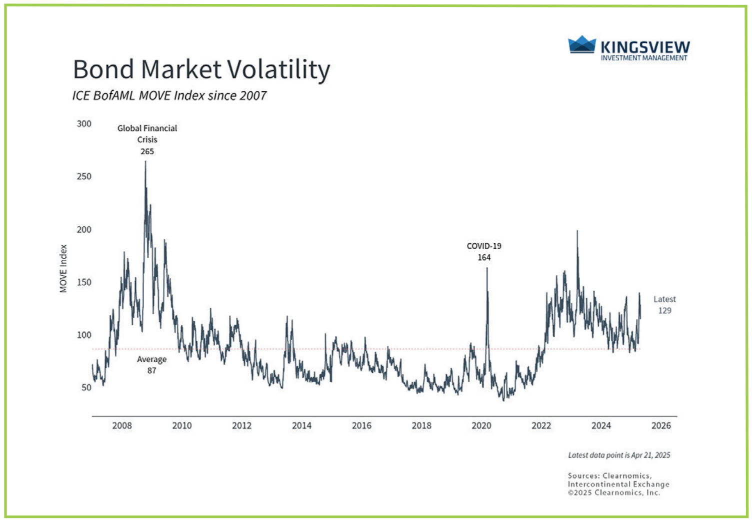
Portfolio Manager Insights

What Bond Volatility and the Battle Over Fed Policy Mean for Investors

Weekly Investor Commentary | April 23, 2025

Investment Committee

THE BOND MARKET HAS BEEN VOLATILE



Just like in the stock market, greater uncertainty has led to swings in the bond market. These moves, driven by tariffs and a dispute between the White House and the Fed, have pushed interest rates and bond yields higher. While short-term volatility can often lead to unexpected results, it's important to remember that periods like these occur periodically, even if the causes are different each time. For bond investors, especially those who rely on their portfolios for income, the current environment may present both challenges and opportunities for their financial plans.

One of the key principles of portfolio diversification is the idea that stocks and bonds are typically uncorrelated. That is, when stocks move one way, bonds tend to move another way. This is not by accident – stocks tend to perform well when the economy is strong whereas bonds have historically performed well during periods of economic uncertainty. This is why combining stocks, bonds, and other asset classes can result in a portfolio that is more stable than holding a single asset class alone, improving the odds of achieving financial goals.

So, what is happening in the bond market and why does it matter? There can be periods of financial market volatility that create exceptions to these historical patterns for short periods. For instance, bond volatility can occur when markets adjust to significant economic or policy changes, such as the ones taking place today around tariffs and the independence of Fed policymaking. When it comes to tariffs, bond investors are weighing two possibly conflicting scenarios: trade wars could raise prices which would be inflationary (usually negative for bonds), and/or they might slow economic growth (usually positive for bonds).

In addition, liquidity concerns, a possible flight from U.S. assets, and technical factors have contributed to recent moves. The U.S. dollar has also declined alongside bonds, which is atypical since higher bond yields typically attract foreign investors. The accompanying chart shows that bond market volatility has been heightened not only in recent weeks, but also over the past three years.

While these might be the events surrounding bond market moves, they all boil down to greater policy uncertainty. Bond prices are highly dependent not only on where interest rates and the economy are headed, but also on how uncertain this path might be. Just as recent government moves around trade have made it harder for households and businesses to plan for the future, so too is it harder to forecast where economic variables might be in a few months, let alone in a year. This includes the direction of Fed policy, which is exacerbated by the headlines surrounding President Trump and Fed Chair Powell. Thus, it's not surprising that bond prices have fluctuated alongside stocks.

