CROSSMARK®
GLOBAL INVESTMENTS

QUARTERLY UPDATE: 1Q 2022
TAXABLE FIXED INCOME COMMENTARY

(Core Fixed Income, Corporate Fixed Income, Current Income Portfolio, Intermediate Fixed Income and Income Opportunities)
Separately Managed Accounts

written by
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Markets and Performance

The first quarter of 2022 proved to be an interesting one for fixed income markets, as inflation concerns and the Russia/Ukraine war drove the ebb and flow of trading around the globe. There was a belief the first quarter would see the peak of inflation as COVID concerns began to wane, allowing supply chain struggles to recede and demand/supply imbalances to alleviate. However, the emergence of new COVID variants worldwide, coupled with higher commodity, food, and rent costs, only pushed inflation higher. This has caused many to see the Federal Reserve (and other central banks) taking on a more hawkish tone, increasing expectations for higher and more frequent rate hikes throughout 2022. Rates across the yield curve moved significantly higher, putting pressure on fixed income markets. In this rising rate environment, all of Crossmark's taxable fixed income model portfolios outperformed their comparable benchmarks for the quarter ending March 31, 2022.

Positive and Negative Contributors to Performance

In previous communications, we mentioned anticipating U.S. 10-year yields to move slightly north of 2.00% (perhaps up to 2.25%) in 2022 before leveling off. In preparation for such a move, we planned to begin extending duration. However, the shift higher in yields across the curve was much quicker and higher than many anticipated, although we did see some pullback from the highest levels of the quarter (around 2.50% on the U.S. 10-year Treasury) reached during March. The shorter duration positioning of our taxable fixed income strategies was the most significant positive contributor to its outperformance versus the benchmarks for the quarter, followed by effects from allocation decisions and the level of income generation. Although we have been working to extend duration, we are averaging 60% to 80% of the benchmark duration for each Strategy, which benefitted performance during the quarter. While the overall shorter duration of the Strategies was beneficial, the overweight of holdings in the shorter portion of the yield curve (1-3-year maturities) compared to the benchmark was a drag on quarterly performance as yields in the 2-year part of the curve rose the most. As spreads moved wider towards the end of March due to investment-grade corporate issues, the shorter duration of our corporate holdings allowed the sector in the model portfolios to outperform the sector of the benchmarks.

Looking Ahead

Even with the jump we have seen in 2022, we still believe there is room for yields to move higher throughout the coming quarters, although at a tempered pace (rather than a steady march higher). We are about to enter a historically active time of year for foreign Treasury purchases, which should keep some pressure on longer-term yields. In addition, if we see inflation trends begin to ease, resulting in a moderation of central bank tightening plans, there could be a slight re-steepening of the curve (which is currently quite flat and inverted in places). Our strategy is to continue extending duration to position the Strategies closer to neutral duration (compared to the benchmarks) as yields take more of a pause on the climb higher. We will remain overweight the investment-grade corporate sector for income purposes while watching spreads for opportunistic trades. Our Strategy will continually develop based on our four-step investment process focusing on duration positioning, yield-curve placement, sector, and security selection.

Our Firm

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Some strategies incorporate values-based screening policies which exclude certain securities issuers from the universe of otherwise available investments. As a result, the strategy may not achieve the same level of performance as it otherwise would have in the absence of the screening process. If the strategy has invested in a company that is later discovered to be in violation of one or more screening criteria and liquidation of an investment in that company is required, selling the securities at issue could result in a loss to the strategy. Further, the strategy's values-based screening policies may prevent the strategy from participating in an otherwise suitable investment opportunity.

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