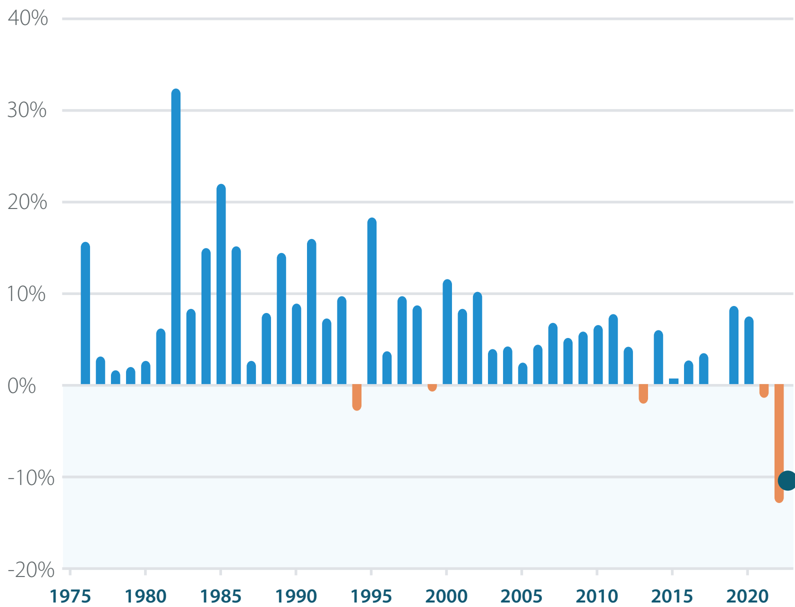
A Great Reset

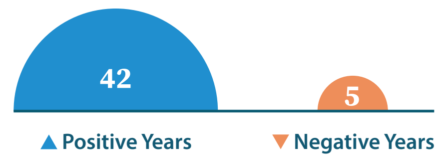
Are Bonds Staged for a Comeback?

NEW YORK LIFE INVESTMENTS

Bonds had a historic year in 2022, posting one of the worst returns ever recorded.

Bloomberg U.S. Aggregate Bond Index





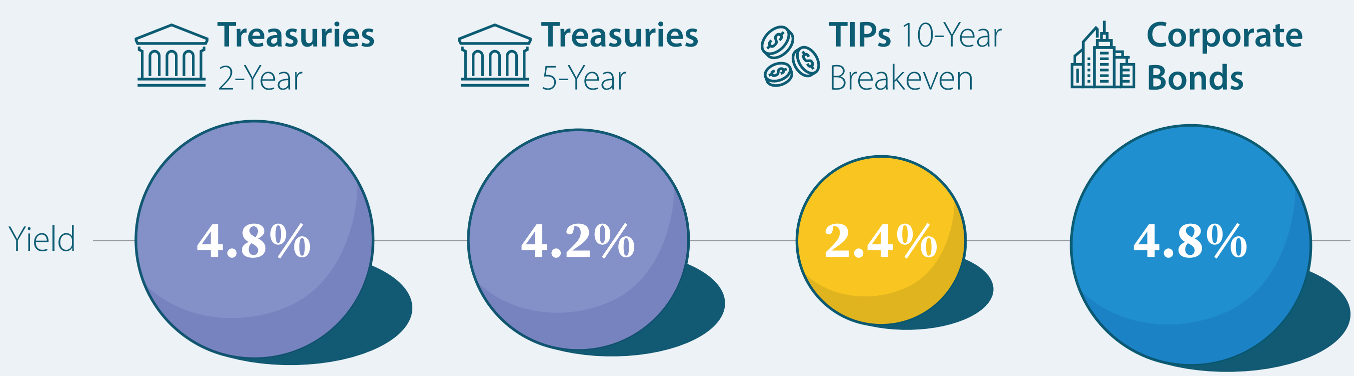
As interest rates rose at the fastest pace in 40 years, it pushed bond prices lower due to their inverse relationship.

In a rare year, bonds dropped **13%**.

