
Intermediate Duration Corporate Fixed Income

First Quarter 2021

Throughout the first quarter the pace of COVID-19 vaccinations in the U.S. gained steam, and the Federal government implemented additional fiscal stimulus while pressing for additional spending. The expectation that vaccines will release pent-up demand from the past year alongside the expected jolt to growth from stimulus packages raised concerns that rising inflation may force the Fed to act decisively in the coming years. These concerns sent intermediate and longer-term interest rates sharply higher. Meanwhile, credit spreads were broadly unchanged from their already tight levels. The result of these moves in rates and spreads was significantly negative corporate bond performance in the first quarter.

While the portfolio's duration was only a few months short of the benchmark during the first quarter, the magnitude of the move upward in interest rates meant that this duration difference was a large positive for relative performance. In addition, while corporate bonds on the whole did not see much change in credit spreads, some issuers did see credit spreads widen, and the portfolio's avoidance of these issuers was an additional boost to relative performance.

A continued increase in vaccination rates and decrease in hospitalizations and deaths will likely result in exceptionally strong economic performance for the rest of 2021, especially when combined with existing and proposed stimulus and spending programs. While the Fed is confident that longer-term inflation pressures will be slow to build and that they can contain them at appropriate levels, the bond market is signaling that monetary tightening may be required sooner and at a quicker pace. Corporate credit spreads already offer historically low levels of compensation for assuming credit risk, and so corporate bonds will need to see a continued strong recovery that does not spark inflation in order to perform well. Given this outlook it is important for corporate fixed income investors to maintain discipline around interest rate and credit risk.

Adherence to our conservative style of fixed income investing has been, and will always be, the hallmark of Reinhart Partners.