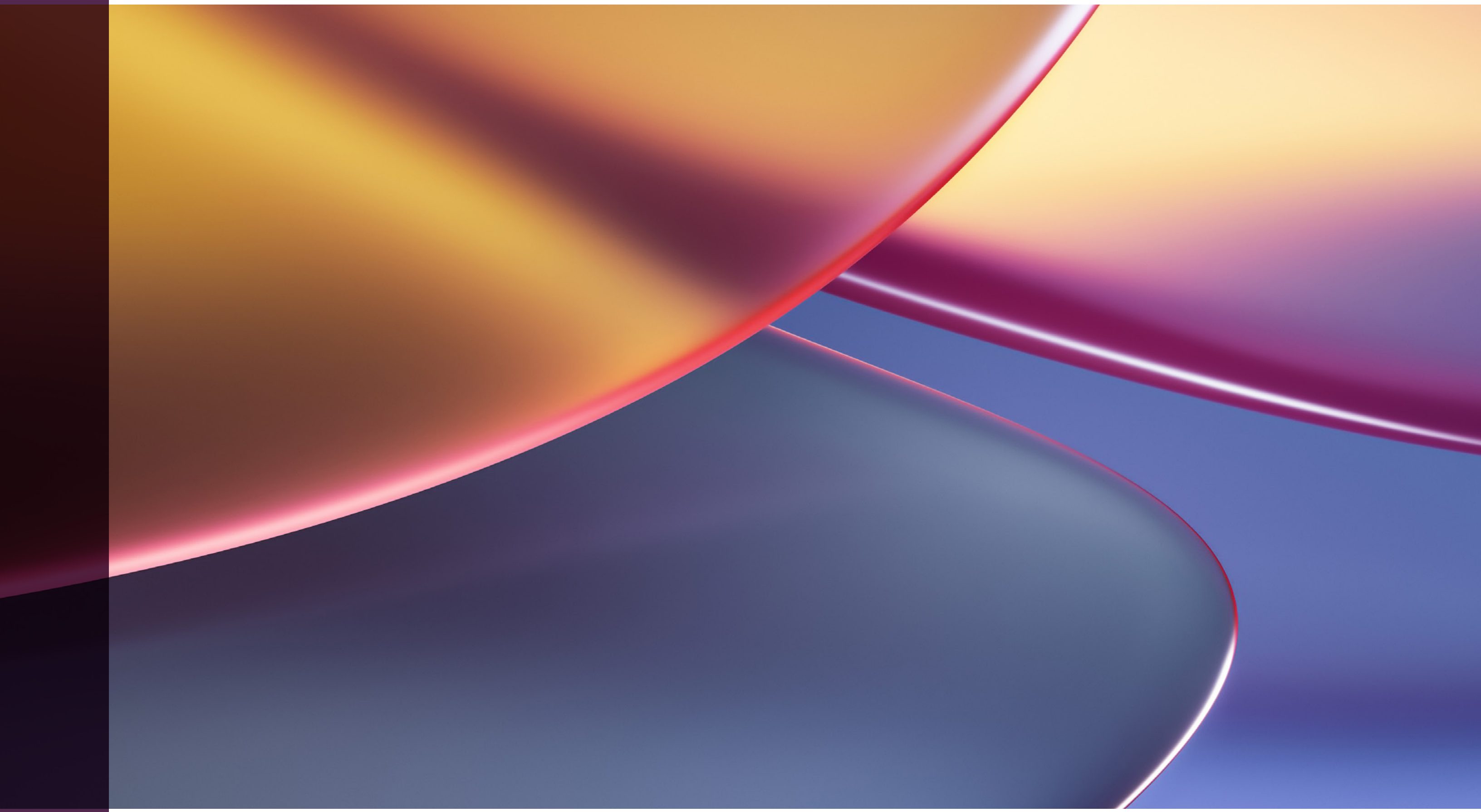
GUGGENHEIM

Third Quarter 2024

Fixed-Income Sector Views



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Portfolio Management Outlook

Preparing for Expected Rate Cuts

Higher quality fixed income has outperformed in previous easing cycles.

Our baseline economic outlook, which helps set the roadmap for our long-term investment strategy, is for a gradual slowdown in U.S. growth as fiscal support fades and a cooling labor market pressures incomes and consumer spending. That said, risks to our growth outlook are weighted to the downside. Our views on the labor market were confirmed by the miss in the July jobs report, which went on to spook global markets. Not surprisingly, one of the common themes from our sector teams in this issue is that rate cuts starting in September have already been discounted by the fixed-income market, but views on how much and how many are still evolving. We continue to expect volatility, particularly around data related to the health of the consumer and economy.

In general, our view is that yields across fixed income remain high and attractive, particularly relative to post-global financial crisis (GFC) norms. Credit fundamentals are healthy overall, but more mixed in lower quality, and we expect to see further dispersion as the economy slows.

Our credit and risk position is driven by fundamentals and relative value. We are prioritizing high carry, shorter duration instruments in areas including non-Agency Residential Mortgage-Backed Securities (RMBS), senior Collateralized Loan Obligation (CLO) tranches, commercial Asset-Backed Securities (ABS), and BB-rated corporate bonds. After the July jobs report there has been some spread movement as the Treasury curve resets lower and flatter, but our expectation is that spreads will remain relatively rangebound. Spreads in high grade sectors are tighter than recent wides, but they remain cheap relative to fundamental risk, particularly in structured credit. We have been maintaining some dry powder for taking advantage of opportunities that may arise and targeting an average level of credit beta.

From a duration perspective, the yield curve has bull flattened in July and into August, and is likely on its way to a steepening once rate cuts begin. In this environment, we prefer to express duration using Agency RMBS, given wide spreads and improved convexity profile, with a marginal bias towards the belly of the curve given its historical outperformance during easing cycles.

As the Federal Reserve (Fed) comes to the end of the pause phase of the cycle and starts easing, historical data show that higher quality fixed income has outperformed money markets and riskier assets like stocks. Investors considering when to reallocate into bonds will also want to consider technical factors that could affect the timing of such a move, including getting ahead of possible outflows from money market instruments and taking advantage of low dollar prices available in the market.

By Anne Walsh, Steve Brown, Adam Bloch, and Evan Serdensky

Macroeconomic Update

Fed Needs to Act to Prevent Normalization Turning into a Downturn

Signs are growing that the Fed is behind the curve.

