Palmer Square Income Plus Fund (PSYPX)

October 2023

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Fund Refresher

As a refresher, the investment objective of the Palmer Square Income Plus Fund ("PSYPX" or the "Fund") is income and capital appreciation. In seeking to achieve that investment objective, the Investment Team employs a flexible mandate to find the best relative value across corporate credit and structured credit. The Fund has also historically maintained low interest rate duration* and high credit quality. Due to the Fund's high-quality bias we are very comfortable with the underlying credit quality of the holdings and ability to avoid credit losses; over 80% of the portfolio is rated investment grade ("IG") and over 59% is rated A or higher. Spread duration* is 2.2 years.

What is the Fund trying to achieve in today's market to benefit clients?

- Diversified Income Generation – The Fund generates income through a diversified exposure to corporate and structured credit, including primarily corporate bonds, bank loans, collateralized loan obligations ("CLOs"), commercial mortgage backed securities ("CMBS"), residential mortgage backed securities ("RMBS"), asset backed securities ("ABS"), commercial paper and U.S. Treasury securities.
- Low Interest Rate Duration – We have had minimal interest rate duration which drives lower correlation to interest rate sensitive fixed income such as those investments which comprise the Bloomberg U.S. Aggregate Bond Index and Bloomberg 1-3 Year U.S. Corporate Index*.
- Capital Preservation – The Fund maintains a high-quality bias.
- Total Return – The Fund also seeks capital appreciation through opportunistic portfolio rotations driven by the Investment Team's assessment of relative value. Please note that the Fund can invest up to 30% in high yield rated ("HY") securities.

Portfolio Snapshot

Please refer to the table below for a portfolio snapshot by quarter.

	9/30/2022	12/31/2022	3/31/2023	6/30/2023	9/30/2023
Interest Rate Duration	0.62 yrs	0.64 yrs	0.79 yrs	0.89 yrs	0.91 yrs
Spread Duration	2.65 yrs	2.70 yrs	2.38 yrs	2.36 yrs	2.22 yrs
Yield to Expected Call*	6.46%	6.49%	6.42%	7.07%	6.90%
Yield to Maturity	6.19%	6.26%	6.17%	6.80%	6.74%
Current Yield	4.15%	4.90%	5.36%	5.72%	5.73%
30-day SEC Yield* (net of fees)	3.84%	5.14%	5.67%	5.97%	6.05%
30-day SEC Yield* (gross of fees)	3.84%	5.14%	5.67%	5.97%	6.05%

The performance data quoted represents past performance and that past performance does not guarantee future results. Investment return and principal value will fluctuate, so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance information quoted. To obtain performance information current to the most recent month-end please call 866-933-9033.

*Please see Notes and Disclosure for definitions.

Relative Value and Current Upside Potential

- We believe the Fund is well positioned for potential upside going forward. We also believe high breakeven spread levels exist which serve as a cushion in a spread widening environment. As shown in the highlighted box below, if spreads were to go back just to average levels over the past 10 years, the 1-year total return is estimated to be about +9%. If we go back to 10-year tights on spreads, that return goes to +10.25%. Also given the very high coupon and spread levels currently, there is a very high hurdle to not capture a positive return over a 1 year holding period. The 1yr forward breakeven column below shows the spread levels each asset class would need to hit to not earn a positive return over the next year. At a Fund level, we would need to see over 270bps of widening from current levels, which would put us at worse levels than we saw during COVID.
- Most notably, we see a lot of value in CLO debt at current levels, as spreads are still well wide of average levels since 2008. If CLO debt levels return to their average post crisis spreads, total return potential is very attractive. We continue to favor shorter duration CLO deals with cleaner portfolios at a discount which we think will continue to deliver high total returns over the near term.

PALMER SQUARE INCOME PLUS FUND							1yr Forward Breakeven[3]	3/31/2020[4]	2/28/2016[5]
Rating	**Allocation**	**Price**	**Spread**	**YTE***	**Average 1yr Upside[1]**	**Tight 1yr Upside[2]**	**Spread**	**Spread**	**Spread**
CLO AAA	11.34%	$99.63	149	6.33%	7.15%	7.46%	586	243	186
CLO AA	2.44%	$97.08	284	6.79%	8.15%	9.11%	403	349	284
CLO A	0.56%	$98.61	271	7.30%	8.03%	10.06%	517	501	394
CLO BBB	12.14%	$96.51	475	9.35%	12.42%	14.94%	698	755	661
CLO BB	8.13%	$95.55	828	13.07%	16.88%	20.86%	1069	1384	1193
CLO B	0.27%	$86.04	1270	17.49%	26.97%	36.58%	1055	1949	1653
ABS	13.06%	$98.81	46	5.95%	5.95%	5.95%	659	313	52
CMBS	4.75%	$86.29	596	10.94%	24.35%	25.54%	1146	225	75
RMBS	12.19%	$89.60	145	6.13%	7.84%	9.98%	323	375	150
Corp HY	4.41%	$92.63	258	7.04%	6.63%	9.07%	419	880	726
Corp IG	16.46%	$95.12	105	6.00%	5.90%	6.49%	230	272	197
Bank Debt	4.53%	$100.16	250	7.06%	7.08%	7.91%	604	844	639
Govt	9.73%	$99.16	0	5.02%	5.02%	5.02%	0	0	0
Total	**100.00%**	**95.62**	**246**	**7.32%**	**8.97%**	**10.25%**	**517**	**467**	**334**

