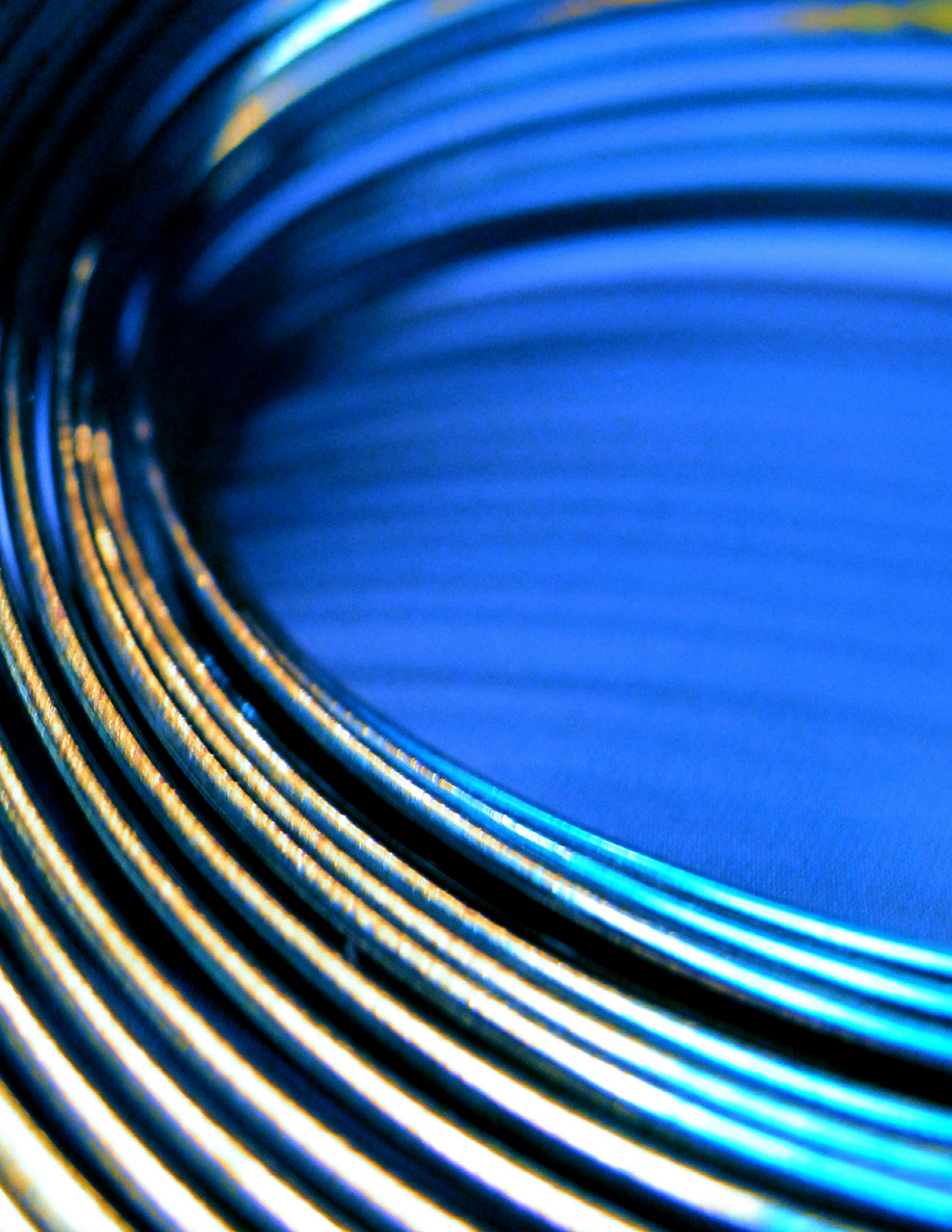
First Eagle Investments

First Eagle Reflections

2024–2025 Edition

For institutional use only.



Inside

Welcome to First Eagle Reflections

Are we living through a generational re-pricing of risk in US Treasuries?

Denominated in the global reserve currency and backed by the full faith and credit of the world's premier economic and military power, Treasuries have long been considered a risk-free asset; boring, perhaps, but unlikely to lose money. A potential "safe haven" during times of trouble.

And this conviction has largely held true since the early 1980s, when US interest rates entered a secular decline and sparked a bull run in bonds that lasted longer than most of us have been involved in the financial markets. Yields did not move monotonically lower over this period, but fluctuations throughout were marked by lower peaks and deeper valleys until the 10-year rate in 2020, amid the massive policy response to the Covid-19 outbreak, fell below 1% for the first time.[1]

The subsequent inflation shock forced the Federal Reserve in March 2022 to launch what turned out to be the most aggressive rate-hike cycle in its history, bringing the long bull market abruptly to heel.[2] The sharp selloff across the yield curve served as a reminder that while Treasuries remain free from credit risk—in theory, at least—they are subject to the same duration risk as any other fixed-rate asset. It also sent the message that the resulting price movements can have real-world impacts, as several midsized US regional banks failed in March 2023 after being forced to liquidate their Treasury holdings at massive losses to meet depositor withdrawals.

For much of the past two years, Treasuries have traded largely in tandem with expectations of near-term monetary policy, which resulted in significant volatility as markets tried—and mostly failed—to get an accurate read on the path of the federal funds rate. Interestingly, longer-term Treasury yields have been biased higher since rate cuts commenced in September 2024; here in mid-January, the yield on 10-year Treasuries is approaching 5%, a level not seen since the early days of the global financial crisis.[3] Though higher Treasury yields at this stage could reflect optimism about future economic growth, they also could be sniffing out something more troubling.

US fiscal policy has been on an unsustainable trajectory since the global financial crisis, as the government provided extensive support in response to two large-scale economic dislocations. This federal largesse was supported by very low interest rates that kept interest expenses manageable and by long-lived, large-scale quantitative easing programs that provided ample demand for government debt. While the rollback of crisis-era monetary accommodations altered the calculus of government borrowing, there are few indications that fiscal policy will be meaningfully adjusted to reflect the new math.

Of course, the US is not the only country on an unviable fiscal course. The International Monetary Fund projects public debt worldwide to approach 100% of gross domestic product by 2030 and notes significant upside risk to this baseline forecast.[4] It's possible that the results of 2024's elections, which were not kind to the political status quo, reflected the electorate's sensitivity to the financial vulnerability such debt represents, if only subconsciously. With more than 70 countries holding national elections, incumbent parties across the political spectrum lost hold of power or saw it weakened, with economic dissatisfaction—and

1. Source: Federal Reserve Bank of St. Louis; data as of January 14, 2025.
2. Source: Federal Reserve Bank of Richmond; data as of August 30, 2024.
3. Source: Federal Reserve Bank of St. Louis; data as of January 14, 2025.
4. Source: International Monetary Fund; data as of October 31, 2024.

First Eagle has deliberately built out an investment platform equipped to provide modern solutions to modern challenges.

the high cost of living, more specifically—helping fuel the anti-incumbency bias.[5] "Voting out the bums" may provide a hit of electoral *schadenfreude*, but it's unclear how some of the measures upon which 2024's victors campaigned will provide the relief voters seek.

Also unclear is how current sovereign debt trends may impact investor perception of risk premia across asset classes. The term premium[6] on 10-year Treasuries—which has been negative more often than not since 2016—turned positive in October and has been biased higher since.[7] This move may reflect a migration to more normal levels of duration-risk assessment, or it could be a sign that markets have begun to recalibrate their view of future US creditworthiness amid a background of high and rising debt. Waning confidence in the stability of Treasuries could threaten the US dollar's role as the preeminent global reserve currency at the same time other currencies and gold have eaten into the dollar's share of central bank reserves, emerging markets are calling for the "de-dollarization" of trade, and crypto continues to make slow inroads into commerce.[8] It could also force a future reckoning of which assets represent perceived "safe havens" for investors.

It seems prudent to consider the impact a meaningful re-rating of Treasury risk could have on the institutions that hold these securities and asset prices more broadly. Highly concentrated, richly valued markets such as US equities may be particularly vulnerable to a rate shock. Lofty returns for the S&P 500 Index in recent years have been driven by the outsized performance of a small handful of very large tech-oriented stocks, a dynamic that camouflaged a market far more nuanced than it appears on the surface while also challenging investors' efforts to achieve portfolio diversification through beta exposure.[9]

Whether or not Treasuries are on the verge of a generational transformation, I'm confident First Eagle will be up for the challenge. Drawing on a heritage dating back to 1864, the firm has served as a prudent steward of client capital across market cycles, varying macroeconomic conditions and numerous disruptive events. In more recent years, we have deliberately built out an investment platform—introducing new teams, new strategies and new vehicles—equipped to provide investors globally with modern solutions to modern challenges.

Sincerely,

Mehdi Mahmud
President and Chief Executive Officer,
First Eagle Investments
January 2025

5. Source: Pew Research Center; data as of December 11, 2024.
6. "Term premium" is the additional return that investors require to hold a longer-dated bond as opposed to rolling over a series of short-term issues over the same time frame, reflecting the risk of higher interest rates over the bond's tenor.
7. Source: Federal Reserve Bank of New York; data as of January 14, 2025.
8. Source: International Monetary Fund; data as of June 11, 2024.
9. Source: FactSet; data as of December 31, 2024.

When We Two Parted

While the synergistic economic bonds that have benefitted the US and China since the latter's arrival on the international stage decades ago have grown increasingly strained, the US seems to be taking the decoupling in stride. Notably, China's ongoing economic malaise has provided a much-needed disinflationary impulse to its trading partners and helped support risk appetites—for a small handful of growth assets, in particular. **Matt McLennan** and **Kimball Brooker**, co-heads of the Global Value team, discuss how changes in this dynamic could usher in a more nuanced investment landscape in which accessing differentiated sources of risk and return again take precedence.

Was "Chimerica" an Illusion All Along?

As in 2023, diversification failed to matter in 2024. For two years now, those seeking outsized equity gains likely would have been best served by focusing their investment on the most concentrated, highest-growth segment of the world's largest stock market; that is, tech-oriented US stocks. As proxied by the "Magnificent Seven," this cohort advanced 67% in 2024 to help fuel a 25% gain in the S&P 500 Index. The S&P 500's gain excluding these seven stocks, which accounted for more than one-third of the index's total market capitalization at year-end, amounted to a far more pedestrian 16%. The MSCI World Index's 19% return was similarly bolstered by the outperformance of these megacap names.[1,2]

> The symbiotic relationship between the US and China has grown strained.

But when we decompose the factors driving the one-dimensional equity market performance of recent years, it's not difficult to arrive at a mindset in which diversification regains its reputation as a potential driver of attractive long-term risk-adjusted returns and an essential element of a well-balanced investment portfolio.

Most notable to us has been the pronounced post-pandemic decoupling of the US and China, whose symbiotic relationship represented a primary driver of global macroeconomic activity and financial markets performance for much of the past several decades. In fact, economic historians Niall Ferguson and Moritz Schularick in 2007 coined the term "Chimerica" to describe the interconnectivity of the world's most rapidly growing emerging market (at the time) and its dominant economic power (still). The US was happy to buy the competitively priced products mass-produced in China, China was happy to lend the resulting trade surplus back to the US through the purchase of Treasuries, and the world's benchmark interest rate was kept in check.[3] But like so many celebrity portmanteaus, Chimerica may not have been built to last.

The decoupling has been most evident in the years since the Covid-19 outbreak. Risk perception in the US has been low, supporting high equity market multiples—for growthier stocks, in particular—and tight credit spreads, as the US has benefitted from a Goldilocks economic scenario that unfolded against most expectations. Consumer and producer prices—though still slightly above target—seemingly have been reined in without torpedoing economic growth, which has helped bolster corporate earnings and raise hopes that a soft landing may be achieved.

In contrast, risk perception in China has been high—and for good reason. While China managed to avoid the early-2020s inflation spike that bedeviled the majority of the world, its economy has faced its own set of complications, some self-inflicted. China's aggressive zero-Covid policy—begun in early 2020 and maintained until the end of 2022, long after most nations had significantly reduced or eliminated pandemic-related restrictions—resulted in an uneven recovery that stymied private investment and household spending. An ideologically driven crackdown on the rapidly expanding domestic tech industry, launched in late 2020, hamstrung what had been among the most dynamic sectors of China's economy and in the process wiped out trillions of dollars in market capitalization and cost countless jobs.[4] The debt-fueled bubble in China's property market—which once accounted for about 25% of the country's gross domestic product (GDP)—burst with the default of developer Evergrande in 2021, and it continues its structural and cyclical reset to a lower base.[5]

As a result of these and other factors, China's animal spirits have all but been put out to pasture; the MSCI China Index finished 2024 down more than 50% from its early-2021 peak, while yields on 10-year government bonds fell to all-time lows.[6] Certain other countries in China's orbit have been similarly afflicted.

1. The term "Magnificent Seven" is widely used in the financial media and elsewhere to refer to these seven US technology-related stocks that drove an outsized share of equity market gains in 2023 and 2024.
2. Source: Bloomberg; data as of December 31, 2024.
3. Niall Ferguson and Moritz Schularick, "'Chimerica' and the Global Asset Market Boom," *International Finance* (10:3, 2007).
4. Source: Bloomberg; data as of September 12, 2024.
5. Source: *The Wall Street Journal*; data as of October 26, 2023.
6. Source: MSCI, Bloomberg; data as of September 30, 2024.

