Second Quarter 2021 Bond Market Review and Outlook

Cincinnati Asset Management, Inc.

Investment Grade & High Yield Bond Specialists

**"The pace of the global recovery is exceeding earlier expectations and with it, consumer and corporate confidence is rising" (source: Jane Fraser, Citigroup CEO as reported in *The Wall Street Journal* 7/14/2021)**

Annual Excess Return Rankings - USD Fixed Income

| 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| High Yield 5.8% | Mtges 0.0% | EM Sov 23.1% | EM Sov 17% | HG Ind 3.7% | Mtges 18% | High Yield 25.6% | EM HY 9.8% | EM Sov 8.2% | High Yield 8.3% | Mtges -2.2% | Mtges -4.2% | EM HY 65.9% | EM HY 12.8% | Munis 0.8% | EM HY 21.8% | High Yield 9.5% | Munis 3.6% | Munis 2.7% | EM HY 17.4% | EM HY 7.7% | Munis -0.2% | EM HY 9.5% | EM HY 4.2% | High Yield 4.8% |
| EM Sov 15% | HG Util -12% | EM HY 22.1% | Mtges -0.8% | High Grade 3.4% | EM Sov 13% | EM Sov 24.2% | High Yield 7.9% | EM HY 7.4% | EM Sov 7.0% | EM Sov -3.1% | Munis -17.7% | High Yield 58.7% | High Yield 9.8% | Mtges -0.8% | EM Sov 14.2% | HG Fin 4.1% | HG Fin 0.9% | EM HY 17% | High Yield 16.2% | EM Sov 6.5% | Mtges -0.5% | High Yield 9.2% | HG Fin 14% | Munis 3.0% |
| Mtges 13% | HG Fin -12% | EM Corp 19.3% | EM Corp -2.0% | HG Fin 3.1% | HG Fin -0.1% | EM HY 23.7% | EM Sov 7.5% | EM Corp 3.7% | EM HY 5.8% | HG Ind -3.7% | HG Util -17.8% | EM Corp 40.0% | EM Corp 6.9% | HG Util -2.6% | High Yield 13.6% | HG Util 3.1% | Mtges 0.7% | HG Fin 0.7% | EM Corp 8.6% | High Yield 6.1% | HG Fin -2.3% | EM Corp 6.9% | High Yield 0.7% | EM HY 2.4% |
| HG Util 0.5% | High Grade -2.2% | High Yield 6.1% | HG Fin -2.7% | HG Util 14% | EM Corp -2.3% | EM Corp 12.0% | EM Corp 5.7% | High Yield 0.6% | EM Corp 3.4% | HG Util -4.5% | HG Ind -19.7% | EM Sov 29.5% | EM Sov 4.5% | HG Ind -3.0% | EM Corp 13.4% | High Grade 2.8% | HG Util 0.4% | Mtges 0.1% | EM Sov 8.0% | EM Corp 5.7% | EM Corp -2.4% | HG Ind 6.9% | EM Corp 0.7% | HG Ind 2.2% |