Source: Bloomberg, Palmer Square, as of 9/30/2023. *YTE, also known as Yield to Expected Call, is a Yield to Call metric that assumes callable bonds are not called at their call date, but some later date prior to maturity. [1]Refers to the potential increase in value of the investment in one year if spreads return to 10-year average levels. [2]Refers to the potential increase in value of the investment in one year if spreads return to 10-year tight levels. The potential increase in value is calculated by determining the return resulting from the positive or negative difference between the current price of the securities and the price of the securities at the respective spread levels noted in the hypothetical performance (i.e., spread levels at 10-year averages) plus the income from anticipated coupon payments over the next 12 months. For purposes of this analysis, anticipated coupon payments incorporate the forward LIBOR/SOFR curve. [3]Refers to the level at which spreads would need to widen in order to cause a negative value in an individual investment over a one-year period. This is determined by reducing a security's price by its expected coupon payments over the next 12 months and then calculating the level of spread widening that would need to occur to move the security's actual price to the reduced price. For purposes of this analysis, anticipated coupon payments incorporate the forward LIBOR/SOFR curve. [4]Month end during Covid dislocation. [5]Month end of energy market dislocation. Below investment grade ratings are subject to higher risks. Figures shown are not indicative of the performance of the Fund. The presented hypothetical performance does not reflect the impact of material economic and market factors on decision-making, any changes to the strategy over time, and was prepared with the benefit of hindsight. Past performance is no guarantee of future returns.

*Please see Notes and Disclosure for definitions.

Summary Themes:

- **Q3 2023 Performance, Attribution and Positioning;**
- **2023 Outlook: Federal Reserve (Fed) Pause, Soft Landing, Earnings Recession, Defaults Contained, Bonds are Back.**

Theme I. Q3 2023 Performance, Attribution and Positioning

- **Q3 2023 Performance and Attribution: The Fund delivered a positive return of 2.36% (net of fees) in Q3 2023 taking the YTD 2023 return to 5.76% (net of fees)**. This compares to YTD returns of -1.21% and +2.30% for the Bloomberg U.S. Aggregate Bond Index and the Bloomberg 1-3 Year U.S. Corporate Index, respectively. The positive absolute performance was driven by a broad-based rally in credit spreads, particularly within our CLO exposure in the month of July, which in turn was driven by cooler than expected inflation data. The Fund's exposure to CLO debt provided the largest contribution at +1.82%, followed by ABS at +0.17% and bank loans at +0.13%. On the negative side, RMBS detracted 0.02% while HY and IG corps only provided 0.02% and 0.09% during the quarter.
- There are a few key takeaways from general Q3 credit market performance. First, the move in long interest rates was the overwhelming negative driver of returns. Indeed, duration continues to run over any and everyone who chooses to stand in her way. Most fixed income benchmarks are back in the red for the year, following the worst year for fixed income in 40 years. Fun fact: the 5Y and 10Y annualized returns of the U.S. Aggregate Index are ZERO percent and +1% respectively, while over that same time period inflation has compounded at 2.8%. Second, current yields are also very high and mitigate the impact of higher rates. For example, high yield managed a positive return in the quarter despite higher rates and modestly wider spreads, all thanks to carry. This was even more pronounced in floating rate products (loans, CLOs) which receive the full benefit of higher short rates without the downside price adjustment. The final takeaway is that CLO debt spreads played a bit of catch up with corporate spreads but are notably still wide of averages. Below we include quarterly performance of the key credit benchmarks.

