MEEDER
INVESTMENT MANAGEMENT

INVESTMENT INSIGHTS MONTHLY COMMENTARY

Meeder Fixed Income Strategies

BY AMISHA KAUS, PORTFOLIO MANAGER · SEPTEMBER 2020

KEY TAKEAWAYS:

» Federal Reserve's lower-for-longer stance on interest rates gets reaffirmed and U.S. treasuries and long-term bonds take a hit from inflation expectations

» Low-quality (high-yield) bonds gain over high-quality securities

» Global negative yielding debt declines as rates rise across the globe, signaling improving economic conditions

» U.S. dollar's weakness could have an inflationary impact

FEDERAL RESERVE SHAKES UP THE BOND MARKET WITH INFLATION TALK

The Federal Reserve's annual Economic Policy Symposium was a major market moving event in August, as the Federal Open Market Committee (FOMC) reviewed the U.S. central bank's monetary policy framework and stated their intention to maintain a flexible and accommodative policy towards inflation and the labor market for an extended period. The Federal Reserve plans to hold short-term interest rates near zero as long as necessary to support the U.S. economic recovery and will seek to keep inflation at an average of 2% over time, which means inflation numbers could run higher than 2% at times. The bond market digested the news by sending long-term Treasury yields higher, perhaps a message that investors expect higher inflation to erode purchasing power over time and will require more compensation for owning longer term bonds.

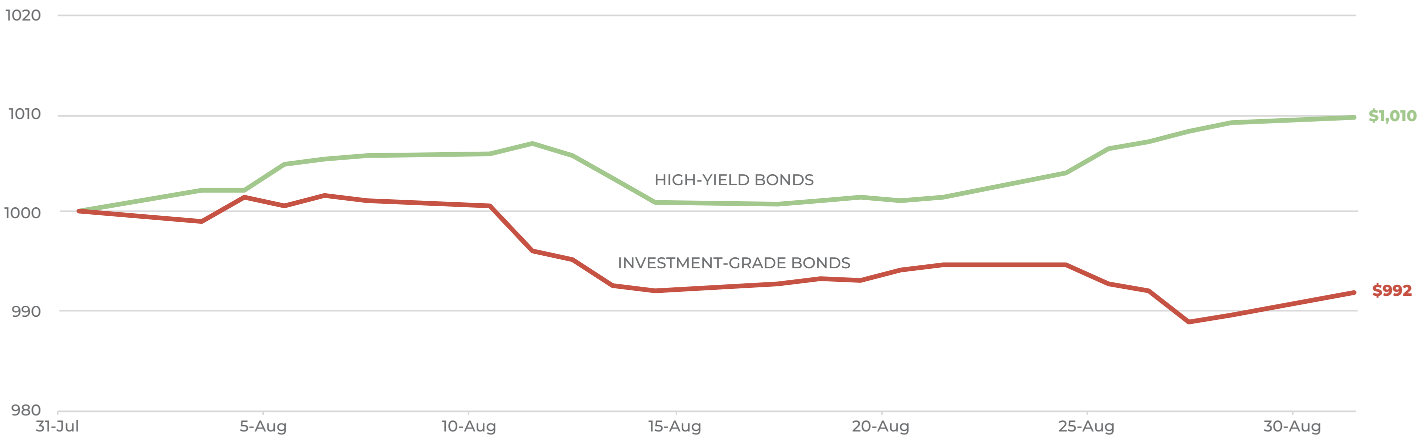
HIGH-YIELD BONDS REMAIN STRONG

With the U.S. continuing to reopen parts of the economy, economic data released in August signaled an increase in consumer and business spending and a decline in the unemployment rate. This sign of optimism led to outperformance by lower credit quality (high-yield) bonds over their higher-quality counterparts in August. The market's appetite for risk and higher income remains robust. U.S. high-yield bond ETFs saw an inflow of nearly $2.9 billion in August, as investors flocked to high-yield bonds that are offering rates that are about 4% above those offered by similar maturity treasuries.

We expect demand for high-yield bonds to continue, but also expect higher volatility in the sector with the upcoming U.S. Presidential election, fiscal stimulus hanging in the balance, and uncertainty surrounding a COVID-19 vaccine.