| HG Fin 0.0% | HG Ind -3.1% | Munis 2.8% | EM HY -3.9% | Mtges -0.6% | High Grade -2.5% | HG Util 7.3% | HG Util 2.4% | Munis 0.5% | HG Fin 13% | High Grade -5.0% | High Grade -21.3% | HG Ind 25.4% | HG Fin 3.6% | High Yield -3.3% | HG Fin 12.7% | EM HY 2.5% | High Grade 0.0% | EM Corp 0.1% | HG Ind 5.7% | HG Util 3.9% | High Grade -2.8% | High Grade 6.5% | High Grade 0.5% | EM Sov 2.0% |
| HG Ind -0.1% | High Yield -5.0% | HG Ind 15% | High Grade -4.7% | EM Corp -0.8% | HG Ind -3.4% | HG Ind 6.5% | HG Ind 2.0% | HG Fin 0.5% | HG Util 13% | EM Corp -5.1% | EM Sov -23.4% | HG Util 23.9% | High Grade 2.8% | High Grade -4.1% | High Grade 7.9% | HG Ind 2.0% | HG Ind -0.6% | EM Sov -0.2% | High Grade 4.7% | High Grade 3.8% | HG Ind -3.0% | EM Sov 6.4% | HG Ind 0.2% | High Grade 2.0% |
| High Grade -0.3% | Munis -7.5% | Mtges 15% | Munis -5.2% | Munis -16% | Munis -7.3% | High Grade 5.9% | High Grade 17% | Mtges -0.2% | Mtges 13% | Munis -5.3% | HG Fin -23.5% | High Grade 23.5% | Mtges 2.7% | EM Sov -4.9% | HG Ind 5.9% | EM Corp 16% | EM Sov -0.9% | High Grade -16% | HG Util 4.4% | HG Ind 3.8% | EM HY -3.2% | HG Fin 5.9% | HG Util 0.1% | EM Corp 19% |
| Munis -4.1% | EM Sov -29.8% | High Grade 14% | HG Util -5.6% | EM Sov -2.1% | EM HY -7.9% | HG Fin 4.4% | Mtges 17% | HG Util -0.3% | Munis 13% | EM HY -5.8% | EM Corp -29.5% | HG Fin 21.7% | HG Ind 2.5% | EM Corp -5.0% | Munis 5.1% | Munis 0.7% | EM Corp -1.1% | HG Util -17% | HG Fin 2.6% | HG Fin 3.7% | HG Util -3.5% | HG Util 5.4% | Mtges -0.5% | HG Util 19% |
| EM Corp na | EM Corp na | HG Fin 10% | HG Ind -6.0% | High Yield -3.3% | HG Util -7.9% | Munis 3.5% | HG Fin 13% | High Grade -0.8% | High Grade 13% | HG Fin -6.6% | High Yield -38.1% | Munis 18.7% | HG Util 15% | HG Fin -6.2% | HG Util 4.8% | Mtges 0.4% | High Yield -13% | HG Ind -2.5% | Mtges 0.1% | Munis 3.3% | High Yield -3.7% | Munis 17% | Munis -1.1% | HG Fin 14% |
| EM HY na | EM HY na | HG Util 0.8% | High Yield -15.3% | EM HY -7.1% | High Yield -13.4% | Mtges -0.2% | Munis 0.2% | HG Ind -18% | HG Ind 12% | High Yield -7.3% | EM HY -40.8% | Mtges 5.2% | Munis -3.5% | EM HY -7.3% | Mtges 13% | EM Sov -12% | EM HY -5.1% | High Yield -5.9% | Munis -0.6% | Mtges 0.6% | EM Sov -4.3% | Mtges 0.5% | EM Sov -3.8% | Mtges -0.6% |