The U.S. has returned to conditions that look more like "normal." The overheated labor market of 2021–2023 has seen demand for workers cool alongside expansion of available labor supply, causing the unemployment rate to drift upward from 3.4 percent to 4.3 percent over the past year and a half. Fed officials now describe the labor market as in "rough balance" and back to conditions seen before the pandemic.

Meanwhile, substantial progress has been made in bringing inflation back down to the Fed's 2 percent target. Following a hot first quarter, recent months have seen renewed progress in the inflation fight, bringing core personal consumption expenditures (PCE) inflation down to 2.6 percent in year-over-year terms and 2.3 percent annualized in the three months through June. This inflation progress looks to be durable for two key reasons: First is the rebalanced labor market and associated cooling in wage growth. Second is the slowdown underway in shelter inflation, which has been the biggest contributor to above target inflation but which finally saw a long-awaited slowdown in the June inflation data. Leading indicators of rent inflation, particularly prices for newly signed leases, suggest this slowdown should stick and help inflation remain low for at least the next few quarters.

With the economy getting back to normal, the Fed should soon follow suit with its rate policy. Fed officials are increasingly acknowledging that if they wait too long to bring interest rates down, they risk turning this normalization into more of a slowdown, or even recession. The July employment report seemed to validate those fears just days after the Fed decided to hold rates steady at the July meeting, with the unemployment rate rising 20 basis points and job growth outside healthcare and government up just 33,000. Compounding downside risks, recession fears, questions around AI, and foreign spillovers have highlighted vulnerability to an equity-led tightening in financial conditions.

The emergence of these downside risks, which we have previously flagged, raises the risk that the normalization the Fed has been seeking turns into a slowdown, or even recession. We expect the Fed will respond by cutting rates faster than previously expected, with at least three 25 basis point rate cuts this year, and the potential for larger cuts if the labor market data continues to weaken. More importantly, we see downside risk to the terminal fed funds rate from what is priced into the market, which is conditional on a soft landing. Easing cycles are usually faster than tightening cycles, and this tightening cycle was historically fast. There is risk around market expectations of a ladder step easing.

By Matt Bush and Maria Giraldo

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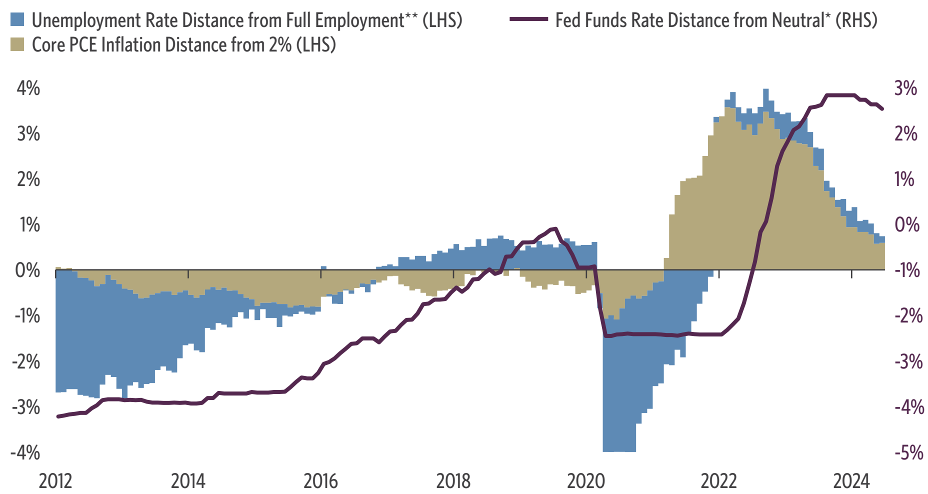
Rebalanced Labor Market and Falling Inflation Should Lead to Fed Rate Cuts



Source: Guggenheim Investments, Haver Analytics. Data as of 6.30.2024. *Neutral is FOMC Median Longer Run estimate in the Summary of Economic Projections. ** Full Employment is FOMC median Longer run estimate.

Rates

Positioning for the Next Phase of Fed Policy

Economic data are finally starting to align with the Fed's targets.

In the upcoming months, the Fed will likely enter an easing cycle as inflation comes down and the labor market softens. Meanwhile, the Congressional Budget Office (CBO) is projecting an increase in fiscal deficits by $400 billion to $1.9 trillion in 2024, which will lead to an uptick in Treasury issuance. The confluence of lower short-term rates and additional reliance on coupon Treasurys to fund the deficit will likely cause the yield curve to steepen, as we expected.

Sector Commentary

- Economic data continue to be generally robust. However, employment and inflation have begun to moderate, opening the door for the Fed to ease policy if the trend continues, as we expect in September.
- Changing market expectations around the depth of the easing cycle have led to an uptick in volatility, which we expect to continue.
- When the Fed begins to cut interest rates, money market fund investors will likely extend duration, which would support Treasury market demand.
- As Treasury issuance continues to remain high for the foreseeable future to fund fiscal deficits, we expect investment funds to continue to be the largest buyers in primary Treasury auctions.

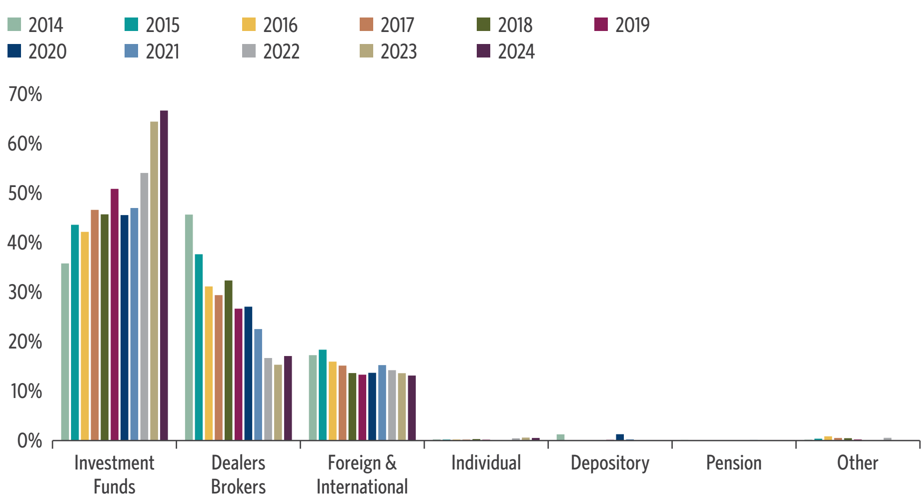
Investment Themes

- The projected increase in the 2024 fiscal deficit should result in increased Treasury coupon issuance needs in future quarterly refunding announcements.
- Our macro view continues to support a steeper yield curve in the medium term. However, the carry in steepening trades remains punitive, and we continue to look for ways to position portfolios for steepening exposure while minimizing the negative carry.
- Elevated real yields in the short end of the Treasury curve and breakeven rates that are generally inside of 2.25 percent continue to make shorter maturity Treasury Inflation-Protected Securities (TIPS) look attractive while enabling investors to position for on-going inflation, albeit at a slowing pace.

