Balancing Act
September 2021

As time goes by, the need for balance in our lives becomes increasingly important. We must maintain a work - life balance to take care of career, family, and self. We need to maintain a balanced budget to make sure we prioritize what we want, what we need, and what we must save for the future. And of course, we need a balanced diet to curtail eating some of the comfort foods we love to ensure health and longevity. It's a balancing act worthy of the Flying Wallendas.

The same could be said for our investment portfolios. The idea of optimizing a portfolio to maximize return based upon an investor's comfort level with risk is as intuitive as balancing your checkbook, or your diet. It can also present similar challenges. Often investors will look to abandon their fixed income allocations when yields are low, when they think rates are set to rise, or when outsized opportunities for gain and/or higher yields present themselves in other income producing investments.

In a balanced diet, the experience of eating kale does not always equal the experience of eating pizza; however, we do it for the health benefits. Cincinnati Asset Management Inc. focuses solely on Corporate Bonds, so here we look at the benefits that Corporate Bonds may bring to the table as part of a balanced portfolio. While Corporate Bonds, like health food, may not always produce the most enjoyable experience, let's explore some of their health benefits for your portfolio.

When we look at total return numbers below[1], we can see the smoothing effect of corporate debt versus other income producing asset classes[2]. Many already know that Investment Grade Corporate Bonds provide limited volatility. However we can see that High Yield Bonds, even with increased risk relative to Investment Grade, can help provide balance by delivering limited drawdown compared to other income producing asset classes.