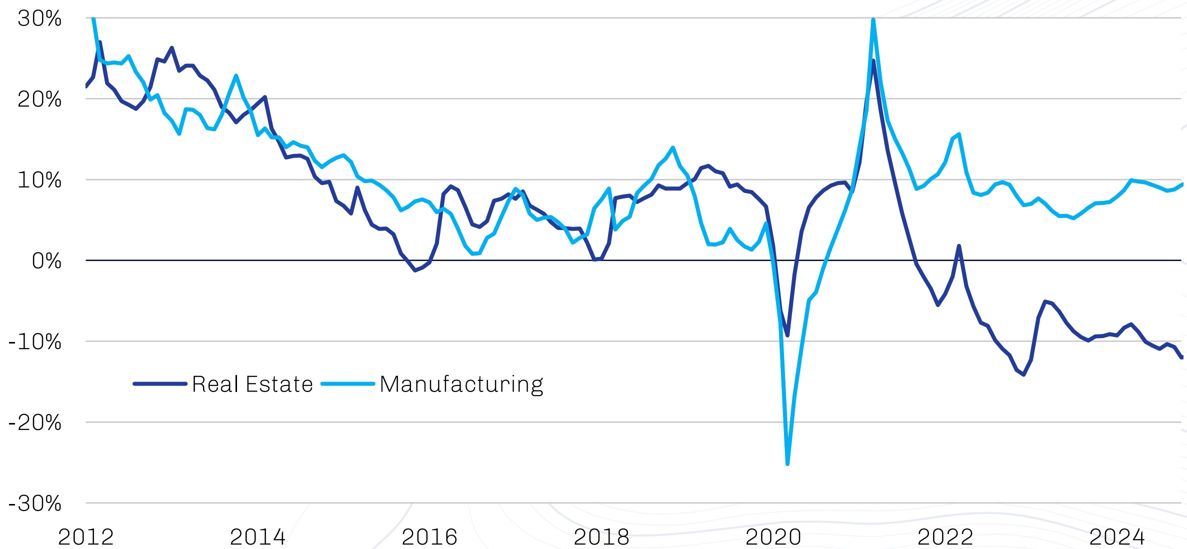
Good News for People Who Love Bad News

In the past, signs of stress in the Chinese economy were typically viewed as bad news for global activity broadly, and risk assets would respond accordingly. This time around, however, the effects of China's malaise have been more nuanced. China's property market collapse, for example, is at least partly responsible for cyclically moderating inflation pressures in the US and many other countries. As shown in Exhibit 1, fixed-asset investment in China has shifted away from real estate and toward manufacturing, and the resulting excess capacity has weighed on export prices and provided China's trading partners with a strong disinflationary impulse. Meanwhile, waning confidence among Chinese businesses and households has depressed imports and caused a range of economically sensitive commodities—everything from oil to copper to wheat—to derate versus gold, which has been another exogenous source of downward pressure on global inflation.

> China's property market collapse is at least partly responsible for the cyclically moderating inflation pressures in the US and many other countries.

Exhibit 1. China's Reemphasis on Manufacturing Has Served as a Disinflationary Impulse Globally

Year-over-Year Percent Change in China Fixed-Asset Investment, Three-Month Moving Average; January 2012 through September 2024



Source: UBS, First Eagle Investments; data as of September 30, 2024.

More recently, however, there are signs that the tides may be changing. With unrelentingly downbeat economic data appearing to disabuse them of any notion that their growth targets remained obtainable without intervention, China's policymakers late in the year announced a series of stimulus measures to combat deflationary pressures, stabilize housing and rebuild market optimism. In September, the People's Bank of China (PBOC) cut the reserve requirement ratio for banks and its benchmark short-term reverse repo rate, while instructing commercial banks to trim rates on outstanding mortgages and introducing new liquidity mechanisms to support equity markets.[7] Though authorities hinted that significant fiscal support was also on tap, the initial package announced by finance officials soon after the November US elections was underwhelming in size and scope—$1.4 trillion in local government bond issuance to refinance maturing and higher-yielding local government debt rather than injected directly into the economy. However, it stands to reason that Beijing may look to keep some of its powder dry until it has better visibility on potential tariffs from the incoming Trump administration.[8]

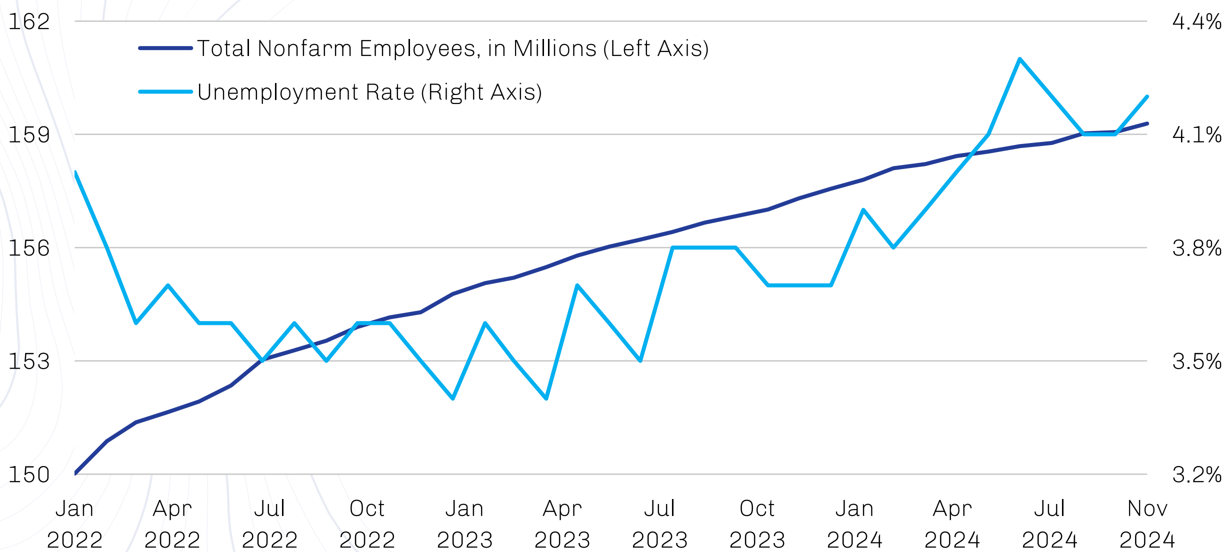
7. Source: Reuters; data as of September 24, 2024.
8. Source: Reuters; data as of November 8, 2024.

The US may find itself vulnerable to a reversal of China's fortunes, in our view, as its battle against inflation to date has reached only a fragile peace. Our concerns are underpinned by the behavior of the US labor market throughout the Federal Reserve's tightening cycle. As shown in Exhibit 2, the labor market—unusually—softened during this period even as payrolls continued to grow, suggesting that the increase in the unemployment rate from its cyclical low of 3.4% to 4.1% by year-end 2024 was driven by increased participation rates.

> With US corporate profits and margins having inflected higher as financial conditions loosened, payrolls and wage growth may follow suit.

One theory for this phenomenon is that the massive increase in public debt outstanding post-Covid led to a nominal rebasing of the US economy that bolstered corporate profits in the face of contracting margins and supported a moderation in payroll growth rather than an outright decline. With financial conditions having since loosened, both corporate profits and profit margins have inflected higher in nominal terms, and it's reasonable to think that payrolls and wage growth may follow suit should this trend continue. Though down from its peak of 6.7%, wage inflation of 4.3% remains inconsistent with the Fed's 2% inflation goal, and this stickiness is likely among the reasons why consumer price index (CPI) prints have stubbornly persisted above target even as other components have retreated.[9]

Exhibit 2. US Payrolls Continued to Expand Even as the Unemployment Rate Increased
January 2022 through November 2024



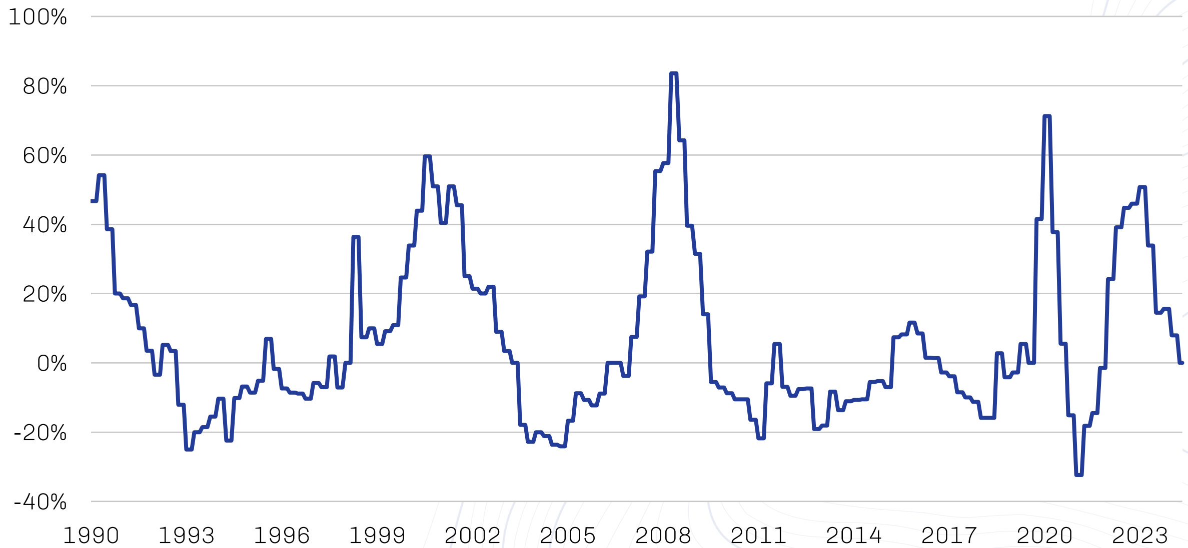
Source: US Bureau of Labor Statistics, Federal Reserve Board of St. Louis; data as of December 9, 2024.

9. Source: Federal Reserve Bank of Atlanta; data as of December 11, 2024.

Easing monetary policy presents another potential source of inflationary pressure. With the inflation rate well off its cyclical peak, the Fed in September began to recalibrate its settings, kicking off a much-anticipated rate-cut cycle with a 50 basis point reduction. The Fed followed up that move with two additional 25 basis point cuts in November and December to bring its key policy rate to 4.25–4.50% by year-end, and the latest summary of economic projections suggest an additional 50 basis points of cuts are coming in 2025.[10] In response to easier policy, bank lending standards have gone from tight to neutral (as shown in Exhibit 3) and credit spreads have retreated. With market valuations high and earnings expectations buoyant, a Fed shift back to a hawkish policy bias sooner than expected could prompt investors to recalibrate their risk appetites and herald an untimely end to the US Goldilocks tale.

Exhibit 3. More Accommodative US Banks Highlight Easing Financial Conditions

Net Percentage of Domestic Banks Tightening Standards for Commercial and Industrial Loans to Large and Middle Market Firms, January 1990 through November 2024



Source: Bloomberg; data as of November 30, 2024.

From Politicking to Policymaking

Though the US and China may be decoupling economically, their mutual affection for public debt persists, and their large and growing debt loads—not unique to them by any means—reflect long-term risks to financial stability even as they support near-term growth. Unrestrained government debt globally has raised the specter of currency debasement and other adverse financial outcomes, and the longer fiscal imbalances go unaddressed, in our view, the more difficult they will be to unwind.

> Unrestrained government debt globally has raised the specter of currency debasement and other adverse financial outcomes.

In the US, the federal fiscal deficit expanded again in fiscal 2024 (ended September) to 6.4% of GDP and has only worsened since, coming in at 7.1% for the last 12 months through November; the 50-year average is 3.8%.[11] While the policy specifics moving forward are uncertain given January's leadership transition, higher deficits and debt levels seem likely under the incoming Trump administration (as they would have with a Harris victory).[12]

10. Source: Federal Reserve; data as of September 18, 2024.
11. Source: Congressional Budget Office, Bloomberg ; data as of November 30, 2024.
12. Source: Committee for a Responsible Federal Budget; data as of October 25, 2024.

Gold: All That Glitters

Our belief that the future is inherently uncertain drives our commitment to a strategic exposure to gold as a potential hedge against adverse market outcomes. Such an approach has been particularly beneficial over the past several years, as gold demonstrated remarkable resilience in the face of conditions not typically associated with price appreciation, establishing a series of new nominal highs in the process.

We've noted previously that gold's inverse relationship with real interest rates—i.e., the difference between the nominal interest rate and the expected rate of inflation—historically has been the most important driver of its price movements over time. While we continue to believe this to be true in the long run, the metal's rally over the past few years is a compelling reminder that numerous factors can affect price movements in shorter time frames.

Gold's reputation as a perceived "safe haven," for example, often attracts buyers of all stripes during periods when threat recognition is high, and the past few years have certainly been one of those periods given the deteriorating geopolitical backdrop and large-scale armed conflicts in Russia/Ukraine and the Middle East. Meanwhile, the massive accumulation of debt by governments worldwide has increased concerns about the potential for currency debasement.

Global central banks are among the potential gold buyers sensitive to these issues, and in recent years they have very actively accumulated the metal in an effort to diversify their reserves, providing a key source of support for the gold price in the face of traditional headwinds. Net purchases of gold by central banks in 2022 and 2023 were the highest on record by far, and the first 11 months of 2024 were strong, if not quite at the pace of the previous two years. Financial buyers were slower to catch the gold bug, but a midyear 2024 pickup of inflows into physically backed gold ETFs—which capture investment demand from both institutional and individual investors—drove North American flows to their first positive year since 2020.[1]

Notably, gold declined in the initial aftermath of the US presidential election while risk assets rallied sharply. Cryptocurrencies—and bitcoin, in particular—were among the biggest post-election gainers, pulled along by the slipstream of what is understood to be a crypto-friendly Trump administration. While it's hard to draw conclusions from such a short period of performance, either positive or negative, we continue to view gold as the best potential hedge against the risks facing investment portfolios. Despite the latest round of risk-on enthusiasm for crypto and the potential for its regulatory legitimacy, in our view it remains an option on becoming digital gold—and thus an option on becoming a potential hedge asset—rather than a replacement for the time-tested store of value.

1. Source: World Gold Council; data as of January 10, 2025.

> Any attempt to meaningfully move the needle on the US debt burden would likely require reforms to popular entitlements like Social Security, Medicare and Medicaid.

