

# Perspectives: Chilton Trust's Current Approach to Fixed Income

Investor sentiment towards Fixed Income has shifted in and out of favor over the years but an unprecedented shift up in interest rates has caught the attention of global and national investors and has lured many back into the asset class. At Chilton we use an in-depth fundamental framework when thinking about Fixed Income.

Our Chief Investment Officer of Fixed Income, Tim Horan, utilizing his extensive experience working in the Federal Reserve, leads in both a top-down focus on Fed watching and a bottom-up approach to managing our fixed income portfolios.

## How does Chilton think of Fixed Income?

Starting with a deep analysis of the macro-economic environment, Tim and his team evaluate economic data points, geo-political risks, and historical trends to couple the fundamentals with a personalized understanding of our client's needs. Our Fixed Income strategies are designed on a risk-reward spectrum and we adjust our exposure as needed. In terms of your portfolio, we think of Fixed Income as the "sleep-at-night", or safe-haven, portion of your asset allocation. However, we also understand how to look for tactical and strategic opportunities within the various fixed income asset classes from pre-refunded Municipal bonds to Preferred Securities. In every instance, the individual needs of our clients are considered as we construct separately managed account portfolios (SMAs) that reflect our best thinking and years of experience.

## What is happening in Fixed Income Markets – and what is to come?

Given the historic and rapid pace of the tightening cycle, Fixed Income markets have had too much to process. At the outset of this year, markets seemed focused on the higher possibility of an outright recession. Yet, as the year unfolded the remarkable resiliency of the labor market translated into very strong consumer performance, with an overall higher level of domestic demand in our GDP, which topped 4.9% annualized in Q3.

We continue to expect a higher for longer Fed regime and we are not necessarily convinced that the Fed will need to do much more to achieve the goal of getting back to a sustainable 2% inflation. While staying tighter for longer will slow the economy down in 2024, that does not necessarily mean we expect an outright recession (defined by two consecutive quarters of diminishing growth).

Since tightening operates with a lag, the delayed impact of higher rates will continue to impact the economy as labor conditions soften; however that softening is not likely to cause the Fed to blink with an early rate cut. Even some of the most dovish Fed members, such as Regional Chicago President Goolsbee or Atlanta Fed President Bostic, are completely committed to the Fed's 2% inflation goal for the intermediate term. An outright recession would have to accelerate and overtake the US economy before the Fed would substantially change

policy direction versus the incremental approach to rate policy currently in place. If rate cuts are required next year in 2024, they are more likely to occur in the back half of the year, despite the fact that the market may be pricing them in earlier due to general uncertainty.

## What opportunities lie within Fixed Income and how has Chilton's approach changed?

As we methodically construct our portfolios in this environment, there are a few themes that we remain loyal towards: patience, income and liquidity. Throughout the first half of the year, we did not agree with the market's resistance to the Federal Reserve message and therefore we were mindful of our duration exposure. As the Fed continued to stress their inflation target, our portfolios were kept intentionally short as we felt rates would increase further and a re-shaping of the curve was inevitable.

Within this current environment, we are witnessing "dis-inversion" taking place and an overall reshaping of the curve, making now the opportune time to start layering in duration. As such, we are taking a very opportunistic and methodical approach by extending portfolios. Currently, we are finding that municipal and government bonds are a very appropriate space to carefully layer in duration. Investors within the municipal market enjoy the tax-advantaged income, reliable coupons, and municipal bonds that are offering rates we have not seen in several years. When evaluating the relative value of municipal bonds to other asset classes, we found investors within the highest tax bracket are

highly incentivized to increase their tax-advantaged municipal bond exposure. With corporate spreads remaining very steady and not reflecting any signs of slowing growth or volatility ahead, we are more inclined to focus on high-grade issuers or emphasize the government or municipal exposure in the portfolios.

We believe that there will be an appropriate time to expand our credit exposure and that spreads will eventually widen as economic conditions warrant. However, that has yet to be seen and we would prefer to enjoy the elevated Treasury and government rate exposures at this time.

## Conclusion

The ability to earn greater coupon income in this environment is notable and advantageous to portfolios. Elevated interest rates have allowed new issue bonds, US Treasury notes and corporate bonds to come to market with a high paying coupon and the potential to be purchased at a discount in pricing. This scenario allows investors to benefit from price appreciation and higher coupon income throughout the life of the bond.

Ultimately, with strategically constructed portfolios, investors can lock in higher rates for several years in durable, defensive credits, municipalities, and US Treasury bonds. At last, Fixed Income investors can enjoy levels of yield that have not been available in 20+ years, while remaining well within their risk budgets. The result of which has prompted a re-evaluation of the traditional asset allocation approach of 60/40, 70/30, 80/20 that is typically split between equity and Fixed Income.

For further insight on transfer planning and strategy, contact one of our experienced wealth advisors or explore our content library [here](#).

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