Source: FactSet, 1/2/2023.
An investment cannot be made directly into an index. Index definitions can be found at the end of this piece. Past performance is no guarantee of future results.

Bond prices are only one part of a bond's total return—the other looks at the income a bond provides.

Interest Rates Drive Higher Bond Yields in 2023

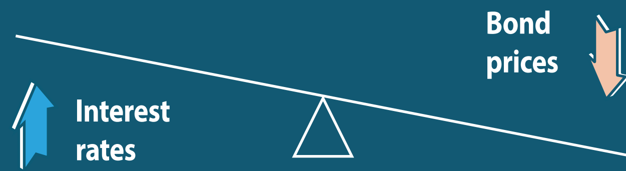


Source: Bloomberg, YCharts 2/28/2023.
Past performance is no guarantee of future results. Corporate Bond yields represented by Moody's Aaa Corporate Bond Yield, a dataset that includes corporate bonds that are rated Aaa, the highest rating for a bond.

Could bonds make a comeback, and what factors may impact their performance?

Factors Impacting Bond Markets

Interest rates play a central role in bond market dynamics. This is because they affect a bond's price. Here are projections for where they are headed in 2023:



2023 Federal Funds Rate Projections

Source: Bloomberg, 3/5/2023.
*Based on median projections stated in the December 2022 meeting.

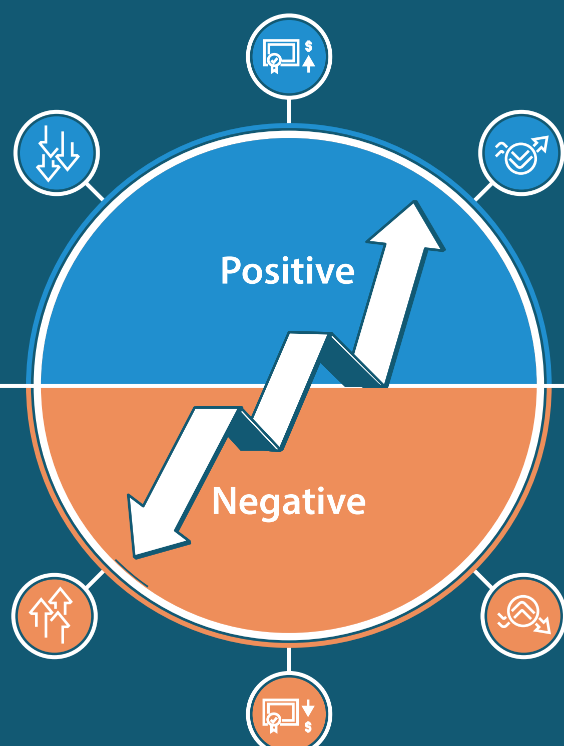
What other factors impact **bond prices?**

Drivers of Bond Prices

Lower Interest Rates
When rates are lower, bond prices are typically higher.

Lower Inflation
Reduces likelihood of interest rate hikes.

Recession
Can prompt a cut in interest rates, boosting bond prices.



Higher Inflation
Can increase likelihood of Federal Reserve to raise interest rates.

Weaker Fundamentals
When a bond's credit risk gets worse, its price can drop. Credit risk indicates the chance of a default.

Rising Interest Rates
Interest rate hikes lead bond prices to fall.