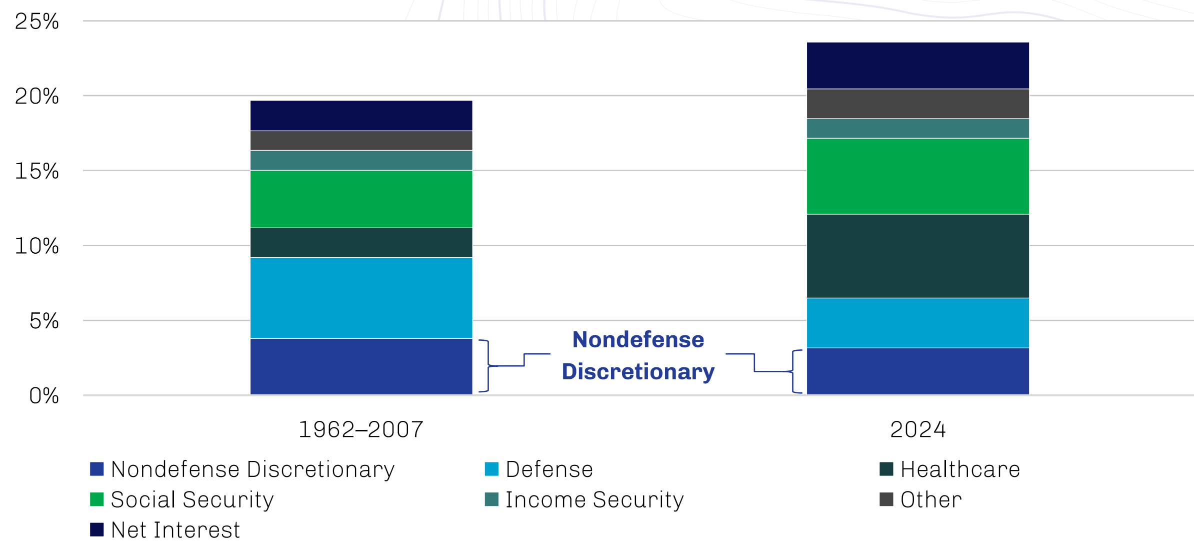
The Tax Cuts and Jobs Act of 2017, which will see many of its provisions for individual taxpayers expire at year-end 2025 absent Congressional action, is likely to take fiscal center stage next year. A unified Republican government suggests a high possibility that the Trump administration's key tax priorities will be extended, but the means by which that lost revenue will be offset remain uncertain.

A reduction of regulatory hurdles impairing business activity seems likely to promote investment and economic growth. Some in the administration—including Scott Bessent, Trump's pick to run Treasury—have argued that tariffs "can increase revenue to the Treasury" if used strategically.[13] But the Congressional Budget Office's review of tariff increases in 2018–19 found that the initial boost in customs revenues soon declined as imports slowed and were sourced from countries subject to lower duties.[14]

Spending cuts are another avenue to reducing the deficit, and Trump tapped public notables Elon Musk and Vivek Ramaswamy to take on the challenge as co-heads of the Department of Government Efficiency (DOGE). While there is certainly room to cut federal spending and eliminate wastefulness, public discussion has been focused mostly on nondefense discretionary spending, which accounts for only about 15% of total federal outlays and has actually decreased slightly as a percentage of GDP in recent years, as shown in Exhibit 4. Any attempt to meaningfully move the needle on the country's debt burden likely would require reforms to popular—and seemingly sacrosanct—entitlements like Social Security, Medicare and Medicaid. Mustering the necessary political will for changes to programs so broadly popular with voters seems like an insurmountable challenge. While there is also talk of slashing the government's workforce of 2.3 million civilians located across all 50 states, their aggregate salary amounts to less than 1.5% of GDP.[15]

Exhibit 4. Nondefense Discretionary Spending Offers US Legislators Limited Savings Opportunities

Federal Spending by Category as a Percentage of GDP



Source: US Department of the Treasury, US Bureau of Economic Analysis; data as of November 30, 2024.

13. Source: Fox News; data as of November 15, 2024.
14. "How CBO Projects Tariff Revenues," Congressional Budget Office (October 2024).
15. Source: *The Wall Street Journal*; data as of November 17, 2024.

Writing Our Own Narrative

Given equity market performance trends over the past two years, it can be tempting to ride the wave of "narrative economics" that has driven index-level performance. Economist Robert Shiller coined this term to describe the emerging stories that capture public attention and ultimately affect individual and collective behaviors—such as the investor enthusiasm around developments like artificial intelligence and GLP-1 agonists that has fueled a surge in narrow segments of the stock market over the past two years.[16] While certain of these narratives are compelling, the valuations of those names overtly benefiting from them are generally less so.

> We have continued to focus on investing in a diversified basket of individual assets we believe represent scarce quality and value.

As investors whose definition of risk is centered on avoiding the permanent impairment of capital rather than tracking error against a benchmark, the Global Value team remains focused on building portfolios that offer truly differentiated sources of risk and return and demonstrate perennial relevance. Selectivity is at the heart of our value-oriented investment process, and the flexibility of our mandate allows us to apply this selectivity to the global opportunity set from the bottom up. We look for assets we believe demonstrate scarce quality and value, and invest in them only when we can do so at a "margin of safety."[17] Our stock selection often is complemented by a structural allocation to gold—a store of value for millennia—as a potential hedge against extreme market outcomes.

While we remain concerned about the many risks facing investors in the current environment, we also see opportunity. But rather than making concentrated bets on the direction of markets, we have continued to focus on investing in a diversified basket of individual assets we believe have the potential to demonstrate resilience across multiple states of the world.

16. Robert J. Shiller, *Narrative Economics: How Stories Go Viral and Drive Major Economic Events*, Princeton University Press (October 2019).
17. First Eagle defines "margin of safety" as the difference between a company's market price and our estimate of its intrinsic value.

The Tide Is High

While the underperformance of small cap stocks relative to larger names over the past decade-plus has been disappointing, a range of factors may be coalescing to ease what has been a key breakwater for the market segment: middling earnings growth. **Bill Hench**, head of the Small Cap team, ponders the forces that in the years ahead could unleash a wave of bottom-line growth, including lower interest rates, a more benign regulatory environment and reenergized mergers and acquisitions and capital markets activity.

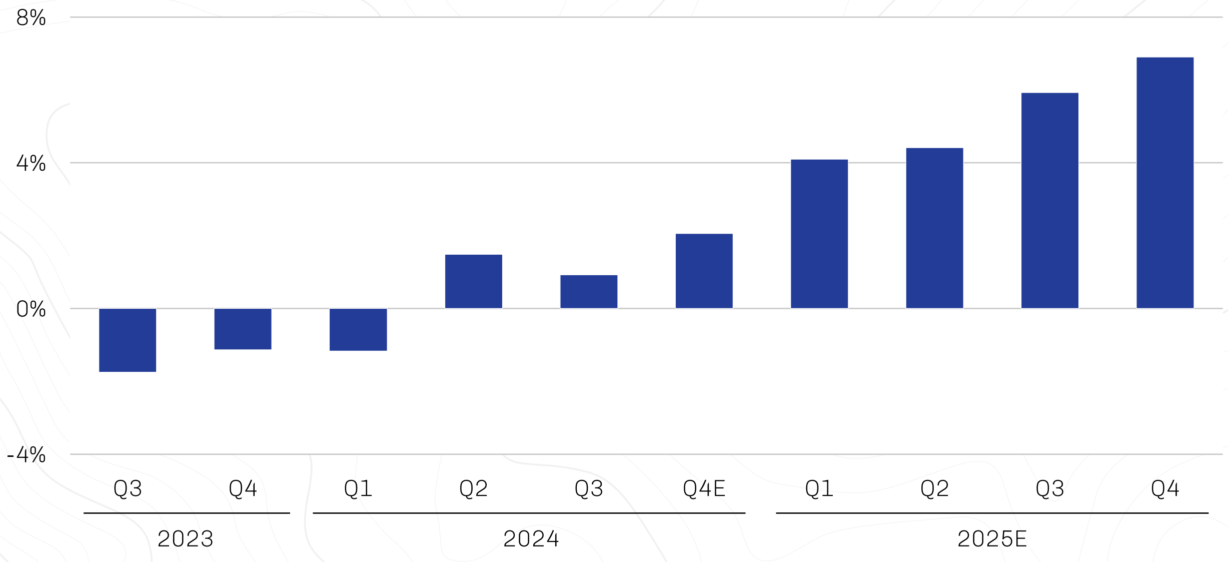
Growth Has Been Elusive, but Change May Be Afoot

Given the increasing number of money-losing small cap companies since the global financial crisis—45% of the Russell 2000 Index lost money on a trailing-12-month basis through the end of the third quarter—lackluster earnings at the benchmark level may be as much to blame for relative under-performance as market capitalization preferences.[1] However, there are reasons to believe resuscitated earnings may finally be in prospect for 2025 as accelerating top-line growth and continued margin improvements filter through to the bottom line, as shown in Exhibit 1 and Exhibit 2. As we discuss below, multiple forces at the industry level could amplify company-specific earnings momementum.

> There are reasons to believe resuscitated earnings growth for small cap stocks may finally be in prospect for 2025.

Exhibit 1. Sales Growth Is Forecast to Accelerate in 2025...

Realized and Estimated Russell 2000 Index Year-Over-Year Sales Growth, Third Quarter 2023 through Fourth Quarter 2025

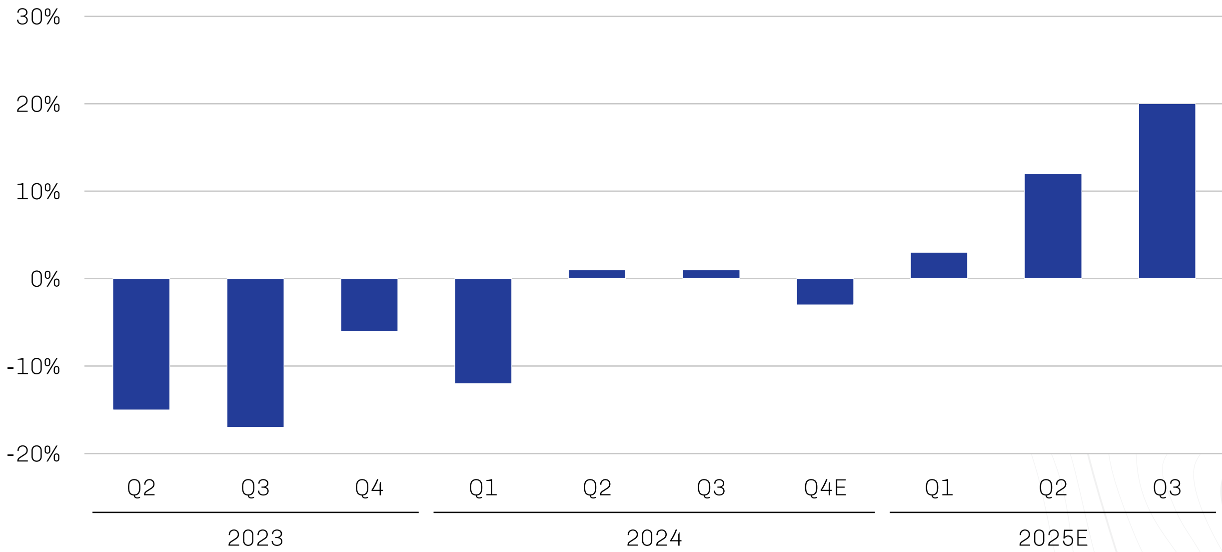


Source. Furey Research Partners, FactSet; data as of November 14, 2024.

1. Source: FactSet; data as of September 30, 2024.

Exhibit 2 ...Boosting Margins and Earnings Growth

Realized and Estimated Russell 2000 Index Year-Over-Year Earnings Growth, Second Quarter 2023 through Third Quarter 2025



Source: Furey Research Partners, FactSet; data as of November 14, 2024.

As small caps overall are more leveraged to floating-rate debt than larger companies, further Federal Reserve policy easing beyond the 100 basis points worth of rate cuts in 2024 would have a meaningfully positive incremental impact on these businesses' interest expenses. While we won't hazard a guess at the trajectory of Fed policy going forward, the latest dot plot Federal Open Market Committee forecasts suggest an additional 50 basis points of cuts are on tap in 2025.[2] A reduced cost of capital across the US economy—for both consumers and levered small cap companies—could trigger a resurgence in small cap stocks, especially those in the housing, consumer discretionary and energy sectors. In addition to reducing borrowing costs and buoying economic activity, lower rates historically have lured investment capital in from the sidelines, propelling small caps higher.[3]

> Small cap balance sheets, in our view, are the strongest they've been since the global financial crisis.

Even without further rate relief, however, small cap balance sheets are the strongest they've been since the global financial crisis, in our view. Improved supply-chain management post-Covid has helped managers rationalize inventories and reduce working capital. Some companies have been able to leverage the proliferation of cloud applications to reduce the capital intensity of their businesses and improve operating leverage; specifically, what had been large, fixed-hardware infrastructure investments financed through capital expenditures become variable operational costs.

2. Source: Federal Reserve; data as of December 18, 2024.
3. Source: JP Morgan; data as of July 22,2024.

Policy Changes and Regulatory Reform May Have an Outsized Impact on Smaller Companies

In addition to wider operating margins, strengthened balance sheets and potentially lower rates, prospective policy changes and easier regulations facilitated by the 2024 Republican sweep of the November US elections could serve as an additional tailwind to earnings growth for US-domiciled companies. This could be especially true for smaller companies, in our view. Not only do large companies have the scale to monitor and adapt to regulatory changes, their lobbying muscle often enables them to influence regulations at the design stage to their benefit. Smaller companies, in contrast, usually are left to "play it as it lays" and bear the fixed costs of compliance over a smaller base. A less restrictive regulatory environment may have an amplified salutary impact on small companies.

A less restrictive regulatory environment may have an amplified salutary impact on small companies.

Tariffs. Given that we already operate in a trade-protected world, the impact of any new tariffs will be incremental rather than de novo, potentially limiting their overall effect. That said, any redomestication of manufacturing would likely benefit US-centric producers, including the small cap companies that in the aggregate source about 90% of revenue from home.[4]

Taxes. While many of the provisions of the Tax Cuts and Jobs Act of 2017 affecting individual taxpayers are set to expire at the end of 2025 barring Congressional intervention—which seems likely given the results of the US election—changes to the corporate tax code were made permanent at the time of the bill's passage. That said, Trump on the campaign trail proposed further easing of corporate taxes, including lowering them to 15% for domestic production.[5] As corporate taxes tend to be regressive, US-focused small cap companies may be particularly well positioned for tax savings that could be redirected to reducing fixed costs and thus enhancing margins and productivity.