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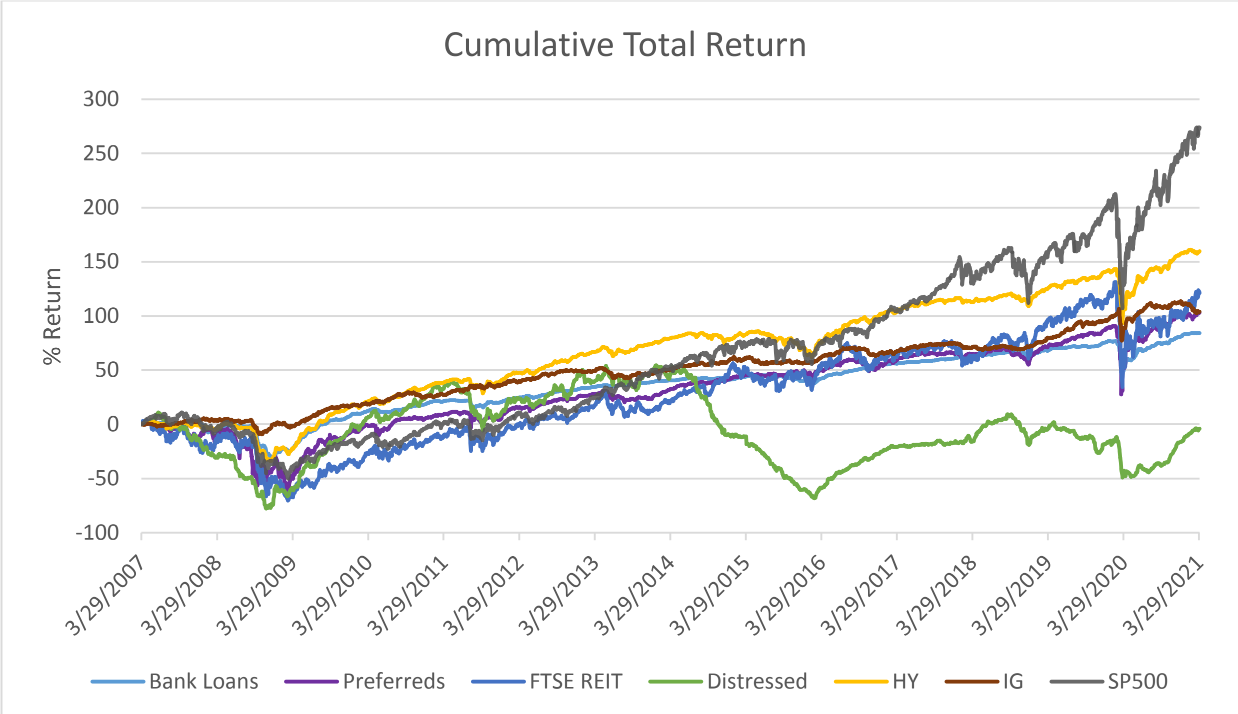
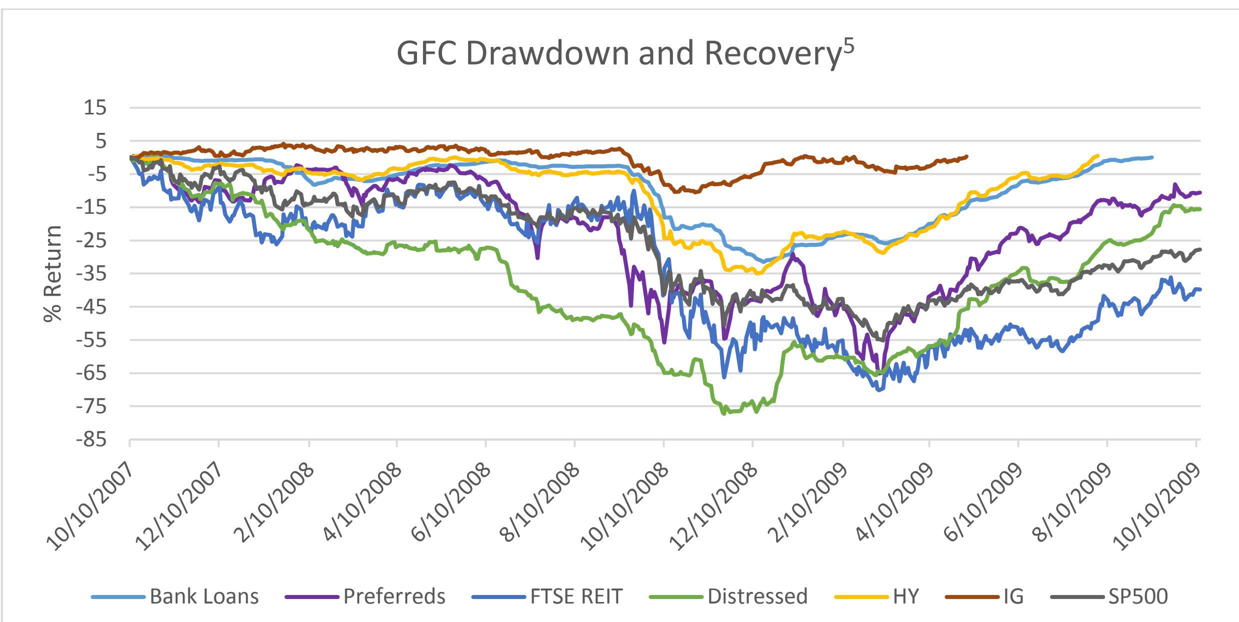
[1] Total Return calculation includes reinvestment of income. Start date of 3/29/07 chosen because it was the first date that the bank loan index changed to daily reporting.

[2] Asset classes were represented by indices:
- Bank Loans - S&P/LSTA Leveraged Loan Total Return Index
- Preferreds - S&P Preferred Stock Index
- REITs - FTSE NAREIT All Equity REITS Total Return Index
- Distressed - Ca to D US High Yield Total Return Index Unhedged
- HY - Bloomberg Barclays US Corporate High Yield Bond Index
- IG - Bloomberg Barclays US Credit Index
- SP500 - S&P 500 Index