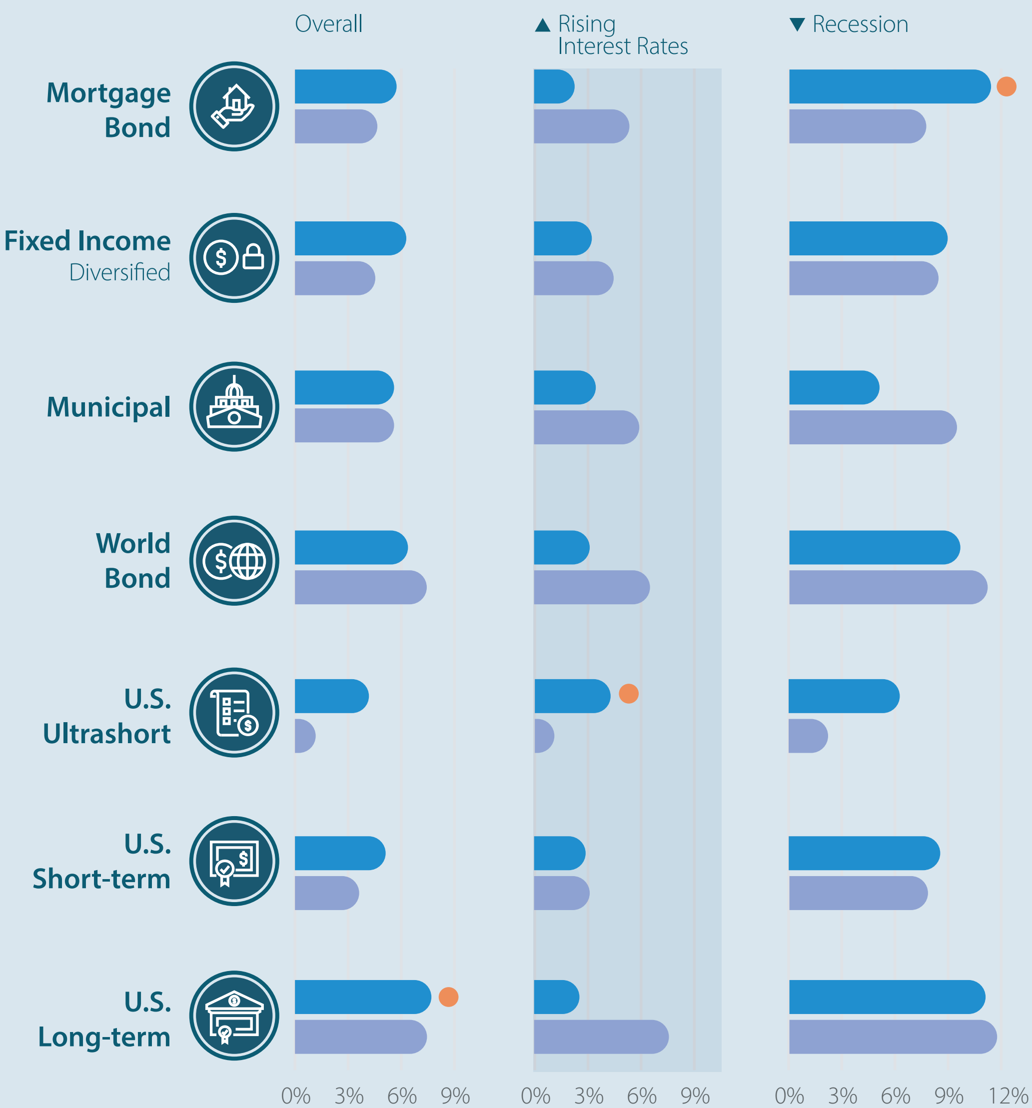
Source: Investopedia, 9/30/2022.

Yet when looking from an income perspective, investors can lock in higher yields as rates rise.

Fixed Income Opportunities

Below, we show the types of bonds that have had the best performance during rising rates and recessions:

50 Years of Bond Returns ● Average Return ● Average Volatility ● Best Average Return



Mortgage bonds outperformed during recessions, averaging **11.4%** returns, but with higher volatility.

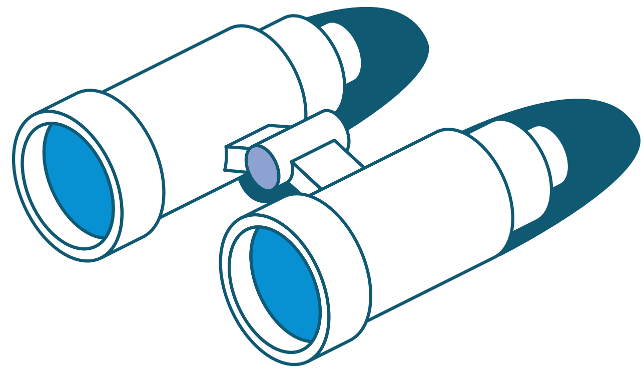
U.S. ultrashort bonds performed the best during **rising rates**, they also had the lowest volatility.