By Kris Dorr and Tad Nygren

As Treasury issuance continues to remain high for the foreseeable future to fund fiscal deficits, we expect investment funds to continue to be the largest buyers in primary Treasury auctions.

Investment Funds Should Remain the Largest Buyers in Primary Treasury Auctions



Source: Guggenheim Investments, Bloomberg. Data as of 6.30.2024.

Investment-Grade Corporate Bonds

Focus on Liquid, Higher Quality Bonds

We expect spreads to widen from here.

In the first half of the year, tight spreads were offset by historically attractive all-in yields. However, the average yield on the Bloomberg U.S. Investment-Grade Corporate Bond Index for the trailing-two years is now 5.4 percent vs 5.2 percent as of Aug. 8, 2024, thus becoming less attractive all in. That said, with recent spread widening, spreads make up a larger portion of the total yield and are closer to long-term medians. Looking forward, we expect spreads to stay range bound or drift wider as a result of weakening growth. In this changing environment, focus on credit risk premium will be increasingly important.

Sector Commentary

- Complacency remains high given positive ratings, higher quality index composition, and favorable primary market dynamics.
- In the first half of 2024, $448 billion of investment-grade bonds were upgraded vs. $88 billion downgraded, with most of those downgrades remaining investment grade.
- Index composition continues to improve, with the share of BBB- bonds falling to 9.8 percent, an eight-year low. Meanwhile, the share of A-rated debt has increased to 45.3 percent, the highest level since 2011. We expect the upgrade/downgrade ratio, currently at a 15-year high, to start to normalize in the second half.
- The $860 billion in first half gross primary issuance represents the second largest first-half issuance ever. However, we expect second half issuance to be tamer on a gross and net basis with nearly $400 million in maturities coming due and $200 billion in coupon payments to bondholders.

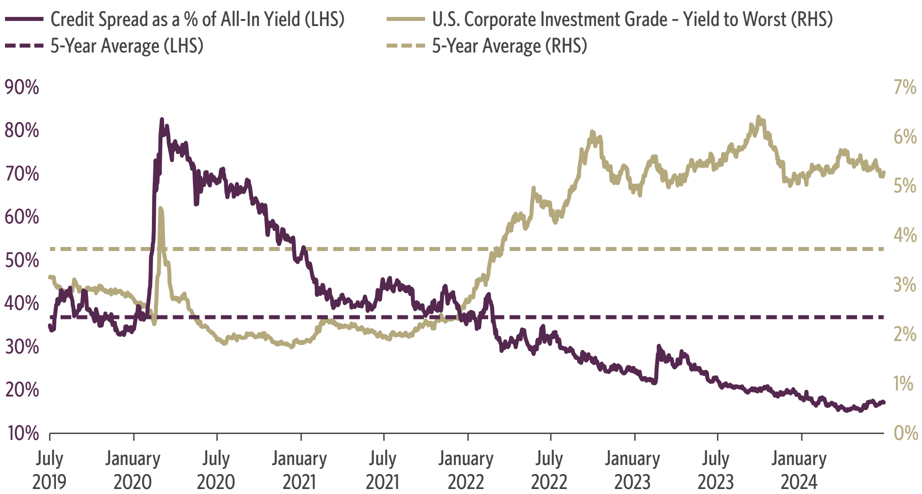
Investment Themes

- We continue to favor banks over industrials as sufficient capital positions and positive regulatory stress test results alleviated concern around the need for increased funding in the near term.
- We see the current environment as an opportunity to rotate into high current dividend/coupon preferred and hybrid securities while reducing exposure to short-dated call structures trading at or near par.
- Credit curves steepened during the second quarter but investors matching longer liabilities may find value in adding exposure as the rate curve bear steepened, adding incremental yield to 20+ year corporate securities.
- Our compression trade of BBB vs A-rated corporates performed well in the first half. Our focus in the third quarter is on more liquid, higher quality securities, which historically perform well in spread widening environments.

By Justin Takata

The average yield on the Bloomberg U.S. Investment-Grade Corporate Bond Index for the trailing-two years is now 5.4 percent vs 5.2 percent as of Aug. 8, thus becoming less attractive all in. That said, with recent spread widening, spreads make up a larger portion of the total yield and are closer to long-term medians.

All-In Yields Are Becoming Less Attractive, Although Spreads Have Recently Widened



Source: Guggenheim Investments, Bloomberg. Data as of 7.19.2024.

High Yield Corporate Bonds

Selectively Constructive on High Yield

High yield bonds remain compelling despite tight spreads.

Despite election volatility starting to impact rate and equity markets, high yield spreads had stayed within a narrow range until the recent selloff induced by the nonfarm payroll miss and broader worries about economic trajectory. Looking forward, limited net supply will likely continue to support the broader market but economic uncertainty could increase dispersion across sectors and issuers. Our focus remains on higher quality credits that can weather high rates through cash flow stability and healthy margins.

Sector Commentary

- High yield bond yields averaged near 8 percent in the second quarter, continuing to offer a compelling entry point despite tight spreads.
- Following some recent volatility in early August that led to spreads retracing to December levels, we have seen some recovery with BBs in the 18th percentile of historical levels and Bs in the 14th percentile. CCCs remain comparatively wider to their own history, in the 56th percentile, as markets remain concerned about some of the recent weakness in labor market data.
- Primary market activity is on pace to reach pre-COVID averages, with a total of $166 billion so far. Over 75 percent of issuance continues to be for refinancing, resulting in modest new paper entering the index.

