Touchstone Investments®
DISTINCTIVELY ACTIVE®

Fixed Income:

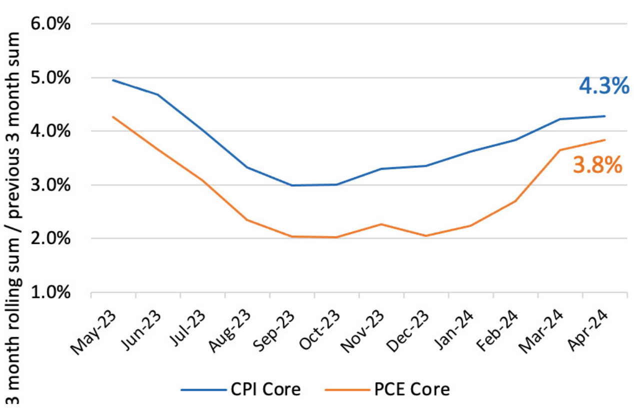
Economic Backdrop

Authors: Crit Thomas, CFA, CAIA / Erik M. Aarts, CIMA / Brian Cheyne, CFA, CIMA

JUNE | 2024

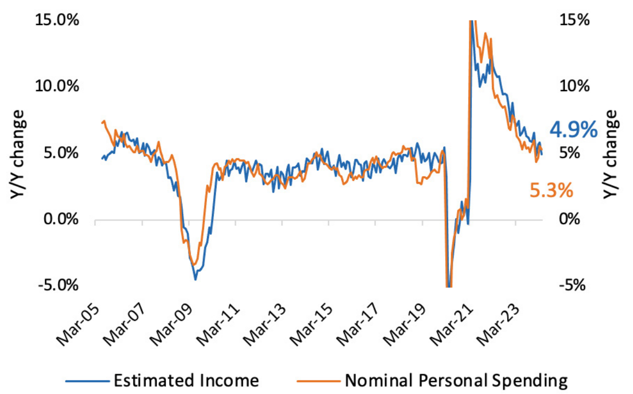
- A bevy of data in May, including a softer payroll report, better than expected CPI print, and flat retail sales, suggested some moderation in economic activity, but was not enough to move up the timeline for a rate cut by the data dependent Fed. The market currently sees the September meeting as the first possible date for a policy change.
- In our opinion economic activity is bifurcated with middle-to-high income consumers doing okay while lower income earners are suffering. And large businesses are doing okay while small business confidence is in recessionary territory.
- The Fed's survey of regional business contacts (the Beige Book) reported that overall outlooks grew somewhat more pessimistic amid reports of rising uncertainty. There were also some signs of continued inflation pressures. Bottomline, the economy is slowly softening while inflation remains a problem. This is a conundrum for the Fed.
- Recently released Fed meeting minutes highlight that many members weren't certain how restrictive current policy is at present with some members thinking the neutral rate of interest may be higher than previously thought and various members willing to consider additional rate hikes if needed.
- We believe that at least three months of benign inflation data is necessary to set the stage for the Fed to cut interest rates. We think that may still allow the Fed to adjust policy before year end.

Core Inflation Q/Q Annualized



Source: Bloomberg. 1 year of monthly data through Apr 2024

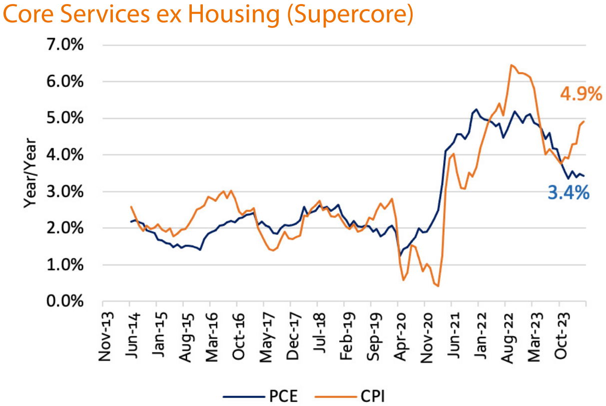
Income and Spending



Source: Bloomberg. 20 years of monthly data through Apr 2024; Estimated Income is the product of number of employed, hours worked, and hourly wage.

