INCOME RESEARCH + MANAGEMENT

TIMING YOUR JUMP: STRATEGIC CASH MANAGEMENT

Q2 2024

Is now the time? While money market funds have remained attractive given the recent higher yields, particularly at the front end of an inverted curve, the market is expecting the Fed to cut rates. Should these rate cuts materialize, money market yields and returns could fall quickly. Investors who modestly extend duration and diversify their exposures can benefit in this environment, while still maintaining their liquidity and protecting their principal.

An extended cash portfolio* utilizes an expanded maturity spectrum and typically has more diversified holdings versus a money market fund. With a portfolio customized for their liquidity, an investor can also lock in current rates for longer.

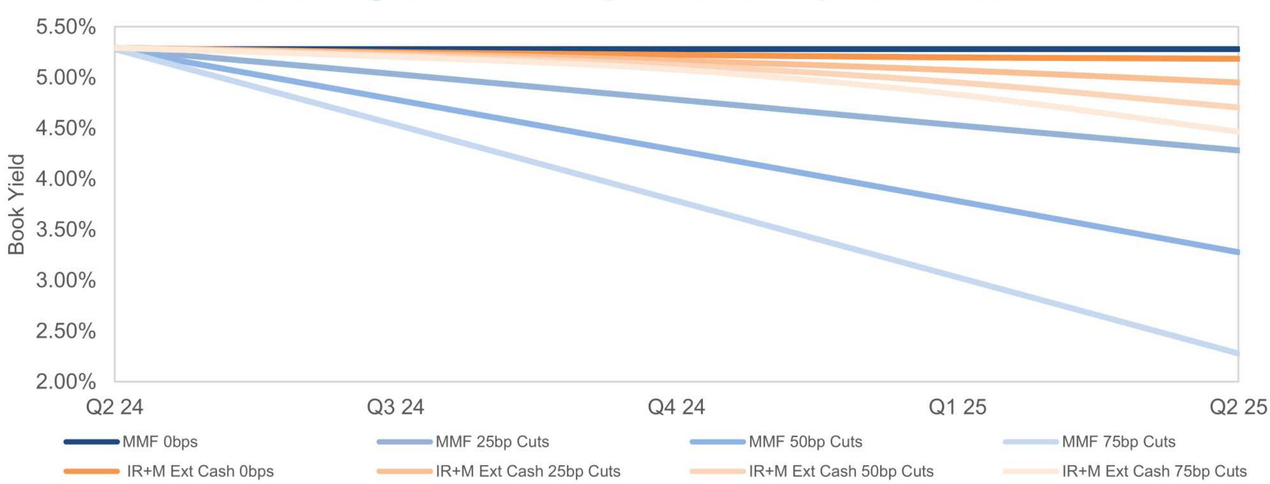
YIELDS REMAIN ELEVATED

- Given stronger-than-expected economic data and still-elevated inflation numbers, the Fed held rates steady at its March meeting. The market and Fed projections are now more closely aligned, with the first rate cut expected in June.
- Money market funds continue to see record balances, with investors earning almost 5% on their cash. If interest rate cuts materialize, these returns are expected to decrease rapidly, making the case for strategically extending cash to lock in the higher rates.
- While perfectly timing your duration extension jump is nearly impossible, waiting too long may create missed opportunities.

...BUT RATE CUTS LOOM

- The Fed is actively discussing changes to the quantitative tightening program, which could add to the process of loosening the restrictive monetary policy that has kept short-term rates elevated.
- Meanwhile, exponential increases in US Treasury issuance have been skewed toward T-bills. As the Treasury looks to term out its debt and issue fewer short-term Treasuries, this could lead to downward pressure on T-bill yields, which make up a large portion of most money market funds.
- The current yield curve inversion is the longest inversion recorded and has led money markets to look attractive on an absolute and relative basis. However, this may be giving money market investors a false sense of security if rate cuts occur and we return to a more normalized curve.

