NEUBERGER | BERMAN

Neuberger Berman Tax-Exempt Intermediate Maturity Fixed Income Portfolio

PORTFOLIO MANAGERS: James Iselin, Stephen Leone, Peter Moukios, Jeffrey Hunn, Kristian Lind and Randy Gross

PORTFOLIO SPECIALIST: Caroline Wenker

Performance Highlights

The Tax-Exempt Intermediate Maturity Fixed Income Portfolio ("Portfolio") posted a positive return in the third quarter of 2024 but underperformed the benchmark.

Market Context

Fixed income market performance was supported by declining interest rates as the Fed cut policy rates by a greater-than-expected 50 basis points in September. There was a significant rally in interest rates at the start of the month due to weaker non-farm payroll data and the expectation that the Fed would announce the first rate cut after two and half years of a tightening regime. A sell-off in equities and credit markets occurred earlier in September but a rally ensued just before and after the Fed announced its 50 bps decision.

The August employment report was weaker than expected, with non-farm payrolls increasing by +142,000 (vs. +165,000 consensus). Average hourly earnings rose by +0.4% MoM (vs. +0.3% consensus). The unemployment rate came in at 4.2% (vs. 4.2% consensus) and declined from the prior month's report. August inflation continued to moderate, with headline inflation meeting expectations, as headline CPI was +2.5% YoY (vs. 2.5% consensus). Core CPI, which excludes food and energy prices, was in line with expectations at +3.2% YoY (vs. +3.2% consensus). Consumer spending was slightly above expectations as seasonally adjusted U.S. retail sales increased by +0.1% MoM (vs. -0.2% consensus).

The Fed announced a 50 basis point reduction in the federal funds rate target range to 4.75 to 5.00%. Economic activity is expanding, but job gains have slowed, and inflation, while progressing towards the 2% goal, remains slightly above the Fed's target. The Fed remains committed to achieving maximum employment and a 2% inflation rate, continuing to reduce its holdings of Treasury and agency securities. The decision had majority support, with one member preferring a smaller rate reduction.

Despite pockets of volatility in the month and quarter, rates eventually settled at lower levels across the Treasury curve and equity and credit markets rallied after the market sell offs. U.S. government yields moved lower across the curve during the quarter, supporting positive performance across fixed income markets. The 2-year decreased by -112 bps to 3.64%, the 10-year decreased by -62 bps to 3.78%, and the 30-year decreased by -44 bps to 4.12%.

Investment grade U.S. municipal bond returns, as measured by the ICE BofA Municipal Securities Index, delivered strong returns of 2.73% during the third quarter. However, returns varied depending on curve positioning. For the quarter, 1-3 year munis generated a return of 1.95% and the 3-7 year part of the curve outperformed at 2.96%. Longer maturities, in the 22+ year range, also performed well with a return of 2.99%. The Bloomberg Taxable Municipal Index significantly outperformed with a return of 5.42%.[1] Per Bloomberg, total municipal issuance (tax-exempt and taxable) for the quarter was $134.4 billion or 44% higher than it was for the same quarter a year earlier. With regard to credit, BBB rated securities slightly outperformed AAA rated bonds during the quarter. Revenue bonds and general obligations delivered comparable returns during the quarter and housing related credits outperformed. Tobacco related bonds underperformed.

Portfolio Review

The Portfolio posted a positive return in the third quarter of 2024 but underperformed the benchmark. Overall duration and sector decisions were positive contributors while positioning across the yield curve and security selection factors were a drag on performance.

Outlook

While elevated supply has caused the muni market to lag other high-quality fixed income asset classes such as U.S. Treasuries, we have been impressed with how orderly the market has been, given that new issue volume is up 40% relative to the first nine months of 2023. Dealers have been careful to build in appropriate price concessions for new issues to make sure they clear the market. Demand is clearly there when you consider that mutual fund flows have been positive by roughly $25 billion since December. Separately, managed account flows are a bit harder to track, but all signs point to strong flows in that investment vehicle, which continues to grow in popularity.

The bright side of all this supply is better valuations and more potential excess income on a taxable-equivalent basis. For example, intermediate munis ended the third quarter yielding roughly 2.83%, which equates to a taxable-equivalent yield of 4.78% or 112 basis points higher than intermediate Treasuries.

From an economic standpoint, our base case remains for a soft landing for the U.S. economy. In our view, that should bode well for municipal credit quality, which already benefits from strong reserve levels and generally prudent fiscal management. Lower-rated investment grade (A and BBB rated) and high yield munis have meaningfully outperformed the highest-rated bonds so far this year. With nearly half of all municipal fund flows in 2024 going into high yield, we believe the market for lower-rated munis is well supported from both technical and economic standpoints. However, given the outperformance of lower-rated bonds over the past two years, security selection will likely be an important differentiator when adding any credit exposure moving forward. Our overall bias is "up in quality."

Looking ahead, we remain constructive on the municipal market. We expect elevated supply to continue as we move closer to the election, which will give investors a unique opportunity to deploy capital and also participate in deals with price concessions. As mentioned, we believe muni valuations are attractive on a tax-adjusted basis. Finally, if volatility increases due to the U.S. election or geopolitical issues, we think munis will continue to deliver for investors as a safe-haven asset class.