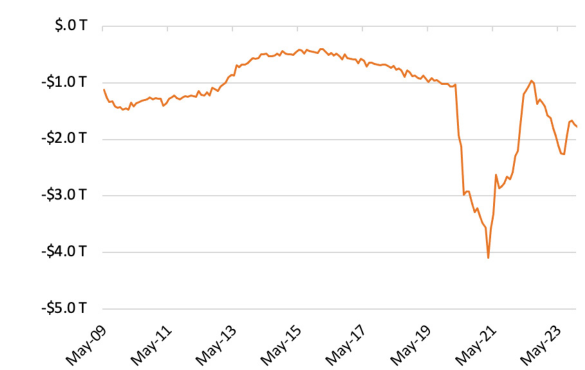
Inflation

Core Services ex Housing (Supercore)



Source: Bloomberg. 10 years of monthly data through Apr 2024

United States Budget Deficit



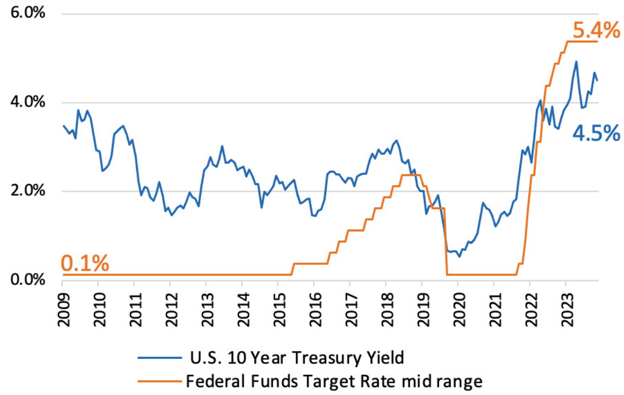
Source: Bloomberg. 15 years of monthly data through Apr 2024

Authors: Crit Thomas, CFA, CAIA / Erik M. Aarts, CIMA / Brian Cheyne, CFA, CIMA

JUNE | 2024

- After declining in the first half of May, interest rates reversed course and ended the month back near April's levels. Most sectors managed to post gains with longer-term bonds besting short-term bonds.
- The bond market is caught between the ebb and flow of economic reporting and shifting expectations for Fed rate cuts. This dynamic could trigger renewed rate volatility by sending yields higher or lower based on the most recent data and that data's impact on policy expectations. May's rate action is a great example of this dynamic.
- Exacerbating the potential for renewed volatility is a decline in demand at Treasury auctions. Stepped up supply at auctions is being met with less interest as demonstrated by the lowest bid coverage ratio since late 2021.
- While we don't see yields retesting the highs of October 2023 because of the growing chances for a soft landing and the Fed's inclination to cut rates, we aren't ruling out the idea that rates stay high for longer.
- All eyes remain focused on inflation reports, looking for renewed signs of slowing. Note that real yields are positive and haven't been this attractive in years. The 10-year TIPS yield at 2.1% is near its highest level since before the GFC.
- Yields remain at the high end of their 10-year history and investors are using the opportunity to rebuild their allocations, as evidenced by strong flows into categories such as ultrashort bond, multisector bond, and core fixed income. We remain constructive on the asset class and remain at our strategic weight and slightly overweight duration.

Interest Rates

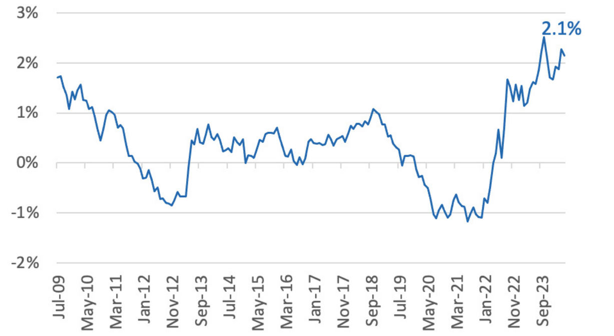


Source: Bloomberg. 15 years of monthly data through May 2024

U.S. Government Securities Liquidity Index

Source: Bloomberg. 10 years of weekly data through Jun 2 2024. The Liquidity Index as calculated by Bloomberg measures prevailing liquidity conditions in the U.S. Treasury market based on intra-day yield dislocations from fair value.