Selected Indices*	Q3 2023 Performance	YTD 2023 Performance
Bloomberg U.S. Treasury Index	-3.06% (Yield +0.48%)	-1.52% (+0.70%)
Bloomberg U.S. Aggregate Bond Index	-3.23% (spread +3bps)	-1.21% (+3bps)
Bloomberg U.S. Corporate Index	-3.09% (spread -1bps)	+0.02% (-8bps)
Bloomberg 1-3 Year U.S. Corporate Index	+0.77% (spread +12bps)	+2.30% (+12bps)
Bloomberg U.S. High Yield Index	+0.46% (spread +3bps)	+5.86% (-75bps)
iBoxx Liquid Leveraged Loan Index	+2.72% (DM -20bps)	+9.06% (-92bps)
Palmer Square CLO Senior Debt Index	+2.44% (DM -26ps)	+6.62% (-49bps)
Palmer Square CLO Debt Index	+5.30% (DM -56bps)	+12.83% (-97bps)
S&P 500 Index	-3.27%	+13.06%
STOXX 600 Index	-4.12%	+10.79%

Source: Bloomberg as of 9/30/2023. *Please see Notes and Disclosure for definitions.

- **Positioning:** There were no significant positioning shifts in the quarter. We have begun to see our macro view on rates play out AND see the Fund's core CLO debt exposure really drive the performance we have been expecting.

Theme II. 2023 Outlook: Fed Pause, Soft Landing, Earnings Recession, Defaults Contained, Bonds are Back

- **Pause, Not Pivot:** Recent inflation data is mixed at best, with "goods" prices decelerating but "services" inflation remaining stubbornly high. Core inflation has also likely peaked, but what is not clear is how long it will take to normalize back to the Fed's target level of 2%. Due to the way core inflation is calculated, the housing component of the Consumer Price Index* (42% weight in headline, 54% in core) works on a lag and will take time to fully reflect the current state of the housing and rental markets. Additionally, the inflation in core services is also unlikely to trend meaningfully lower without a sustained loosening in the labor market, which remains incredibly robust (unemployment at record lows and job openings still near record highs). Therefore, our base case is core y/y numbers, currently +4.8% y/y, will remain stubbornly high throughout 2023. And until the Fed feels core inflation has normalized, they will be forced to keep rates in restrictive territory (i.e. > 5%). That said, we also believe the Fed will pause the current hiking cycle in 2H 2023 once the Fed Funds Rate reaches 5.50% in order to observe the cumulative impact of higher interest rates on the economy. Furthermore, we do not see the Fed cutting rates in 2023, nor in early 2024, without a material weakening of the labor market combined with negative GDP (Gross Domestic Product) growth, which is not our base case. In summary, we believe short term interest rates will remain higher for longer than the market is currently pricing in. This would be positive for floating-rate securities as their coupons would remain higher for longer than the market currently anticipates.
- **Soft(ish) Landing:** Our view that rates will stay higher for longer is, in part, based on our view that the macro picture looks resilient. The labor market is as strong as ever, literally. In fact, so strong that the Fed would like to see it cool a bit to ease inflation pressure. We have seen some layoffs starting, but so far this has been isolated to the tech space. The consumer remains in decent shape, with debt/income levels still historically low and excess savings still high. In Europe, the macro picture has improved substantially thanks to warmer weather and government actions. And lastly, geopolitical risks have eased as well – Russia in a stalemate in Ukraine, Ukraine exporting grain, China reopening, European unity, etc. Growth will undoubtedly slow as high interest rates restrict investment, but we don't envision a hard landing.
- **Earnings Headwinds to Stabilize in 2H23:** Corporate earnings have been under pressure recently, particularly in the cyclical sectors like housing, construction, industrials and chemicals. However, we are starting to see signs of green shoots, with a consensus building that Q3 2023 will be the earnings trough. In any case, as we have highlighted previously, corporates started this current cycle from a period of strength, particularly when compared to previous cycles when corporates entered recessions over-levered and under prepared. Moreover, the Fund's non-cyclical bias has mitigated the recent earnings headwinds. On the whole, most measures of credit metrics are strong: debt leverage, interest coverage, liquidity, maturity profile, etc. As such, we think most corporates are well positioned to withstand several quarters of weak earnings without a deterioration in credit profiles. The exception to this will be the weakest cohort of companies with bad business models and/or bad capital structures (i.e., CCCs and cyclical single Bs). But this is why fundamental credit research and selection remains so important, now more than ever.

*Please see Notes and Disclosure for definitions.

- **Defaults Contained:** The current cycle started with default rates practically at zero. So to say they will increase is certainly no hot take. In fact, they have already increased to around 1.25-1.50% depending on how one treats distressed exchanges. From a historical perspective, around half of CCCs default in an economic downturn. The weight of CCCs in the HY and bank loan market are 10% and 6% respectively. So you could make the argument that half of those might default in 2023. You might also make the argument that another 1-3% in defaults from companies with 1) bad/ disrupted business models and/or 2) bad capital structures and inadequate liquidity/ maturities could potentially put total defaults at 4-5%. However, with respect to our managed CLOs and this Fund specifically, we are not concerned with a contained rise in defaults given our bias on larger, higher quality, less cyclical issuers.
- **Floating Rate Is the Place to Be:** As the 3rd quarter showed, even if the Fed hiking cycle is nearly finished, there is still significant risk being exposed to the long end of the curve. We believe floating rate credit provides significant opportunity. Current yields still benefit from base rates at the highest part of the curve, but credit spreads are also more attractive than their fixed rate cohorts. And we believe floating rate yields could even be understated if the projected interest rate cuts in 2024 don't materialize.