Source: CreditSights, ICE BofAML Indexes data through 06/30/2021

Excess return = the total return of the asset class minus the total return of a duration matched basket of government securities. Essentially the excess return metrics remove the yield curve piece of the return picture. In its basic form, it is mainly a function of coupon differentials and spread changes).

Inflation concerns subsided in the second quarter. The first half 2021 Investment Grade Index total return of -1.06% was a sharp reversal of the first quarter's -4.5% (source: *CreditSights* and BAML). The High-Yield Index resiliency strengthened with a first half 2021 total return of 3.70% versus the 90 basis point positive return for the first quarter (source: ibid).

The 10-year Treasury yield fell to 1.29% today (7/15), from its high of 1.74% on 3/31/21. It started the year at 0.91%. At the same time U.S. inflation continued to accelerate in June at its fastest pace in 13 years (source: *Wall Street Journal* 7/14/21) with the consumer price index (CPI) rising 5.4% from a year ago.

*(Continued on page 3)*

| **Yields* on 06/30/2021** | **Yield*** |
|---|---|
| **CAM Broad Market (corporate core plus) Strategy** (7.6 year maturity; 5.9 duration) | **2.41%** |
| **CAM Investment Grade (100% corporate bonds) Strategy** (7.5 year maturity; 6.4 duration) | **1.88%** |
| **CAM High-Yield Strategy (only BA & B rated purchased)** (7.8 year maturity; 4.8 duration) | **3.61%** |
| **CAM Short Duration Strategy** (4.2 year maturity; 3.0 duration; 50% IG & 50% HY) | **2.00%** |
| **CAM Short Duration Investment Grade Strategy** (3.6 year maturity; 3.2 duration) | **0.96%** |
| **U.S. Treasury**** (10 year maturity) | **1.47%** |
| **U.S. Treasury**** (5 year maturity) | **0.89%** |
| **U.S. Treasury**** (2 year maturity) | **0.25%** |

* The lower of yield to maturity or yield to worst call date ** Source: Bloomberg Barclays

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## CAM's Key Strategic Elements

- Bottom-up credit analysis determines value and risk.
- Primary objective is preservation of capital.
- Larger, more liquid issues preferred.
- Target is always intermediate maturity.
- No interest rate forecasting.
- <u>All</u> clients benefit from institutional trading platform and multi-firm competitive bids and offers.

| CAM returns are after CAM's average management fee & all transaction costs but before any broker, custody or consulting fees. **The indices are unmanaged and do <u>not</u> take into account fees, expenses, and transaction costs.** | **Total Return (%)** | **Annualized Returns (%)** | | | |
|---|---|---|---|---|---|
| | 2Q '21 | 1-YEAR | 3-YEARS | 5-YEARS | 10-YEARS |
| **CAM Broad Market Strategy—Net** 1/3 high yield, 2/3 investment grade | 2..64 | 5.40 | 7.25 | 4.70 | 4.70 |
| **CAM High Yield "Upper Tier" Strategy—Net** only purchase BB and B; no purchases of CCC & lower | 2.53 | 12.07 | 7.82 | 6.32 | 4.64 |
| Bloomberg Barclays US Corporate High Yield Index | 2.75 | 15.37 | 7.44 | 7.48 | 6.66 |
| **CAM Investment Grade Strategy—Net** 100% corporate bonds | 2.72 | 2.58 | 7.05 | 3.95 | 4.73 |
| Bloomberg Barclays US Corporate Index | 3.55 | 3.31 | 7.79 | 4.91 | 5.17 |
| **CAM Short Duration Strategy—Net** 1/2 investment grade, 1/2 high yield | 1.26 | 6.76 | 5.63 | 4.38 | 3.33 |
| **CAM Short Duration Investment Grade Strategy—Net** 100% corporate bonds | 0.72 | 1.89 | 4.43 | 2.61 | 3.20 |

**Relative Performance Review 06/30/2021**

CAM's **Investment Grade Strategy** ("**IG**") produced a gross total return of 2.78% in the quarter ended June 30, 2021, compared to 3.55% for the Bloomberg Barclays U.S. Corporate Index. CAM always positions a majority of the portfolio within intermediate maturities. Longer dated securities (10+ years) returned 6.79% for the period, dramatically outperforming the broader index. CAM's zero weighting in this duration bucket produced a -114 basis point contribution to excess return. The YTD return for the CAM IG strategy was -0.81% compared to the Index return of -1.27%. Conversely, longer dated securities underperformed the broader index. CAM's zero weighting produced a 45 basis point contribution to excess return, highlighting the benefit of being patient through brief periods of volatility.

The **High Yield Strategy** ("**HY**") delivered a gross total return of 2.61% in Q2 while the Bloomberg Barclays High Yield Index returned 2.75%. CAM does not purchase securities rated CAA and lower. The allocation effect of CAM's structural underweight to lower quality credit was a -12 basis point contribution to excess return during the quarter. The HY YTD return was 2.59% while the Bloomberg Barclays High Yield Index returned 3.62%. In this period, the allocation effect of CAM's underweight to lower quality credit was a -53 basis point contribution to excess return.

