

FIRST QUARTER 2024

# Tax-Advantaged Preferred Securities Commentary

March 31, 2024

## PERFORMANCE

The Tax-Advantaged Preferred Securities Composite (Composite) returned 3.89% on a net-of-fees basis during the quarter. The Composite underperformed the benchmark by 126 basis points (bps) in the quarter. The current yield on the portfolio is 7.69% with a taxable equivalent yield of 9.77%.

\$25 par retail preferreds' positive performance in January and the underweight to this asset class were the causes of relative underperformance. With rates likely stabilizing, we are beginning to take a closer look at the relative value of the fixed-for-life structures but still view spreads as nonattractive compared to institutional preferreds. The Composite's allocation to retail preferreds is still aggressively underweight.

	1Q24	YTD	1 Year	3 Years	ITD <sup>†</sup>
Composite Gross [%]	3.99	3.99	14.81	1.37	0.99
Composite Net [%]	3.89	3.89	14.37	1.06	0.67
Index [%]	5.15	5.15	10.38	-1.74	-1.76
<b>Outperformance [%]</b>	<b>-1.26</b>	<b>-1.26</b>	<b>3.99</b>	<b>2.79</b>	<b>2.44</b>

<sup>\*</sup>ICE BofA Core Plus Fixed Rate Preferred Index

Periods greater than 12 months are annualized

<sup>\*\*</sup>Outperformance=Composite Net-Index

Source: Bloomberg, Clearwater Analytics

<sup>†</sup>Performance calculated from inception date 1/1/2021

## PREFERRED AND HYBRID MARKET OVERVIEW

Passive \$25 retail preferred ETFs have had an increase in inflows in the first quarter due to the possibility of an easing cycle beginning in an election year. Given the increased sensitivity to interest rates for the fixed-for-life structures, we are starting to see slightly more value in these structures than we did the previous quarter. However, our relative value analysis still shows further value in the low coupon, low dollar priced \$1000 par fixed-to-float institutional securities compared to the highly volatile \$25 retail preferreds.

Regional and super regional banks outperformed in the institutional preferred space despite the volatility around New York Community Bank (NYCB) during the first quarter. We feel that this was an isolated event due to NYCB's unique and concentrated commercial real estate portfolio compounded by rapid growth and the consequent increased regulatory attention. Furthermore, NYCB's ability to access equity capital as a going concern is a credit positive the regional banking system.

## CURRENT POSITIONING

The strategy is low turnover by its nature (in order to qualify for Qualified Dividend Income/Dividend Received Deduction treatment, holding must be long term), therefore, current positioning is very consistent with the recent past. The portfolio will have a slow turnover rate as positions are called away by the issuer and must be replaced. As the curve steepened from its maximum inversion in March 2023, the Composite has slowly and methodically extended duration without sacrificing too much in the way of current yield, and we expect to continue with this rotation in 2024 to the extent that our current positions are called away and the curve continues its recent trajectory of steepening.

The portfolio remains up in quality relative to other preferred securities strategies with a complete list of holdings below. A large percentage of the portfolio is invested in the big six U.S. money center banks with the balance invested in high-quality super-regional and regional banks.

## PORTFOLIO MANAGEMENT TEAM


**Brandon F. Bajema, CFA, CPA**

 Co-Chief Investment Officer  
 Senior Portfolio Manager  
 Industry start date: 2003  
 Joined Red Cedar: 2021

**John L. Cassady III, CFA**

 Co-Chief Investment Officer  
 Industry start date: 1987  
 Joined Red Cedar: 2018

**David L. Withrow, CFA**

 Senior Market Strategist  
 Industry start date: 1988  
 Joined Red Cedar: 2018

## KEY FACTS

Current Yield	7.71
QDI Yield [%]	9.79
DRD Yield [%]	8.71
Duration	1.78
Sherman Ratio	4.38
Average Credit Quality	BBB
Number of Holdings	22

Top 10 Issuers	Wgt [%]	Cur Yld [%]	QDI Yield [%]	DRD Yield [%]
JPM	7.89	8.82	11.20	9.97
BAC	7.87	8.70	11.06	9.84
C	7.01	7.26	9.22	8.21
MS	6.44	8.49	10.78	9.59
USB	6.35	7.33	9.31	8.28
GS	6.26	7.06	8.97	7.98
WFC	6.26	7.13	9.06	8.06
TFC	5.90	8.63	10.97	9.76
CFG	5.23	9.13	11.60	10.32
KEY	5.22	6.75	8.58	7.63

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### DISCLOSURES

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The securities discussed do not represent the Composite's entire portfolio. Actual holdings will vary depending on the size of the account, cash flows, and restrictions. It should not be assumed that any of the securities transactions or holdings discussed will prove to be profitable, or that the investment recommendations or decisions we make in the future will be profitable or will equal the investment performance of the securities discussed herein.

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All information and performance are reported in U.S. dollars.

The "Net" returns presented are net of fees. Investing involves the risk of loss and investors should be prepared to bear potential losses. Past performance is not indicative of future results.

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Tax-Advantaged Preferred Securities Composite (Composite) was created on December 18, 2020. The inception date of the Composite was January 1, 2021. The Composite includes all fully discretionary institutional portfolios that invest in tax efficient preferred securities. At the time of purchase the issuing company's senior unsecured debt rating must be investment grade by any one NRSRO or equivalent as determined by Red Cedar Investment Management at time of purchase. Under normal circumstances a minimum of 80% of the portfolio will be invested in QDI eligible preferred securities. The account minimum for this composite is \$100,000. Prior to February 1, 2023, the name of the Composite was \$25 Preferred Securities Composite. The Sherman Ratio is defined as an interest rate risk measure and represents the yield per unit of duration.

#### Benchmark Definition:

The benchmark is the ICE BofA Core Plus Fixed Rate Preferred Securities Index (POP4). The ICE Core Plus Fixed Rate Preferred Index (POP4) is a preferred securities index for \$25 retail prefs including investment grade and high yield securities. The ICE BofA Core Plus Fixed Rate Preferred Securities Index includes preference shares (perpetual preferred securities), both DRD-eligible and non-DRD eligible preferred stock and senior and subordinated debt issued in \$25, \$50 or \$100 par/liquidation increments. An index is an unmanaged portfolio of specific securities, the performance of which is often used as a benchmark in judging the relative performance of certain asset classes. Investors cannot invest directly in an index. An index does not charge management fees or brokerage expenses, and no such fees or expenses were deducted from the performance shown.

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