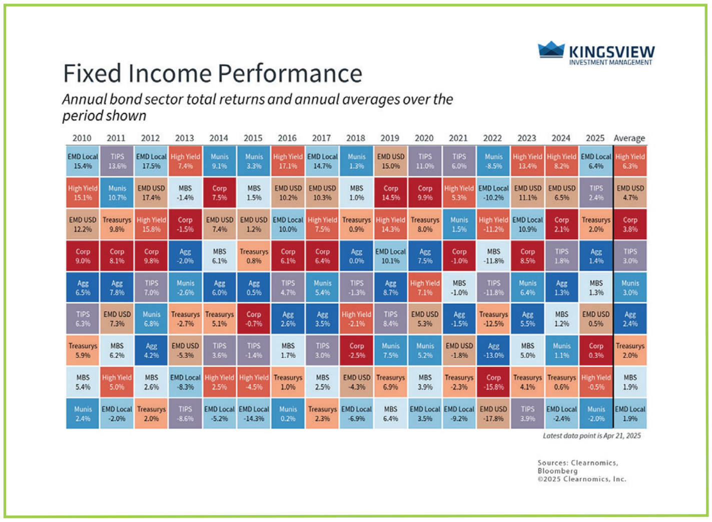
(continued on next page)

INVESTMENTS@KINGSVIEW.COM | 312.870.6701 | KINGSVIEWIM.COM

Of course, some perspective is needed. The 10-year Treasury yield is currently around 4.3% – well within its range over the past two years. In general, interest rates are higher than many investors expected at the start of the year.

Despite this, most bond sectors are still showing positive year-to-date returns including the U.S. Aggregate Bond Index, Treasurys, and investment grade corporate bonds. High yield, which is highly correlated withthe stock market, is only slightly negative.

BONDS HAVE STILL HELPED TO STABILIZE PORTFOLIOS THIS YEAR


Fixed Income Performance

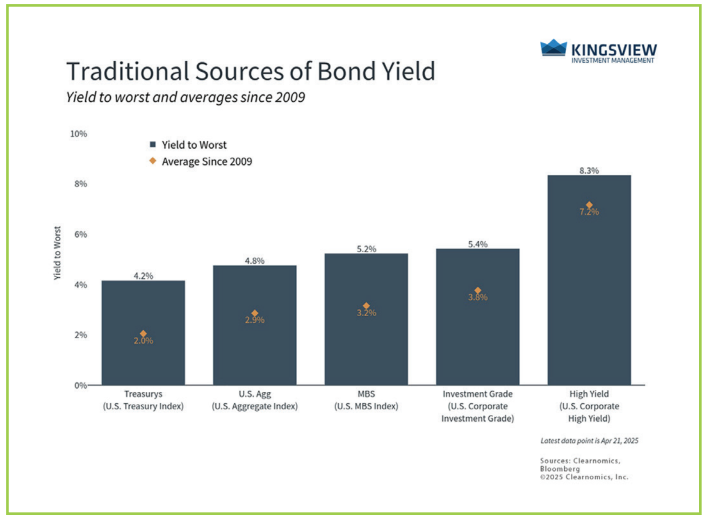
Annual bond sector total returns and annual averages over the period shown