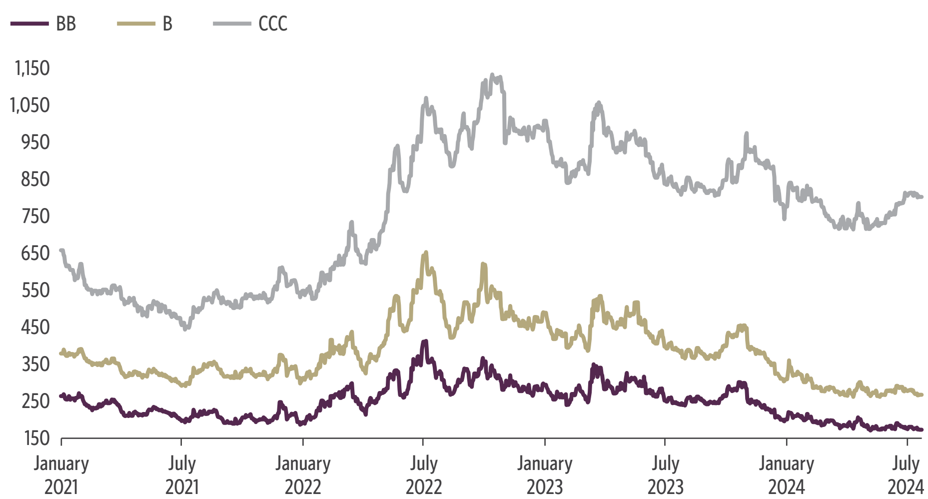
Investment Themes

- The risk of defaults in lower rated credits requires a selective approach. The CCC-rated par-weighted default rate over the last 12 months has been 12 percent, according to BofA Merrill Lynch Research, compared to no defaults and a 0.3 percent default rate for BB-rated and B-rated corporates, respectively.
- Rate cuts potentially beginning in September could boost returns for the sector and improve the outlook for credits with scheduled maturities in the next two years (only 8 percent of the market).
- We prefer higher quality high yield bonds (rated B or above) due to their stronger fundamentals and lower default risk. These bonds offer a balance of attractive yields and relative safety.
- Given elevated refinancing costs, closely monitoring issuers' balance sheets and their ability to service debt is crucial. We favor companies with strong cash flows and manageable debt levels.

By Thomas Hauser and Maria Giraldo

Following some recent volatility in early August that led to spreads retracing to December levels, we have seen some recovery with BBs in the 18th percentile of historical levels and Bs in the 14th percentile. CCCs remain comparatively wider to their own history, in the 56th percentile, as markets remain concerned about some of the recent weakness in labor market data.

As BB and B Spreads Approach Three-Year Tights, CCC Spreads Hit Resistance



Source: Guggenheim Investments, Bloomberg. Data as of 7.19.2024.

Bank Loans

Credit Selection Remains Paramount

Elevated short-term rates should continue to support loan performance in the second half.

Managing through the current high interest rate environment remains the focal point for the sector. Some borrowers are only able to avoid bankruptcy through some form of debt restructuring or maturity extension. Others are reducing interest expense via repricing or refinancing. Eventually, rate cuts will become a debt service tailwind. Assessing credit quality remains dependent on a qualified judgement of idiosyncratic situations, but with loans still paying 9 percent yields, we believe the market offers attractive opportunities for investors focused on quality.

Sector Commentary

- The three-year discount margin on the Credit Suisse Leveraged Index ended the second quarter at 495 basis points with the yield around 9.4 percent.
- Loans have delivered strong performance year to date, with a second quarter return of 1.9 percent and first half return of 4.4 percent. Leveraged loans continue to outpace fixed-rate corporates this year due to their high all-in coupons and lack of duration, and we see coupons continuing to support performance.
- Almost 60 percent of loans were trading above par during the second quarter, but by quarter end that number had declined to 40 percent due to elevated repricing activity. Loan valuations remain near their 40th percentile of historical levels since 1994.
- Issuers have repriced or extended $625 billion of loans, or 45 percent of the total loan market outstanding, allowing borrowers to reduce interest burdens and extend maturities.

Investment Themes

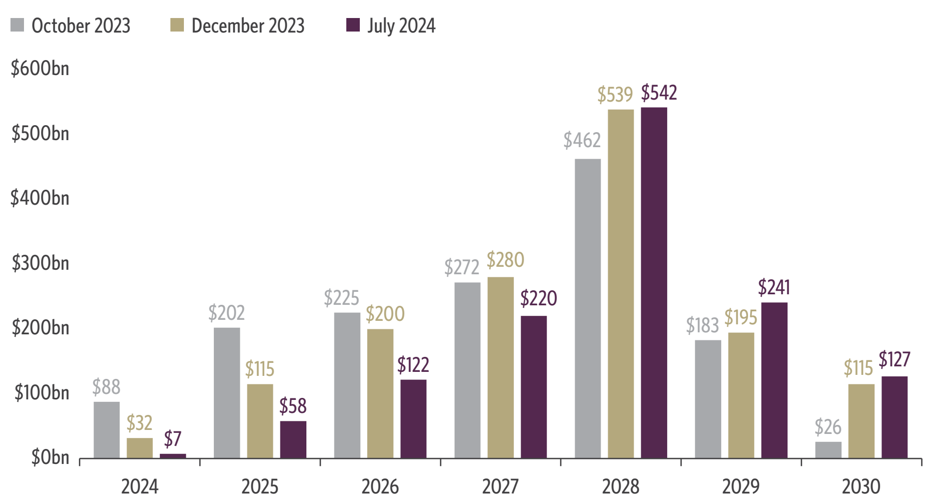
- The weighted average nominal spread of the index is down 12 basis points to 386 basis points, amounting to nearly $2 billion of annual interest savings for issuers.
- Only $65 billion, or 5 percent of term loans outstanding, are maturing through 2025, limiting default risk.
- The pace of interest and payment defaults has plateaued, indicated by the gradual decrease in the Morningstar LSTA Leveraged Loan default rate from 2 percent at year-end 2023 to 1.6 percent currently. However, we continue to see liability management transactions to stave off actual defaults, so if we include distressed exchanges the default rate would be notably higher at 4.3 percent.
- We remain cautious over the tail risk in loans given the impact of high rates on interest costs and expect loan recoveries to remain lower due to weaker loan documentation.