Regulations. As president, Trump reportedly is prepared to nullify "thousands" of rules and regulations he and his team deem to represent executive overreach.[6] Generally speaking, such a dismantling of the regulatory state would reduce outlays on compliance—with consumer protection laws, for example, or environmental requirements—and thus operating costs, boosting margins and profitability. Meanwhile, looser antitrust provisions could unleash a spate of mergers and acquisitions (M&A), potentially triggering buyout premiums for targeted small cap companies.

Enhanced Efficiency/Reduced Government Spending. Improved efficiency and the elimination of unnecessary federal expenditures could reduce government spending and Treasury issuance, enabling assets that would otherwise be invested in government debt to be put to better use in the private sector. That said, discretionary nondefense spending represents only about 15% of total federal outlays; efforts to rein in government spending without reform to popular and politically untouchable entitlements like Social Security, Medicare and Medicaid seem unlikely to have a meaningful impact on the country's fiscal trajectory.[7]

4. Source: Cambridge Associates; data as of May 1, 2024.
5. Source: S&P Global; data as of November 12, 2024.
6. Source: *The Wall Street Journal*; data as of November 20, 2024.
7. Source: US Department of the Treasury; data as of December 12, 2024.

Industry-Specific Trends Could Lift a Narrower Swath of Small Cap Companies

Beyond the potentially broad sweep of policy changes under the new administration, industry-specific developments could benefit a more focused range of small cap companies.

> Sectors already deep in the digital space could be especially well positioned to benefit from emerging technologies like AI.

Artificial Intelligence (AI). AI could be even more meaningful over a long cycle than the dawn of the internet was in 2000, transforming companies across industries and capitalizations into more efficient digital- and data-driven operations, resulting in reduced costs and faster innovation. Sectors already deep in the digital space like finance, healthcare and logistics could be especially well positioned to benefit from emerging technologies. Additionally, much as the telcos had early-mover advantage into broadband communications in the 1980s, many smaller companies may be able to tweak their business models for relevance in a new AI-driven world rather than embark upon a whole-scale reinvention. For example, one small cap manufacturer in the Midwest has leveraged its century-plus of expertise in thermal management for trucks and tractors to produce cooling systems for data centers.[8]

Energy/Industrials. AI's broad penetration across industries is driving a spike in demand for energy; data centers are projected to account for 11–12% of US power demand by 2030, up from 3–4% today.[9] Meeting this demand will present opportunities for an array of businesses, from drillers and oil servicers to the providers of power infrastructure.

Biotech. Well represented by small caps, the biotech industry is almost purely domestic and therefore leveraged to positive effects from regulatory easing. Looser policies for developing and approving new drugs could facilitate major improvements—perhaps even breakthrough discoveries—in a range of treatment and therapies, unleashing heretofore unseen earnings power.

Financials. While potential regulatory reform and lower capital requirements could compromise the balance sheets of small banks over the long term, a less burdensome regulatory environment likely would reduce compliance costs in the short term. Separately, continued market share gains by private capital providers could squeeze out the weakest local banks, forcing mergers and/or closures and paving the way for a new breed of small cap banks—notably, semi-regionals centered in the South and lower-tax states—with higher profitability and faster growth.

8. Source: Company reports; data as of September 11, 2024.
9. Source: McKinsey & Company; data as of September 1, 2024.

Security Selection and Price Discipline Underpin Resilience

Within the context of a long period of relative underperformance, it's worth remembering that small caps historically have been the most rewarding sector of the market over the long run back to 1927.[10] Although a lagging market can be unsettling in the short term, it can also provide opportunity to buy good companies at attractive valuations. Should growth prospects broaden beyond a narrow cohort of megacap tech stocks, thoughtful active management rather than passive beta exposure may once again be the key to investment success.[11]

Should growth prospects broaden beyond a narrow cohort of megacap tech stocks, thoughtful active management rather than passive beta exposure may once again be the key to investment success.

Regulatory Shift May Result in Both More Takeouts and New Names

The installation of more business-friendly leadership in such US offices as the Department of Justice and Federal Trade Commission may grease the wheels for M&A activity, as well-financed businesses perceive fewer impediments to growth through strategic acquisitions of smaller companies. Initial public offerings (IPOs), too, could see an uptick. For example, reduced regulation may facilitate the development of new drugs/therapeutics, increasing private market valuations for biotech companies and incenting early investors to cash out through a public listing. In the industrial space, new "pick and shovel" companies may emerge to provide essential services and support to facilitate the propagation of new technologies like AI, not unlike the late-1990s facilitators of the internet boom. On the demand side, investors previously skeptical of AI could reevaluate the opportunity cost of their lack of exposure to the sector, supporting a wave of IPO interest.

10. Source: Fama-French Data Library; data as of November 30, 2024.
11. Source: Morningstar; data as of December 31, 2024.

Let the Circle Be Unbroken

Though middle market direct lending volumes have firmed relative to a moribund 2022–23, Federal Reserve easing has yet to unleash the massive wave of mergers and acquisitions (M&A) activity needed to truly open the floodgates. But as First Eagle Alternative Credit's **Michelle Handy** and **Larry Klaff**—chief investment officer of Direct Lending and head of Asset-Based Loans, respectively—explain, private lenders able to offer borrowers a range of financing options that includes both traditional cash-flow loans and asset-based lending facilities may have the potential to generate attractive risk-adjusted returns for investors across the credit cycle.

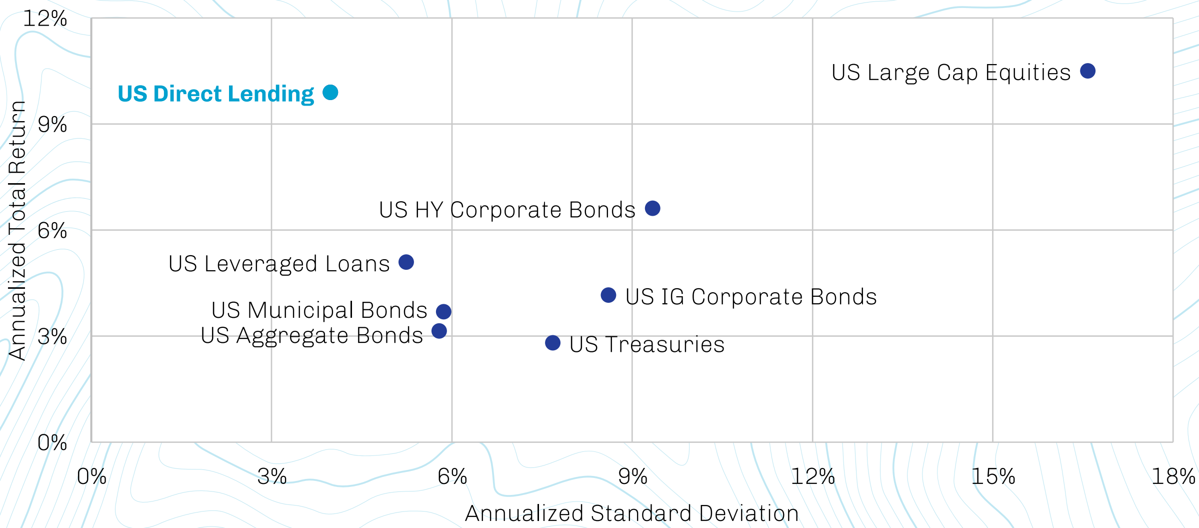
The Lower Middle Market Direct Lending Trifecta: Yield, Leverage and Structure

Unrated and without a secondary market, middle market loans offer investors complexity and illiquidity premia alongside credit premia, risks that can be mitigated through vigorous underwriting and structuring. Typically positioned at the top of the borrower's capital structure, these senior-secured loans provide lenders first recourse on the borrower's assets in case of default/restructuring, and a conservative loan-to-value ratio—often 30–50%—provides a substantial equity cushion. Strong documentation and traditional financial covenants are standard, and a floating interest rate minimizes duration risk. Additionally, directly originated senior-secured loans historically have exhibited low to negative correlations with traditional fixed income and only moderate correlation to equities, as shown in Exhibit 1, offering potential portfolio diversification benefits.

> Direct lending in the lower middle market can provide private lenders and their investors an attractive combination of yield, leverage and structure.

Exhibit 1. Private Credit Can Provide Attractive Risk/Reward Characteristics and Potential Diversification Benefits

Annualized Total Return per Unit of Risk, January 2005 through March 2024



Correlation, January 2005 through March 2024

	US Treasuries	US Aggregate Bonds	US IG Corporate Bonds	US HY Corporate Bonds	US Large Cap Equities
US Direct Lending	-0.51	-0.16	0.22	0.74	0.68

Note: US Direct Lending = Cliffwater Direct Lending Index; US Leveraged Loans = Morningstar LSTA US Leverage Loan Index; US Treasuries = ICE BofA Current 10-Year US Treasury Index; US Aggregate Bonds = Bloomberg US Aggregate Bond Index; US Municipal Bonds = Bloomberg Municipal Bond Index; US IG Corporate Bonds = Bloomberg US Corporate Bond Index; US HY Corporate Bonds = Bloomberg US Corporate HY Bond Index; US Large Cap Equities = S&P 500 Index.

Source: Bloomberg, Cliffwater, Morningstar; data as of March 31, 2024. Index definitions can be found in the back of the book.

While competitive pressures in recent years have eroded lenders' negotiating power on larger loans, we believe lending to the lower middle market—companies with annual EBITDA (earnings before interest, taxes, depreciation and amortization) of $5–$50 million—may represent a sweet spot, particularly those businesses with private equity sponsors. Direct lending in the lower middle market can provide private lenders and their investors an attractive combination of yield, leverage and structure, while smaller deal sizes facilitate diversification across borrowers and industries. In addition, such loans tend to facilitate greater access to management teams, allowing for more comprehensive due diligence by lenders as well as closer collaboration that can help contain default exposure and maximize recoveries during challenging times.

Asset-Based Lending: Differentiated Return Profiles Secured by Pledged Collateral

Asset-based lending (ABL) facilities have long represented a differentiated, if somewhat unheralded, source of return in a private debt portfolio and a strong complement to traditional loans, given the low 0.25 correlation between the two.[1] Borrower demand for financing via ABL has grown in recent years as retrenchment in bank lending and reduced investor appetite for certain types of credit assets have predominated, thanks to tightening liquidity conditions and asset impairments that accompanied the onset of the Fed's rate-hike cycle in early 2022.

> Asset-based lending facilities represent a differentiated, if somewhat unheralded, source of return in a private debt portfolio and a strong complement to traditional loans.

The traditional middle market loans referenced in the previous section typically are underwritten based on an assessment of the borrower's cash flows and governed by a range of maintenance covenants tied to those cash flows; asset-based loans, in contrast, are secured by specific assets of the borrower and feature provisions designed to maintain collateral coverage and loan-to-value ratios. Providers of ABL facilities seek to generate attractive returns while taking advantage of market dislocations and transitions within companies or industries.

As a result, collateral is the primary focus of lenders' initial ABL underwriting and ongoing oversight. Valuing collateral on the basis of net orderly liquidation value (NOLV) rather than current fair-market value can provide lenders an element of risk mitigation, as can a focus on collateral assets expected to retain value across a range of economic conditions. Loan term sheets outline frequent and detailed monitoring requirements for collateral, along with a variety of triggers intended to mitigate downside impact and keep the loan within formula. While liquidating collateral assets is an option for a nonperforming loan, it typically is a last recourse; backed explicitly by assets that are expected to retain value and bolstered by tightly structured loans terms that preserve the lender's interests, ABL facilities historically have had low loss-given-default rates.

Borrowers in the ABL space often are companies that have high working-capital needs and substantial assets but sometimes inconsistent or seasonal cash flows, such as retailers that maintain large inventories or industrials renting high-capex equipment. With limited access to more traditional capital market channels as a result, these borrowers often turn to ABL for competitively priced funding for a variety of purposes, from expanding their senior debt capacity, to monetizing assets while retaining control of them, to serving as a source of acquisition capital for a private equity sponsor.

1. Source: Nomura Capital Markets; data as of September 30, 2024.

Nimble Providers Can Benefit from the Countercyclical Interplay between Direct Loans and ABL

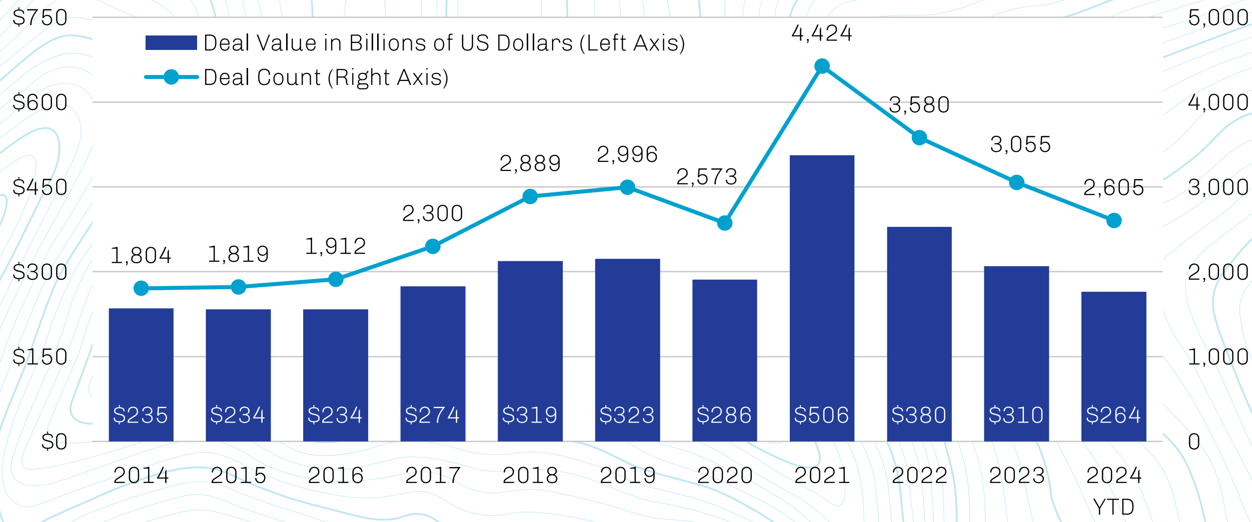
Given the low correlation between direct lending and ABL, comprehensive lenders able to offer borrowers both cash flow-based loans and ABL facilities may be well positioned to provide their investors with differentiated, complementary sources of return throughout credit cycles.[2]

> Lenders able to offer both cash flow-based loans and ABL facilities may be well positioned to provide investors with differentiated, complementary sources of return throughout credit cycles.