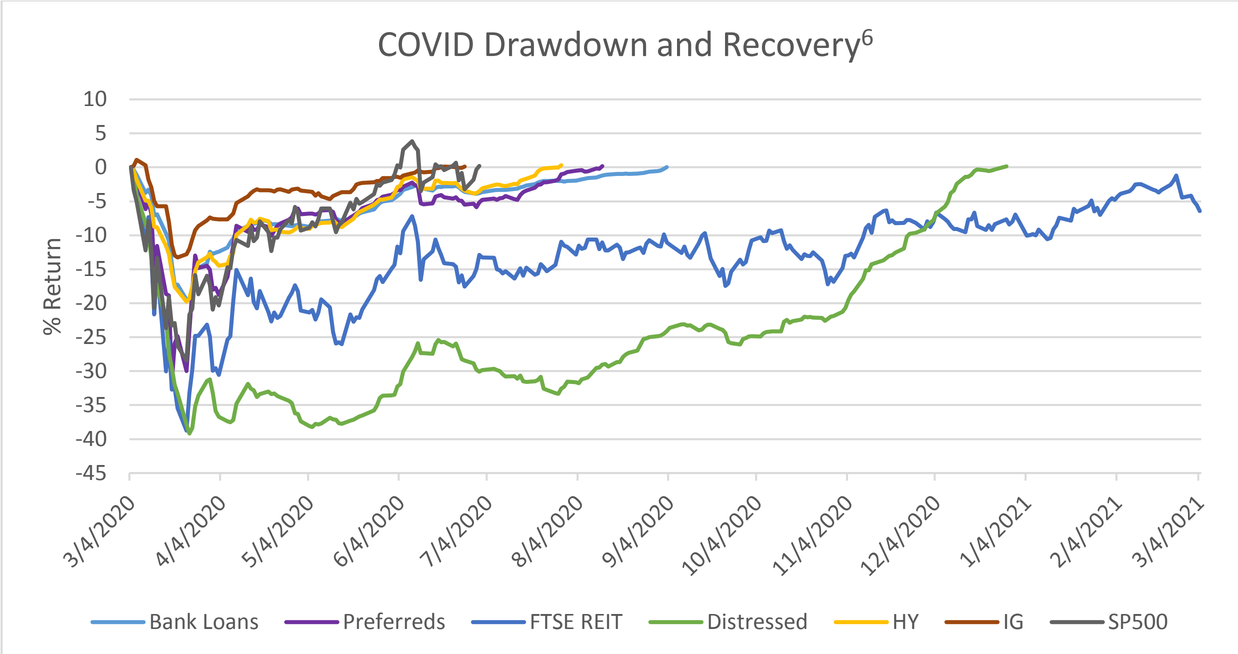
The limited drawdown benefits of corporate bonds become more apparent when we look at recovery time. The below charts highlight the recovery time from the shocks of the Global Financial Crisis[3] and the shocks to the market caused by COVID-19. In both cases, Investment Grade Corporate was the first of the highlighted asset classes to recover[4]. The High Yield market trailed only the Investment Grade market coming out of the Global Financial Crisis and trailed Investment Grade and the S&P 500 in recovery from the COVID-19 shock.



[3] Start date of the Global Financial Crisis of 10/10/2007 reflects the first date where the majority of the indices reviewed were showing drawdown.

[4] Recovery defined as one sustained week where the price of the index was greater than or equal to that of its price on the start date of the observation period.

[5] Recovery period for the Global Financial Crisis shown as 2 years past the date of initial drawdown, not all asset classes fully recovered.



The diversification benefits of corporate fixed income can also be observed when looking at correlations. Investment Grade Corporate Bonds maintain a low to negative correlation with the asset classes disclosed herein over the return period. With the exception of Bank Loans, the story is similar in the High Yield market.

CORRELATION TABLE OF RETURNS BY ASSET CLASS*

	Bank Loans	Preferreds	FTSE REIT	Distressed	HY	IG	SP500
Bank Loans	1.0000	0.3028	0.1555	0.3774	0.7485	0.2574	0.2420
Preferreds	0.3028	1.0000	0.5264	0.2224	0.4130	0.0066	0.5938
FTSE REIT	0.1555	0.5264	1.0000	0.1413	0.2223	-0.0998	0.7808
Distressed	0.3774	0.2224	0.1413	1.0000	0.5730	0.0534	0.2361
HY	0.7485	0.4130	0.2223	0.5730	1.0000	0.2364	0.3719
IG	0.2574	0.0066	-0.0998	0.0534	0.2364	1.0000	-0.2053
SP500	0.2420	0.5938	0.7808	0.2361	0.3719	-0.2053	1.0000

*3/30/2007-3/31/2021

The task of achieving Balance is challenging whether you are a Wallenda walking a tight rope or just trying to work enough vegetables into your diet. Balance requires focus, discipline, and may not always seem comfortable or beneficial in the moment. Much like we need to focus on avoiding the traps that disrupt the work - life, budget, and diet balance, the same should be said for our portfolios. The "health benefits" of limited drawdown and lower correlation must be taken into consideration when making allocation decisions. Both Investment Grade Corporate and High Yield Bonds could play an important role in creating a balanced and "healthy" portfolio.

[6] Recovery period for COVID shown as 1 year past the date of initial drawdown.

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