U.S. long-term bonds had **7.7%** average returns, the best overall.

Source: Derek Horstmeyer, George Mason University 12/3/2022.
Past performance is no guarantee of future results. An investment cannot be made directly into an index. Index definitions can be found at the end of this piece.

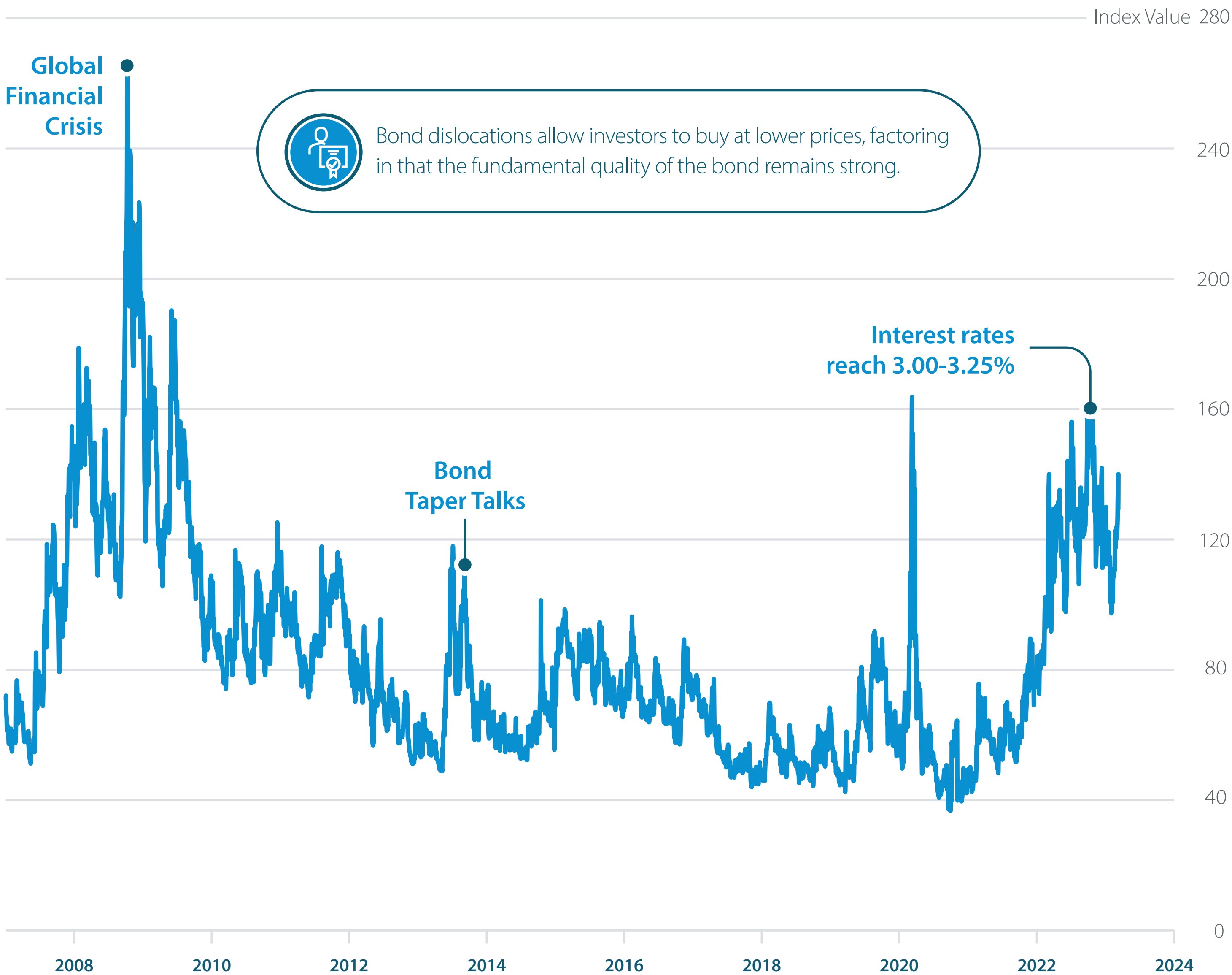
When rates are rising, ultrashort bonds allow investors to capture higher rates when they mature, often with lower historical volatility.