M&A activity—the primary driver of lending volume across the middle market—slowed considerably in conjunction with the start of the Federal Reserve's rate-hike cycle in early 2022, as shown in Exhibit 2. With the central bank now having turned to rate cuts as it continues to negotiate a soft landing for the economy, and interest rates having receded in response, a rebound in M&A activity could be a potential tailwind for direct lending demand in 2025, particularly as private equity sponsors eventually unleash $2.7 trillion in dry powder.[3] Though improved from the low levels of 2022–23, the rebound in M&A activity was somewhat muted in 2024, and refinancings have underpinned demand for lower middle market direct loans.

Exhibit 2. Decreased Private Equity Deal Flow Has Weighed on Direct Lending Volumes

US Private Equity Middle Market Deal Activity, 2014 through September 2024



Source: Pitchbook | LCD; data as of September 30, 2024

Although the need for ABL facilities is persistent, demand strength historically has been countercyclical to direct lending; borrower interest in ABL tends to increase when rates rise and cash flow-based loans become less affordable or accessible. While stricter requirements for cash-flow loans are the norm during periods of economic uncertainty or tightening credit—as tougher credit standards challenge coverage ratios and other credit metrics—the backstop of collateral allows ABL providers to take advantage of attractive risk-adjusted opportunities, a dynamic that was particularly evident in the aftermath of 2023's regional bank failures.

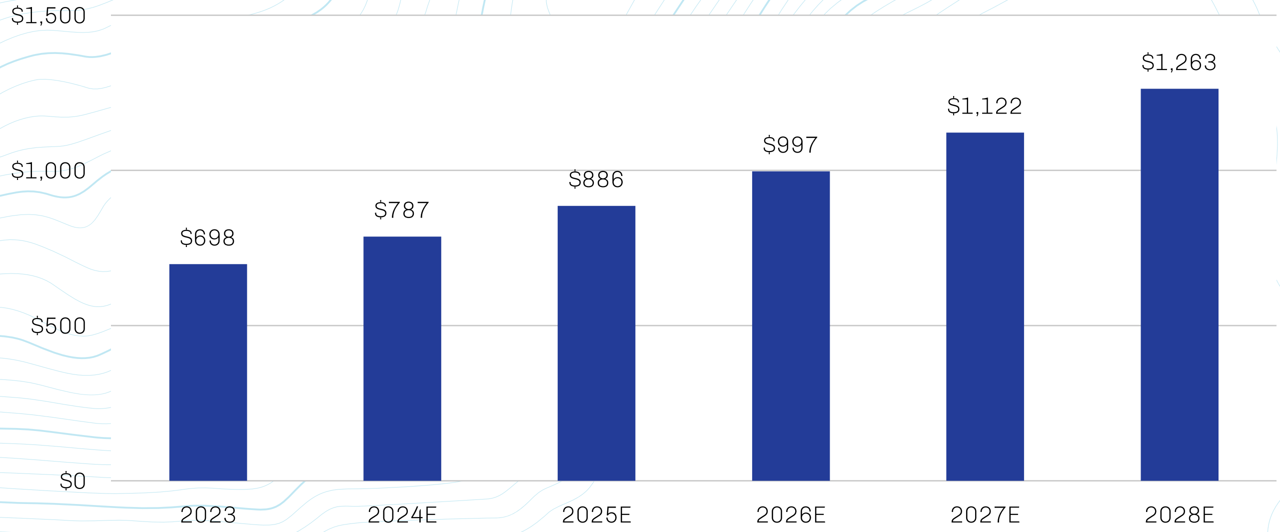
2. Source: Preqin, Cliffwater; data as of December 31, 2023.
3. Source: Pitchbook | LCD; data as of September 1, 2024.

While the direct lending market awaits a resurgence in M&A activity to fuel a significant pickup in demand, ABL facilities serve as an all-weather alternative financing option for asset-rich but cash-constrained companies. As shown in Exhibit 3, ABL activity has picked up in recent years as higher rates have weighed on direct lending origination, and demand for these facilities is projected to grow at an 12.6% compounded annual rate between 2023 and 2028.

While the direct lending market awaits a significant pickup in demand, ABL facilities serve as an alternative financing option for asset-rich but cash-constrained companies.

Exhibit 3. Demand for ABL Is Expected to Increase Through the Decade

Projected Size of Global Asset-Based Lending Market in Billions of US Dollars, 2023 through 2028



Source: EvaluServe; data as of December 31, 2023.

In our view, the playing field for experienced, disciplined ABL providers is wide open. Regional and midsized banks—traditional providers of ABL facilities to middle market borrowers—remain highly selective and risk-averse following the regional bank failures of 2023, and in many cases are more focused on their liquidity profiles and capital reserves than on writing new business. Meanwhile, $2.2 trillion of commercial real estate loans, anticipated to come due by 2027, could create an additional source of demand for financing options.[4]

4. Source: S&P Global; data as of August 19, 2024.

Underwriting and All-Weather Relationships Underpin Success in Private Credit

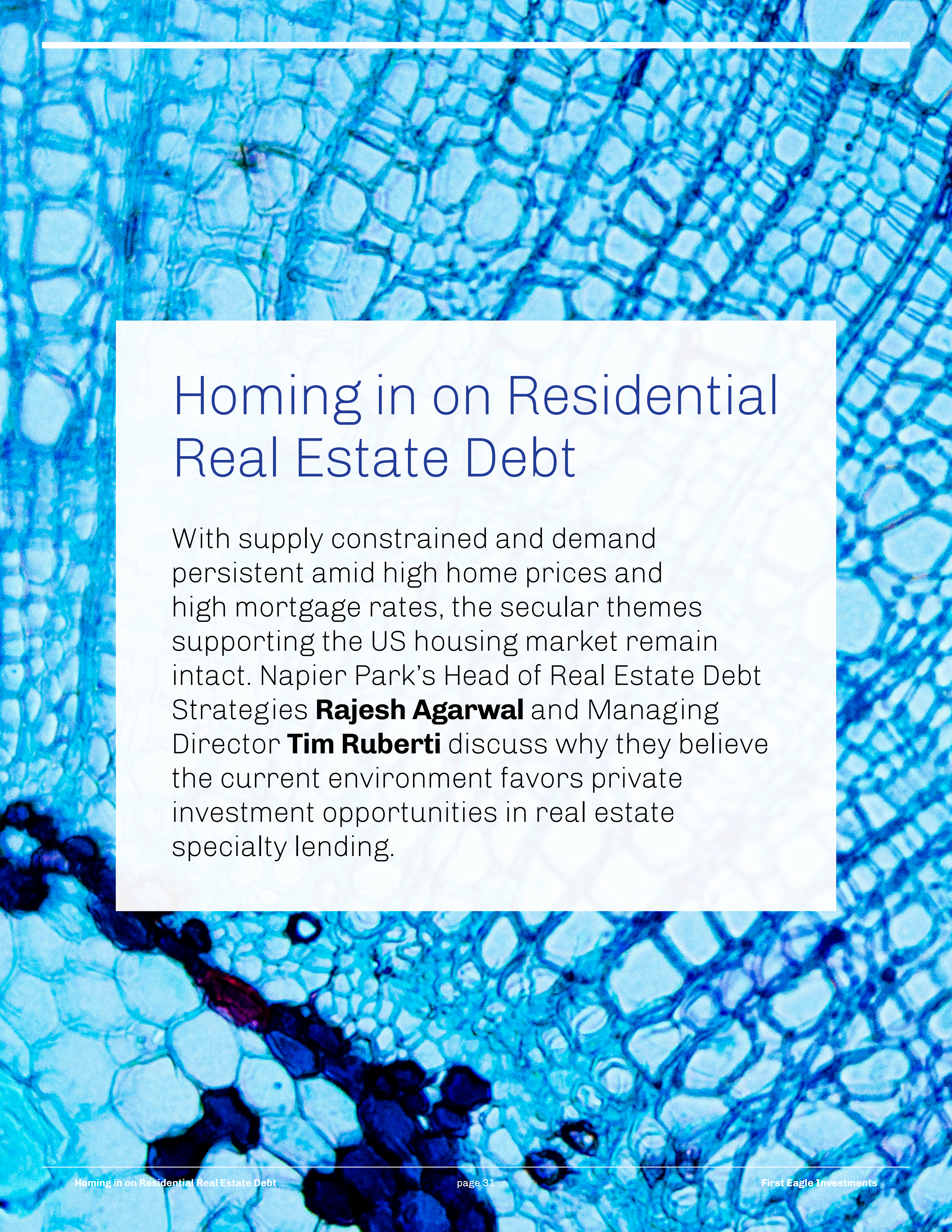
A successful, full-cycle lender must be creative and flexible—toggling between cash-flow loans and ABL as risk-adjusted opportunity dictates. Committed capital, with the promise of certainty to close, is a prerequisite. Beyond that, true success in the lower middle direct lending and ABL markets ultimately comes down to quality underwriting, loan structuring, portfolio composition and relationships.

> A lender able to provide flexible financing solutions across credit cycles may drive attractive risk-adjusted returns for investors.

In direct lending, creditworthiness can reliably be found in borrowers with stable historical earnings, strong cash flows and, ideally, private equity sponsorship, often in growth industries with resilient businesses and deep management insights into broader industry trends. A first-lien position in the borrower's capital structure—complemented with financial covenants—provides potential mitigation of idiosyncratic risk.

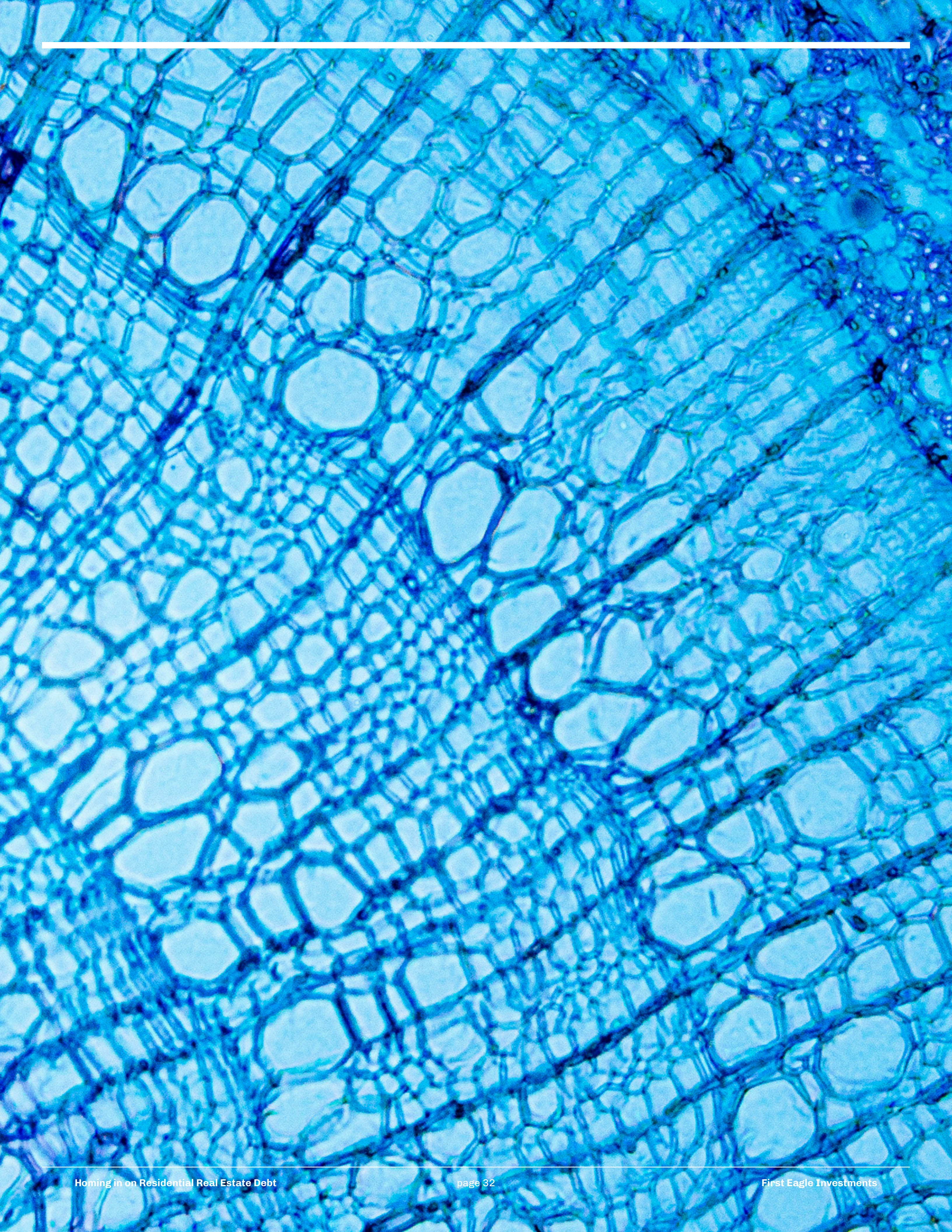
ABL facilities usually focus first and primarily on the collateral available to secure the loan, with all other considerations flowing from there. While the highly structured nature of ABL is a key element of risk management, it is also a double-edged sword; while disciplined underwriting, proper controls and diligent monitoring can mitigate potential loss, the complexity of these tasks can expose inexperienced lenders to considerable risk.

In the final analysis, lending—whether through traditional cash flow loans or ABL facilities—is a collaborative activity, and the all-weather relationships that prove most durable are those that enable borrowers to thrive and grow their companies when conventional sources of capital may be scarce. A lender able to provide flexible financing solutions across credit cycles—without compromising their underwriting standards—may solidify relationships with borrowers and support consistent access to deal flow while driving attractive risk-adjusted returns for their investors.



Homing in on Residential Real Estate Debt

With supply constrained and demand persistent amid high home prices and high mortgage rates, the secular themes supporting the US housing market remain intact. Napier Park's Head of Real Estate Debt Strategies **Rajesh Agarwal** and Managing Director **Tim Ruberti** discuss why they believe the current environment favors private investment opportunities in real estate specialty lending.