By Christopher Keywork and Maria Giraldo

Only $65 billion of loans, or 5 percent of USD-denominated term loans outstanding, are maturing through year-end 2025, representing limited default risk driven by missed principal repayment.

Less than 5% of the Loan Market Is Scheduled to Mature Before 2026

USD Loans Maturity Schedule by Year, as of Varying Calendar Dates



Source: Guggenheim Investments, Bloomberg. Data as of 7.22.2024. Based on all USD term loans outstanding, and therefore includes loans that may not be index eligible.

Municipal Bonds

Light Supply Meets Steady Demand

Strong summer technicals should provide support.

Both tax-exempt and taxable municipal bonds continue to experience supportive market conditions. Reinvestment demand from large principal and coupon payments provides a tailwind to tax exempt valuations. Taxable spreads have inched tighter on the back of lackluster supply. Credit quality is plateauing as tax receipts flatten while certain states continue to enact tax cuts.

Sector Commentary

- Tax exempts continue to perform well despite the headwinds of heavy issuance and volatile Treasury rates. Tax exempt/Treasury yield ratios are essentially unchanged over the last 12 months, with 5/10/30-year AAA ratios hovering around 67 percent, 68 percent, and 86 percent, respectively.
- We are in the midst of the two biggest months of the year for principal and interest (P&I) payments, averaging $64 billion per month during July and August. Heavy reinvestment demand from P&I flows should provide a strong technical tailwind for the summer months.
- Taxable issuance remains light, down 16 percent year over year to just $21 billion, while demand from institutions remains steady.

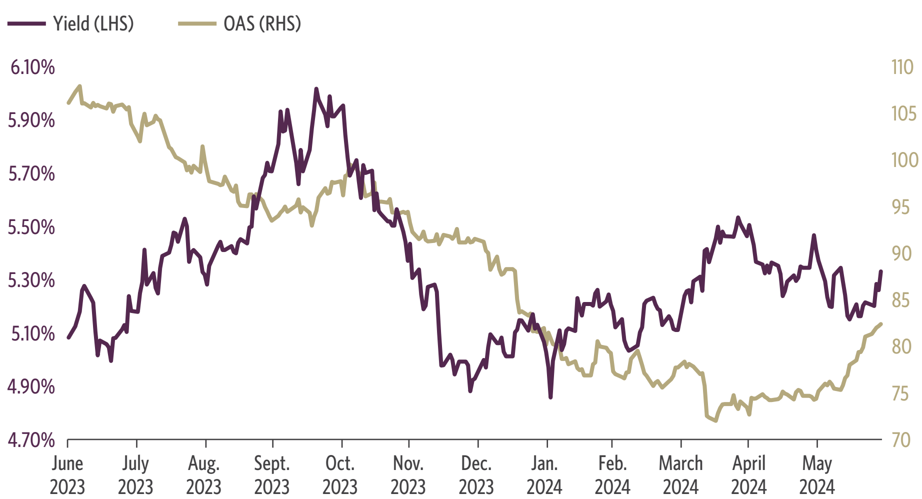
Investment Themes

- At current ratios and spreads, we prefer taxables over tax exempts for institutional investors due to their low tax rates.
- For retail investors, the taxable equivalent yields on tax exempts remain attractive, and the strong summer technicals should provide support at current valuation levels into late third quarter.
- Despite flat to declining tax receipts for most states, some are still enacting cuts to tax rates. Since 2021, 26 states have reduced income tax rates, so we think tax receipts will have a difficult time outperforming overall economic growth. Given the concurrent drawdown of stimulus funds, we are keeping an eye on how states budget for the upcoming fiscal year 2025 and whether they are using realistic assumptions for revenue and expenditure growth.

By Allen Li and Michael Park

Taxable issuance remains light, down 16 percent year over year to just $21 billion, while demand from institutions remains steady. At current ratios and spreads, we prefer taxables over tax exempts for institutional investors due to their low tax rates.

Taxable Muni Spreads Have Inched Tighter, But Remain Attractive



Source: Guggenheim Investments, Bloomberg. Data as of 6.30.2024.

Asset-Backed Securities and CLOs

Record Issuance Meets Investor Demand

ABS and CLOs continue to offer attractive opportunities.

While ABS continue to offer excess yield relative to similarly rated corporate bonds, this spread is compressing. The spread has supported ABS issuance, which is on track to outpace 2023 levels for the year. Meanwhile, both middle market (MM) and broadly syndicated loan (BSL) CLOs offer attractive absolute yields and compelling relative value. New issuance has been at near record levels, and we have seen an increase in refinance and reset activity as spreads have tightened.

Sector Commentary

- **ABS:** The credit spread difference between ratings matched ABS and corporate bonds currently ranks at its 60th percentile, suggesting moderately attractive relative value for commercial sectors. New issuance has been biased toward whole business securitizations and high growth sectors such as fiber networks.
- **CLOs:** Robust issuance has been met with strong investor demand, leading to spread tightening. As spreads tightened, refinance and reset activity has increased, which we expect to continue for the remainder of the year.

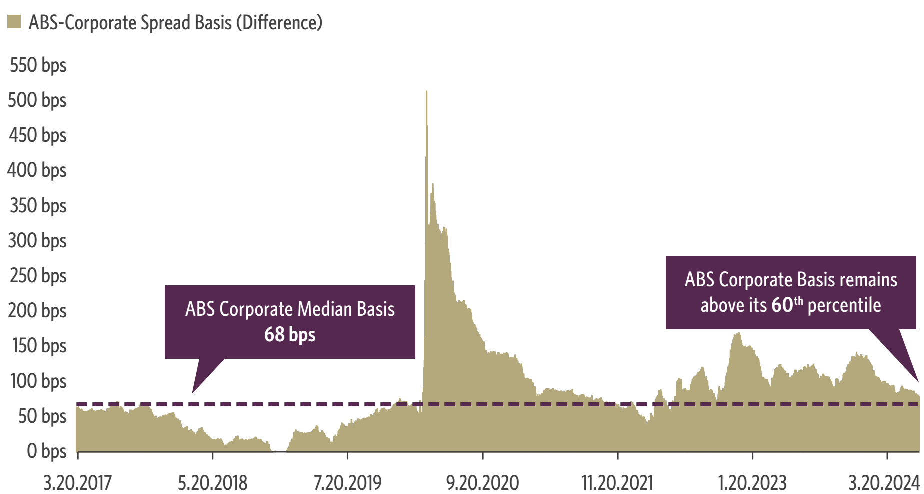
Investment Themes

- **ABS:** We favor senior exposures in longer duration commercial ABS backed by high quality collateral, such as franchise royalties, fiber networks, and maritime containers for their stable credit profile and relative value compared to investment-grade corporate credit. Additionally, selected senior tranches in consumer ABS also provide attractive relative value.
- **CLOs:** A-rated to AAA-rated tranches offer attractive relative and absolute value with low levels of credit risk. We prefer new issue deals as the secondary market has seen senior CLO tranches trade tight relative to the primary market, and most senior tranches trade above par dollar prices. The spread pickup for AAA MM versus BSL CLO tranches is currently at 25 basis points, compared to a historical average of 45 basis points. Thus, while MM CLOs offer attractive carry, the relative value has shifted in favor of BSL CLOs.