Our **Broad Market Strategy ("BM")** – a 67%-33% blend of IG-HY bonds – produced a gross total return of 2.71% for the quarter ended June 30, 2021 compared to 3.28% for the Bloomberg Barclays blended Index. It is important to note that our BM strategy achieves its Baa average credit quality via a barbell strategy of higher and lower rated securities. On average through the second quarter 17.7% of the portfolio was positioned in Baa-rated credit subsectors, while the Index's exposure was 33.3%. The net effect of this structural allocation accounted for -22 basis points of underperformance versus the Index. The YTD return for the CAM Broad Market strategy was 0.24% compared to blended Index return 0.35%. For this period, our barbell strategy produced a +34 basis point contribution to excess return.

The CAM **Short Duration Strategy** ("**SD**") blends equal weights of IG and HY short duration bonds with a target duration of 3 years. The strategy's gross total return in the quarter ended June 30, 2021 was 1.32% while the Index, a similar blend of the intermediate components of Bloomberg Barclays IG and HY corporates, returned 1.57%. CAM's duration profile is shorter than the blended index, and longer paper (5+ years) dramatically outperformed, producing a -14 basis point contribution to excess return during the period. The YTD gross total return was 1.64% compared to the blended Index return of 1.80%. Notably, our structural avoidance of Caa credit produced a -33 basis point contribution to excess return, which was partially offset by our positioning in the Airlines and Consumer Cyclical Services industries.

The **Short Duration Investment Grade Strategy ("SD-IG")** delivered a gross total return of 0.78% for Q2 while the Bloomberg Barclays U.S. Corporate 1-5 Index returned 0.70%. CAM's weighting and positioning within the Airline and Technology industries were positive contributors to performance with +5 and +4 basis point contributions to excess return, respectively. Over the YTD period, SD-IG approximated the Index, by delivering 0.05% gross total return versus an Index return of 0.10%. Again, CAM's weighting and positioning within the Airline industry was the largest single positive contribution to performance, which generated a +17 basis point contribution to excess return.

**Bloomberg Barclays Bond Indices Returns vs. CAM Gross (annualized %)**

| Periods ended 06/30/2021 | 10-yrs | 20-yrs |
|---|---|---|
| **U.S. Aggregate** | 3.39 | 4.56 |
| **U.S. Corporate** | 5.17 | 5.75 |
| **CAM Investment Grade Strategy** | 4.99 | 5.66 |

**<u>Better Asset Allocation Might Result from More Exacting Analysis</u>**

The chart to the right shows that BA rated bonds returned approximately 50% of S&P 500 stocks for the 5 and 10-year periods and modestly underperformed the returns of the S&P 500 over the last 20-years. Lower rated CAA bonds have approximated the S&P 500 for the 20-year period, while the lowest rated (CA & D) have produced negative returns for the 10-year and 20-year periods.

The chart also indicates that CAA rated securities outperformed B rated and BA rated bonds for all periods. However, not shown in the table is the pronounced volatility that has characterized the CAA subsector. For example, during 2008, when the High Yield Index was down 26%, CAA rated bonds were down 44%, and during 2009, the Index was up 58% while CAA bonds were up 91%. In each calendar year since 1997, CAA rated bonds ranked either best or worst in Credit Sights Annual Excess Return Rankings for US corporate credit tiers, a trend that was finally upset in 2019, although it returned in 2020 and 2021.

Finally, BA rated bonds have outperformed the Bloomberg Barclays US Aggregate Index for all periods shown. Even inclusive of the annualized double digit S&P 500 returns over the past 10-years, they modestly underperformed the S&P 500 for the 20-year period by an annualized 87 basis points. Notably, they have done so with about half the volatility of that Index (Ibbotson), suggesting that better credit quality high yield bonds deserve consideration as a core holding in an investor's portfolio allocation.