Extending Duration Can Help Cushion the Impact of Rate Cuts



- Money market funds (blue lines above) and IR+M's Short Extended Cash portfolio* (orange lines) yields are currently aligned, but assumed rate cut shocks show the wider range of scenarios for a shorter duration money market fund.
- If rate cuts happen, money market funds will feel the impact almost immediately and have more downside risk.
- Extending duration and diversifying holdings can help to lock in the high rates for longer, thereby softening the impact of rate cuts and protecting against the downside.
- Aligning portfolio construction with known liability and liquidity needs can further optimize returns.

*IR+M's Short Extended Cash Representative portfolio is benched against the Bloomberg 1-Year US Treasury Bellwether Index and had a duration of 0.94 years as of 3/31/24.
Source: Bloomberg as of 3/29/24 unless stated otherwise. Chart: The largest prime money market fund is based on a Bloomberg Fund Screen, which compiles all funds that are open-end funds, money markets, primary share class, and a geographic focus on the United States. The prime money market fund uses a fund strategy of Taxable First Tier. The yield shown for money market funds is the 7-day SEC yield. The yield of the money market fund is sourced from Fidelity. First rate cut occurs 7/1/24 after both the IR+M Short Extended Cash (IR+M Ext Cash) Representative portfolio and money market fund (MMF) have reinvested at 6/30/24. Subsequent rate cuts occur quarterly and instantaneously at the respective shocks of 25bps, 50bps and 75bps.This is a forward-looking analysis. Yields can vary from these scenarios. The above forward-looking analysis does not take into account the effects that market conditions and trading may have on the portfolio. The views contained in this report are those of Income Research + Management ("IR+M") and are based on information obtained by IR+M from sources that are believed to be reliable but IR+M makes no guarantee as to the accuracy or completeness of the underlying third-party data used to form IR+M's views and opinions.

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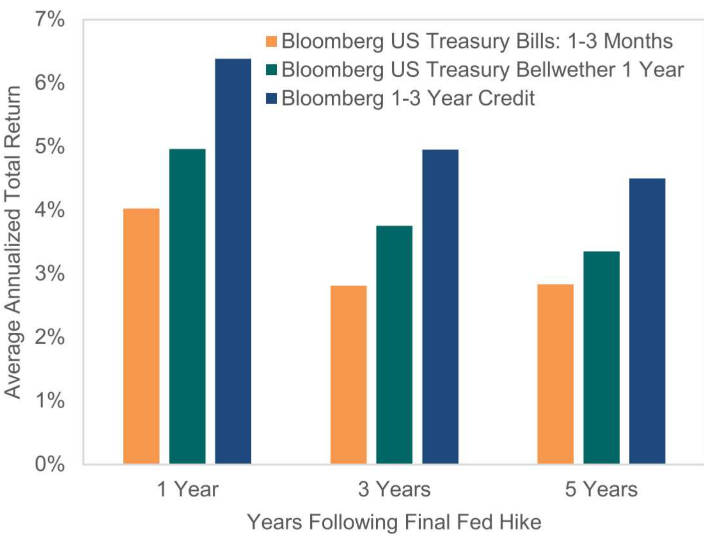
April 5, 2024

BETTER TO BE EARLY THAN LATE

Average Historical Annualized Total Return Following Final Fed Rate Hike

Extending duration and/or adding spread sectors historically outperforms



Timing a duration extension jump exactly is nearly impossible, but waiting too long may create missed opportunities.

While the market contemplates the timing and magnitude of potential rate cuts, yields remain elevated and spreads in the short end provide a robust opportunity set.

Extending cash from money market funds ahead of a rate cut can lock in these higher yields for longer, capture total return, and provide additional diversification while maintaining liquidity options.

In addition, the current yield environment provides a cushion against any future rate increases. Front-end rates would need to rise by over 500 basis points for the 1-Year Treasury Bellwether Index to return 0%. Additional cushion is obtained with the inclusion of spread product.