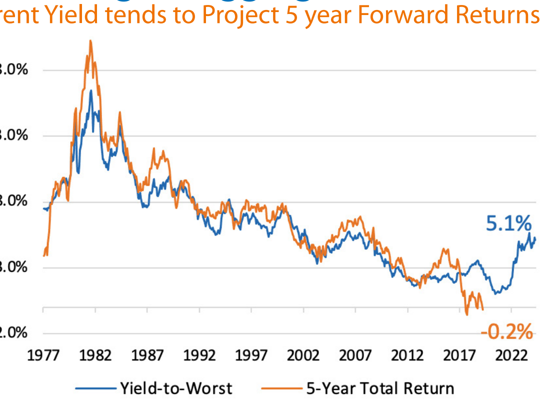
U.S. Treasury Inflation-Protected (TIPS) Yields



Source: Bloomberg. 15 years of monthly data through May 2024

Bloomberg US Aggregate Bond Index

Current Yield tends to Project 5 year Forward Returns



Source: Bloomberg. 47 years of monthly data through May 2024

Touchstone Investments®
DISTINCTIVELY ACTIVE®

Fixed Income:

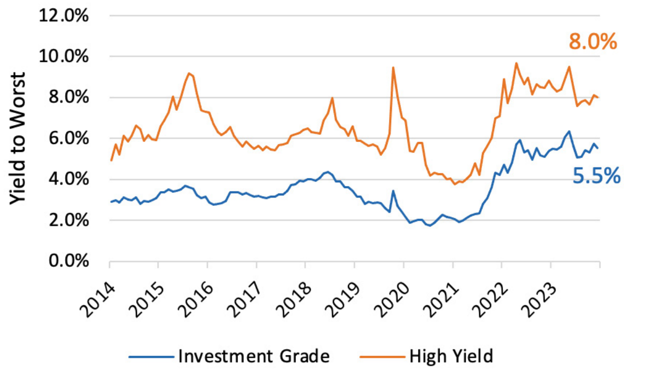
Credit Risk

Authors: Crit Thomas, CFA, CAIA / Erik M. Aarts, CIMA / Brian Cheyne, CFA, CIMA

JUNE | 2024

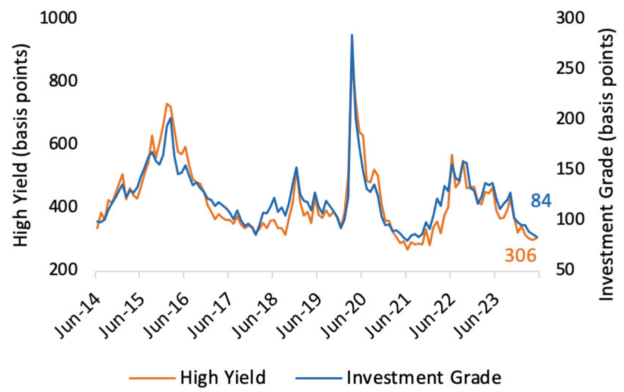
- Credit sensitive sectors posted positive returns in May, with investment grade corporates and securitized credit leading the way. Higher quality high yield credit posted positive returns as well.
- Corporate yields generally followed a similar path to Treasuries, falling in the first half of the month only to reverse course later in the month. Credit spreads were little changed again this month but have been grinding tighter since the start of the year. Corporate bond issuance remained strong in May as corporations took advantage of easier credit conditions.
- Absolute yields remain attractive in our eyes, well above their median levels of the past 10 years. The income cushion bonds provide has increased across the board in this higher rate environment, which could help offset modestly wider credit spreads down the road as the economy softens. In that scenario Fed rate cuts would help ease default concerns.
- Within high yield it is key to recognize the index is higher in quality today versus history, supporting lower spreads today, and that strong demand for new issuance is reducing what little near-term refinancing needs exist.
- That said active risk management via bottom-up security selection will be key going forward as we expect volatility may pick up within credit as the economy comes in for a soft landing.
- We remain constructive on credit exposure and continue to maintain our full allocation to below investment grade exposure in our models.

Bloomberg U.S. Corporate Bond Indexes



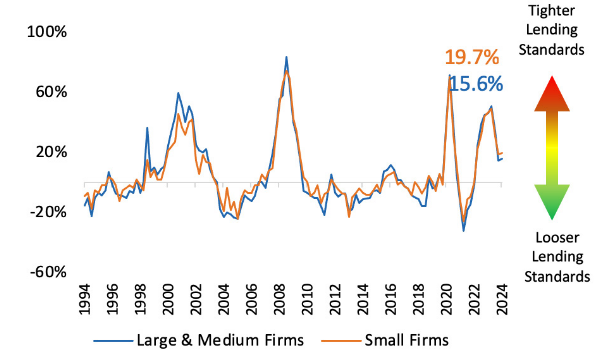
Source: Bloomberg. 10 years of monthly data through May 2024