**Total Return of High-Yield Bonds by Credit Quality**
(periods ended 06/30/2021) Source: Credit Suisse First Boston
**(annualized %)**

| High-Yield Bond Sectors | 5-years | 10-years | 20-years |
|---|---|---|---|
| **BA-rated bonds** | 6.89 | 6.63 | 7.70 |
| **B-rated bonds** | 6.74 | 6.17 | 7.29 |
| **CAA-rated bonds** | 10.74 | 7.27 | 8.73 |
| **CA & D-rated bonds** | 2.26 | -6.84 | -1.79 |

**Performance of Other Asset Classes**
**(periods ended 06/30/2021) Source: Bloomberg Barclays & Lipper**

| | 5-years | 10-years | 20-years |
|---|---|---|---|
| **S & P 500 Stocks** | 17.64 | 14.84 | 8.57 |
| **Bloomberg Barclays U.S. Aggregate** | 3.03 | 3.39 | 4.56 |

The June 30 spread levels (shown at the right) enhance the value of corporate bonds versus U.S. Treasuries. The 10-year U.S. Treasury ended Q2 2021 at 1.47% compared to 1.74% at Q1, representing a 27 basis point decrease over the quarter. As of 6/30/2021, absolute spreads for all credit subsectors tightened versus 3/31/2021.

Notably, this dynamic helped the Investment Grade Corporate market nearly recover all of its drawdown from Q1.

| Credit Rating | 20-Year Average Spread | 06/30/21 | 12/31/20 | 12/31/19 | 12/31/18 | 12/31/17 | Tightest This Decade |
|---|---|---|---|---|---|---|---|
| A | 1.22% | 0.63% | 0.73% | 0.70% | 1.18% | 0.73% | 0.69% |
| BAA | 1.92% | 1.00% | 1.21% | 1.20% | 1.97% | 1.24% | 1.12% |
| BA | 3.80% | 2.00% | 2.64% | 1.82% | 3.54% | 2.11% | 1.30% |
| B | 5.26% | 2.94% | 3.79% | 3.24% | 5.31% | 3.43% | 2.28% |
| CAA | 9.50% | 4.91% | 7.15% | 9.20% | 9.89% | 6.15% | 3.78% |

**Annual Excess Return Rankings - USD Corporate Credit Ratings Tiers**

| 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| US CCC 13.6% | US AA -1.0% | US CCC 8.4% | US AAA -1.4% | US A 3.5% | US AA 0.5% | US CCC 58.5% | US CCC 13.2% | US B 1.7% | US CCC 15.2% | US AAA -2.3% | US AAA -9.3% | US CCC 97.4% |
| US B 6.3% | US A -1.4% | US B 6.7% | US AA -2.4% | US BBB 3.4% | US AAA 0.1% | High Yield 25.6% | High Yield 7.9% | US BB 0.8% | High Yield 8.3% | US AA -4.4% | US AA -14.0% | High Yield 58.7% |
| High Yield 5.8% | US AAA -1.5% | High Yield 6.1% | US A -4.2% | High Grade 3.4% | US A -0.1% | US B 23.5% | US B 7.5% | High Yield 0.6% | US B 7.8% | High Grade -5.0% | High Grade -21.3% | US B 48.7% |
| US BB 3.9% | High Grade -2.2% | US BB 4.4% | High Grade -4.7% | US BB 3.2% | High Grade -2.5% | US BB 16.9% | US BB 6.0% | US AA 0.1% | US BB 6.5% | US BBB -5.4% | US A -22.4% | US BB 46.8% |
| US BBB 0.3% | US BB -3.1% | US BBB 2.7% | US BBB -6.7% | US AA 3.0% | US BBB -5.9% | US BBB 9.1% | US BBB 2.3% | US AAA 0.1% | US BBB 1.6% | US A -5.5% | US BBB -25.6% | US BBB 35.0% |
| US AA 0.0% | US BBB -4.2% | High Grade 1.4% | US BB -10.6% | US AAA 2.2% | US B -10.6% | High Grade 5.9% | High Grade 1.7% | US A -0.2% | High Grade 1.3% | US B -6.4% | US BB -31.5% | High Grade 23.5% |
| High Grade -0.3% | High Yield -5.0% | US A 0.8% | High Yield -15.3% | High Yield -3.3% | High Yield -13.4% | US A 3.6% | US A 1.4% | High Grade -0.8% | US A 1.2% | US BB -7.3% | High Yield -38.1% | US A 20.0% |
| US AAA -0.3% | US B -5.6% | US AA 0.4% | US B -17.2% | US B -6.9% | US BB -15.0% | US AAA 2.6% | US AAA 1.1% | US BBB -2.0% | US AAA 1.1% | High Yield -7.3% | US B -39.6% | US AA 12.4% |
| US A -0.8% | US CCC -9.5% | US AAA 0.1% | US CCC -21.7% | US CCC -8.6% | US CCC -16.2% | US AA 2.0% | US AA 1.0% | US CCC -2.4% | US AA 1.0% | US CCC -9.2% | US CCC -48.7% | US AAA 4.1% |