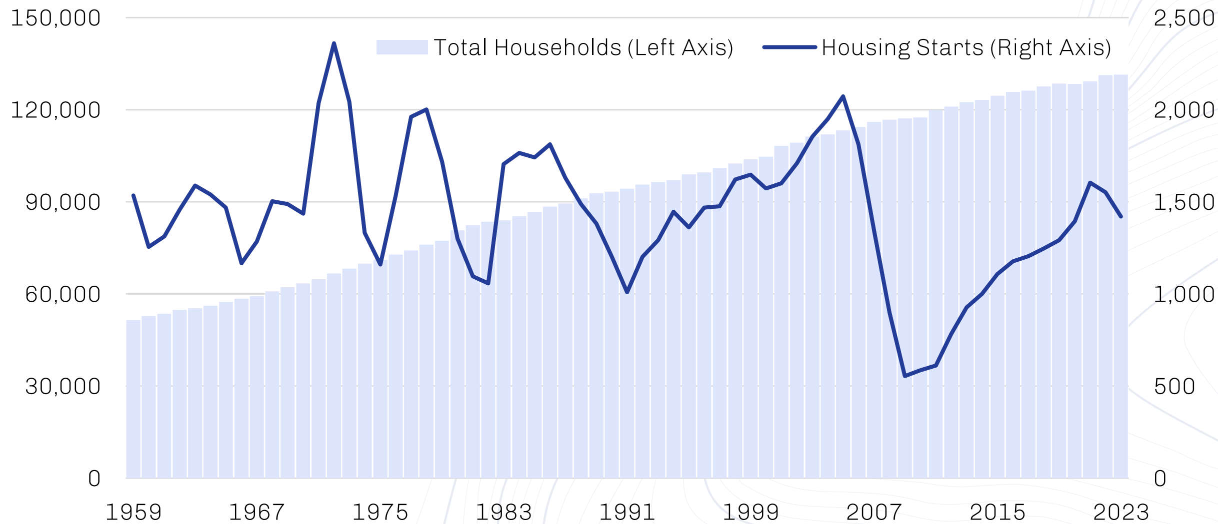
US Residential Real Estate Market Remains Imbalanced

The supply of housing in the US has grown increasingly strained in the years following the global financial crisis, as a credit crunch amid the turmoil of that period prompted a massive decline in housing starts from which the construction industry has yet to fully recover. The demand side of the equation, meanwhile, has been well supported by unabated household formation. As shown in Exhibit 1, the number of US households has doubled since 1970 while housing starts remain stuck at the same level.

> Housing starts have yet to fully recover from the global financial crisis.

Exhibit 1. New Housing Supply Has Lagged Household Formation for Most of This Century

In Thousands, 1959 through 2023



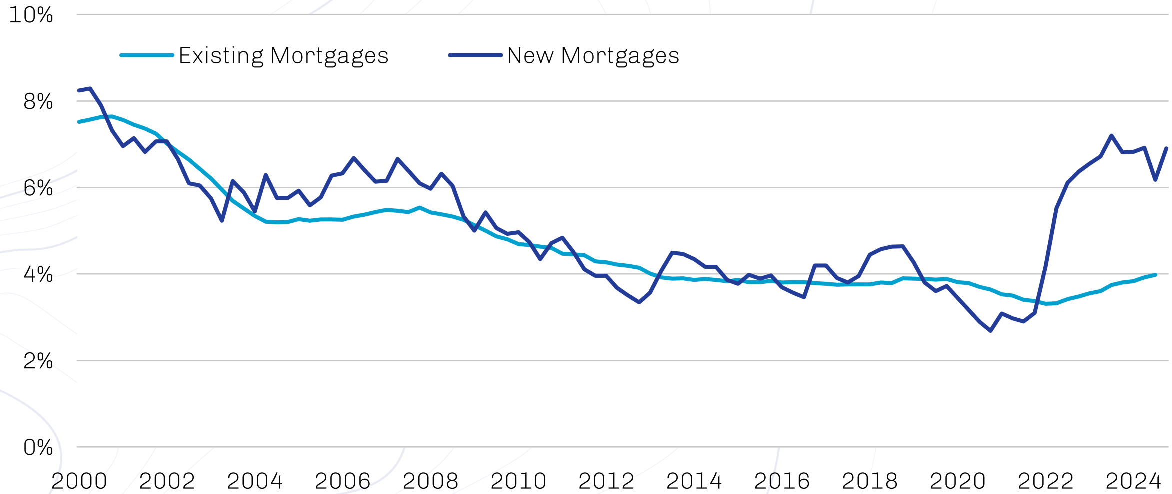
Source: Federal Reserve; data as of December 31, 2023.

The impact of new-home underbuilding has been exacerbated by the limited supply of existing homes for sale. This is primarily due to the “lock-in effect” of the higher mortgage rate regime, as demonstrated in Exhibit 2. Though the 30-year fixed-rate mortgage ended 2024 down from 2023’s peaks, it far exceeds the 4% average on existing mortgages and remains a significant disincentive to sell.[1] This locked-in cohort includes many of the country’s 65 million baby boomers, who account for 36% of homeowner households in the US; a recent survey found that nearly 70% of this group plan to age in place in their current homes.[2]

1. Source: Freddie Mac, National Mortgage Database; data as of December 31, 2024.
2. Source: Freddie Mac; data as of December 19, 2024.

Exhibit 2. Much Higher Interest Rates on New Mortgages Have "Locked In" Current Homeowners

30-Year Fixed-Rate Mortgage Average, January 2000 through December 2024



Source: Morgan Stanley Research, National Association of Realtors, Freddie Mac, US Census Bureau, Bureau of Labor Statistics; data as of December 26, 2024. Reflects latest available data for each series.

Housing demand remains well supported by consumer fundamentals, which, together with a shortage in supply, have buoyed home prices. Household net worth stands at a record high, debt levels remain manageable even off Covid-19-era lows, and indicators of consumer confidence have been biased higher.[3] This is evidenced in Exhibit 3 by Fannie Mae's Home Purchase Sentiment Index, which has reclaimed levels consistent with pre-tightening trends as consumers acclimate to the environment of higher home prices and higher mortgage rates.

Exhibit 3. Consumer Housing Sentiment Has Rebounded from All-Time Lows

Fannie Mae Home Purchase Sentiment Index, December 2019 through December 2024

Source: Fannie Mae; data as of January 7, 2025.

3. Source: Federal Reserve Board of St. Louis; data as of September 30, 2024.

Such acclimation may continue to be necessary. Mortgage rates have been on the rise since the Federal Reserve began cutting its policy rate in September, contrary to what many observers may have expected. This is because mortgage rates are based on long-term Treasury yields, which in turn are impacted by expectations for future short-term interest rates rather than their current levels. Due in large part to persistent inflation, expectations for future rates have been biased higher, pulling long Treasury and mortgage rates along with them.

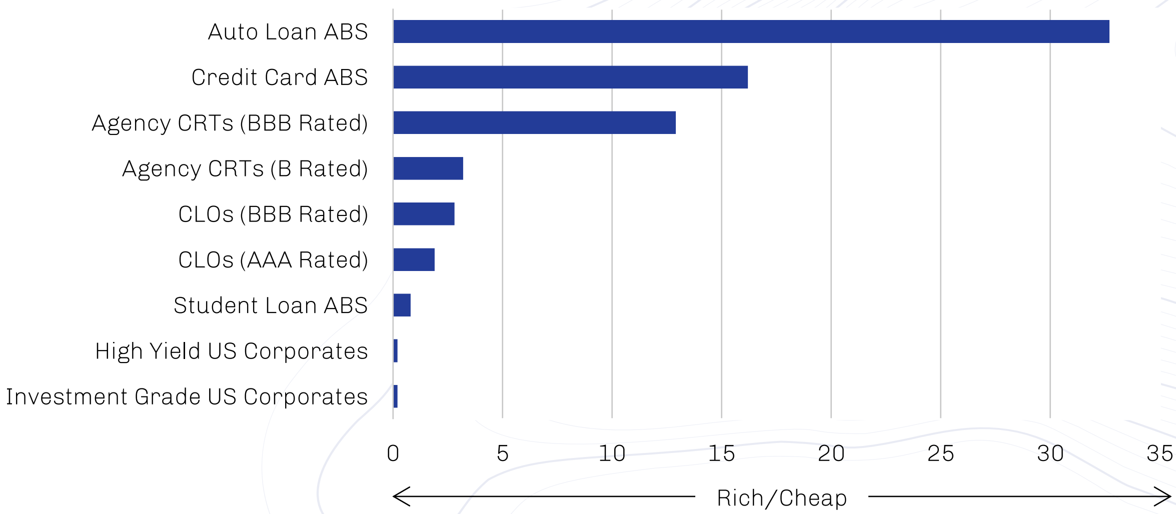
> Though affordability has become challenging, supply is likely to remain the US housing market's main problem.

But while improved affordability could drive additional demand, supply is likely to remain the US housing market's main problem.

Credit Risk Premia in Public Markets Has Shrunk...

The strong performance of credit over the last 18 months has driven spreads for most public securities markets well below their long-term averages. This is particularly true of traditional public fixed income products, which enter 2025 facing the most severe valuation constraints seen in more than two decades, as shown in Exhibit 4.

Exhibit 4. Valuations Are Constrained Across Many Public Credit Segments
Spread Percentile Ranks, January 2010 through December 2024



Note: Auto Loan ABS = ICE BofA AA-BBB US Fixed Rate Automobile ABS Index; Credit Card ABS = ICE BofA AA-BBB US Floating Rate Credit Card ABS Index; Agency CRTs (BBB Rated) and Agency CRTs (B Rated) = Goldman Sachs Global Investment Research calculations using outstanding prices; CLOs (BBB Rated) = Palmer Square CLO BBB Index; CLOs (AAA Rated) = Palmer Square CLO AAA Index; Student Loan ABS = ICE BofA AA-BBB US Floating Rate Student Loan ABS Index; High Yield US Corporates = Bloomberg US Corporate High Yield Index; Investment Grade US Corporates = Bloomberg US Corporate Index.

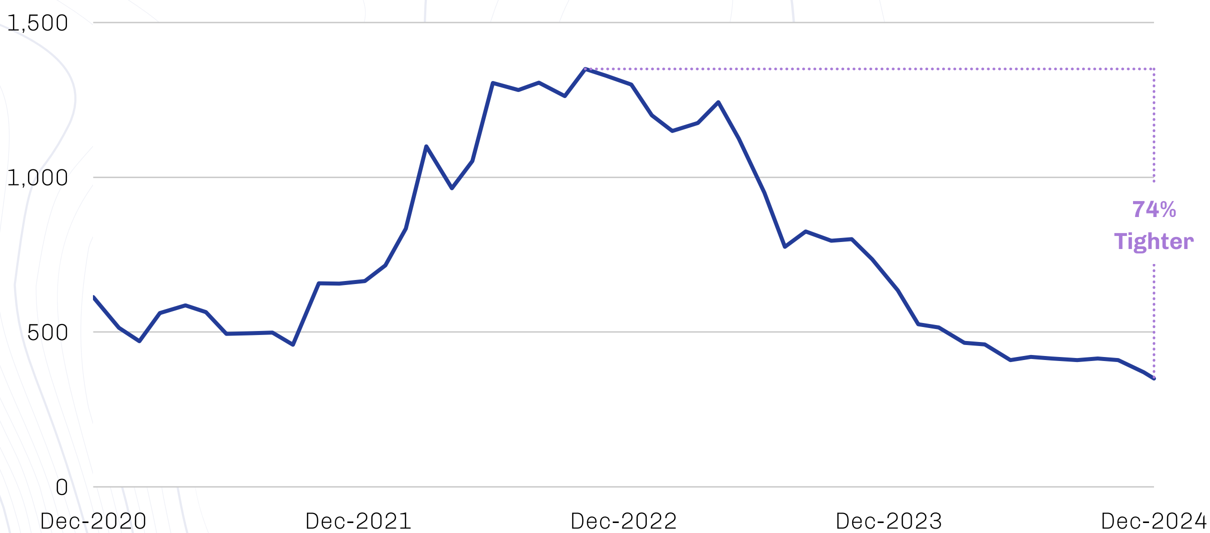
Source: PitchBook | LCD, Goldman Sachs Global Investment Research; data as of December 3, 2024. Index definitions can be found in the back of the book.

There are a range of real estate-backed structured credit products that trade publicly. In addition to the spread pressures felt across the fixed income complex, many of these products have been further squeezed by the "technical" bid for absolute yield as well as the resilient macro backdrop for US residential real estate. Credit risk transfer (CRT) securities—non-guaranteed mortgage-backed securities issued by US government sponsored enterprises Fannie Mae and Freddie Mac—are one such example.

CRTs have been particularly successful of late. CRTs pay a fixed spread over 30-day SOFR (Secured Overnight Financing Rate), which is highly sensitive to changes in the federal funds rate and rose from near zero to well above 5% during the Fed's 2022–23 hiking cycle.[4] At the same time, CRT spreads to SOFR widened significantly on concerns that central bank tightening would trigger a recession and an associated increase in mortgage delinquencies. As a result of higher rates and wider spreads, these securities offered very high yields despite containing attractive structural provisions; through the Covid-19 dislocation, for example, no CRT transaction experienced a loss greater than two basis points.[5] With the US economy proving resilient despite tighter financial conditions, risk appetites soon returned and CRT spreads have tightened by about 1,000 basis points since late 2022, as shown in Exhibit 5. This tightening provided CRT investors with robust returns, but we believe the entry point for these vehicles appears less attractive at current levels.

Exhibit 5. Credit Risk Transfer Spreads Have Tightened Meaningfully Over the Past Two Years

CRT B2 Spread to 30-Day SOFR in Basis Points, December 2020 through December 2024



Source: Citi Research; data as of December 13, 2024.

...but We Believe Opportunities in Private Residential Real Estate Debt Remain Attractive

With public credit spreads near all-time tights entering 2025, the returns on residential mortgage securities like CRTs are likely to be more modest in the months ahead.[6] At this time, we believe there are more attractive opportunities to be found on the private side of the real estate debt market, including residential transitional loans and land banking. Private markets tend to have a delayed and lagged response to changes in lending costs, and their structural complexity and illiquidity typically provide an additional boost to yields. Further, the short durations and robust cash flows typical of these assets enable the frequent reinvestment of proceeds, providing investors optionality to migrate into public credit opportunities should market conditions shift.