Bloomberg U.S. Corporate Bond Indexes: Option Adjusted Spreads



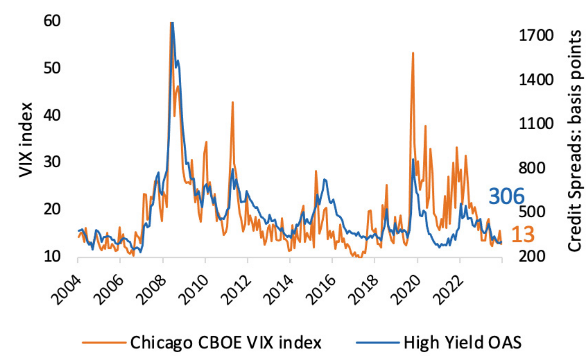
Source: Bloomberg. 10 years of monthly data through May 2024

Net % Tightening Lending Standards for Commercial & Industrial Loans



Source: Bloomberg. 20 years of quarterly data through Apr 2024

Credit Spread versus Implied Stock Volatility



Source: Bloomberg. 20 years of monthly data through May 2024

Touchstone Investments®
DISTINCTIVELY ACTIVE®

Fixed Income:
Market Characteristics

Authors: Crit Thomas, CFA, CAIA / Erik M. Aarts, CIMA / Brian Cheyne, CFA, CIMA

JUNE | 2024

The Indexes mentioned are unmanaged statistical composites of stock market or bond market performance. Investing in an index is not possible.

Total Returns

	May 2024	YTD	2023	2022	2021	Duration years
Bloomberg Long Term Treasury	2.9%	-6.6%	3.1%	-29.3%	-4.6%	15.3
Bloomberg U.S. TIPS	1.7%	-0.1%	3.9%	-11.8%	6.0%	6.7
Bloomberg U.S. Aggregate	1.7%	-1.6%	5.5%	-13.0%	-1.5%	6.2
Bloomberg U.S. Agg Corporate	1.9%	-1.1%	8.5%	-15.8%	-1.0%	7.1
Bloomberg U.S. Agg ABS	0.9%	1.0%	5.5%	-4.3%	-0.3%	2.7
Bloomberg U.S. Agg MBS	2.0%	-2.1%	5.0%	-11.8%	-1.0%	5.8
Bloomberg U.S. Agg CMBS	1.5%	0.6%	5.4%	-10.9%	-1.2%	4.2
Bloomberg Municipal Bond	-0.3%	-1.9%	6.4%	-8.5%	1.5%	6.3
Bloomberg 1-3 year Corporate	0.8%	1.4%	5.5%	-3.3%	-0.1%	1.9
ICE BofA Listed Preferreds	2.9%	4.7%	9.8%	-18.1%	7.7%	NA
Bloomberg High Yield	1.1%	1.6%	13.4%	-11.2%	5.3%	3.7
Credit Suisse Leveraged Loan (discount margin)	0.9%	4.2%	13.0%	-1.1%	5.4%	NA
Bloomberg Global Agg	1.3%	-3.3%	5.7%	-16.2%	-4.7%	6.6
Bloomberg Emerging Markets USD	1.7%	1.6%	9.1%	-15.3%	-1.7%	6.2

Yields

			Last 10 years			
	May 2024	YTD Change bps	Current Percentile	Median	Min	Max
10 year Treasury	4.5%	62	98	2.3%	0.5%	5.0%
2 year Treasury	4.9%	62	96	1.3%	0.1%	5.2%
10 year TIPS	2.1%	44	98	0.4%	-1.2%	2.5%
Bloomberg U.S. Aggregate	5.1%	57	97	2.5%	1.0%	5.7%
Bloomberg U.S. Agg Corporate	5.5%	46	94	3.3%	1.7%	6.4%
Bloomberg U.S. Agg ABS	5.4%	45	95	1.9%	0.4%	6.0%
Bloomberg U.S. Agg MBS	5.3%	66	98	2.8%	0.9%	6.1%
Bloomberg U.S. Agg CMBS	5.6%	32	94	2.7%	1.4%	6.6%
Bloomberg Municipal Bond	3.9%	71	96	2.2%	0.9%	4.5%
Bloomberg 1-3 year Corporate	5.4%	36	93	2.0%	0.5%	6.2%
Bloomberg High Yield	8.0%	41	81	6.3%	3.5%	11.7%
Credit Suisse Leveraged Loan (discount margin)	9.5%	35	90	5.3%	3.6%	13.1%
Bloomberg Global Agg	4.0%	46	97	1.7%	0.8%	4.4%
Bloomberg Emerging Markets USD	7.2%	17	86	5.1%	3.5%	8.7%