Higher Yields Provide Total Return Cushion Against Rate Increases

Front end rates must rise over 500bps to return 0%

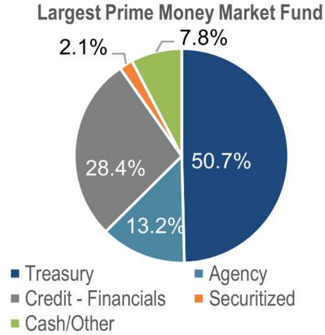
ENHANCING YOUR CASH

Money market funds typically have concentrated positions in select government issuers and counterparties. While these are high quality exposures, they may be susceptible to extreme volatility, particularly in the overnight markets.

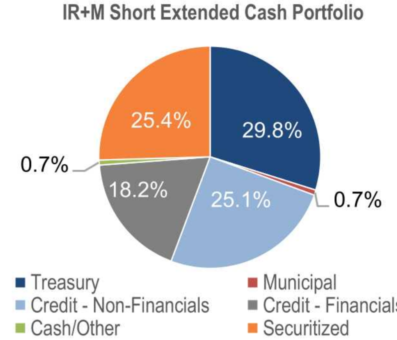
IR+M's Short Extended Cash strategy is well-diversified across Treasuries, corporate bonds, securitized assets, and municipal bonds. The strategy aims to mitigate investment and credit risk via short maturity, high-quality, investment grade ideas and thorough bottom-up credit research. The strategy can also be customized to meet specific requirements or preferences.

Money market reforms adopted by the SEC require increased liquidity buffers, allowing prime funds to impose liquidity fees and temporarily suspend withdrawals in certain circumstances. IR+M offers the flexibility to liquidate a portfolio at any time and can work with clients to customize portfolios to meet specific, known cash flow needs to optimize market exposure and minimize transaction costs.

Largest Prime Money Market Fund



IR+M Short Extended Cash Portfolio



At IR+M, we do not predict interest rate moves when managing our portfolios. However, the market and the Fed have indicated the likelihood of a rate cut in 2024 and many clients have contemplated a move out of their excess cash accounts. Given current yield levels, we believe that there is limited downside risk to moderately extending duration and caution against waiting too long to take that jump. Don't let your cash drag you down - getting ahead of the expected interest rate cut(s) can provide investors with similar yields and the opportunity to benefit when rates fall.

Sources: Bloomberg as of 3/31/24 unless stated otherwise. Top left chart: bars represent the annualized total return comparing across duration and credit exposure. Top right chart: Bloomberg 1-Year US Treasury Bellwether Index. Rate move needed to offset carry is calculated by dividing the yield to worst by the duration as of each month-end. Bottom right chart: The largest prime money market fund is based on a Bloomberg Fund Screen, which compiles all funds that are open-end funds, money markets, primary share class, and a geographic focus on the United States. The prime money market fund uses a fund strategy of Taxable First Tier. Sector weights of money market fund are sourced from Fidelity as of 2/29/24. Sector distribution shown is for the IR+M Short Extended Cash Representative portfolio as of 2/29/24. Cash/other sector is cash, other non-negotiable time deposits, other repo agreements, and net other assets. Some statistics require assumptions for calculations which can be disclosed upon request. A similar analysis can be provided for any portfolio we manage. Source: IR+M Analytics. The views contained in this report are those of Income Research + Management ("IR+M") and are based on information obtained by IR+M from sources that are believed to be reliable but IR+M makes no guarantee as to the accuracy or completeness of the underlying third-party data used to form IR+M's views and opinions. "Bloomberg®" and Bloomberg Indices are service marks of Bloomberg Finance L.P. and its affiliates, including Bloomberg Index Services Limited ("BISL"), the administrator of the index (collectively, "Bloomberg") and have been licensed for use for certain purposes by IR+M. Bloomberg is not affiliated with IR+M, and Bloomberg does not approve, endorse, review, or recommend the products described herein. Bloomberg does not guarantee the timeliness, accurateness, or completeness of any data or information relating to any IR+M product.