Summary on Attribution, Allocation and Positioning

Select Portfolio Attribution and Characteristic Dashboard

	Allocation	% Allocation	Q3 2023 Attribution	Average Price	Yield to Expected Call*
IG	ABS (100% AAA)	13%	0.17%	$98.8	5.95%
IG	Treasury Bills	9%	0.11%	$99.2	5.02%
IG	CLO AAA	11%	0.27%	$99.6	6.33%
IG	CLO AA	2%	0.04%	$97.3	6.78%
IG	CLO A	1%	0.02%	$98.6	7.30%
IG	CLO BBB	12%	0.77%	$96.6	9.34%
IG	RMBS (98% AAA, 100% A and above)	12%	-0.01%	$90.5	6.13%
IG	CMBS (88% A- and above, 97% IG)	5%	-0.14%	$90.5	10.93%
IG	IG Corp Bonds - Fixed	13%	0.05%	$94.5	5.98%
IG	IG Corp Bonds - Floating	3%	0.04%	$100.0	6.07%
IG	IG Bank Loans	1%	0.01%	$101.4	6.12%
HY	Bank Loans - Non IG	4%	0.12%	$100.0	7.17%
HY	HY Corp Bonds	4%	0.02%	$93.0	7.03%
HY	CLO BB	8%	0.67%	$86.1	17.49%

Source: Palmer Square as of 9/30/2023. The performance data quoted represents past performance and that past performance does not guarantee future results. Investment return and principal value will fluctuate, so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance information quoted. Fund holdings and sector allocations are subject to change and should not be considered a recommendation to buy or sell any security. To obtain performance information current to the most recent month-end please call 866-933-9033.

*Please see Notes and Disclosure for definitions.

Historic Positioning Detail by Asset Type:

	9/30/2022 Allocation	12/31/2022 Allocation	3/31/2023 Allocation	6/30/2023 Allocation	9/30/2023 Allocation
CLO Debt	34%	35%	34%	35%	34%
IG Corp Debt	27%	26%	19%	17%	16%
ABS	8%	10%	8%	12%	13%
Gov't Bonds	5%	5%	15%	9%	9%
RMBS	5%	5%	5%	9%	12%
Bank Loans	7%	7%	4%	5%	4%
CMBS	6%	7%	5%	5%	5%
HY Corp Bonds	3%	2%	7%	5%	4%
Cash/Other	3%	3%	3%	3%	3%

Please note allocation and attribution above is a % of NAV and does not include hedges. Gross attribution does not include hedges, expenses and fees if applicable. Fund holdings and sector allocations are subject to change and should not be considered a recommendation to buy or sell any security. Asset-backed Securities (ABS), Mortgage-backed Securities (MBS), Commercial mortgage-backed securities (CMBS), Residential mortgage-backed securities (RMBS).

- **Investment Grade Corporate Bond Allocation** – The IG corporate bond exposure was modestly reduced further this quarter, from 17% to 16%. Credit spreads hit YTD tights early in the quarter and we continued to trim risk into this strength. However, later in the quarter as yields widened out significantly we took our exposure back up with a focus on 1.5-2Y bonds in the 6-6.25% yield range (unhedged). *Even though spreads are somewhat tight, the price and yield is attractive from a buy-and-hold perspective. And if rates do decrease these bonds may pull to par.*
- **High Yield Bond Allocation** – As of quarter-end, HY corporate bond exposure was 4.3% of the portfolio, down modestly from 5.0% from last quarter. The HY allocation was largely static throughout the quarter, but we did slightly reduce our allocation in early September as HY Index OAS (Option-Adjusted Spread)* hit the lowest level since April 2022. We remain singularly focused on BB-rated bonds with an additional bias toward defensive sectors and issuers. Since quarter-end, spreads and yields have widened moderately, which could present an opportunity to tactically re-add some HY exposure in the near-term.
- **CLO Allocation/Opportunity to Capture Income and Total Return** – As of quarter-end, 34% of the portfolio, which was a decrease of 0.9% from last quarter. Our largest exposure in the capital stack continues to be AAA, which still offer tremendous value in the 150-180bps spread range and yields in the 6-7% range. AAA spreads are still well wide of historical averages and yields have never been higher. Breakeven spread widening also looks very attractive at current levels. For example, over a one year holding period AAA spreads on shorter duration profiles would need to reach over 500bps in order to not make money, a level wider than during the depths of the COVID pandemic.[1]
  - » CLO mezzanine exposure also stayed relatively stable with BBBs at 11.9% and BBs at 7.9%. Spreads tightened throughout the quarter and BBB/BB CLO debt were some of the best performing asset classes with Q3 returns of +5.33%/+7.79%. Forward looking yields still look very attractive with the average price/yield on our BBBs at $96.5/9.35% and BBs at $95.6/13.07%.