[1]Source: Bloomberg

This material is not intended to constitute research and is merely intended to articulate the thoughts of the Portfolio's portfolio managers regarding the activity of the Portfolio. The portfolio managers' views may differ from those of other portfolio managers as well as the views of Neuberger Berman Investment Advisers LLC ("NBIA") or its affiliates. This material should not be construed as an offer to sell or the solicitation of an offer to buy any security. This material is based upon information that we consider reliable, but we do not represent that it is accurate or complete and it should not be relied on as such. Portfolio characteristics are subject to change without notice. Opinions expressed are current opinions as of the date hereof only. No part of this material may be copied or duplicated in any form, by any means, or redistributed without NBIA's prior written consent. This material is not intended to address every situation, nor is it intended as a substitute for the legal, accounting or financial counsel of your professional advisors with respect to your individual circumstances. Indices are unmanaged, and the figures for any index shown include reinvestment of all dividends and capital gain distributions and do not reflect any fees or expenses. Investors cannot invest directly in an index. We strongly recommend that these factors be considered before an investment decision is made. **Past performance is not indicative of future results, which may vary**.

The information in this material may contain projections, estimates, market outlooks or other "forward-looking statements" regarding future events, including economic, asset class and market estimates, outlooks or expectations, and is only current as of the date indicated. Due to a variety of factors, there is no assurance that such events, outlook, market behavior, and expectations will be achieved, and actual results may differ significantly from any views expressed. Information is based on current views and market conditions, which will fluctuate and may be superseded by subsequent market events or for other reasons.

This Portfolio is available only through a wrap fee or similar program sponsored by a third-party financial intermediary ("Financial Intermediary") that has engaged Neuberger Berman Investment Advisers LLC ("NBIA") to manage certain of the Financial Intermediary's client accounts on a discretionary basis or to provide the Financial Intermediary with recommendations in the form of model portfolio. Please refer to the GIPS® compliant composite presentation, which reflects NBIA's calculations with respect to the Portfolio that are not specific to any Financial Intermediary or client account ("Composite"). Portfolio information is based on the Composite and is subject to change without notice. Specific client account performance is reflected in the official books and records maintained by the Financial Intermediary or other custodian selected by the Financial Intermediary or client ("Custodian"). When the client account is held by the Custodian, foreign or otherwise, other than NBIA and/or its affiliates ("Neuberger Berman"), Neuberger Berman shall have no responsibility, liability, duty or obligation with respect to the selection of the Custodian, custody arrangements or the acts of the Custodian, information provided by the Custodian, omissions or other conduct of the Custodian, including investment by the Custodian of cash in the account, pricing, reporting functions, foreign exchange execution services, the security of data maintained by the custodian, whether electronically stored or otherwise, or the Custodian's failure to obtain and maintain adequate insurance for the account, including but not limited to that which is offered by the Securities Investor Protection Corporation or the Federal Deposit Insurance Corporation, nor for any fees, charges or expenses that may be owed to the Custodian.

A bond's value may fluctuate based on interest rates, market conditions, credit quality and other factors. There may be a gain or loss if bonds are sold prior to maturity. Of course, bonds are subject to the credit risk of the issuer.

The municipal securities market could be significantly affected by adverse political and legislative changes, the financial health of a municipality or the financial condition of municipal securities market, as well as uncertainties related to taxation or the rights of municipal security holders.

Third-party economic or market estimates discussed herein may or may not be realized and no opinion or representation is being given regarding such estimates. Target yields are based on current market conditions. There is no guarantee, and investors should not assume, that any estimates or target yields will be realized.

Through December 31, 2023 the Index consists of 80% ICE BofA 3-7 Year US Municipal Securities Index and 20% ICE BofA 7-12 Year US Municipal Securities Index. From January 1, 2024 and onward, the Index consists of ICE BofA 2-12 Year US Municipal Securities Index.
ICE BofA 2-12 Year US Municipal Securities Index is a subset of ICE BofA US Municipal Securities Index including all securities with a remaining term to final maturity greater than or equal to 2 years and less than 12 years. ICE BofA US Municipal Securities Index tracks the performance of US dollar denominated investment grade tax-exempt debt publicly issued by US states and territories, and their political subdivisions, in the US domestic market. Qualifying securities must have at least one year remaining term to final maturity, at least 18 months to final maturity at the time of issuance, a fixed coupon schedule and an investment grade rating (based on an average of Moody's, S&P and Fitch). Minimum size requirements vary based on the initial term to final maturity at time of issuance.The index is rebalanced on the last calendar day of the month, based on information available up to and including the third business day before the last business day of the month.

The benchmark is an unmanaged blend of indices. NBIA advises according to the Portfolio characteristics which may differ from those of the benchmark. Additional disclosures for complete benchmark descriptions are available upon request.

Any third party mark(s) appearing above is/are the mark(s) of its/their respective owner(s).

This material is general in nature and is not directed to any category of investors and should not be regarded as individualized, a recommendation, investment advice or a suggestion to engage in or refrain from any investment-related course of action. Investment decisions and the appropriateness of this material should be made based on an investor's individual objectives and circumstances and in consultation with his or her advisors.

Neuberger Berman Investment Advisers LLC is a registered investment adviser. The "Neuberger Berman" name and logo are registered service marks of Neuberger Berman Group LLC.