| 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| US CCC 13.2% | US AAA -2.2% | US CCC 18.7% | US CCC 14.4% | US BB 0.7% | US AAA 0.0% | US CCC 35.2% | US CCC 9.6% | US AA -1.2% | US BB 10.2% | US BB 2.7% | US CCC 10.0% |
| High Yield 9.8% | US BB -2.5% | High Yield 13.6% | High Yield 9.5% | US A 0.0% | US AA 0.0% | High Yield 16.2% | High Yield 6.1% | US AAA -1.7% | US B 9.3% | High Yield 0.7% | High Yield 4.8% |
| US B 9.0% | US B -2.6% | US B 13.2% | US B 9.2% | High Grade 0.0% | US A -0.3% | US B 15.7% | US BB 5.6% | US A -2.6% | High Yield 9.2% | US AA 0.6% | US BB 4.1% |
| US BB 8.9% | High Yield -3.3% | US BB 12.2% | US BB 7.8% | US AA -0.1% | High Grade -1.6% | US BB 11.9% | US B 5.4% | High Grade -2.8% | US BBB 8.1% | US A 0.6% | US B 4.0% |
| US BBB 4.0% | US AA -3.6% | US BBB 9.4% | US BBB 3.3% | US BBB -0.1% | US BB -2.4% | US BBB 6.9% | US BBB 4.6% | US B -3.0% | High Grade 6.5% | High Grade 0.5% | US BBB 2.5% |
| High Grade 2.8% | High Grade -4.1% | High Grade 7.9% | High Grade 2.8% | US AAA -0.4% | US BBB -3.2% | High Grade 4.7% | High Grade 3.8% | US BBB -3.4% | US A 5.2% | US BBB 0.5% | High Grade 2.0% |
| US A 2.3% | US BBB -4.3% | US A 7.5% | US A 2.2% | High Yield -1.3% | High Yield -5.9% | US A 3.2% | US AAA 3.3% | High Yield -3.7% | US AAA 4.3% | US AAA 0.1% | US AA 1.5% |
| US AA 1.5% | US A -4.3% | US AA 5.3% | US AA 1.9% | US B -2.0% | US B -6.3% | US AA 2.4% | US A 3.1% | US BB -3.8% | US CCC 4.2% | US B -1.5% | US AAA 1.5% |
| US AAA 1.3% | US CCC -7.6% | US AAA 2.1% | US AAA 1.0% | US CCC -5.2% | US CCC -16.2% | US AAA 2.3% | US AA 2.4% | US CCC -5.8% | US AA 3.4% | US CCC -2.1% | US A 1.3% |

Source: CreditSights, ICE BofAML Indexes data through 06/30/2021

(Excess return = the total return of the asset class minus the total return of a duration matched basket of government securities. Essentially the excess return metrics remove the yield curve piece of the return picture. In its basic form, it is mainly a function of coupon differentials and spread changes).

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However, the CPI is up just 3% over 2 years (source: *Wall Street Journal* 7/13/21). The difference derives from the 2020 covid lockdowns which crushed demand, driving prices down.

Pandemic induced bottlenecks, such as semiconductor chip shortages for automobiles, are a major factor in the price increases. Hiring difficulties is also cited as a transitory factor of inflation. This, in part, stems from the extra payments by the Federal Government that results in unemployment benefits equaling or exceeding average wages in 38 states (see map on page 4). So, in most states there is little to induce lower wage earners to seek jobs.

