Week of March 25, 2025

Notes from the week We were able to attend the Exchange Conference this past week. The ETF-focused gathering was an opportunity for us to run due diligence on asset managers collected in one location. I had two big takeaways from the event. 1.) The best products are made by people who directly solve simple problems. These teams identify something missing from the market that people want anyways and fill the void. The least convincing pitches are "WOW this thing in the market is really good right now, why not make it even GOODER in an ETF?!". 2.) Income-focused funds are an important contributor to future returns. While this category includes bonds and fixed income, this is not all about bonds and fixed income. We heard a lot of pitches on income-producing option strategies overlaid on an underlying basket of equity products. We're intrigued by the idea but have not been sold yet. We need to understand how the creation/redemption process interacts with the capacity to write covered calls. If shares of an ETF are redeemed and securities are returned to a market maker, how does that affect the extent pool of options? However, the biggest movement in the ETF space is the rise of actively managed funds. The early ETFs were focused on passive strategies pegged to indices. This works well for equities, which has a limited number of options –there are about 4,300 public companies in the US. Income faces more market fragmentation – there are about 80,000 active bonds in the US. Active management can be advantageous in this field as managers need to parse through multiple issues from individual issuers, changes in underlying interest rates, differentiating between collateralizations, and evaluating tactical opportunities. We believe, with our long experience in credit and fixed income, Bray Farm IA is well positioned to take advantage of this trend.

On the macro side… Today we had a release of the February results for the Personal Consumption Expenditures (PCE), the Fed's favorite measure of prices. The number came in a little hotter than expected with a year-over-year core increase of 2.8%.

And this is before tariffs…. However, rather than driving bond yields higher, we saw yields *drop,* especially in the belly of the curve (5-10 years). The short term – less than one year – is still anchored by the Fed's holding power. In the near term – 2 to 5 years – the focus is marginally on a slowing of growth rather than a change in prices. In the belly of the curve, the focus is *really* on growth. In a strange contradiction, a hot inflation reading makes the bond market *less worried* about inflationary pressure and more worried about growth. I think it's a fair bet to assume that the Fed would deal with growth issues first. *An important side note—much of the discussion from Treasury Secretary Bessent is around the 10-year yield. At some point, we should listen and accept the administration may take regulatory action to make this happen. The big options on the table are limiting auction sizes and changing capital requirements on banks.*

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