Voya Limited Maturity Bond Portfolio

Focus on short-duration, US investment grade credit

Strategy overview

The Short Duration High Quality strategy seeks to outperform over a full market cycle via a broadly diversified portfolio, with a focus on risk-adjusted returns, emphasizing opportunities across the full range of US investment grade corporate bonds while maintaining a short duration profile.

Key takeaways

- The first quarter of 2025 was marked by volatility in fixed income markets, primarily driven by tariff policies and associated economic uncertainty. Despite robust job gains and a low unemployment rate, fixed income spreads widened, leading to broadly negative excess returns.
- For the quarter, the Strategy outperformed its benchmark, the Bloomberg Gov/Credit 1-3 yr Index on a gross- and net-of-fees basis. Sector allocation decisions contributed, security selection decisions detracted, while duration and yield curve positions had minimal impact.
- While spreads have widened, the macro-outlook has clearly weakened. As a result, the overall risk profile of the portfolio has changed only marginally.

Portfolio review

The first quarter of 2025 was marked by volatility in the fixed income markets, primarily driven by tariff policies and associated economic uncertainty. Despite robust job gains and a low unemployment rate, fixed income spreads widened, leading to broadly negative excess returns.

The labor market remained strong, with job gains averaging around 200,000 per month and an unemployment rate only slightly above 4%. However, tariff policies were the primary driver of market moves. President Trump announced tariffs on Mexico, Canada and China at his inauguration, with tariffs on China going into effect on February 1. Tariffs on Mexico and Canada were delayed until March 4, and additional tariffs on China were imposed on the same day. The uncertainty surrounding these tariffs, along with the potential for an escalating trade war, negatively impacted risk assets, with credit spreads finishing the quarter wider, despite solid labor market dynamics. Similarly, rates fell during the quarter in response to lower growth expectations, which helped deliver positive total returns for most sectors.

The U.S. Federal Reserve maintained a cautious stance in the first quarter of 2025, resisting further interest rate cuts after having cut rates by 100 basis points in 2024. The Fed cited stronger than expected economic data, including robust job gains and a low unemployment rate, as reasons for not cutting rates further. However, in response to tariffs, the updated Summary of Economic Projections (SEP) released following the March meeting showed the median projection for growth moving lower. Meanwhile, the median projection for inflation moved higher, however there was no change to rate expectations, with the median projection still indicating one to two cuts through year end, and another two cuts in 2026.

In markets, spreads began to widen in mid-February when tariff threats intensified. Investment grade (IG) corporates and asset-backed securities (ABS) delivered negative excess returns, as did high-yield (HY) corporates, although the higher carry profile of HY helped the sector modestly outperform its IG counterpart. Agency mortgage-backed securities (MBS) experienced a roller-coaster ride, but ultimately finished the quarter flat. Premium-priced pools (coupons of 6% or higher) outperformed, while lower coupons, particularly 2.5%, performed negatively. Commercial mortgage-backed securities (CMBS) was flat at the benchmark level, but similar to HY, higher carry allowed non-agency to outperform agency, and below IG outperformed IG. Non-agency residential mortgage-backed securities (RMBS) was a notable exception, with the sector outperforming, led by Prime Jumbo.

For the quarter, the Strategy outperformed its benchmark, the Bloomberg Gov/Credit 1-3 yr Index on a gross- and net-of fees basis. Sector allocation decisions contributed to relative performance. This was primarily driven by off-benchmark allocations to ABS, CMBS and agency MBS. Meanwhile, security selection decisions detracted, primarily within IG corporates due to our allocation to more intermediate term bonds. Finally, with a neutral position for most of the quarter, duration and yield curve positioning had minimal impact on relative performance.

Outlook

Looking ahead, fundamental factors remain supportive. Growth has been roughly 2–3% for the last 3 years, most recently delivering 2.5% in 4Q24. The labor market is healthy with only 4.1% unemployment. And on the consumer side, balance sheets remain healthy.

That said, survey data has indicated tariffs have negatively impacted both business and consumer sentiment. We have already seen consumers pull back (negative growth numbers in both Personal Consumption Expenditure (PCE) and retail sales numbers for January) and we will likely see a similar reaction on the business investment side. Even if tariffs are watered down, the associated uncertainty will remain a headwind.

That said, while a recession is not our base case, the probability has clearly increased. While there will likely be an impact on personal consumption and investment, household and corporate balance sheets still remain healthy. In addition, the downside to growth should be limited as the Fed has the room to cut rates, especially if employment numbers weaken. However, much depends on how much, and for how long, the announced tariffs remain in place.

Over the past several quarters, we have been constructive on fundamental factors, but believed valuations were ignoring potential risks. As a result, we came into the quarter positioned with a higher quality, shorter spread duration bias. While spreads have widened, the macro-outlook has clearly weakened. As a result, the overall risk profile of the portfolio has changed only marginally, while quarter over quarter portfolio changes are more reflective of relative value opportunities. For example, we further reduced our overweight to IG corporates, while also increasing our allocation to high quality CMBS and floating rate agency collateralized mortgage obligations (CMO). Looking forward, as spreads continue to widen, we are well positioned to add risk where appropriate.

The **Bloomberg US Government/Credit 1-3 Year index** covers US Treasury securities, agencies, publicly issued US corporate and foreign debentures and secured notes that meet specified maturity, liquidity and quality requirements. The index is fully invested, which includes the reinvestment of income. Indexes are unmanaged and index returns do not include fees or expenses. **An individual cannot invest directly in an index.**

The **Bloomberg US Aggregate index** is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market. The index includes US Treasury securities, government-related and corporate securities, fixed-rate agency mortgage-backed securities, asset-backed securities and commercial mortgage-backed securities, both agency and non-agency issues. Indexes are unmanaged and index returns do not include fees or expenses. **An individual cannot invest directly in an index.**

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