proper policy outcome. To quote Taylor Swift, "Old habits die screaming."

As we enter the New Year one of the biggest questions facing the market and the Fed is what is the neutral fed funds rate? Most fundamental data suggest it may ultimately be higher than many are forecasting, including the Fed itself. If this is the case, will Fed policy be flexible and adaptable enough to respond or will it continue to be beholden to *old habits*?

Credit markets finished the year on a strong note. Yield spreads continued to hover near the lowest levels in several decades, but investors appear to be less concerned with the limited additional compensation that current yield spreads offer in favor of attractive total yields, buoyed by U.S. Treasury rates at significantly higher levels than a few years ago. The corporate bond market continues to be priced for perfection in our view, placing a premium on credit analysis and security selection going forward.

Portfolio Performance
In the fourth quarter, the Brandes Core Plus portfolios delivered negative returns but had positive relative performance versus their benchmark, the Bloomberg U.S. Aggregate Bond Index. For the full year, the portfolios outperformed the benchmark by 1.21%.

Term-structure positioning was a positive factor during the quarter. U.S. Treasury yields rose during the period – finishing the quarter near the highest levels of the year. Near the end of September 2023, we moved the duration of the portfolios to 90% of the benchmark's duration. We continued to maintain that level throughout the quarter.

The portfolios' underweight to agency mortgage-backed securities (MBS) aided returns as the MBS sector was the only major taxable fixed income sector to post negative returns versus U.S. Treasuries. Agency MBS generally underperform during periods of elevated interest rate volatility. The 10-year U.S. Treasury security certainly experienced elevated volatility with a gap of 100 basis points between its high and low yields during the quarter.

Corporate bonds provided a positive contribution to returns during the quarter. Within that sector, performance during the period was led by corporate bond holdings in banking (US Bank and Goldman Sachs), telecom (Sprint and Telecom Italia), and Media (Univision).

The portfolios' focus on shorter-maturity corporate bonds detracted from returns. Longer-maturity corporate bonds outperformed shorter maturity corporate bonds by approximately 100 basis points.

Portfolio activity was modest during the quarter. We added to our existing position of Spirit AeroSystems (9.375% coupon, maturing 11/30/29, rated Ba2/BB-).

Outlook

This is the time when many investment managers and economists put forth their forecasts for the new year. Many of these predictions are well crafted by intelligent and thoughtful individuals at respected firms. In our view, however, very few of the forecasts will be accurate. No one truly knows what the future will bring. At their best, forecasts are educated guesses, often anchored on short-term trends; at worst, forecasts are pure speculation, in our opinion.

Chinese philosopher Lao-Tzu once said, "Those who have knowledge don't predict. Those who predict, don't have knowledge."

As we embark on 2025, we don't have any predictions to share, but we do have several observations and beliefs that will guide our thinking and investment decisions.

- Market yields are attractive, but corporate and mortgage-backed bonds are not cheap. The move in yields upward over the past three years has largely been driven by the rise in underlying Treasury rates. Yield spreads – or the extra compensation investors receive over U.S. Treasuries - are lower. The corporate bond market is largely priced to perfection now, placing a premium on security selection in our view.
- The market may be underestimating the ultimate neutral (also known as terminal) fed funds rate. Most economic markers are still positive, and financial conditions are easier than when the Fed began raising rates in March 2022. This suggests that the ultimate neutral fed funds rate may be higher than expected. Additionally, the last seventeen years of unconventional monetary policy may have skewed investors' perception of what a *normal* fed funds rate is.
- Inflation could continue to prove to be *sticky*. While headline inflation continues to march downward towards the Fed's target of 2%, the movement has primarily been driven by a steep decline in goods inflation. Goods price changes have been negative each month for the past ten months, but services inflation has been sticky and did not register a monthly level below 4.25% during 2024. The services component comprises about one-third of the inflation measures - suggesting that the *last mile* of inflation reduction may continue to prove challenging.
- The U.S. fiscal situation is a *hot mess* in our opinion. It is unlikely to get better anytime soon. The markets do not seem to care, but at some point, the long dormant *bond vigilantes* may awaken from their slumber and seek to impose some discipline on the fiscal situation.

We continue to share optimism around fixed income as overall yields in the core plus portfolios are near the highest they have been since 2009. Our main caution, however, is that we believe it is important to remain disciplined in what one buys.

The takeaway in our view is that deep, measured, fundamental research is essential as we move forward in an environment where idiosyncratic risks appear to be on the rise. We believe it's critical to be patient in adding to a portfolio: not just know what you own but why you own it.

For a considerable period now, we have attempted to tilt the Brandes Core Plus portfolios into what we believe is a defensive posture to mitigate some of the potential detrimental impact of rising interest rates and widening yield spreads. We believe that this remains a risk. Accordingly, the portfolios continue to favor shorter-maturity corporate bonds and those that we believe exhibit strong, tangible asset coverage. We are managing duration approximately 10% shorter than the portfolios' benchmark. We have a meaningful allocation to U.S. Treasuries and if market uncertainty and volatility continue to cause credit fundamentals to become mispriced relative to our estimates of intrinsic value, then we will look to redeploy some of those Treasury holdings thoughtfully and effectively to take advantage of opportunities.

We remain underweight agency mortgage-backed securities.

As we move forward, we believe prudence dictates that we continue our search for value in a measured and deliberate manner while continuing to tilt the portfolios to what we believe is a relatively defensive posture.

We remain optimistic about the prospects for the Brandes Core Plus Portfolios.

Sincerely,

Timothy M. Doyle, CFA
Fixed Income Portfolio Manager

Term definitions: https://www.brandes.com/termdefinitions

The Bloomberg U.S. Aggregate Bond Index is a broad-based benchmark that measures the investment-grade, U.S. dollar-denominated, fixed-rate taxable bond market. This index is a total return index which reflects the price changes and interest of each bond in the index.

The neutral rate is the theoretical federal funds rate at which the stance of Federal Reserve monetary policy is neither accommodative nor restrictive. It is the short-term interest rate consistent with the economy maintaining full employment with associated price stability.

The portfolio characteristics shown relate to a single account deemed by Brandes to be generally representative of the strategy as of date noted. Not every account will have these exact characteristics. The actual characteristics with respect to any particular account will vary based on a number of factors including but not limited to: (i) the size of the account; (ii) investment restrictions applicable to the account, if any; and (iii) market exigencies at the time of investment. Data is updated on a quarterly basis.

Bond ratings are grades given to bonds that indicate their credit quality as determined by a private independent rating service such as Standard & Poor's. The firm evaluates a bond issuer's financial strength, or its ability to pay a bond's principal and interest in a timely fashion. Ratings are expressed as letters ranging from 'AAA', which is the highest grade, to 'D', which is the lowest grade. In limited situations when the rating agency has not issued a formal rating, the Advisor will classify the security as nonrated.

Past performance is not a guarantee of future results.

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Unlike bonds issued or guaranteed by the U.S. government or its agencies, stocks and other bonds are not backed by the full faith and credit of the United States. Stock and bond prices will experience market fluctuations. Please note that the value of government securities and bonds in general have an inverse relationship to interest rates. Bonds carry the risk of default, or the risk that an issuer will be unable to make income or principal payment. There is no assurance that private guarantors or insurers will meet their obligations. The credit quality of the investments in the portfolio is no guarantee of the safety or stability of the portfolio. Investments in Asset Backed and

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Although the statements of fact and data in this report have been obtained from, and are based upon, sources that are believed to be reliable, we cannot guarantee their accuracy, and any such information may be incomplete or condensed

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