  We continue to add to CLO portfolios that are higher quality and more liquid as we believe they will continue to outperform portfolios with more risky collateral.

*Please see Notes and Disclosure for definitions. [1]This example is provided for illustrative purposes only.

- **ABS/MBS Allocation has Provided Diversification and Income Capture** – As of quarter-end, 29% of the portfolio had exposure to ABS/MBS. During the quarter, our allocation to ABS and MBS increased as we slightly decreased across other products.
  - **ABS** exposure (primarily prime auto ABS with a weighted average life (WAL)* of 6 months or less) ended 1% higher relative to Q2, currently 13% of the Fund.
  - **CMBS** exposure at quarter-end was 5%, approximately flat to Q2 2023. Our preference in CMBS continues to be single asset/single borrowers and in sectors where we find most relative value, notably industrials. At this time, we feel there are still macro headwinds for commercial real estate in certain sectors. While we remain cautious toward the sector, we may opportunistically increase exposure to assets with strong fundamentals when attractive entry points present.
  - **RMBS** exposure ended the quarter 3% higher compared to Q2 2023. The incremental 3% was in agency CMOs. Our exposure in non-agency is still primarily AAA- rated debt which are backed by collateral from borrowers with FICOs (Fair Isaac Corporation*) greater than 700 and in some cases as high as 750. Agency spreads are at historical wide levels as rate volatility created an attractive entry point in the space relative to corp IG sector.

ABS/MBS Positions	**9/30/2023**
Prime Autos	11%
Equipment	2%
ABS (100% AAA)	**13%**
Conduit	1%
Single Asset/Single Borrower	4%
CMBS (99% A- and above)	**5%**
Agency	6%
Non-Agency	6%
RMBS (99% AAA)	**12%**

Source: Palmer Square.

- **Bank Loan Allocation** – As of quarter-end, bank loan exposure was 4% of the portfolio, a decrease of 1% over the last quarter. Loan exposure was largely unchanged and remained low throughout the quarter. This is mainly due to cash prices in the BB loan space being well above par. The bulk of our limited bank loan exposure remains in shorter-dated BB loans, which we believe offer attractive current income and should be well insulated from volatility given CLO technicals related to investment periods and WAL constraints. *We continue to be fundamentally constructive on the higher quality part of the U.S. bank loan asset class and would look to increase exposure if prices moved lower.*

Given the recent market moves and the continued dislocation in credit, we believe the Fund is well-positioned to not only generate a strong yield, but also meaningful capital appreciation going forward. As mentioned in our last quarter's letter, we believe our Fund's positioning has the potential to deliver a higher Sharpe* ratio as we continue to navigate these markets. We feel we are opportune in our approach to relative value and could not be more excited about how this portfolio is positioned and its outlook.

*Please see Notes and Disclosure for definitions.

Detailed Fund Performance History

The Fund returned 2.36% (net of fees) for the third quarter of 2023.

Fund Performance Net of Fees as of 09/30/2023 (inception 2/28/2014)

	Q3 2023	YTD 2023	2022	2021	2020	2019	2018	2017	2016	2015
PSYPX	2.36%	5.76%	-0.76%	1.17%	3.65%	5.29%	1.17%	4.03%	5.24%	1.21%
Bloomberg 1-3 Year U.S. Corporate Index*	0.77%	2.30%	-3.32%	-0.13%	3.79%	5.30%	1.56%	1.85%	2.36%	1.00%
Bloomberg U.S. Aggregate Bond Index*	-3.23%	-1.21%	-13.01%	-1.54%	7.51%	8.72%	0.01%	3.54%	2.66%	0.57%

Fund Performance Net of Fees as of 09/30/2023 (inception 2/28/2014)

	1 Year	3 Years	5 Years	Since Inception Annualized
PSYPX	7.99%	2.67%	2.83%	2.87%
Bloomberg 1-3 Year U.S. Corporate Index*	3.73%	-0.18%	1.70%	1.59%
Bloomberg U.S. Aggregate Bond Index*	0.64%	-5.21%	0.10%	0.98%

