DECEMBER 2023

ARISTOTLE PACIFIC CAPITAL

THE INVESTOR Compass

NAVIGATING THE CREDIT MARKETS

TWELVE FOR ‘23

2023 was a year filled with shifting expectations and unexpected outcomes. On the back of the greatest inflationary environment in four decades, 2023 demonstrated resiliency in the face of tightening credit conditions, a regional banking crisis, a near government shutdown and escalating geopolitical uncertainties. Odds makers missed their bets this year.

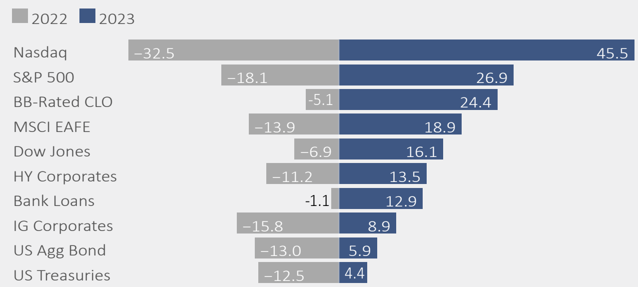
Central to the year's narrative was the inescapable influence of the Federal Reserve. While the Fed reacted in a more measured response, culminating in a pause at a post-GFC high in July, it was the shifting of longer-term rate expectations that sent waves throughout financial markets. As 2023 ends, "higher for longer" expectations have given way to speculation around multiple rate cuts in 2024. There is no question Fed policy and outlook will continue to be a primary contributor to market volatility in 2024.

A main storyline in 2023 was the remarkable performance of the technology sector. Leading the way were the "Magnificent 7" stocks (Apple, Microsoft, Alphabet, Amazon.com, Nvidia, Tesla, and Meta Platforms) which capitalized on the optimism surrounding AI's potential. These tech giants saw their valuations surge by 75%, following a 40% down year in 2022, markedly outpacing the broader S&P 500's increase.

(Continued on pg. 4)

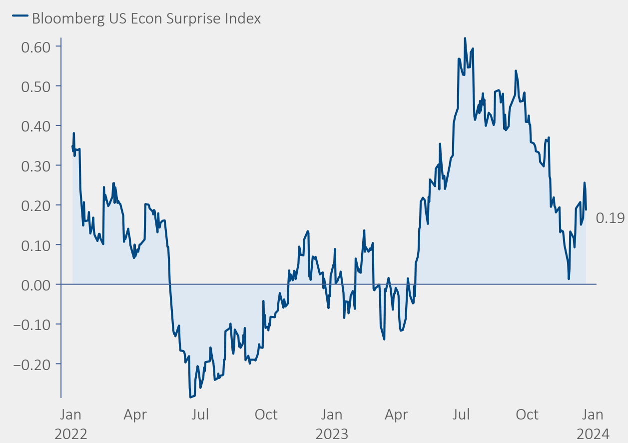
Performance Rebounds

Asset Class Performance 2022 vs 2023 (%)



Source: MSCI, Bloomberg, Credit Suisse, as of December 27, 2023

Surprise! It was a good year.



Higher values indicate economic data exceeds Street estimates
Source: Bloomberg, as of December 27, 2023

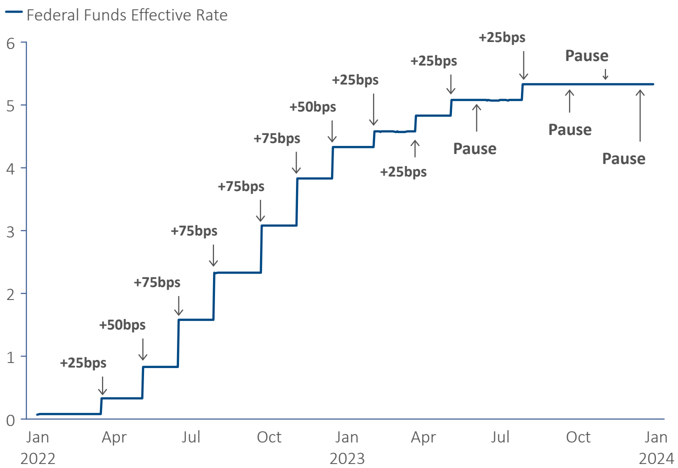
Table 1: Inflation is cooling, but not quite cold