The chart below shows the change in value of $1,000 invested in high-yield bonds and high-quality bonds in the month of August.

HYPOTHETICAL GROWTH OF $1,000 IN AUGUST 2020



Source: Bloomberg

DECLINE IN GLOBAL NEGATIVE YIELDING DEBT SIGNALS ECONOMIC STRENGTH

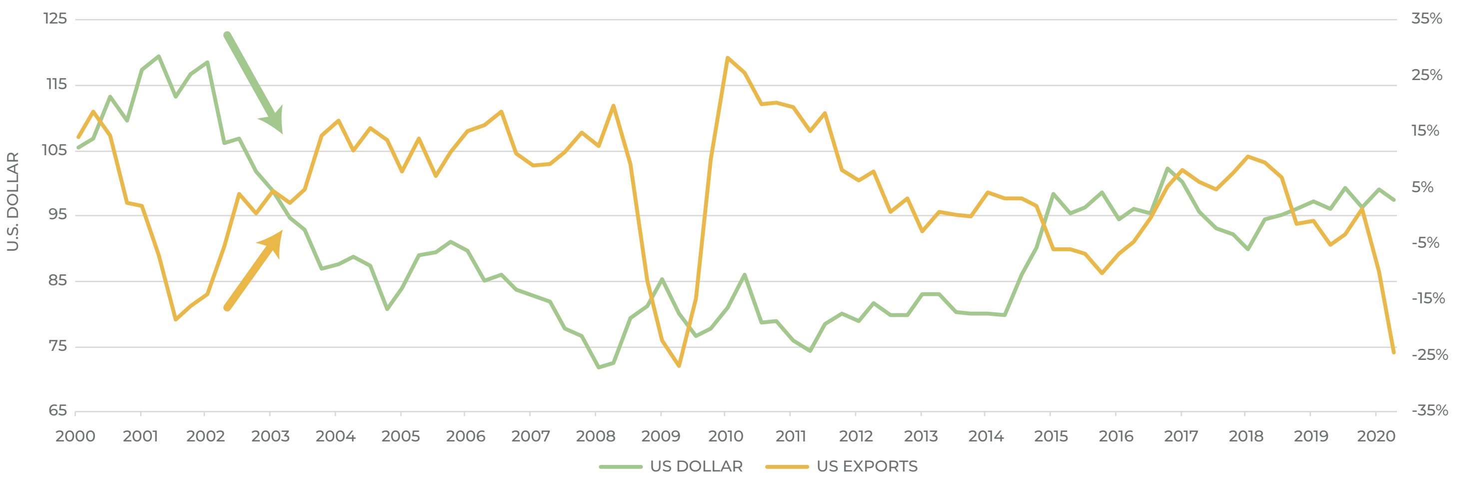
A decline in the amount of negative yielding bonds is a positive sign for the global economic recovery. As interest rates rose across the globe in August, the pool of negative interest rate bonds dropped by $2 trillion, returning to pre-COVID level of $14 trillion. Negative yielding bonds, where lenders (investors) are effectively paying borrowers (corporations & governments) to lend capital, are a sign of economic weakness. Global central banks introduced accommodative interest rate policies to combat the recent economic slowdown, while already facing low and negative interest rates, resulting in the total negative yielding bonds pool to grow to more than $16 trillion in size by early August. If global economic data continues to strengthen, we could see this pool of negative yielding bonds shrink even further, signaling an improvement in global economic recovery.

US DOLLAR'S WEAKNESS COULD MEAN HIGHER INFLATION

Typically, an increase in the federal funds rate leads to higher interest rates throughout the economy, attracting foreign investors – who invest in U.S. dollar-denominated assets. This increase in demand often strengthens the U.S. dollar. With interest rates at record low levels, we are seeing the opposite occur, as the U.S. dollar continues to plummet. As a result of the Federal Reserve's near zero interest rate mandate, the U.S. dollar declined to a 2-year low at the end of August.

