Commentary | 4Q20

Voya Intermediate Fixed Income SMA

Multi-Sector Approach Focused on Total Return

Strategy overview

A total return approach, utilizing a multi-sector approach with a higher quality posture through the use of Treasury, Agency and Corporate Credit securities with 1-10 year maturities. The primary drivers of our investment grade fixed income performance are our positioning for rate trends and sector relative value assessments across governments, mortgages and corporates.

Portfolio review and outlook

The Voya Intermediate Fixed Income SMA underperformed its benchmark, the Bloomberg Barclays U.S. Intermediate Government/Credit index, for the quarter.

The portfolio remained overweight in high-quality corporate bonds versus an underweight to U.S. Treasury bonds. Corporate exposure was concentrated in less-aggressive, liquid and higher credit quality debt issues. While the decision to overweight to these high-quality investment-grade (IG) corporates versus the benchmark added to relative results, some of the individual securities detracted, as lower-quality securities performed better in 4Q20 than higher-quality securities, thereby offsetting the asset allocation gain over the period.

Yields rose and spread sectors continued their outperformance in the final quarter of 2020. The United States and global economy showed signs of re-emerging from economic challenges earlier in the year, and the approval of two vaccines extended the outperformance of risks assets and triggered a cyclical rotation favoring sectors that had been lagging in the summer rebound. U.S. GDP rose 33.4% on an annualized basis in the third quarter, after a decline of -31.4% in the second quarter. U.S. unemployment levels declined to 6.7% in November, albeit at a slower pace, but a meaningful reduction from the peak level of 14.7% recorded in April. Fiscal stimulus, varying levels of re-openings around the country and simply adjusting to living in a “Covid world” supported healing in the economy. While the U.S. elections were expected to be the center of attention, the announcement of two vaccines and their rapid approval by the Food and Drug Administration (FDA) stole the spotlight. The news from both Moderna, and then Pfizer, fueled hope for a return to normalcy and added momentum to the demand for risk assets.

Heading into 2021, the market backdrop for cyclical sectors is extraordinarily positive. We believe consumers, supported by excess savings, robust net worth and additional fiscal aid, will drive a recovery in discretionary spending, leading to a full re-engagement of the service sector as the vaccine rollout becomes more widespread. The recovery in services spending, coupled with resilience in goods demand, should usher in an extended period of synchronous, above-trend global growth, easing pressures on the income divide.

In the near term, cyclical sectors are relatively attractive. We believe that a rebound in economic growth, fostered by fiscal and central bank support, will push yield spreads uncomfortably tight in 2021. However, we also recognize the market seems to be very aligned on the near-term positive direction of risk assets. This one-way sentiment opens the door for volatility. The vaccine news is overwhelmingly positive, and we believe the vaccine ultimately will succeed. However, the potential for episodic market stresses, whether connected to the vaccine or other global factors, should not be overlooked.

The heavy use of economic stabilizers creates vulnerability to shocks and will leave investors exposed to increasingly asymmetric risk profiles. Security selection, which is always important, will be critical as the dispersion between “winning” and “losing” investments within sectors will remain extremely wide. Diversification and careful analysis of cyclical versus structural factors are necessary to mitigate downside risks and prepare portfolios for the income-starved world we face ahead.

The **Bloomberg Barclays U.S. Intermediate Government/Credit Index** includes fixed rate, dollar-denominated, investment grade securities with maturities of 1-10 years held within both the Bloomberg Barclays U.S. Government Index (public obligations of the U.S. Treasury, U.S. Government agencies, quasi-federal corporations, and corporate or foreign debt guaranteed by the U.S. Government) and the Bloomberg Barclays U.S. Credit Index (publicly issued U.S. corporate and foreign debentures and secured notes).

The principal risks are generally those attributable to bond investing. Holdings are subject to market, issuer, credit, prepayment, extension, and other risks, and their values may fluctuate. Market risk is the risk that securities may decline in value due to factors affecting the securities markets or particular industries. Issuer risk is the risk that the value of a security may decline for reasons specific to the issuer, such as changes in its financial condition. The strategy may invest in mortgage-related securities, which can be paid off early if the borrowers on the underlying mortgages pay off their mortgages sooner than scheduled. If interest rates are falling, the strategy will be forced to reinvest this money at lower yields. Conversely, if interest rates are rising, the expected principal payments will slow, thereby locking in the coupon rate at below market levels and extending the security's life and duration while reducing its market value. High yield bonds carry particular market risks and may experience greater volatility in market value than investment grade bonds. Foreign investments could be riskier than U.S. investments because of exchange rate, political, economics, liquidity, and regulatory risks. Additionally, investments in emerging market countries are riskier than other foreign investments because the political and economic systems in emerging market countries are less stable.

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The strategy employs a quantitative model to execute the strategy. Data imprecision, software or other technology malfunctions, programming inaccuracies and similar circumstances may impair the performance of these systems, which may negatively affect performance. Furthermore, there can be no assurance that the quantitative models used in managing the strategy will perform as anticipated or enable the strategy to achieve its objective.

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The opinions, views and information expressed in this commentary regarding holdings are subject to change without notice. The information provided regarding holdings is not a recommendation to buy or sell any security. Portfolio holdings are fluid and are subject to daily change based on market conditions and other factors.

Past performance does not guarantee future results.

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