Option Adjusted Spreads (bps)

			Last 10 years			
	May 2024	YTD Change	Current Percentile	Median	Min	Max
Bloomberg U.S. Corporate Agg	84	-15	2	120	80	373
Bloomberg 1-3 year Corporate	50	-17	21	66	31	390
Bloomberg U.S. Agg ABS	52	-16	52	52	22	325
Bloomberg U.S. Agg MBS	50	4	81	31	7	132
Bloomberg U.S. Agg CMBS	94	-32	63	95	62	275
Bloomberg High Yield	306	-17	6	391	262	1100
Credit Suisse Leveraged Loan (discount margin)	492	-36	52	501	379	1275
Bloomberg Emerging Markets USD	256	-41	7	312	211	720

For Index Definitions see: TouchstoneInvestments.com/insights/investment-terms-and-index-definitions

2021 – Pandemic continued in waves. Fed held rates near zero and continued to grow its balance sheet at a moderate pace. Long duration bonds sold off while Treasury Inflation Protected Securities rallied on inflation concerns. Exclusive of duration credit exposed securities generally earned their yield.

2022 – The Fed embarked on one of its most aggressive tightening paths seen in decades as the inflation rate surged well above their goal. Interest rates rose across all maturities leading to one of the worst years for fixed income returns.

2023 – Inflation fell broadly while the economy grew with the labor market and consumer spending resilient. The Fed paused midyear helping rates and credit spreads fall late in the year and turning returns positive for the year.

Touchstone Investments®
DISTINCTIVELY ACTIVE®

Authors: Crit Thomas, CFA, CAIA / Erik M. Aarts, CIMA / Brian Cheyne, CFA, CIMA

JUNE | 2024

The Touchstone Asset Allocation Committee (TAAC) consisting of Crit Thomas, CFA, CAIA – Global Market Strategist, Erik M. Aarts, CIMA – Vice President and Senior Fixed Income Strategist, and Brian Cheyne, CFA, CIMA – Senior Investment Strategy Specialist, develops in-depth asset allocation guidance using established and evolving methodologies, inputs and analysis and communicates its methods, findings and guidance to stakeholders. TAAC uses different approaches in its development of Strategic Allocation and Tactical Allocation that are designed to add value for financial professionals and their clients. TAAC meets regularly to assess market conditions and conducts deep dive analyses on specific asset classes which are delivered via the Asset Allocation Summary document. Please contact your Touchstone representative or call 800.638.8194 for more information.

A Word About Risk

Investing in fixed-income securities which can experience reduced liquidity during certain market events, lose their value as interest rates rise and are subject to credit risk which is the risk of deterioration in the financial condition of an issuer and/or general economic conditions that can cause the issuer to not make timely payments of principal and interest also causing the securities to decline in value and an investor can lose principal. When interest rates rise, the price of debt securities generally falls. Longer term securities are generally more volatile. Investment grade debt securities which may be downgraded by a Nationally Recognized Statistical Rating Organization (NRSRO) to below investment grade status. U.S. government agency securities which are neither issued nor guaranteed by the U.S. Treasury and are not guaranteed against price movements due to changing interest rates. Mortgage-backed securities and asset-backed securities are subject to the risks of prepayment, defaults, changing interest rates and at times, the financial condition of the issuer. Foreign securities carry the associated risks of economic and political instability, market liquidity, currency volatility and accounting standards that differ from those of U.S. markets and may offer less protection to investors. Emerging markets securities which are more likely to experience turmoil or rapid changes in market or economic conditions than developed countries.

Performance data quoted represents past performance, which is no guarantee of future results. The investment return and principal value of an investment in the Fund will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be higher or lower than performance data given. ***For performance information current to the most recent month-end, visit TouchstoneInvestments.com/mutual-funds.***

Please consider the investment objectives, risks, charges and expenses of a fund carefully before investing. The prospectus and the summary prospectus contain this and other information about a fund. To obtain a prospectus or a summary prospectus, contact your financial professional or download and/or request one at TouchstoneInvestments.com/resources or call Touchstone at 800.638.8194. Please read the prospectus and/or summary prospectus carefully before investing.