4. Source: Federal Reserve Bank of St. Louis; data as of August 31, 2024.
5. Source: Fannie Mae, Freddie Mac and Napier Park; data as of December 31, 2024.
6. Source: ICE Data Indices; data as of January 9, 2025.

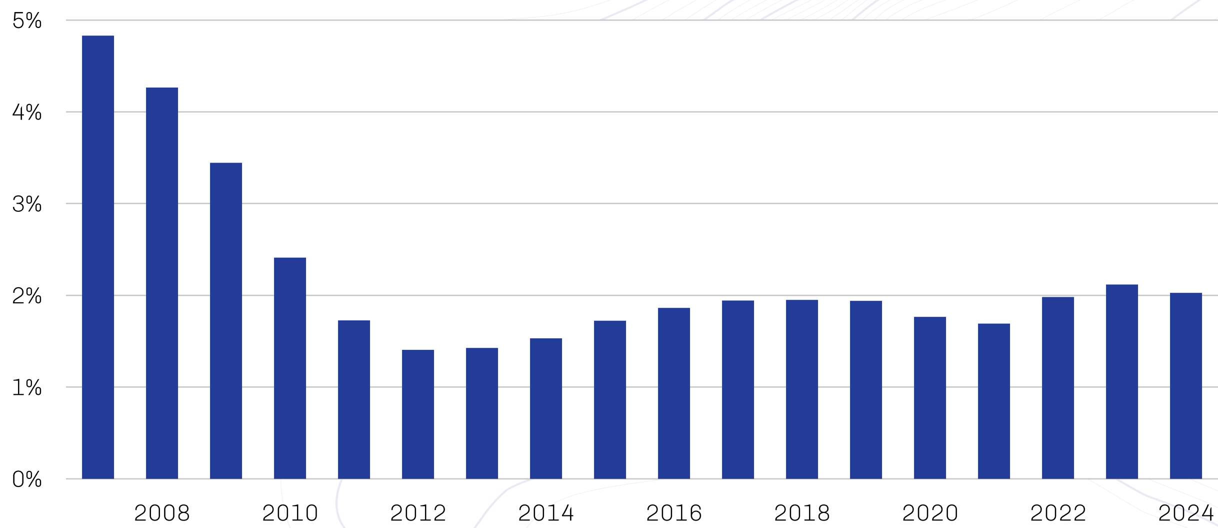
While high home prices and strong demand would seem to be powerful motivators for homebuilders to aggressively fill the housing gap, significant headwinds persist. Notably, rising construction costs have weighed on builders' profit margins and put further upward pressure on home prices. Materials, equipment and labor costs are all up sharply post-Covid, and the price of land has outstripped the rise in housing prices nationally.[7] The explicit and/or implicit costs of regulatory compliance in order to develop buildable lots—which include a range of requirements from zoning approval to permitting to environmental studies—have remained high as well; a study from 2021 found that regulations imposed by all levels of government account for nearly 24% of the final price of a new single-family home.[8]

> Rising construction costs have weighed on builders' profit margins and put further upward pressure on home prices.

Given high costs and lengthy timelines, homebuilders have long relied heavily on credit to finance new construction or the renovation of existing properties for resale. But commercial banks, their traditional source of funding, have pulled back from certain types of real estate activities—including acquisition, development and construction lending—due to regulatory changes enacted in the wake of the global financial crisis. As shown in Exhibit 6, construction loans as a percentage of bank total assets today are less than half of what they were in 2007.

Exhibit 6. Traditional Banks Have Pulled Back from Certain Types of Real Estate Lending

Construction Loans as a Percentage of Total Bank Assets, 2007 through 2024



Source: Federal Deposit Insurance Corporation; data as of December 31, 2024.

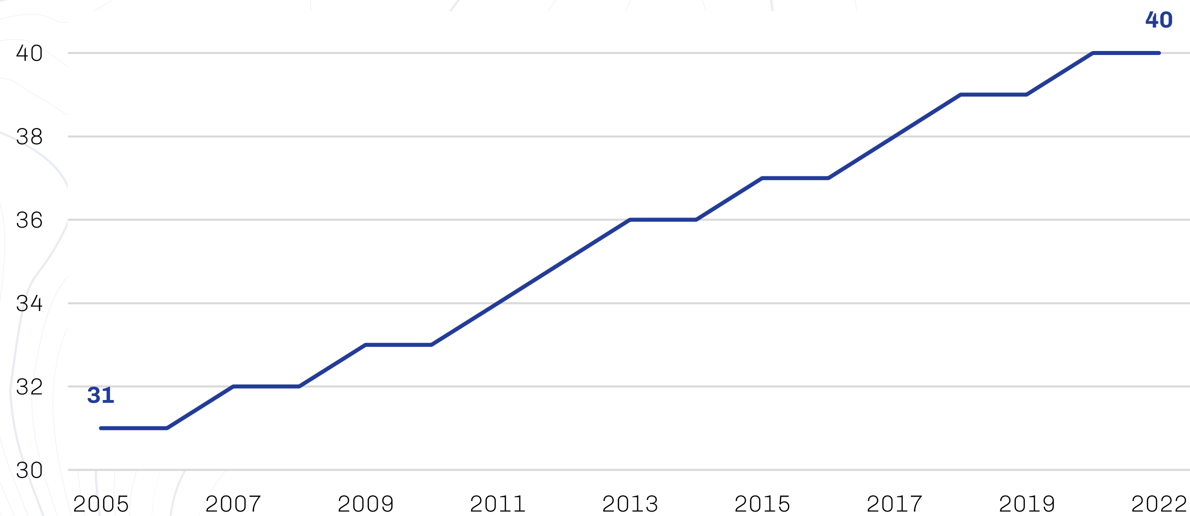
As commercial bank activity has receded, a fragmented collection of specialty lenders have stepped in. The majority of these lenders lack the capital to underwrite and hold these loans at meaningful scale, however, which has presented an opportunity for asset managers to provide necessary liquidity to the real estate industry at attractive terms.

7. Source: Federal Housing Finance Agency; data as of August 6, 2024.
8. Source: National Association of Home Builders; data as of May 5, 2021.

Residential transitional loans are an example of one such opportunity. To many buyers, a refurbished home in an established neighborhood with proven infrastructure like schools, parks and retail is more desirable than a new home in a new area. As could be inferred from the aged state of the US housing stock depicted in Exhibit 7, not every legacy property is in turnkey condition, which has fueled the proliferation of "fix and flip" activity. Real estate developers purchase single-family residences with the intent of renovating and reselling them at a profit within a short period of time. There is a similar dynamic evident in the multifamily space, as existing rental properties are upgraded to standards that can command higher rents.

Exhibit 7. Aged US Housing Stock Fuels Demand for Renovation Capital

Estimates of Median Age in Years of US Owner-Occupied Housing, 2005 through 2022



Note: The Census Bureau did not release the standard American Community Survey in 2020 due to data-collection disruptions experienced during the Covid-19 pandemic.

Source: US Census Bureau, American Community Survey; data as of December 31, 2022. Reflects latest data available.

Residential transitional loans provide the capital for these rehabs. These loans are typically 12 to 18 months in tenor and secured by a first lien on the property, with interest-only payments until the principal is due at maturity. Frequently, these loans are originated by small, regional private lenders focused exclusively on this type of financing and related services. Lacking the scale to hold these loans to maturity, originators often sell them to large, nonbank asset managers looking to build diversified portfolios of residential transitional loans they believe will generate compelling risk-adjusted long-term returns.

Land banking is another area where we see opportunity. The limited supply of buildable land is among the factors constraining the rebound in US new-home construction, a fact often overlooked in a country with a land area in excess of 3.5 million square miles.[9] Beyond the limitations of local zoning laws, the process of preparing raw land for construction—from design to infrastructure build—often takes two years or more as a result of significant local, state and national regulations.[10]

> The process of preparing raw land for construction often takes two years or more.

9. Source: US Census Bureau; data as of December 31, 2024.
10. Source: National Association of Home Builders; data as of May 5, 2021.

This lag can be a challenge for homebuilders trying to maintain robust development pipelines without compromising liquidity and financial flexibility, and many have moved toward "land-light" business models in response. As such, off-balance-sheet financing solutions like land banking—in which a capital provider, in exchange for a fee, acquires and holds property on behalf of a builder that has agreed to purchase lots on the property at a predetermined schedule—have become a staple of builders' land inventory-management strategies. Large public homebuilders, in particular, have demonstrated a willingness to pay a significant premium to the prevailing interest rate on corporate debt for the benefits of such an arrangement.

Staying Nimble Within a Secular Growth Story

While dynamics remain supportive of the US housing market as a whole, we believe current return prospects favor private lending opportunities. However, history has shown that public markets can quickly grow volatile, especially in an environment of tight credit spreads; it would not be surprising to see spreads widen significantly should some sort of near-term dislocation occur. We believe investors able to nimbly adjust their public and private exposures and seize upon unique opportunities as they emerge may be well positioned for success in the residential real estate debt space.

> We believe investors able to nimbly adjust their public and private real estate debt exposures may be well positioned for success.

Breaking Ground in Search of Hidden Gems

After two years of declining net issuance and heavy investor outflows, the municipal bond market began to recover on both fronts in 2024. While the favorable tailwinds that emerged last year may continue in 2025 to support the market broadly, **John Miller**, head and chief investment officer of the High Yield Municipal Credit team, walks a differentiated path. As he discusses, this includes directing the team's underwriting knowledge toward the large, diverse cohort of nonrated municipal bonds.

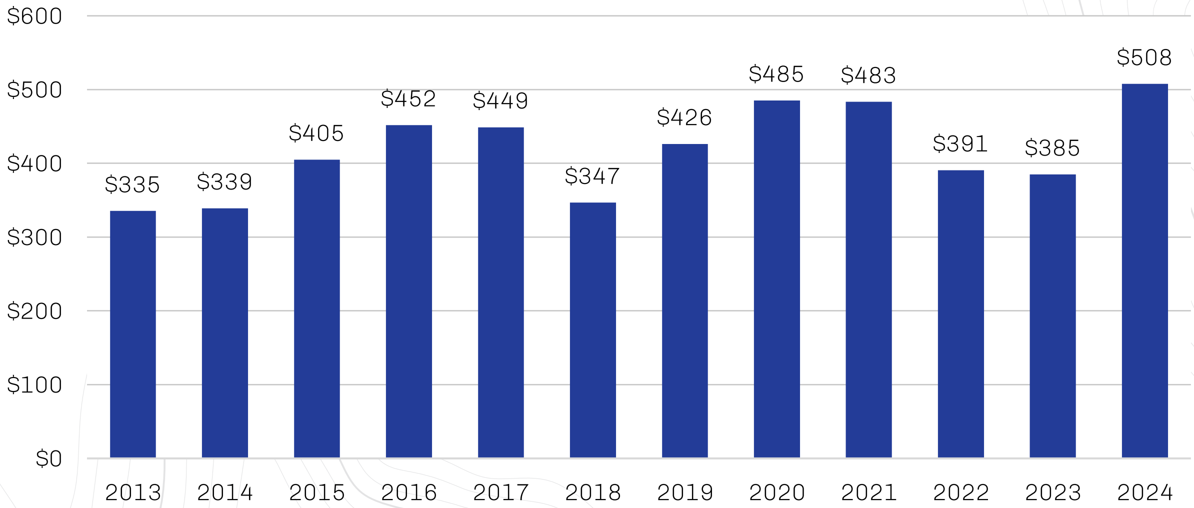
Supportive Muni Dynamics May Continue

As the Federal Reserve steadily raised its policy rate across 2022 and 2023 in the face of decades-high inflation, many state and local municipalities—their coffers generally well stocked thanks to Covid-era federal stimulus and a large post-Covid rebound in tax revenue—curtailed bond issuance in what was a volatile interest rate environment. As shown in Exhibit 1, annual issuance of new muni bonds during the two years of the rate-hike cycle was off about 20% from previous levels. With the Fed on hold and ultimately moving to cut rates in 2024, tax-exempt issuance bounced back to a record high last year, and we believe a healthy level of supply is likely to persist as the benefit of federal support wanes and interest rates continue to moderate.

We believe a healthy level of supply is likely to persist as the benefit of federal support wanes and interest rates continue to moderate.

Exhibit 1. With Interest Rates off Their Peaks, Muni Bond Issuance Recovered in 2024

Annual Municipal Bond Issuance in Billions of US Dollars, 2013 through 2024



Source: Securities Industry and Financial Markets Association; data as of January 2, 2025.

Fed tightening also weighed on the demand side of the muni bond market, as higher yields on cash equivalents like money market funds lured investors away from other, riskier fixed income assets.[1] Investors began to move back into muni mutual funds and ETFs in 2024, but inflows to date remain far from recouping all of the outflows from 2022 and 2023.[2] In our view, the potential for lower interest rates in 2025 may provide durable support for inflows and help absorb renewed muni issuance.

Meanwhile, the fiscal positions of municipalities—unlike that of the US federal government—continue to be strong. The overall amount of municipal bond debt outstanding has not materially changed in the last 20 years; over the same period, total US corporate debt has doubled and federal debt has tripled.[3] Total financial assets for state and local governments are at an all-time nominal high, with notable strength in reserve funds, and expenditures have begun to moderate.[4] Ratings agencies maintain a positive bias toward muni bonds, as upgrades continue to outpace downgrades; moreover, most of the defaults we saw last year were idiosyncratic in nature.[5]

1. Source: Morningstar; data as of October 31, 2024.
2. Source: Investment Company Institute; data as of November 4, 2024.
3. Source: Securities Industry and Financial Markets Association; data as of December 2, 2024.
4. Source: Board of Governors of the Federal Reserve System, US Bureau of Economic Analysis, National Association of State Budget Officers; data as of November 30, 2024.
5. Source: Moody's Investors Service; data as of November 15, 2024.

