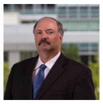
Municipal Fixed Income

Commentary | Quarterly update: 3Q24

Separately managed account



Patrick Garboden Sr. Portfolio Manager

Markets and performance

Municipal bonds experienced positive volatility to end the third quarter, as investment grade municipal yields moved lower across all maturities from July, driven by signals from the FOMC that rate cuts could begin in September (ultimately resulting in a surprise-to-many 50-basis point cut.) Separately managed accounts (SMAs), ETFs, funds and money manager flows continued to focus on the short end and belly of the curve for attractive yield and extending duration heading into the fourth quarter. The narrative of possible Fed funds short-term rate cuts for 2024 has shifted to potentially one or two more by year-end, depending on economic data.

Positive and negative contributors to performance

Crossmark Municipal Fixed Income composite portfolio posted a gain of 2.12% for the quarter versus a gain of 2.78% for the Bloomberg Quality Intermediate Municipal Index. Investing in high-quality credit of essential service revenue and general obligation bonds with a premium coupon slightly underperformed the benchmark index, as BBB and A rated bonds as well as lower coupon bonds outperformed. For the period, airports, transportation and essential services such as water, sewer and utility sectors performed well. The strategy benefited from lower coupon bond spreads widening, giving up some performance from last quarter in the index.

Looking ahead

Fourth quarter redemptions appear to be less than scheduled new issuance coming to the market, which may place negative price pressure on the municipal bond market through year-end. Municipal bonds appear to be in an overbought scenario as the quarter ends. It is possible that yields begin a slow move higher now that the first rate cut in this cycle has taken place. This volatility could continue to be an opportunity to establish or add to municipal bond SMAs in 2024 and 2025.

The yield curve should flatten out then normalize as the rate cycle matures, with potential rate cuts in November and December. For those uncertain about the yield curve normalization, longer duration with a five- to seven-year bond call feature appears most advantageous.

Holding cash or market timing the fixed income yields may not be the best strategy, as cash positions usually underperform during Fed easing cycles. Opportunistically extending duration going forward may be a more favorable option than market timing.

Crossmark continues to find value in the primary and secondary municipal market with bonds rated A or better by Moody's, Standard & Poors, or Fitch at the time of purchase and involved with essential services like water, sewer, power, streets, highways, public education, and general obligations. Our strategy focuses on maturities in the 12- to 20-year range with call features between 2029 and 2034. The municipal bond yield curve has increased in the five- to 20-year maturities making these call features an ideal area to focus on during volatile periods. The strategy will utilize longer duration positioning than the benchmark index on reinvestments as the FOMC continues their battle with inflation, focusing on higher-quality municipalities with a goal to move duration longer as the interest rate curve normalizes.

Composite performance (%)	Quarter	YTD	1-year	3-year	5-year	10-year
Municipal Fixed Income (Wrap) – Gross	2.12	2.25	8.46	1.12	1.46	1.66
Municipal Fixed Income (Wrap) – Net[1]	1.37	-0.01	5.27	-1.88	-1.55	-1.35
Bloomberg Quality Intermediate Municipal Index	2.78	1.71	7.67	0.38	1.33	1.99

1 Net performance was calculated using the hypothetical highest annual all-inclusive wrap fee of 3.00%, with a deduction of 0.25% from each month's return. Gross performance is shown as supplemental information and represents pure gross returns, as they have not been reduced by transaction costs or fees. Wrap fees include Crossmark's portfolio management fee, trading costs, custody, and other administrative fees. Due to the effect of compounding, annual returns shown net of fees may be lower than the return that would be shown if the fee were deducted from the gross return at a single point in time.

Crossmark uses a model account to manage the individual client accounts that have selected this investment strategy. All performance information shown is composite performance derived from the aggregate of all accounts included in the composite.

Our firm

Crossmark Global Investments is a faith-based firm that creates and manages values-based investment strategies for financial intermediaries and their clients. Founded in 1987, the firm has a rich history of inspiring and equipping its clients to go further in aligning their investments with their values. Crossmark is based in Houston, Texas. For more information, visit crossmarkglobal.com.

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