Class I shares – Annual Expense Ratio: Gross 0.75%/Net 0.75%. Palmer Square has contractually agreed to waive its fees and/or pay for operating expenses of the Fund to ensure that total annual fund operating expenses (excluding any taxes, leverage interest, brokerage commissions, dividend and interest expenses on short sales, acquired fund fees and expenses (as determined in accordance with Form N-1A), expenses incurred in connection with any merger or reorganization, and extraordinary expenses such as litigation expenses) do not exceed 0.75% of the average daily net assets of the Fund. This agreement is in effect until October 31, 2023, and it may be terminated before that date only by the Trust's Board of Trustees. The Fund's advisor is permitted to seek reimbursement from the Fund, subject to certain limitations, of fees waived or payments made to the Fund for a period ending three full fiscal years after the date of the waiver or payment. **Shares of the Fund are available for investment only by clients of financial intermediaries, institutional investors, and a limited number of other investors approved by the Advisor. The performance data quoted represents past performance and that past performance does not guarantee future results. Investment return and principal value will fluctuate, so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance information quoted. To obtain performance information current to the most recent month-end please call 866-933-9033.**

Summary

The Fund's diverse portfolio across corporate and structured credit is positioned in predominately investment grade securities, yet has offered a strong current yield* and potential opportunity for capital appreciation. We believe we are opportune in our approach to relative value and could not be more excited about how this portfolio is positioned and its outlook.

Please do not hesitate to contact us at investorrelations@palmersquarecap.com or 816-994-3200 should you desire more information. We would also be happy to set up a call and/or meeting at your convenience.

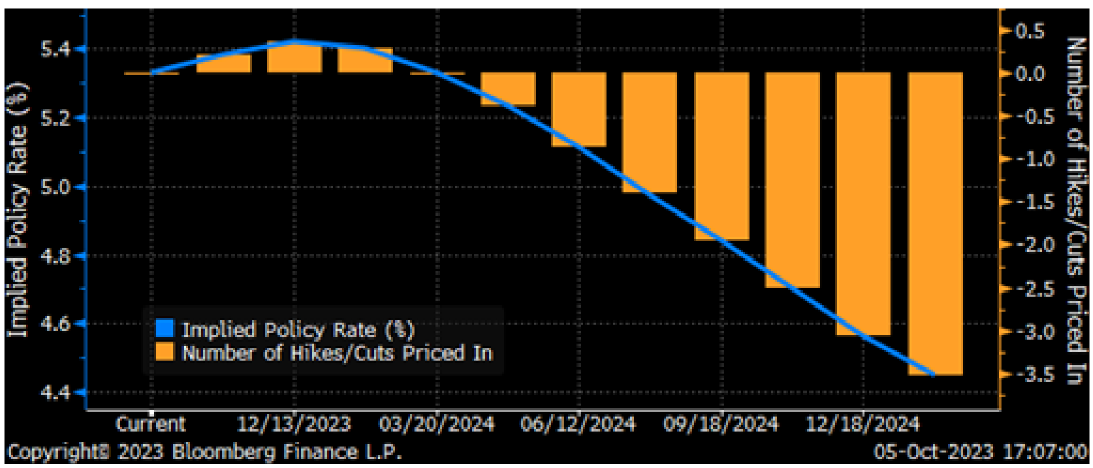
*Please see Notes and Disclosure for definitions.

APPENDIX: Macro Musings: James Carville, Fiscal Irresponsibility, Higher for Longer(er)