Also, the rebound in travel and other services hit hard by the pandemic experienced healthy price increases. Delta Airlines just projected profitable third and fourth quarters, noting that domestic leisure has "fully recovered".

Corporate/business travel is expected to rise to 60% of 2019 pre-pandemic levels by September, up from 20% in March (source: *Bloomberg* 7/14/21).

The Delta earnings release cited above also noted that 94% of large corporations plan to have their offices open before year end (source: ibid). This foreshadows more demand for services through the year-end.

The sharp escalation in GDP too is indicative of a transitory spike in demand growth. The *Wall Street Journal's* survey of economists' forecasts second quarter GDP growth of 9.1% (source: *Wall Street Journal* 7/13/21) following the first quarter's 6.4%. This is in stark contrast to the pre-pandemic 2015-2019 5-year average of 2.43% and 2020's -3.49% (source: The World Bank).

The U.S. Treasury market is pricing in significant moderation in inflation both in yield declines noted previously and yield curve changes.

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**Footnotes and disclosure**

Cincinnati Asset Management, Inc., ("CAM") an independent privately held corporation established in 1989, is registered with the United States Securities and Exchange Commission as an investment advisor. The CAM High Yield, Investment Grade, Broad Market, Short Duration, and Short Duration-Investment Grade composites consist of all discretionary portfolios under management, including all securities and cash held in the portfolios, and have been appropriately weighted for the size of the account. All accounts are included after they are substantially invested.

Returns are calculated monthly in U.S. dollars and include reinvestment of dividends and interest. Figures for periods of less than one year are cumulative returns. All other figures represent average annual returns. Past performance is no guarantee of future results.

When compared to indices' performance, CAM results are after deduction of all transaction costs and CAM advisory fees. CAM advisory fees used are the composite averages. Accounts managed through brokerage firm programs usually will include additional fees. "Net of fees" herein refers only to CAM's management fee. Returns audited annually. Most recent audit available upon request.

S&P 500 averages are published quarterly in Barron's as supplied by Lipper Analytics.

The indices and information shown for comparative purposes are based on or derived from information generally available to the public from sources believed to be reliable. No representation is made to its accuracy or completeness.

High yield bonds may not be suitable investments for all individuals. Before investing a thorough reading of all materials and consultation with an independent third party financial consultant may be appropriate. Fixed Income securities may be sensitive to changes in prevailing interest rates. When rates rise the value generally declines. For example, a bond's price drops as interest rates rise. For a depository institution, there is also risk that spread income will suffer because of a change in interest rates. The Indices are referred to for informational purposes only and the composition of the Index is different from the composition of the accounts included in the performance shown above. Index returns do not reflect the deduction of fees, trading costs or other expenses.

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The 3-month to 10-year spread has steadily slid from a March high of 170 basis points to 127 basis points, today (7/15/21) (source: Bloomberg).

The FED's Williams forecasts 3-3.5% GDP growth in 2022 with inflation of 2% (source: *Forexlive* from *Bloomberg TV* 6/22/21). The FED's Bullard forecasts 2022 inflation at 2.5% and 2% in 2023 (source: *Wall Street Journal* 7/13/21).

FED chairman Powell commented, "Measures of longer-term inflation expectations have moved up from their pandemic lows and are in a range that is broadly consistent with the FOMC's longer-term inflation goal" (source: *Bloomberg* 7/14/21). This confirms the FED's intention to keep interest rates low along with their long term inflation target of 2% and a labor market that has returned to "maximum employment". The committee in June stated it is now planning 2 rate increases in 2023.

Also, the FED's influence on longer term rates through the monthly purchase of $120 billion in Treasury and mortgage securities will continue for some time, according to statements by Powell. He commented that those purchases will continue until achieving "substantial further progress" toward its inflation and employment goals (source: *Wall Street Journal* 7/14/21).