By Michael Liu, Scott Kanouse, and Pooja Shendure

The credit spread difference between ratings matched ABS and corporate bonds currently ranks at its 60th percentile, suggesting moderately attractive relative value for commercial sectors.

Commercial ABS Spreads Remain Attractive vs. Similarly Rated Corporates



Source: Guggenheim Investments. Data as of 6.30.2024. Indexes represented include ICE BofA AA-BBB ABS Index and Bloomberg U.S. Investment-Grade Corporate Bond Index.

Opportunities in non-Agency RMBS Subsectors

Closed-End Second (CES) lien and Home Equity Lines of Credit (HELOC) transactions offer attractive valuations relative to their credit risks.

Positive credit fundamentals and technical tailwinds reinforce our favorable view of the non-Agency RMBS sector. Built-up home equity, the supply/demand imbalance for housing, and improved consumer credit provide a positive backdrop for mortgage credit performance. Despite increased new issue volume relative to 2023, RMBS valuations should benefit from limited supply due to low home sales activity and the effect of homeowners locking in historically low interest-rate mortgages.

Sector Commentary

- Housing market fundamentals continue to benefit from limited supply. The April Case-Shiller Index reading showed year-over-year growth in home prices of 6.3 percent. Combined with a resilient labor market, these conditions lay the foundation for stable mortgage credit performance.
- While new issue volume is 50 percent higher year over year versus the same period in 2023, overall issuance for 2024 is forecasted to be near the lowest level since 2017.
- Areas for growth for Non-Agency RMBS have been the CES and HELOC subsectors. These products allow consumers to tap the record levels of built-up home equity. However, this subsector represents only 10 percent of this year's volume and is unlikely to significantly affect new issue levels for 2024. Consequently, spread movement is expected to follow the movement in the larger Agency market.

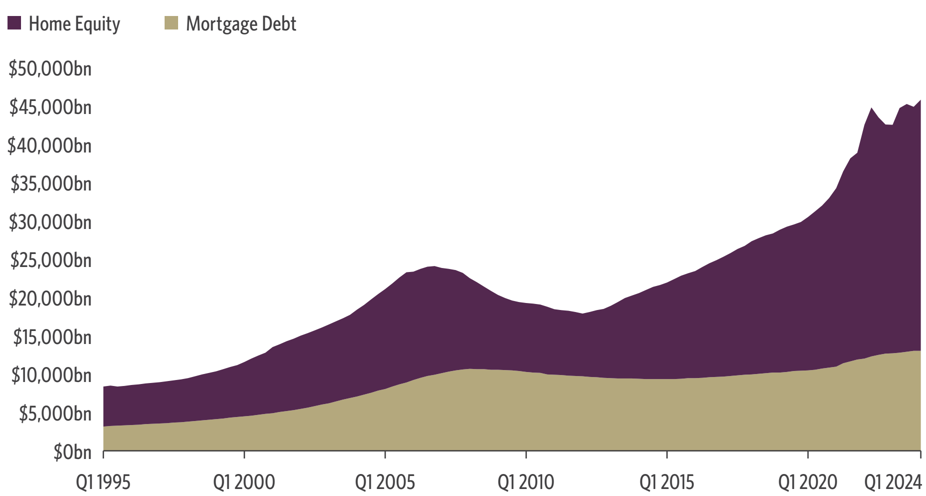
Investment Themes

- We favor transactions with structures that limit extension risk and can withstand deterioration of credit performance from severe economic conditions. Such opportunities include investment-grade securities from non-qualified mortgage (non-QM) transactions and senior securities from CES lien and HELOC transactions, which offer attractive valuations relative to their credit risks.

By Karthik Narayanan and Roy Park

Areas for growth for Non-Agency RMBS have been the CES and HELOC subsectors. Senior securities from CES lien and HELOC transactions offer attractive valuations relative to their credit risks.

Rising Home Equity Creates a Growth Opportunity for CES Loans and HELOCs in the Non-Agency RMBS Sector



Source: Guggenheim Investments, Bloomberg, and Federal Reserve. Data as of March 2024.

Commercial Mortgage-Backed Securities

Not a Lot of Bright Spots

Avoiding office properties and staying senior in structure.

AAA-rated conduit Commercial Mortgage-Backed Securities (CMBS) bond prices decreased by 0.5–2.0 percent quarter over quarter while BBB-rated conduit CMBS prices increased by 2 percent or more. We attribute this credit curve flattening dynamic to technical factors rather than credit fundamentals. CMBS supply continues to underwhelm investor demand given strong annuity and fund flows, causing investors to pay up to source bonds, especially higher-yielding bonds. We remain selective in CMBS as markets offer limited return for elevated risk in many cases.

Sector Commentary

- Approximately $50 billion in CMBS was issued in the first half, compared to $20 billion for the same period in 2023, powered by higher investor demand for yield products, especially credit-enhanced structured products.
- Over $30 billion of CMBS issuance has been in single asset/single borrower (SASB) transactions financing specific, well-performing properties, especially industrial, lodging, and multifamily properties.
- Legacy CMBS loans backed by over levered or underperforming properties—especially offices—struggle to refinance. Just 63 percent of conduit CMBS loans were refinanced on time, meaning over one-third of loans scheduled to repay this year are in some state of extension, modification, or other workout.
- Performance issues, including continued deterioration in demand for office space, will continue to weigh on Commercial Real Estate performance in coming months and expose CMBS to heightened risk.