- One of our favorite finance quotes comes from someone not even in the finance industry, James Carville, who once quipped "I used to think that if there was reincarnation, I wanted to come back as the President or the Pope or as a .400 baseball hitter. But now I would want to come back as the bond market. You can intimidate everybody." Indeed, the proverbial bond vigilantes must have seen the various labor protests around the world and decided to join the picket line and dump their treasury holdings in protest of persistent inflation and, increasingly, fiscal profligacy. Mr. Carville knows a thing or two about the relationship between the bond market and federal largesse. He was an advisor to President Clinton, and witnessed treasury yields increase from 5% to 8% in 1994, commonly referred to the Great Bond Massacre. It was only until fiscal spending was reigned in via the Omnibus Budget Reconciliation Act did treasury yields rally back to 5.0%. This was also that last time the U.S. Federal Government ran a budget surplus. Imagine that!
- Another great, and relevant, quote we like is "History never repeats itself, but it often rhymes." That one is not from Mr. Carville but rather Mark Twain. Are we rhyming with 1994? We hope not, but the parallels are unnerving. The latest PCE Deflator data showed inflation cooled more than expected and confirmed the steady, albeit slow, path back to 2% core was intact. But the rates market shrugged this off with the 10Y yield widening out 35bps 3 days later. This fading of positive inflation data indicates the bond market is concerned with more than just inflation. There's a growing supply/demand imbalance that has been largely ignored until recently. And it appears it is going to get much worse before it gets better.
- The Federal budget balance was -8.5% of GDP in Q2 2023, the largest "non-crisis" quarterly deficit ever. That's $575Bn in new debt in just Q2 2023 alone. Federal debt-to-GDP has increased from 65% in 2007 to 121% in 2022. And the nominal amount of federal debt has increased from $20T to $34T just since 2016. That's 10x the amount of federal debt in 1994. As we know, excessive government spending can only be financed in two main ways, higher taxes and/or higher borrowing. While we do think tax rates will have to move higher, it is unquestionable that the market is going to have to absorb significantly more treasury supply in the near/medium term (NB: the Fed is also a net seller of treasuries). And this tidal wave of supply is coming at the same time foreign demand for U.S. debt is shrinking. Japan and China are the largest holders of U.S. treasuries and are both net reducing. U.S.-China trade peaked in 2018 and is headed lower. Lower Chinese exports means less USD to recycle into the U.S. debt market. And Japan is poised to end its policy of Yield Curve Control which will make domestic assets relatively more attractive. Plus, USDJPY hedging costs have skyrocketed. The picture for domestic treasury demand is more mixed but still not great. Most banks are paralyzed with existing unrealized losses and prefer to remain liquid in case deposit outflows resume. The retail and asset management community does have demand, but anyone who went long rates has been steamrolled, and probably stop-lossed out. Lastly, we haven't even mentioned yet the toxic political environment, persistent debt ceiling near-misses, rating downgrades and general lack of fiscal seriousness by either of the major parties.

- Switching gears a bit, the *Higher for Longer* narrative continues to play out, as evidenced by the latest FED DOT* plot and economic data, which continues to show significant tightness in the labor market. We think the market consensus has been slow to adopt the higher for longer narrative because it's still anchored to a low-rate world. We suppose years of financial repression will do that to a person. But as we have highlighted repeatedly in past updates, there have been several structural changes in the global economy that suggest inflation is here to stay, for a while at least. The era of offshoring production to low wage economies, and importing deflation back is mostly over. This is partially due to emerging market countries becoming richer and seeing wage growth catch up with the west, but also due to reshoring in various industries deemed of national interest. Namely, semiconductor manufacturing, pharmaceuticals, steel production, battery and green tech, etc. The cost of this deglobalization is higher prices. Environmental sustainability, while noble and just, is also inflationary by and large. It simply costs more to be sustainable. These factors are admittedly high-level and slow moving, but significant enough to argue the neutral rate is no longer 2.5%.

Fed Funds Projection: Market expects cuts starting in summer 2024



Source: Bloomberg 10/5/2023

*The FOMC (Federal Open Market Committee) DOT plot, alternatively called the Fed's dot plot, is a chart that summarizes the FOMC's outlook for the federal funds rate. It is published quarterly and watched closely by investors and economists for indications on the future trajectory of the federal funds rate. Please see Notes and Disclosure for definitions.

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Bloomberg U.S. Treasury Index measures US dollar-denominated, fixed-rate, nominal debt issued by the US Treasury. **Bloomberg U.S. Aggregate Bond Index** is an unmanaged index of publicly issued investment grade corporate, U.S. Treasury and government agency securities with remaining maturities of one to three years. **Bloomberg U.S. Corporate Index** measures the investment grade, fixed-rate, taxable corporate bond market. **Bloomberg 1-3 Year U.S. Corporate Index** measures the performance of investment grade, U.S. dollar-denominated, fixed-rate, taxable corporate and government-related debt with 1 to 2.9999 years to maturity. It is composed of a corporate and a non-corporate component that includes non-U.S. agencies, sovereigns, supranationals and local authorities. **Bloomberg U.S. High Yield Index** measures the USD-denominated, high yield, fixed-rate corporate bond market. **iBoxx Liquid Leveraged Loan Index** tracks the total return of the 100 most liquid loans from the USD LLI index universe, offering a powerful insight into the loan market. **Palmer Square CLO Senior Debt Index** is a rules-based observable pricing and total return index for collateralized loan obligation debt for sale in the United States, rated at the time of issuance as AAA or AA (or an equivalent rating). Such debt is often referred to as the senior tranches of a CLO. **Palmer Square CLO Debt Index** is a rules-based observable pricing and total return index for collateralized loan obligation debt for sale in the United States, rated at the time of issuance as A, BBB or BB (or equivalent rating). Such debt is often referred to as the mezzanine tranches of a CLO. **S&P 500 Index** is a market-capitalization-weighted index of 500 leading publicly traded companies in the U.S. **Bloomberg Commodity Index** is a broadly diversified commodity price index distributed by Bloomberg Index Services Limited. **The Credit Suisse Liquid Leveraged Loan Index** is designed to represent a subset of the Leveraged Loan Index, based on the following criteria: Facilities rated at least Caa3/CCC- and no higher than Ba1/BB+ by Moody's/S&P, facilities with an amount outstanding of at least $1 billion, facilities which rank first lien in seniority, institutional facilities, such as facility types Term Loan B ("TL-b""), Term Loan C ("TL-c"), Term Loan D ("T- d"), etc. Bank-held facilities, facility types TL and TL-a, are excluded, only the largest facility per issuer is eligible; in the case of a tie, the facility with the longer maturity is selected, eligible new loans are added at the beginning of the month following issuance. **Bloomberg CMBS AAA Index** measures the AAA-rated market of US Agency and US Non-Agency conduit and fusion CMBS deals with a minimum current deal size of $300mm. The **Cboe Volatility Index (VIX)** is a real-time index that represents the market's expectations for the relative strength of near-term price changes of the S&P 500 Index (SPX). **Credit Default Swap Index (CDX)**, formerly the Dow Jones CDX, is a benchmark financial instrument made up of credit default swaps (CDS) that have been issued by North American or emerging market companies. The **AAII** Sentiment Survey measures the percentage of individuals who are bullish, bearish, and neutral about the stock market over the next six months. Unlike mutual funds, indices are not managed and do not incur fees or expenses. It is not possible to invest directly in an index. The **option-adjusted spread (OAS)** is the measurement of the spread of a fixed-income security rate and the risk-free rate of return.

