

March 31, 2025

## First Quarter Fixed Income Letter to Clients

In the first quarter of 2025, the U.S. economy has demonstrated resilience in the face of shifting macroeconomic conditions. While the quarter began with optimism regarding economic growth, recent indicators have suggested a moderation in activity. GDP growth projections have varied, with the Federal Reserve Bank of Philadelphia forecasting a 2.5% annualized growth rate, while other estimates point to a potential slowdown due to policy uncertainties and global trade dynamics. Inflation remains a focal point for policymakers, with core inflation readings suggesting a measured but persistent upward trend. Labor markets have remained tight, contributing to wage growth but also raising concerns over long-term inflationary pressures.

Fixed income markets have experienced notable fluctuations as investors digest economic data and Federal Reserve policy signals. The first quarter saw periods of volatility as the Fed maintained a cautious stance, balancing inflation concerns with the need to support economic expansion. Treasury yields have remained range-bound, reflecting a market that is awaiting clearer direction from monetary authorities.

Municipal bonds have continued to offer a compelling investment opportunity, particularly for tax-sensitive investors. The supply-demand imbalance remains a key theme, with new issuance constrained while demand has remained strong. This technical backdrop has provided price support and helped municipal bonds outperform relative to other fixed-income assets.

Credit fundamentals in the municipal sector remain robust. State and local governments have maintained strong reserve balances, and overall credit ratings remain favorable, with 48 states holding an AA rating or higher. The market continues to benefit from historically low default rates and the essential-service nature of many municipal bond issuers.

Given the current market environment, we remain constructive on high-quality fixed income, with an emphasis on municipal bonds for tax-efficient income generation. Our approach focuses on:

- Identifying high-quality municipal issuers with strong credit profiles.
- Managing duration exposure to balance interest rate risk and income potential.
- Actively assessing market conditions to take advantage of pricing inefficiencies.

In summary, the first quarter of 2025 has presented a complex economic landscape, with municipal bonds standing out as a prudent choice for investors seeking tax-efficient income amid favorable supply-demand dynamics and strong credit fundamentals.

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