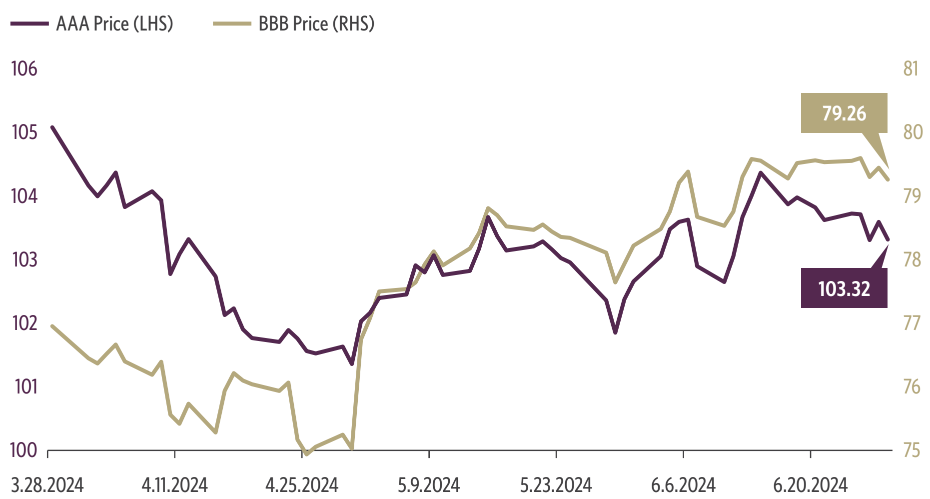
Investment Themes

- Broadly, we maintain a relatively low exposure to the sector.
- In CMBS, we maintain a preference for senior securities with higher credit enhancement, capable sponsorship, and limited office exposure.
- Select SASB transactions and CRE CLOs continue to offer the potential for attractive risk-adjusted returns.
- Conversely, we continue to find that most mezzanine and junior bonds across CMBS subsectors fail to appropriately compensate investors at current levels.

By Tom Nash and Hongli Yang

AAA-rated conduit CMBS bond prices decreased by 0.5–2.0 percent quarter over quarter while BBB-rated conduit CMBS prices increased by 2 percent or more. We attribute this credit curve flattening dynamic to technical factors rather than credit fundamentals.

BBB Conduit CMBS Prices Rose While AAA Conduit CMBS Fell



Source: Guggenheim Investments, JP Morgan. Data as of 6.30.2024.

Agency Mortgage-Backed Securities

Carry Is King in Agency MBS

Par Coupon MBS generated positive excess returns due to elevated spreads.

The Bloomberg U.S. MBS Index posted flat returns relative to similar duration Treasurys over the first half of the year, trailing the Bloomberg U.S. Aggregate Index. Recent production 5.5 percent and 6 percent coupon MBS generated positive excess returns by merit of elevated spreads and thus higher all-in yields, while interest rates and mortgage spreads were rangebound. Outperformance vs. corporates was pronounced in the recent selloff. Once the Fed begins to ease and the election cycle is behind us, we expect relative outperformance of recent production coupons to continue as interest rate volatility normalizes.

Sector Commentary

- The Bloomberg U.S. MBS Index outperformed duration matched U.S. Treasurys in May and June as inflation data cooled off and the uncertainty over the direction of Fed's next move has diminished.
- Rangebound rates and a benign prepay environment have favored income over price appreciation. Production coupons have offered the widest spreads and highest yields. In addition, in certain to be announced (TBA) market subsectors such as Ginnie Mae and 15-year MBS, favorable financing rates via the dollar roll market further boost total returns.
- For those with a slightly bullish rates view, it makes sense to move some exposure down into $95–$100 priced bonds. This gives up some carry but greatly reduces prepayment risk in a moderate rate rally.

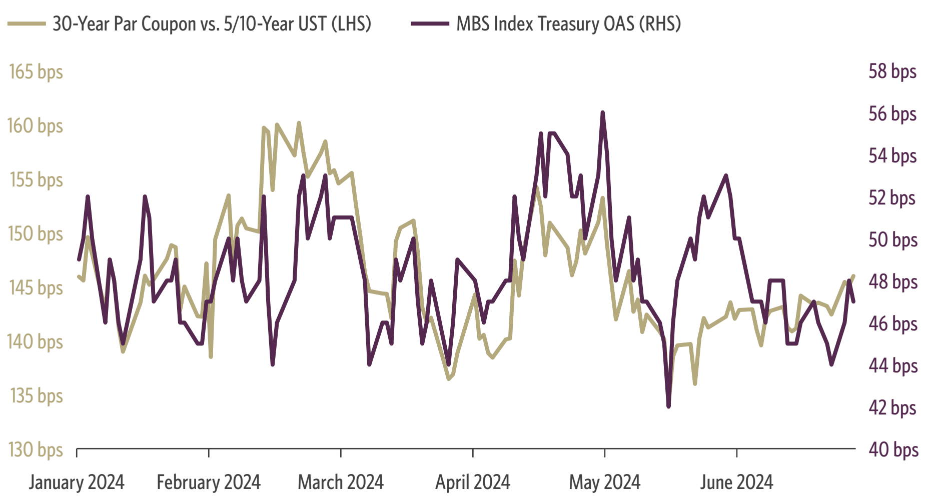
Investment Themes

- The MBS market has become bifurcated into lower index coupons and higher production coupons, which offer the potential for increased returns at the expense of a worse convexity profile. At historically low convexity levels, the index continues to present a favorable duration alternative, while production coupons remain an expression of short interest rate volatility.
- Agency CMBS performance remains steady and spreads are at year-to-date tights, especially in the longer duration segments where supply is minimal and asset swappers focusing on Secured Overnight Financing Rate (SOFR) spreads have inverted the sector spread curve. As a result, we continue to prefer structured cashflows in the single family space over multifamily for any longer duration targets.

By Louis Pacilio

Rangebound rates and a benign prepay environment have favored income over price appreciation. Production coupons have offered the widest spreads and highest yields.

Rangebound Mortgage Spreads Favor Positioning in Higher Carry Bonds



Source: Guggenheim Investments, Bloomberg. Data as of 6.30.2024.

Commercial Real Estate

Commercial Real Estate May Be Nearing a Trough

After two years of falling prices, values begin to stabilize.