Interest Rate Duration measures a portfolio's sensitivity to changes in interest rates. **Spread Duration** measures the sensitivity of a bond price based on basis point changes of more than 100. **Yield to Expected Call** is a Yield to Call metric that assumes callable bonds are not called on their call date, but at some later date prior to maturity. Yield to Expected Call considers contractual terms in a bond's indenture or other similar governing document. A bond may be called before or after this date, which has the potential to increase or decrease the Yield to Expected Call calculation. All else equal, when a bond's price is below par, Yield to Expected Call is a more conservative yield metric than Yield to Call. If a bond is not callable, Yield to Expected Call calculates the bond's Yield to Maturity. **Yield To Maturity**

Notes and Disclosure cont'd

is the rate of return anticipated on a bond if held until the end of its lifetime. **Current Yield** is annual income divided by price paid. **Sharpe Ratio** is used to measure risk-adjusted performance. The Sharpe ratio is calculated by subtracting the risk-free rate - such as that of the 10-year U.S. Treasury bond - from the rate of return for a portfolio and dividing the result by the standard deviation of the portfolio returns. **WARF** The weighted average rating factor is a measure that is used by credit rating companies to indicate the credit quality of a portfolio. The **Weighted Average Life (WAL)** is the average length of time that each dollar of unpaid principal on a loan, a mortgage, or an amortizing bond remains outstanding. **Credit Spreads** are often a good barometer of economic health - **widening (bearish sentiment)** and **narrowing/tightening (bullish sentiment)**. A **tight market (tight-trading)** is a market characterized by narrow bid-ask spreads and abundant liquidity with frenetic trading activity. A mutual fund's **30-Day SEC Yield** refers to a calculation that is based on the 30 days ending on the last day of the previous month. The yield figure reflects the dividends and interest earned during the period, after the deduction of the fund's expenses. **Basis points (BPS)** refers to a common unit of measure for interest rates and other percentages in finance. The relationship between percentage changes and basis points can be summarized as follows: 1% change = 100 basis points and 0.01% = 1 basis point. **The London Interbank Offered Rate (LIBOR)** is a benchmark interest rate at which major global banks lend to one another in the international interbank market for short-term loans. The **Secured Overnight Financing Rate (SOFR)** is a benchmark interest rate for dollar-denominated derivatives and loans that is replacing the London interbank offered rate (LIBOR). **Dry powder** refers to cash or marketable securities that are low-risk and highly liquid and convertible to cash. A **discount margin (DM)** is the average expected return of a floating-rate security (typically a bond) that's earned in addition to the index underlying, or reference rate of, the security. A FICO score is a credit score created by the **Fair Isaac Corporation (FICO)**. Lenders use borrowers' FICO scores along with other details on borrowers' credit reports to assess credit risk and determine whether to extend credit.

Past performance is not indicative of future results. Different types of investments involve varying degrees of risk and there can be no assurance that any specific investment will be profitable. Please note that the performance of the funds may not be comparable to the performance of any index shown. Palmer Square has not verified, and is under no obligation to verify, the accuracy of these returns. Diversification does not assure a profit, nor does it protect against a loss in a declining market

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