CPI Component (%YoY)	Nov-23	Oct-23	Sep-23	Aug-23	Jul-23	Jun-23	May-23	Apr-23	Mar-23	Feb-23	Jan-23	Dec-22
Headline CPI	3.14%	3.24%	3.70%	3.67%	3.18%	2.97%	4.05%	4.93%	4.98%	6.04%	6.41%	6.45%
Food	2.95%	3.30%	3.69%	4.25%	4.86%	5.74%	6.69%	7.65%	8.50%	9.49%	10.13%	10.41%
Energy	-5.44%	-4.53%	-0.45%	-3.62%	-12.47%	-16.74%	-11.66%	-5.06%	-6.42%	5.19%	8.70%	7.31%
Core CPI	4.01%	4.03%	4.15%	4.35%	4.65%	4.83%	5.33%	5.52%	5.59%	5.54%	5.58%	5.71%
Core Goods	-0.04%	0.02%	-0.03%	0.39%	0.93%	1.41%	2.02%	2.08%	1.59%	0.96%	1.29%	2.18%
Core Services	5.49%	5.51%	5.69%	5.89%	6.12%	6.16%	6.57%	6.84%	7.12%	7.27%	7.17%	7.03%
Shelter	6.51%	6.72%	7.15%	7.27%	7.69%	7.83%	8.04%	8.11%	8.18%	8.10%	7.88%	7.51%

Green is lower relative inflation / **Red** is higher relative inflation
Source: The BofA Inflation Heatmap, as of December 27, 2023

Chart 1:

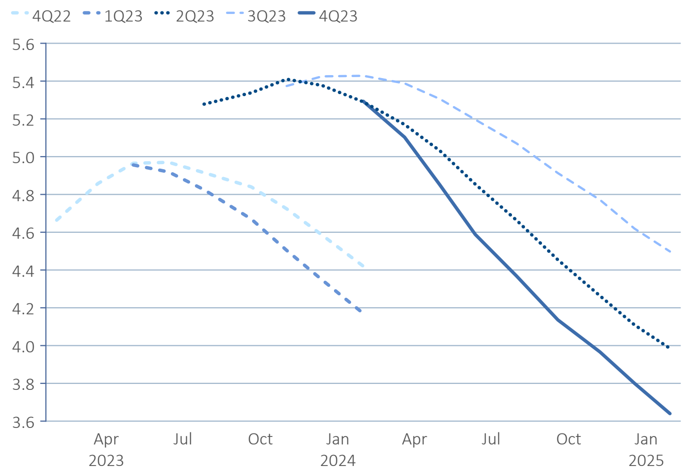
Peak rates?



Source: St. Louis FRED, as of December 27, 2023

Chart 2:

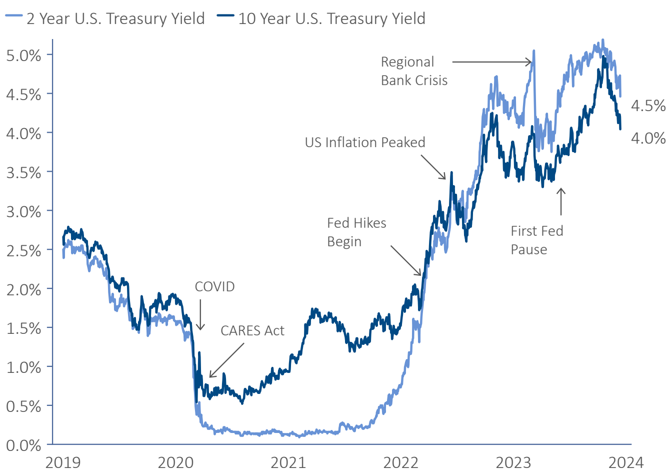
Rate cuts are ~six months ahead..for the past 12 months



Source: Bloomberg, as of December 27, 2023

Chart 3:

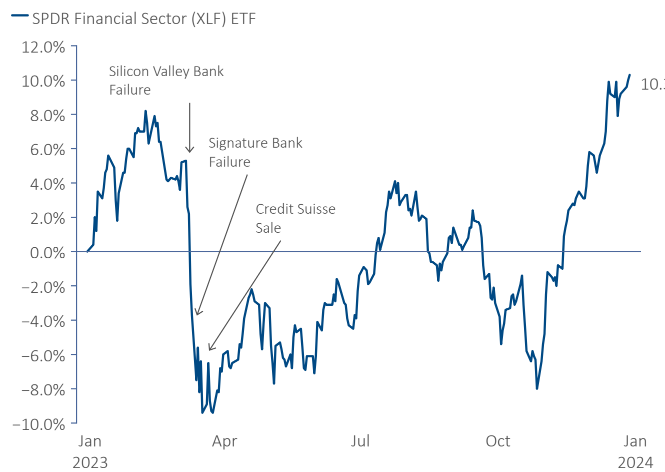
Interest rate volatility impacted returns across asset classes in 2023



Source: St. Louis FRED, as of December 27, 2023

Chart 4:

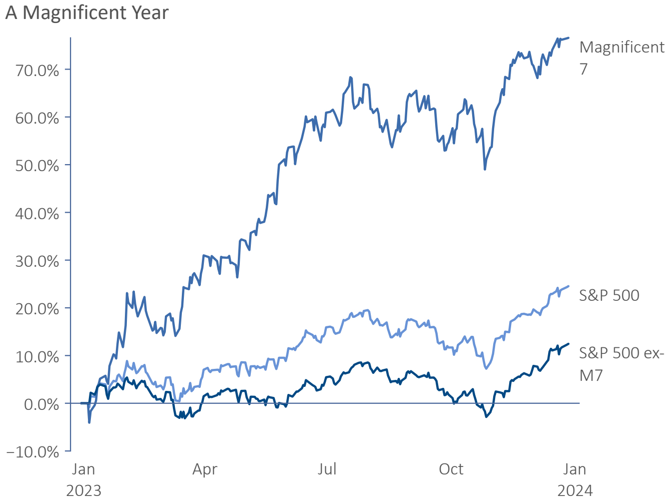
There were bank failures? (Financial sector back at 52-week high)



Source: Bloomberg, as of December 27, 2023

Chart 5:

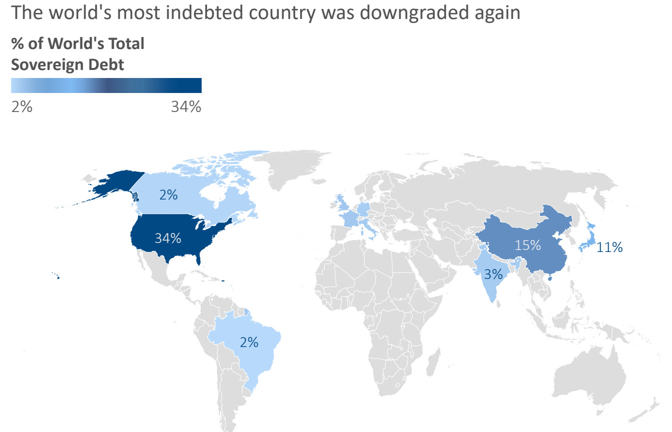
A Magnificent Year



Source: Bloomberg, as of December 27, 2023

Chart 6:

The world's most indebted country was downgraded again

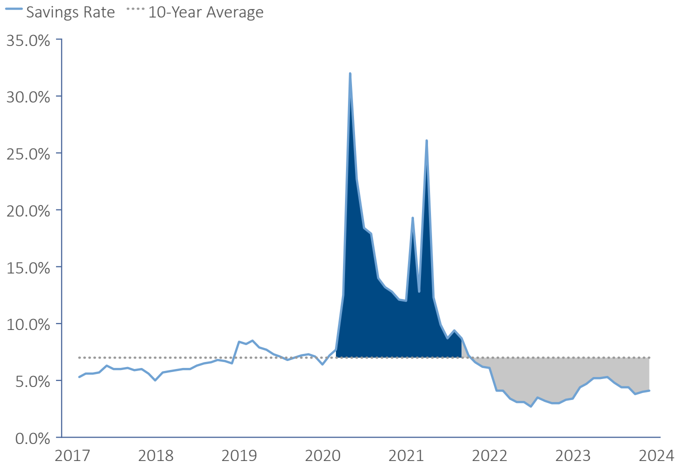


U.S. Sovereign downgrade to AA+ by Fitch Ratings in Aug 2023

Source: International Monetary Fund, as of December 27, 2023

Chart 7:

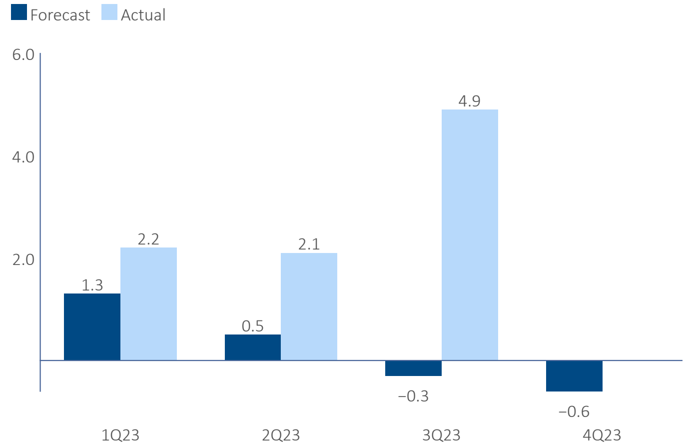
COVID "savings" are being spent..



Source: U.S. Bureau of Economic Analysis, as of December 27, 2023

Chart 8:

..Leading to much better than expected GDP

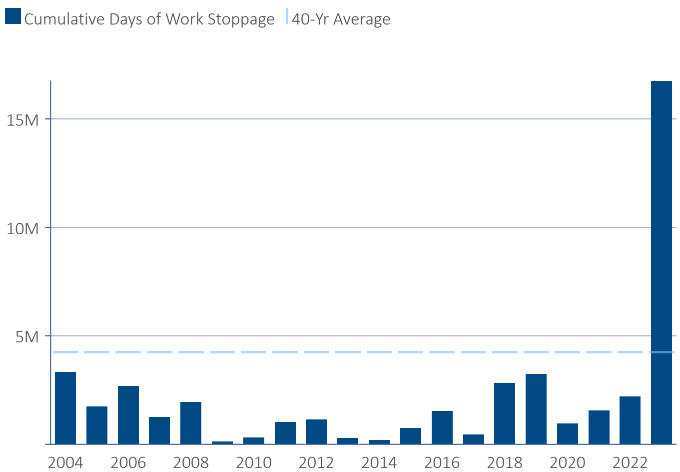


Real GDP: Actual vs Forecasts (Dec '22)

Source: U.S. Bureau of Economic Analysis, as of December 27, 2023

Chart 9:

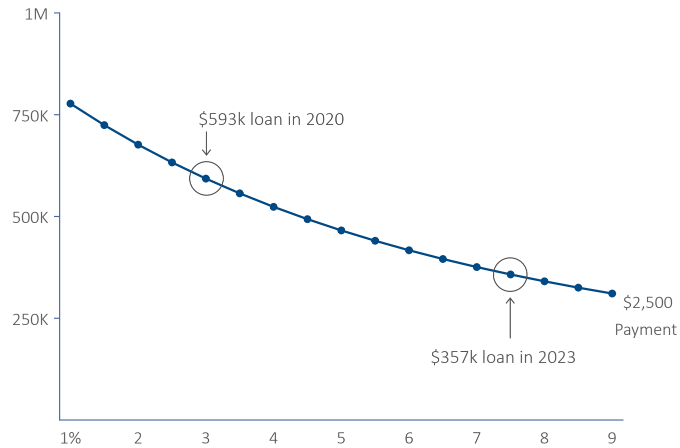
A Laborious 2023 – A 40-year high in union strikes



Source: U.S. Bureau of Labor Statistics, YTD through 11/30/2023

Chart 10:

Interest rates are crushing home affordability

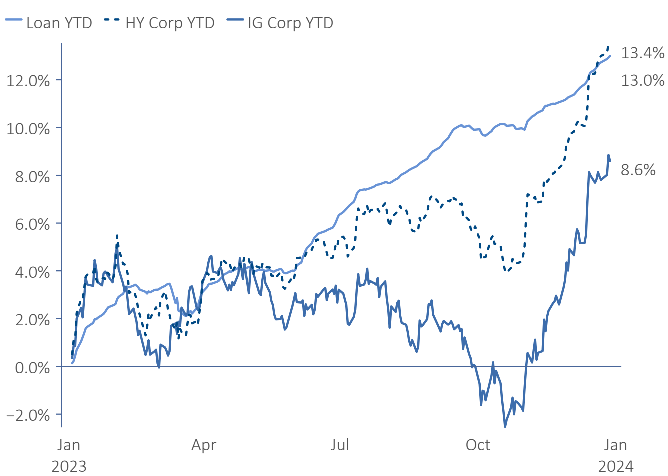


Mortgage a borrower can afford, by monthly budget and 30yr fixed rate.

Source: Redfin, as of December 27, 2023

Chart 11:

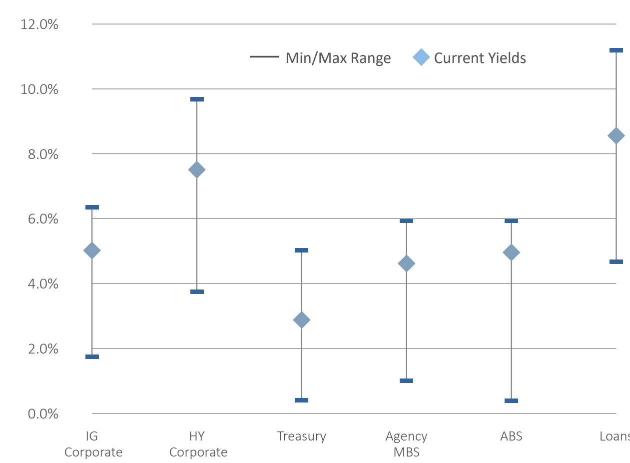
Corporate credit shines – returns through 12/27/23



Source: Bloomberg, Credit Suisse, as of December 27, 2023

Chart 12:

Yields remain historically attractive



10-year yield history

Source: Bloomberg, Credit Suisse as of December 27, 2023

Both headline and core Consumer Price Index (CPI) measurements showed signs of cooling as the year progressed. Notable is the relevance of shelter within CPI's weighting – as it remains stubbornly high. While the impact of elevated shelter inflation has a more limited downstream impact, contained to the roughly 35% of renting Americans, these are often the most vulnerable to effects of inflation. Housing affordability reached its lowest point in recent history, driven by record low housing supply and soaring mortgage rates. Despite these challenges, consumer resilience was significant. Americans continued to fuel GDP growth through their spending, navigating rising costs, a slowing labor market, dwindling savings, and costly access to credit. This enduring consumer spending behavior, along with labor market trends, will likely garner significant attention in the coming year.

Looking to 2024, we expect next year's roadmap to be shaped by the intricate blend of economic data, consumer resilience, and central bank policies. We further anticipate additional economic softening, influenced by high interest rates.

In light of our considerations, we see a strong argument for fixed income investments. Highlighted are elevated starting yields seen in many asset classes as well as the potential impact of rate cuts in 2024. With expectations for only a mild economic slowdown, the yield pickup offered in liquid credit asset classes remains attractive. Reinforcing our stance from last year, we believe the substantial carry in corporate credit offers a buffer against potential market volatility and presents opportunities for total returns. As we move into the new year, we extend our wishes to all for a safe, happy, and healthy year ahead.

Aristotle Pacific Capital
December 2023

ABOUT ARISTOTLE PACIFIC CAPITAL

Aristotle Pacific Capital, LLC specializes in institutional fixed income management with a focus on corporate credit. As of November 30, 2023 the firm managed $23bn across bank loan, high yield, corporate, and CLO strategies.

IMPORTANT NOTES AND DISCLOSURES

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