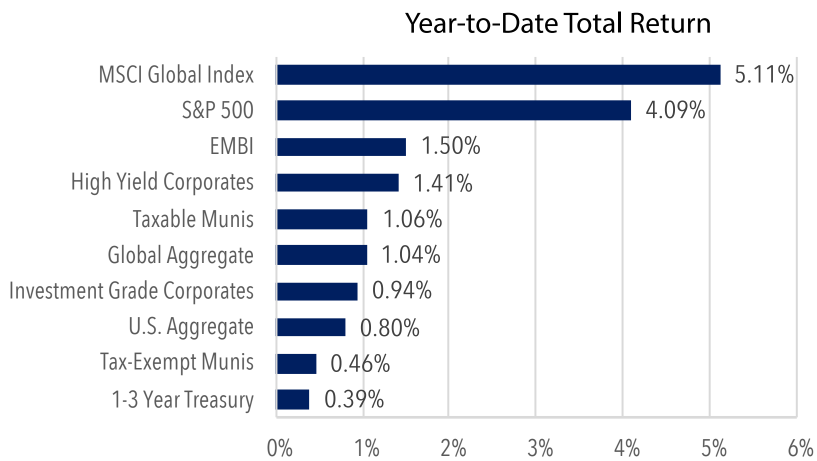
Week Ending: **February 14, 2025**

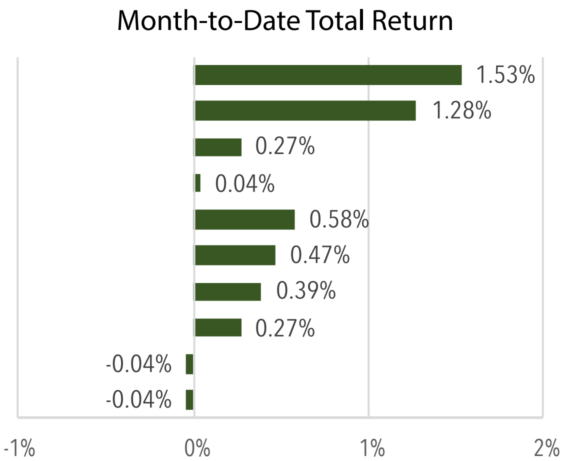
Well-Seasoned

Economic Overview:

This week, the January Consumer Price Index (CPI) showed the highest monthly core inflation reading since March 2024. As a result, bond investors, already worried about inflation re-acceleration, only see one rate cut in 2025. However, we find more clarity by zooming out. First, in the past two years, core inflation registered strong readings in the first quarter before receding as the year progressed. Firms may adjust prices at the start of the year, boosting first-quarter readings, and seasonal adjustment factors may not have captured the post-Covid change in behavior. Second, the shelter component may cool with a lag, following the trends evident in falling new market rents. Third, 60% of the rise in services ex-shelter prices in January was from transportation services, which is unlikely to repeat. Consequently, we could still see core inflation moderating this year—just as in 2023 and 2024. So, while higher core inflation readings in the first quarter may delay the Fed's next move, it's premature to conclude that inflation has reignited, and the Fed is done cutting.

Total Returns by Asset Class





Source: Bloomberg

Highlights of the Week:

High Yield: Since the CCC bond rally started in early August, CCC bonds have returned +12.6% compared to +4.2% for CCC loans. Rate moves explain only around 4% of this return differential, while compositional differences between the two buckets explain the rest. This demonstrates that a "basket approach" to investing in CCCs is unlikely to be effective—active management in CCCs is critical.

Municipals: For the fourth consecutive week, muni inflows remained in positive territory. Inflows totaled $238 million, driven by $260 million flowing to mutual funds, more than offsetting the roughly $22 million of ETF outflows.

Equities: The U.S. equity market posted a strong week of returns, as better-than-expected corporate earnings results offset mixed economic data. Nearly all sectors posted gains, with technology, materials, and energy leading markets higher, while health care, consumer discretionary, and financials were the market laggards.

Securitized Products: The USD CLO market remains resilient despite economic uncertainties, bolstered by strong investor demand for floating-rate assets amid rising interest rates. The primary market volume continues to be heavy, with over $50 billion in refinancings year to date and about $12 billion in new issues. Spreads were unchanged this week, having already experienced tightening year to date.