2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	Average
EMD Local 15.4%	TIPS 13.6%	EMD Local 17.5%	High Yield 7.4%	Munis 9.1%	Munis 3.3%	High Yield 17.1%	EMD Local 14.7%	Munis 1.3%	EMD USD 15.0%	TIPS 11.0%	TIPS 6.0%	Munis -8.5%	High Yield 13.4%	High Yield 8.2%	EMD Local 6.4%	High Yield 6.3%
High Yield 15.1%	Munis 10.7%	EMD USD 17.4%	MBS -1.4%	Corp 7.5%	MBS 1.5%	EMD USD 10.2%	EMD USD 10.3%	MBS 1.0%	Corp 14.5%	Corp 9.9%	High Yield 5.3%	EMD Local -10.2%	EMD USD 11.1%	EMD USD 6.5%	TIPS 2.4%	EMD USD 4.7%
EMD USD 12.2%	Treasurys 9.8%	High Yield 15.8%	Corp -1.5%	EMD USD 7.4%	EMD USD 1.2%	EMD Local 10.0%	High Yield 7.5%	Treasurys 0.9%	High Yield 14.3%	Treasurys 8.0%	Munis 1.5%	High Yield -11.2%	EMD Local 10.9%	Corp 2.1%	Treasurys 2.0%	Corp 3.8%
Corp 9.0%	Corp 8.1%	Corp 9.8%	Agg -2.0%	MBS 6.1%	Treasurys 0.8%	Corp 6.1%	Corp 6.4%	Agg 0.0%	EMD Local 10.1%	Agg 7.5%	Corp -1.0%	MBS -11.8%	Corp 8.5%	TIPS 1.8%	Agg 1.4%	TIPS 3.0%
Agg 6.5%	Agg 7.8%	TIPS 7.0%	Munis -2.6%	Agg 6.0%	Agg 0.5%	TIPS 4.7%	Munis 5.4%	TIPS -1.3%	Agg 8.7%	High Yield 7.1%	MBS -1.0%	TIPS -11.8%	Munis 6.4%	Agg 1.3%	MBS 1.3%	Munis 3.0%
TIPS 6.3%	EMD USD 7.3%	Munis 6.8%	Treasurys -2.7%	Treasurys 5.1%	Corp -0.7%	Agg 2.6%	Agg 3.5%	High Yield -2.1%	TIPS 8.4%	EMD USD 5.3%	Agg -1.5%	Treasurys -12.5%	Agg 5.5%	MBS 1.2%	EMD USD 0.5%	Agg 2.4%
Treasurys 5.9%	MBS 6.2%	Agg 4.2%	EMD USD -5.3%	TIPS 3.6%	TIPS -1.4%	MBS 1.7%	TIPS 3.0%	Corp -2.5%	Munis 7.5%	Munis 5.2%	EMD USD -1.8%	Agg -13.0%	MBS 5.0%	Munis 1.1%	Corp 0.3%	Treasurys 2.0%
MBS 5.4%	High Yield 5.0%	MBS 2.6%	EMD Local -8.3%	High Yield 2.5%	High Yield -4.5%	Treasurys 1.0%	MBS 2.5%	EMD USD -4.3%	Treasurys 6.9%	MBS 3.9%	Treasurys -2.3%	Corp -15.8%	Treasurys 4.1%	Treasurys 0.6%	High Yield -0.5%	MBS 1.9%
Munis 2.4%	EMD Local -2.0%	Treasurys 2.0%	TIPS -8.6%	EMD Local -5.2%	EMD Local -14.3%	Munis 0.2%	Treasurys 2.3%	EMD Local -6.9%	MBS 6.4%	EMD Local 3.5%	EMD Local -9.2%	EMD USD -17.8%	TIPS 3.9%	EMD Local -2.4%	Munis -2.0%	EMD Local 1.9%

Latest data point is Apr 21, 2025

Sources: Clearnomics, Bloomberg
©2025 Clearnomics, Inc.

BOND YIELDS CONTINUE TO BE ATTRACTIVE



As demonstrated by these returns, corporate bond investors are differentiating between higher and lower quality issuers as economic uncertainty persists. Corporate bond spreads, which show how much yield these bonds generate versus Treasurys, are one way to measure this. Investment-grade spreads have remained fairly tight, while high-yield spreads have widened considerably. Still, spreads are significantly narrower than during previous crises such as in 2008, 2020, and 2022.

Municipal bonds have also faced greater volatility in recent weeks. The muni ratio, which compares municipal bond yields to Treasury yields, jumped on the tariff announcement and remains elevated. The higher ratio means that munis are more attractive today compared to Treasurys, particularly for investors in higher tax brackets and in high tax states.

Regardless of how bond prices move in the coming weeks, bond yields remain attractive compared to the past two decades, creating opportunities across the bond market for those who need portfolio income. Investment grade corporate bonds, for instance, currently have an average yield of 5.3%, compared to an average of 3.8% since 2009.

The case for bonds may also be favorable since the Fed is expected to cut rates again later this year, regardless of how the dispute with the White House plays out. For income-focused investors, current yields are attractive across many fixed income sectors and can help support portfolios amid ongoing uncertainty.

The bottom line? Policy headlines continue to rattle financial markets. While bonds have been volatile in recent weeks, attractive yields and still-healthy returns can help long-term investors achieve financial goals.