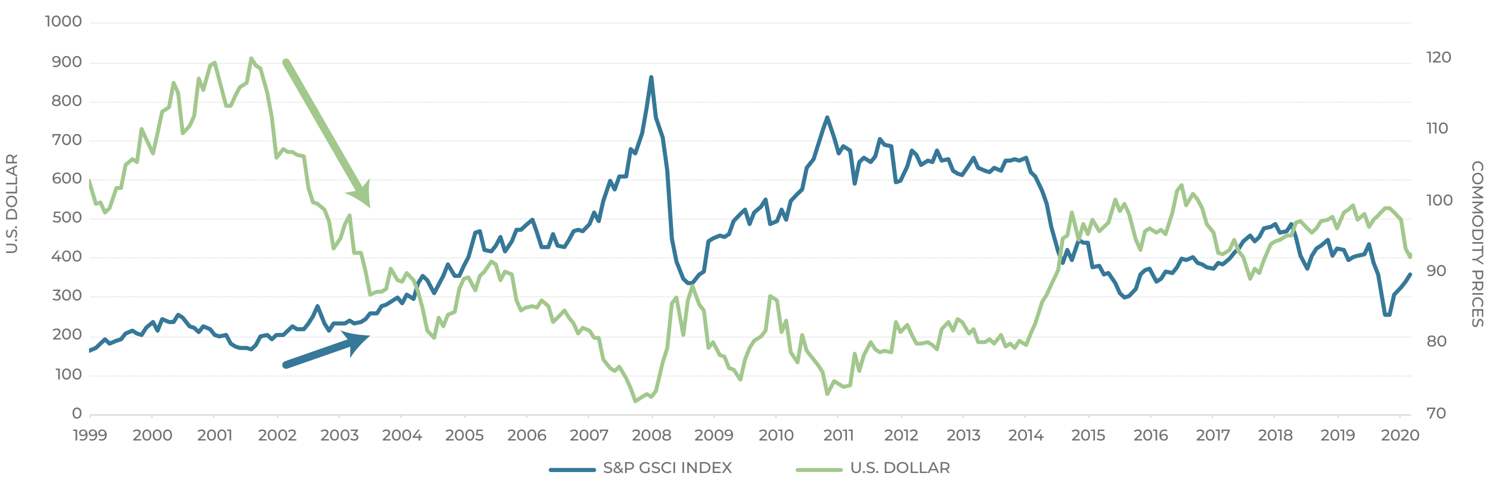
The silver lining with a weaker U.S. dollar is that it can foster a favorable export environment for U.S. companies and bolster commodity prices. Both actions may increase inflationary pressures, as imports and commodities become more expensive, adding even more importance to the Federal Reserve's inflation mandate.

US DOLLAR AND EXPORTS



Sources: Bloomberg, Bureau of Labor Statistics

US DOLLAR AND COMMODITY PRICES



Source: Bloomberg

PORTFOLIO POSITIONING AND PERFORMANCE

Meeder fixed income portfolios maintained the following positions for the duration of the month:

+ **OVERWEIGHT HIGH-YIELD CORPORATE BONDS**
  » High-yield corporate bond exposure was a contributor to portfolio performance as high-yield bonds were up an impressive 0.95% in August, relative to a decline of 1.38% for investment-grade corporate bonds.

+ **OVERWEIGHT USD-DENOMINATED EMERGING MARKET BONDS**
  » Emerging market bond exposure was a positive contributor to performance as the sector gained 0.54% in August vs. a decline of 0.81% for the investment-grade bond benchmark, Bloomberg Barclays U.S. Aggregate Bond Index.

– **U.S. TREASURIES AND INVESTMENT GRADE BONDS**
  » U.S. Treasury prices declined along with investment-grade bonds in August, as economic data and Federal Reserve's monetary policy raised inflationary fears in the bond market. These exposures were a detractor to portfolios' absolute performance.

– **DURATION POSITIONING**
  » Meeder fixed income portfolios maintained an intermediate-term duration of roughly 5.5 years, in line with the market benchmark.

OUR TOP POSITIONS

+ Investment-Grade Corporate Bonds
+ High-Yield Corporate Bonds
+ Emerging Market Bonds (USD)

Sources: Bloomberg, Bureau of Labor Statistics

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6125 Memorial Drive, Dublin, OH 43017 | 1.866.633.3371 | meederinvestment.com

0116-MAM-09/02/20