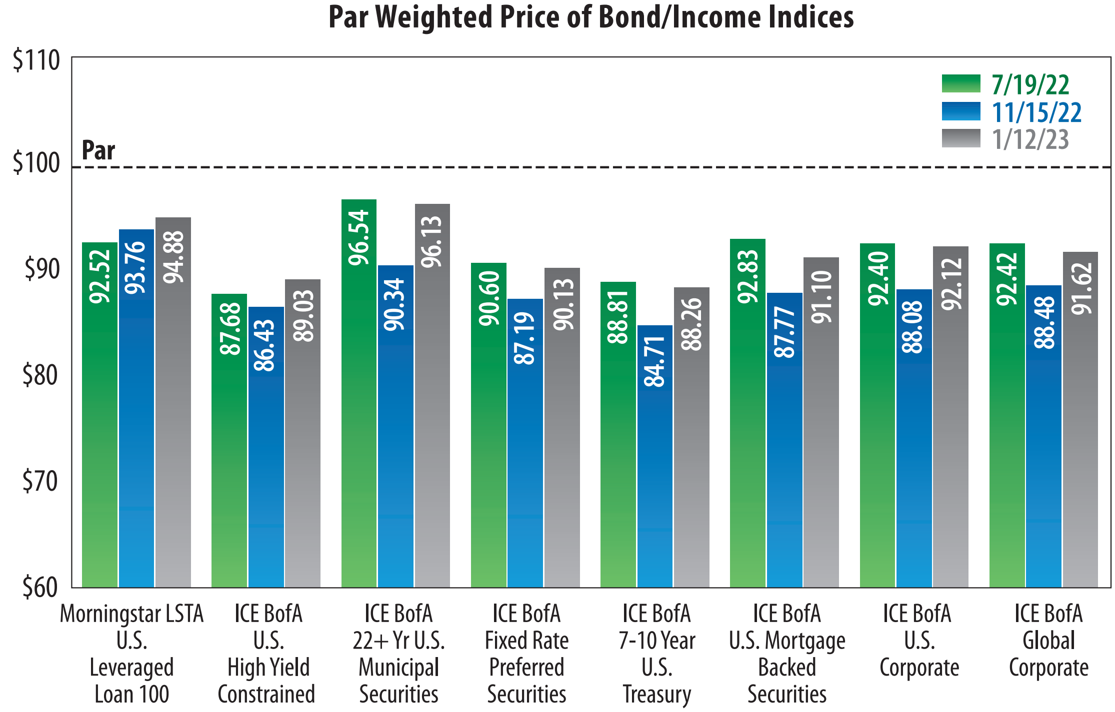
A Snapshot of Bond Valuations



Source: Bloomberg, Bank of America. **Past performance is no guarantee of future results.**

VIEW FROM THE OBSERVATION DECK

This chart is intended to provide an update on bond prices, which are typically sensitive to changes in interest rates. The dates in the chart are from prior posts.

- **All eight of the indices represented in the table show price improvements since 11/15/22**

The Federal Reserve ("Fed") remained steadfast in its commitment to battle inflation in 2022, raising the federal funds rate (upper bound) from 0.25% (where it stood in March) to 4.50% in December. Bond yields, which can be sensitive to interest rate movement, increased in response. This was reflected in price declines (bond yields and prices move inversely) in seven of the eight indices, as can be seen in the chart from mid-July to mid-November.

Conversely, bond prices recovered during the mid-November to mid-January time period. The Consumer Price Index (CPI), a common indicator of inflation, fell from 7.7% at the end of October to 6.5% at December's end, giving some investors reason to believe that the Fed might reverse its policy of monetary tightening. The next Fed policy meeting regarding the federal funds rate is scheduled for February 1, 2023.

- **Negative real yields (yield minus inflation) persist**

As mentioned in our blog post from 1/10/23, most government bonds continue to pay negative real yields. Despite the recent rally in bond prices, investors should be aware that if inflation remains elevated above the Fed's 2% target, bond valuations could be pushed lower. As of 1/12/23 only three of the indices in the chart have positive real yields. They are: the Morningstar LSTA U.S. Leveraged Loan 100 Index (9.01%), the ICE BofA High Yield Constrained Index (8.18%), and the ICE BofA Fixed Rate Preferred Securities Index (6.78%).

TAKEAWAY

Recent price improvements in the U.S. bond market are a welcome sight, but bond investors would be well-served to watch the Fed's next move carefully. Real yields are negative across most of the indices represented in today's chart. If the Fed continues to tighten monetary policy, we may see further downward price pressures in fixed income, in our opinion.

This chart is for illustrative purposes only and not indicative of any actual investment. The illustration excludes the effects of taxes and brokerage commissions or other expenses incurred when investing. Investors cannot invest directly in an index. The Morningstar LSTA U.S. Leveraged Loan 100 Index is a market value-weighted index designed to measure the performance of the largest segment of the U.S. syndicated leveraged loan market. The ICE BofA U.S. High Yield Constrained Index tracks the performance of U.S. dollar denominated below investment grade corporate debt publicly issued in the U.S. domestic market. The ICE BofA 22+ Year U.S. Municipal Securities Index tracks the performance of U.S. dollar denominated investment grade tax-exempt debt publicly issued by U.S. states and territories, and their political subdivisions with a remaining term to maturity greater than or equal to 22 years. The ICE BofA Fixed Rate Preferred Securities Index tracks the performance of investment grade fixed rate U.S. dollar denominated preferred securities issued in the U.S. domestic market. The ICE BofA 7-10 Year U.S. Treasury Index tracks the performance of U.S. dollar denominated sovereign debt publicly issued by the U.S. government with a remaining term to maturity between 7 to 10 years. The ICE BofA U.S. Mortgage Backed Securities Index tracks the performance of U.S. dollar denominated fixed rate and hybrid residential mortgage pass-through securities publicly issued by U.S. agencies in the U.S. domestic market. The ICE BofA U.S. Corporate Index tracks the performance of U.S. dollar denominated investment grade corporate debt publicly issued in the U.S. domestic market. The ICE BofA Global Corporate Index tracks the performance of investment grade corporate debt publicly issued in the major domestic and Eurobond markets.

The information presented is not intended to constitute an investment recommendation for, or advice to, any specific person. By providing this information, First Trust is not undertaking to give advice in any fiduciary capacity within the meaning of ERISA, the Internal Revenue Code or any other regulatory framework. Financial professionals are responsible for evaluating investment risks independently and for exercising independent judgment in determining whether investments are appropriate for their clients.