So the outlook for the US bond markets appears to be stable. We appreciate your confidence and encourage you to contact us to discuss your concerns.

## Sharpe Ratios (risk & reward relative value) Inception-Q2 2021

**CAM Investment Grade Strategy 0.49**
Bloomberg Barclays U.S. Corp Bonds 0.46

**CAM High Yield Strategy 0.55**
Bloomberg Barclays High Yield Corp Bonds 0.51

**CAM Short Duration 0.56**
Bloomberg Barclays Weighted Benchmark
(1/2 Interm. HY & 1/2 U.S. Corporate 1-5) 0.64

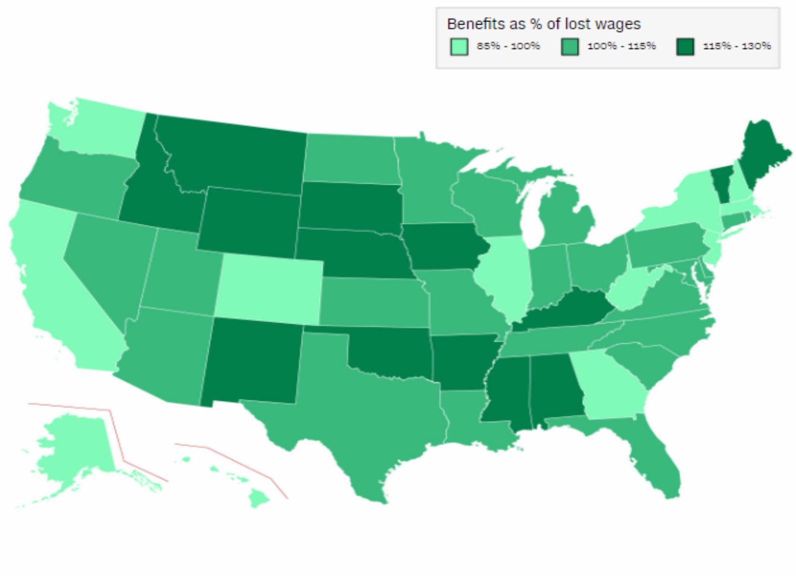
**CAM Short Duration IG Strategy 1.16**
Bloomberg Barclays U.S. Corporate 1-5 Yr 1.18

**CAM Broad Market Strategy 0.79**
Bloomberg Barclays Weighted Benchmark
(2/3 Corporate and 1/3 High Yield) 0.78

An important objective for all Cincinnati Asset Management investment strategies is to deliver superior risk-weighted returns. A quantitative indication of our success is the Sharpe Ratio that calculates total return per unit of risk. The data on the left indicates we have largely been successful. Sharpe Ratios of the Investment Grade and High Yield Strategies exceeded their respective benchmarks by approximately 7% and 8%, respectively. The Short Duration Investment Grade and Broad Market strategies approximated their benchmarks. The Short Duration Strategy's Sharpe Ratio trailed the benchmark primarily due to total return underperformance in the 5-year and older periods.

**Unemployment benefits are now bigger than paychecks for many**

Unemployment pays more than laid-off workers' average weekly wages in many states, thanks to a $600 boost from Congress. On the high end, the combined state and federal unemployment benefit covers 129% of lost wages, on average, in Maine and New Mexico.




Note: Figures compare the sum of each state's average weekly unemployment benefit and the $600 federal boost with the state's average weekly wage for lost jobs. Data is from the last quarter of 2019.

Source: Department of Labor; Ernie Tedeschi, Evercore ISI
Graphic: Christopher Hickey, CNN

| Rating | BA | B | CAA |
|---|---|---|---|
| **Avg Spread** | 369 | 527 | 957 |
| **Std. Dev.** | 170 | 228 | 429 |
| **06/30/2021** | **200** | **294** | **491** |
| **Lowest Spread** | 151 | 228 | 378 |

**<u>Spreads to Treasuries by Credit Rating</u>** show significantly lower risk of BA and B rated bonds. Source: Bloomberg Barclays Capital (12/31/99 to 06/30/21)