A Closer Look at Bond Market Volatility



While bond market volatility has jumped this year, current dislocations may provide investment opportunities.

Bond Volatility Index



Source: TradingView, 3/13/2023.
Index definitions can be found at the end of this piece. The Bond Volatility Index is represented by the ICE BofAML U.S. Bond Market Option Volatility Estimate Index.

With this in mind, here are two areas of the bond market that may provide opportunities for investors:

Investment-Grade Corporate Bonds

Higher credit quality makes them potentially less vulnerable to increasing interest rates.

Intermediate Bonds (2-10 Years)

Allow investors to lock in higher rates.

Source: Morningstar, 1/3/2023.

Finding the Upside

Today's steep discount in bond markets could present an attractive opportunity for price appreciation.

At the same time, investors can potentially lock in strong yields as inflation may subside in the coming years ahead.

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The **Bloomberg U.S. Aggregate Bond Index** broadly tracks the U.S. investment-grade bond market including U.S. Treasuries, corporate bonds, municipal bonds, mortgage-backed securities, and asset-backed securities. **Treasuries (2-Year)** represent the effective annual interest rate paid by the U.S. government on a Treasury bond with a two year maturity. Treasuries (5-Year) represent the effective annual interest rate paid by the U.S. government on a Treasury bond with a five year maturity. **TIPS 10-Year (Breakeven)** represents the rate that inflation would need to average over 10 years in order to outperform the nominal 10-year Treasury. The breakeven rate equals the difference in a TIPS yield and a nominal Treasury with a similar maturity.

Corporate Bond yields are represented by Moody's Seasoned Aaa Corporate Bond Yield which includes corporate bonds that are rated Aaa, the highest rating for a bond. The **Federal Funds Rate** is a target interest rate determined by the Federal Reserve. It is the interest rate at which banks and credit unions lend reserve balances to each other, most often overnight.

Mortgage Bonds are represented by funds that invest in mortgage-backed securities issued by the Government National Mortgage Association. **Fixed Income (Diversified)** are represented by mutual funds that invest in a combination of fixed-income sectors such as U.S. government bonds, U.S. corporate bonds, foreign bonds, and U.S. high-yield bonds. Typically these funds hold 35% to 65% of their assets in bonds that are rated at the level of BB and below according to Moody's or Standard & Poor's. **U.S. Ultrashort Bonds** are represented by mutual funds that invest in investment-grade fixed-income securities with durations of under one year. These can include government or corporate bonds. World Bonds are represented by mutual funds that invest at least 40% of bonds in non-U.S. markets.

U.S. Short-Term Bonds are represented by funds that invest in investment-grade fixed-income securities with durations of one to three and a half years. These can include government or corporate bonds. **Municipal Bonds** are represented by fixed-income funds that distribute income that is not subject to federal, state, and sometimes municipal taxation. **U.S. Long-Term Bonds** are represented by funds that invest in corporate and other investment-grade fixed-income securities with durations over six years.

The **ICE BofAML U.S. Bond Market Option Volatility Estimate Index** tracks U.S. Treasury yield volatility represented by the prices of one-month OTC options. **Investment-Grade Corporate Bonds** represent bonds with a rating of Baa3 and above, according to Moody's or BBB- and above according to Standard & Poor's and Fitch ratings. **Intermediate Bonds** are issued with maturity dates between two and 10 years.

It is not possible to invest directly in an index. Past performance is not indicative of future results. Different time periods may have different results. This material represents an assessment of the market environment as of a specific date; is subject to change; and is not intended to be a forecast of future events or a guarantee of future results. This information should not be relied upon by the reader as research or investment advice regarding the funds or any particular issuer/security.

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