NEWFLEET ASSET MANAGEMENT

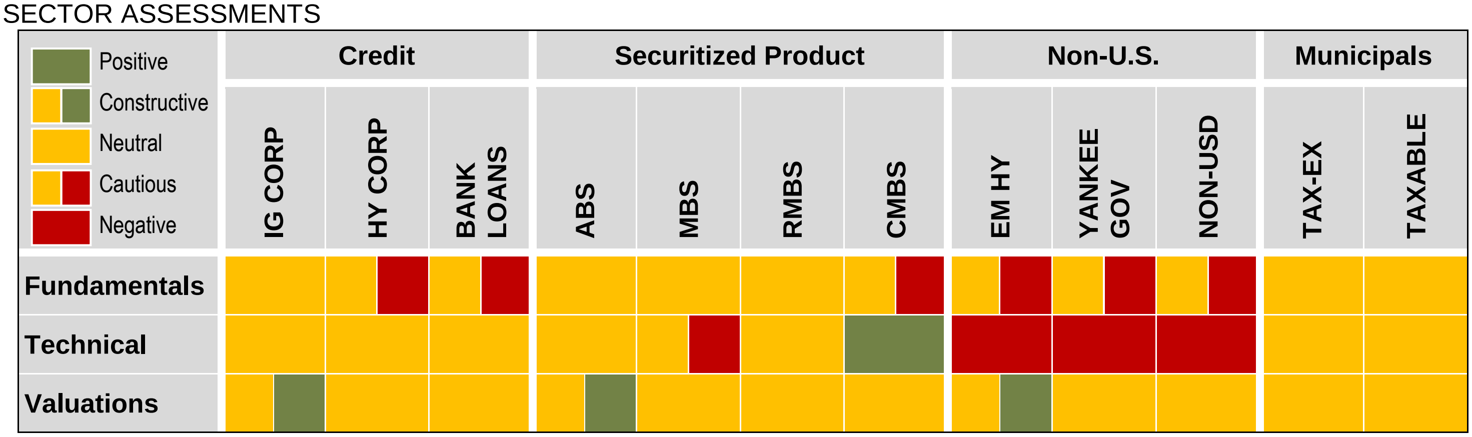
Fixed Income Sector Review

As of October 31, 2022

OBSERVATIONS ON THE MACRO ENVIRONMENT & MARKET CONDITIONS

- We are not chasing rallies yet to add to our low levels of emerging markets (EM) exposure. However, we have modified our conservative approach to include adding exposure to bonds we like.
- We still have our macro concerns, which include the potential for the Federal Reserve (Fed) to overtighten, China's COVID policy-driven growth concerns, and Russia's underlying tactical nuclear threat. However, all of these factors are already priced into financial markets, which have corrected a lot this year. The key is whether prices have corrected enough, and thus whether the recent bounce is sustainable.
- Fundamentally, we do not think the Fed is likely to pivot yet. We expect it to do so only when:
    - The labor market starts to cool
    - Actual inflation starts to decline
- As a result, we see high odds of overtightening. However, this Fed has been very responsive to signals from markets. Thus, if they overdo it, we think they will tack in the other direction quickly enough to not disrupt growth too much.
- Thus, while ongoing volatility is likely, financial assets are likely shifting from a path straight down to more of a range.

SECTOR ASSESSMENTS



Newfleet's assessments of non-government spread sectors as of October 31, 2022. Assessments are determined by analyzing a sector's fundamental data, technical indicators, and relative valuations. Sectors (l to r): **Credit**: Investment Grade (IG) Corporate Bonds, High Yield (HY) Corporate Bonds, Bank Loans. **Securitized Product**: Asset-Backed Securities (ABS), Agency Mortgage-Backed Securities (MBS), Non-Agency Residential MBS (RMBS), Non-Agency Commercial MBS (CMBS). **Non-U.S.**: Emerging Markets HY, Yankee Government, Non-U.S. Dollar. **Municipals**: Tax-Exempt, Taxable.

SELECT SECTOR HIGHLIGHTS

Investment Grade Corporate Bonds

- Credit metrics are in a strong position ahead of a potential 2023 recession as interest coverage metrics have improved to a near ten-year high. The average maturity is over 11 years, and rising rates will not impact interest coverage for years, allowing companies to adjust to a new cost of capital.
- The relative value of investment grade (IG) has improved as high yield spreads have compressed 90 basis points (bps), with IG spreads unchanged.
- Third quarter earnings were far from the catastrophe many feared, with 69% of companies beating estimates. That said, estimates for the fourth quarter and 2023 are declining as macroeconomic headwinds mount.

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High Yield Corporate Bonds

- Optimism in October leading up to the early November Federal Open Market Committee (FOMC) meeting helped high yield recoup most of its losses from September with a 2.60% return.
- The rally was supported by both fundamentals and technicals – issuers reported better-than-expected earnings, while the market saw almost zero net new issuance, positive fund flows, and a supply shortfall driven by $18 billion in rising stars.
- Looking ahead to November, we will continue to monitor economic data and the FOMC's stance on future rate decisions, but we will also closely evaluate earnings, as November will be a busy month for high yield issuers.

Bank Loans

- Higher-rated credits outperformed as investors increased scrutiny on lower-rated tiers, especially credits with downgrade risks. BBs were up 1.83%, B risk was up 0.87%, and CCCs declined 0.94%. BB risk is now positive for the year, up 0.91%.
- Retail and institutional demand continue to slow, but material par repayments and nearly non-existent primary loan issuance keep the technical in balance.
- As we digest third quarter earnings, we are finding pockets of opportunity in higher-quality credits – both primary and secondary – and expect to add in that cohort at the margin while maintaining an underweight to lower-rated cohorts.

Securitized Product

- Spread product, which continued to weaken due to recession concerns, are now approaching pandemic spread levels. We continue to invest in high-quality securitized assets to take advantage of these wider spread levels and higher yields.
- Negative fixed income mutual fund flows continue to put pressure on spread product overall. As an offset, higher interest rates will slow down issuance for securitized product.
- CMBS fundamentals are challenged due to rising financing costs and shrinking deal activity. Higher interest rates do not bode well for CRE valuations.

Emerging Markets Debt

- EM declined in the first three weeks of October, but bounced enough during the last week to post 0.08% for the whole month. This looks good compared with the broader bond market, which was down by 1.30% in October.
- We expect China to slow more than expected due to its COVID lockdowns and our view that the property bond crisis will hit the domestic market. Meanwhile, the war in Ukraine's impact to the rest of the world should be limited, as Russian gas supply to Europe is already down by 80%.
- We have been adding exposure when EMD risk spread trades in the upper 400s, while reducing exposure when the risk spread trends toward the lower 400s. We are still finding value in restructuring opportunities in Africa where double-digit yields compensate for the risk.

Municipal Bonds

- Municipal bond performance for the month returned -0.83%, the largest October decline since 2016. Year-to-date, municipals are down -12.86%
- Municipal mutual funds have lost $14 billion in October, bringing year-to-date redemption to more than $115 billion. ETFs, on the other hand, have seen more than $19 billion inflows.
- Year-to-date supply ($318 billion) continues to trail 2021 ($378 billion) and may well end the year below market expectations of $400 billion.

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For information about Newfleet's fixed income strategies, please visit www.Virtus.com.

IMPORTANT INFORMATION