Real estate markets have been volatile for the last 18 months. According to MSCI, the volume of transactions for all property types dropped materially, creating price instability. We believe prices for most properties are nearing a trough and that fundamentals for commercial real estate support income and price growth as we move into 2025. Office properties, however, continue to struggle with a pandemic hangover and can expect to see significant price pressure for years to come.

Sector Commentary

- Industrial property, having seen price appreciation following the pandemic, limited price declines over 2023, and a return of price growth in 2024, remains the bright spot for investors.
- Apartments saw greater price declines in the last two years, but values remain much higher than before the pandemic.
- Hotels continue to rebound from their pandemic stress and have seen positive momentum in 2024. Due to limited supply and high demand, neighborhood retail prices have seen limited volatility and have been trending up in 2024.
- Offices and malls continue to see sharp price declines. Investors are evaluating prospects to redevelop these properties for other uses, but conversion costs are high, and some properties may be functionally obsolete.

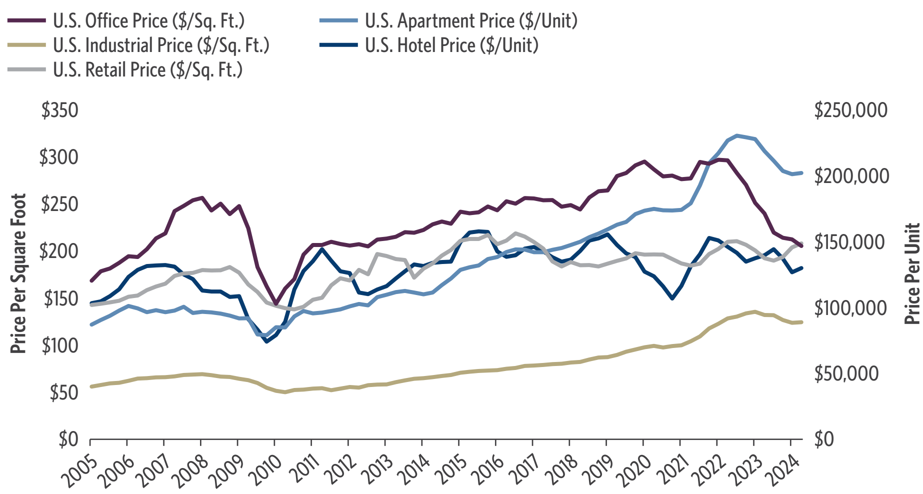
Investment Themes

- Putting offices and malls to the side, we do not believe real estate prices will fall as much as they did during the GFC.
- We see values stabilizing through 2024 and prices starting to rebound into 2025. Post-pandemic shifts toward re-shoring and near-shoring, the increasing demand for power and technology infrastructure, and the migration of people and business will create demand for real assets.
- Expectations of lower interest rates will alleviate the pressure on values, reduce carry costs, spur more transactions, and create a more stable market than we saw in 2023 and the first half of 2024.
- High construction, labor, insurance, and other operating costs are limiting new construction starts for all property types at a time when vacancies are low, and demand is increasing. This lack of new supply makes existing properties more attractive given the high costs of developing competing sites.

By Jennifer A. Marler and Karen Karwoski

We see values stabilizing through 2024 and prices starting to rebound into 2025. Post-pandemic shifts toward re-shoring and near-shoring, the increasing demand for power and technology infrastructure, and the migration of people and business will create demand for real assets.

Commercial Real Estate Prices Steadily Declined Through the First Half of 2024



Source: Guggenheim Investments, Real Capital Analytics. Data as of 6.30.2024.

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S&P bond ratings are measured on a scale that ranges from **AAA** (highest) to **D** (lowest). Bonds rated **BBB-** and above are considered investment-grade while bonds rated **BB+** and below are considered speculative grade.

One **basis point** is equal to 0.01 percent. Likewise, 100 basis points equals 1 percent. **Beta** is a statistical measure of volatility relative to the overall market. A positive beta indicates movement in the same direction as the market, while a negative beta indicates movement inverse to the market. Beta for the market is generally considered to be 1. A beta above 1 and below -1 indicates more volatility than the market. A beta between 1 to -1 indicates less volatility than the market. **Carry** is the difference between the cost of financing an asset and the interest received on that asset. **Dry powder** refers to highly liquid assets, such as cash or money market instruments, that can be invested when more attractive investment opportunities arise. Duration is a measure of sensitivity of a price of a bond to a change in interest rates. In general, the higher the duration, the more the bond's price will change with interest rate movements.

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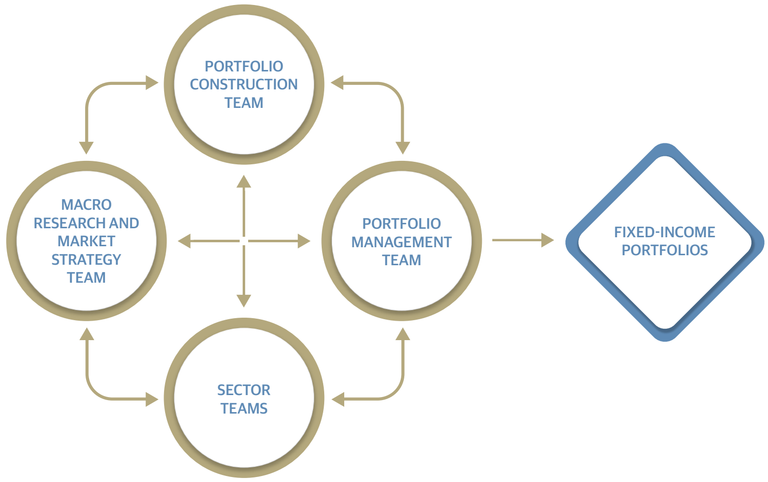

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Guggenheim Investments is the global asset management and investment advisory division of Guggenheim Partners, with more than $235 billion[1] in total assets across fixed income, equity, and alternative strategies. We focus on the return and risk needs of insurance companies, corporate and public pension funds, sovereign wealth funds, endowments and foundations, consultants, wealth managers, and high-net-worth investors. Our 235+ investment professionals perform rigorous research to understand market trends and identify undervalued opportunities in areas that are often complex and underfollowed. This approach to investment management has enabled us to deliver innovative strategies providing diversification opportunities and attractive long-term results.

Guggenheim Partners

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