We believe both technical and fundamental dynamics may continue to be supportive of municipal bonds in 2025. While munis declined in tandem with Treasuries immediately following the outcome of the US presidential election in November, the market reversed shortly thereafter.[6] There has been much rhetoric around potential policy impacts of Trump's victory, but specifics remain to be seen. An extension of the individual taxpayer provisions in 2017's Tax Cuts and Jobs Act seems likely given a unified Republican government, but narrow majorities in the House and Senate mean there are no guarantees. More importantly, ongoing economic growth and labor-market strength is likely to support robust tax revenues and healthy fiscal dynamics for municipalities, as well as high recovery rates in the event of bond defaults. Continued monetary easing—the latest projection from the Fed suggests an additional 50 basis points worth of cuts to the policy rate in 2025, which would bring it to a range of 3.75–4.00%—could provide additional support to muni bonds.[7]

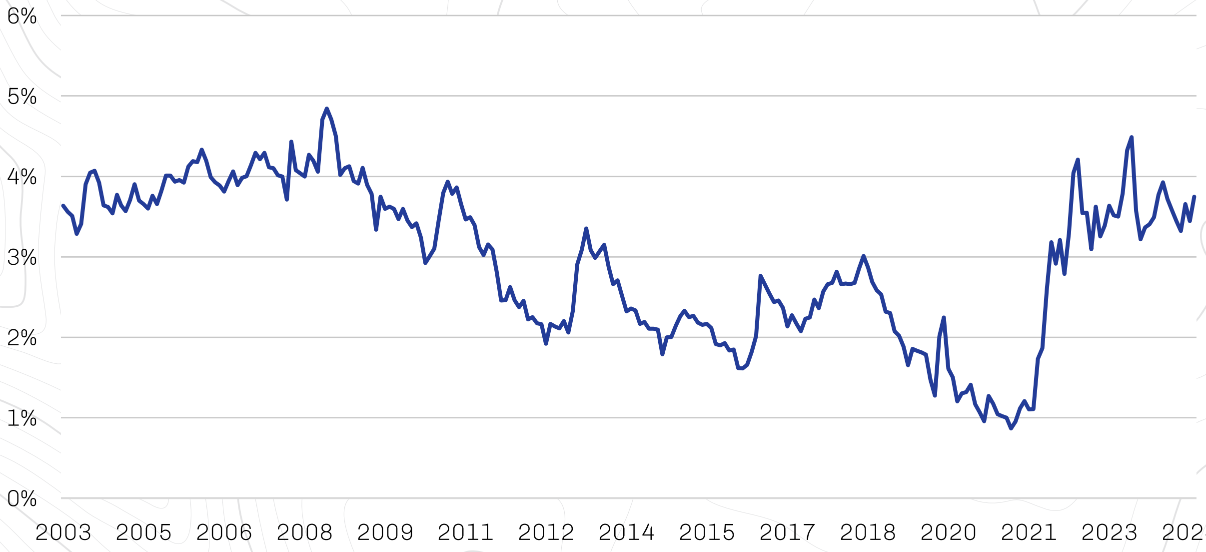
Ongoing economic growth and labor-market strength is likely to support robust tax revenues and healthy fiscal dynamics for municipalities.

Dispersion Brings Opportunity

Though it has pulled back alongside Treasuries, the muni bond market continues to offer investors yields above the historical average, as shown in Exhibit 2. Importantly, however, the fragmentation of the very large muni market results in significant dispersion of yields and prices for similar bonds, particularly lower in the credit-quality spectrum. This is most notable among those bonds not assigned a credit rating by a nationally recognized statistical rating organization (NRSRO)—i.e., unrated bonds. Exhibit 3 depicts the much wider range of yields and prices among unrated bonds within the S&P Municipal Yield Index compared to the AA/Aa2-rated cohort. In our view, this dispersion represents a bountiful hunting ground where active managers can leverage their credit underwriting skills to identify bonds that are undervalued relative to the overall market.

Exhibit 2. Muni Yields Remain Higher than the Historical Average at the Index Level...

Bloomberg Municipal Bond Index Yield to Worst, January 2003 through December 2024



Note: Yield to worst is a financial metric that helps investors assess the minimum yield they can expect from a bond under various scenarios. It accounts for the bond's yield in the worst-case scenario, considering factors like call provisions, prepayments and other features that may affect the bond's cash flows.

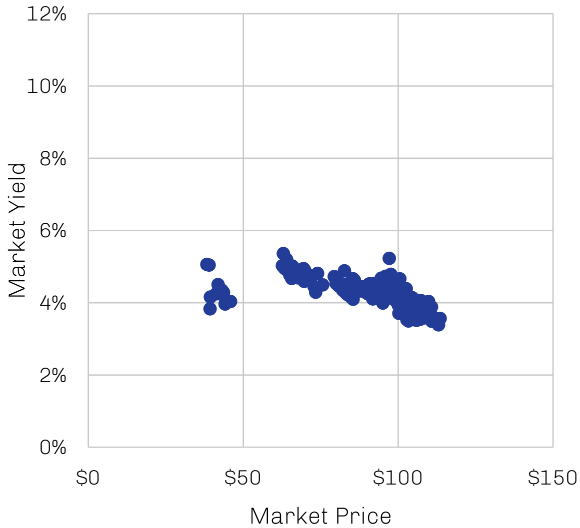
Source: Bloomberg; data as of December 31, 2024.

6. Source: FactSet; data as of December 31, 2024.
7. Source: Federal Reserve; data as of December 18, 2024.

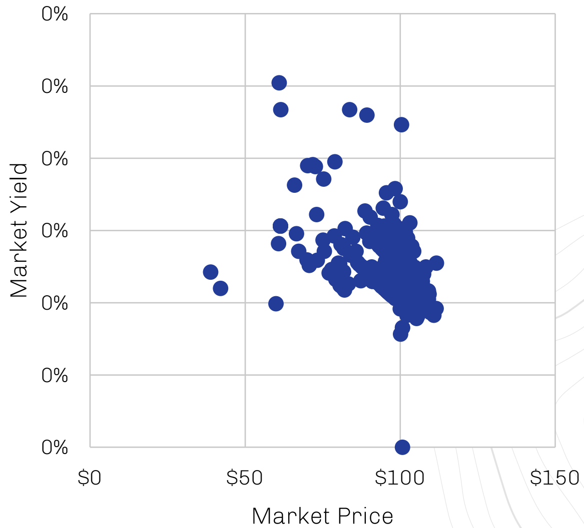
Exhibit 3. ...but Significant Price and Yield Dispersion Exists Among Individual Credits

Comparison of Bonds in the S&P Municipal Yield Index with 2044 Maturities

AA/Aa2 Rated Issues



Unrated Issues



Source: Bloomberg; data as of December 31, 2024.

Unrated ≠ Uninvestable

The High Yield Municipal Credit team's investment philosophy often leads us to areas of our universe where we believe our expertise in credit analysis and security selection gives us an advantage. Unrated bonds—a segment that comprises approximately two-thirds of the S&P Municipal Bond High Yield Index based on number of issues—are a prominent example.[8]

> We don't believe a lack of rating should be interpreted as a reflection of the borrower's capacity to meet its financial commitments.

While unrated bonds have not been subject to the proprietary scrutiny of the likes of Moody's or S&P Global Ratings, we don't believe their lack of rating should be interpreted as a reflection of the borrower's capacity to meet its financial commitments. There are a number of reasons a muni bond may go unrated at the time of issuance, the most straightforward of which is the cost. Issuers must pay a fee to the agency for its rating and also typically incur additional costs associated with preparing information for the agency; small offerings—which are not unusual in the muni space—may not find the expense of achieving a rating worthwhile relative to the proceeds raised.

Though not necessarily riskier than any other muni bonds, the lack of rating lands not-rated bonds in the noninvestment grade bucket. To compensate for greater complexity and information risk involved with these bonds, they typically pay investors a higher yield compared to rated issuers of similar quality; as a result, skilled credit managers may find favorable yields relative to credit quality and default risk.

As an example, let's consider land-secured muni bonds—aka, "dirt bonds". Typically unrated, dirt bonds are issued by a public agency in partnership with a developer to finance infrastructure improvements such as roads, sidewalks and utilities for new residential communities. As the bonds' proceeds fund a capital improvement that provides a public benefit, they typically are issued tax exempt. They are secured by a tax lien assigned to the property that is commonly paid off over a 30-year term through an annual special assessment coequal with property taxes. Development projects can be risky, especially in the early stages, but dirt bonds typically offer

8. Source: S&P Global; data as of December 31, 2024.

yields that we believe more than compensate for these risks compared to other forms of municipal financing, along with structural features that further enhance their appeal.

As the performance of dirt bonds is dependent on the progression of the project being financed and ultimately its sale to end users once developed, underwriting these opportunities entails the analysis of a great number of factors. For example, we would look at the master developer's financial resources and ability to maintain the project through any potential downturns in the real estate market. We would assess the ratio of debt to equity for the project to determine the developer's skin in the game. From a top-down prospective, we evaluate local and national economic trends—such as job growth in the area and prevailing mortgage rates—that may impact the project's success. Finally, we would evaluate the structure of the deal, including any security features or credit enhancements built into the bond indentures.

As these projects progress and begin to generate revenue from a diversified tax base, the bonds may appreciate in price as the risk level recedes. Moreover, upon achieving certain development and revenue milestones, issuers may be able to refinance (or "refund" in muni parlance) the bonds, potentially at a lower interest rate and with an NRSRO rating.

Within this important high yield category, we currently focus much of our attention on Florida, Texas and Utah, where population growth is being fueled by low taxes, above-average job creation and better housing affordability. There continues to be a severe housing shortage across the US because of a structural undersupply of new construction following the global financial crisis. More than one million single-family homes need to be built every year to keep pace with the country's household formation, but commercial homebuilders are falling short.[9] The impact of new-home underbuilding has been exacerbated by the limited supply of existing homes for sale, as the "lock-in effect" of low mortgage rates has disincentivized homeowners from selling. This dynamic also has enabled homebuilders to take share from the resale market; new-home sales now account for more than 30% of all homes sold, double the pre-Covid rate.[10] With new housing developments selling quickly and taxpayers/revenue streams thus diversifying at a similar pace, the credit quality of many dirt bonds has improved.

> Not all speculative bonds are created equal, which highlights why the differentiated risk/reward profile of unrated bonds may offer opportunity.

This improved credit quality also illustrates that not all speculative bonds are created equal and highlights why the differentiated risk/reward profile of unrated bonds may offer opportunity. Further, high yield municipal bonds have a far lower historical default rate than comparable corporate issues. While a typical unsecured corporate bond is backed by nothing other than the issuer's creditworthiness and a contractual obligation to repay, municipal bonds generally include some sort of structural enhancement bolstering their risk profiles. General obligation bonds, for example, are backed by the full faith and credit of the issuing municipality, which includes its taxing power. Revenue bonds are linked to income streams generated by specific projects or public works, such as those generated by a toll road or hospital. All told, speculative-grade municipal bonds had an average trailing-12-month default rate of just under 1% for the period 1970 to 2022 compared to 4% for similarly rated corporates.[11]

9. Source: Freddie Mac; data as of May 15, 2024.
10. Source: US Census Bureau, US Department of Housing and Urban Development, National Association of Realtors; data as of November 26, 2024.
11. Source: Moody's Investors Service; data as of December 31, 2022.

Seeking Resilience in Fertile Ground

While we are constructive on the municipal market as a whole, our investment process takes us to unloved, overlooked or contrarian areas of the market where we believe fundamental, research-driven investment managers may be able to uncover particularly attractive opportunities. With about $4 trillion distributed across more than one million distinct municipal bonds and 50,000 issuers, the highly fragmented municipal bond market is subject to significant yield dispersion among its constituents, particularly those without ratings.[12] We believe this dispersion offers rigorous, fundamental credit managers an opportunity to source bonds whose yields and prices more than adequately compensate for the credit risk involved.

> We believe the dispersion of the highly fragmented bond market offers rigorous, fundamental credit managers an opportunity to source bonds whose yields and prices more than adequately compensate for the credit risk involved.

12. Source: Securities Industry and Financial Markets Association; data as of December 2, 2024.

About Us

Disciplined, unconventional thinking. Global perspective. Long-term alignment.

First Eagle Investments is an independent, privately owned asset management firm dedicated to serving the investment needs of individuals and institutions worldwide. With a heritage dating back to 1864, First Eagle seeks to help clients avoid the permanent impairment of capital. Our active, absolute return-oriented portfolios are rooted in fundamental research and strive to generate strong real returns over time while attempting to mitigate downside risk. We offer a range of equity and equity-oriented, public and private credit, multi-asset and alternative strategies that are distinguished by disciplined, unconventional thinking, a global perspective and the long-term alignment of interests.

$149B
in assets under management†

Private and independent* asset management firm with a heritage that dates back to
1864

626
employees, including 154 investment professionals

9
offices globally, with headquarters in New York

Seeking to Preserve Wealth since 1864

1864
Gebr. Arnhold (Arnhold Brothers) founded in Dresden
The firm financed a range of local businesses, including brewers.

1931
Arnhold and S. Bleichroeder formed in Berlin
The combination of two storied banks created one of the leading merchant and investment banks in Europe.

1937
All business activities moved to New York City
Faced by the realities of a deteriorating global political and economic environment, the firm relocated to New York.

1995
Became an SEC-registered investment adviser

1999
Acquired majority share of Société Générale Asset Management Corp.

2002
Sold investment banking and global securities businesses
The firm now focused exclusively on investment management.

2009
Renamed First Eagle Investment Management

2015
Private equity funds managed by Blackstone Inc. and Corsair Capital invested in the firm
The long-term investment of these companies ensured a continuation of First Eagle's investment culture and philosophy.

2020
Acquired alternative credit manager THL Credit, forming Alternative Credit team
Acquisition bolstered First Eagle's position as one of the leading managers of broadly syndicated loan and direct-lending strategies.

2021
Established Small Cap team
Experienced team brought a time-tested, opportunistic approach to active management in a particularly inefficient market.
Rebranded as First Eagle Investments

Source: First Eagle Investments; data as of September 30, 2024.
† The total AUM represents the combined AUM of (i) First Eagle Investment Management, LLC, (ii) its subsidiary investment advisers, First Eagle Separate Account Management, LLC, First Eagle Alternative Credit ("FEAC") and Napier Park Global Capital ("Napier Park"), and (iii) Regatta Loan Management LLC, an advisory affiliate of Napier Park. The total AUM includes $0.9 billion of committed and other non-fee-paying capital from FEAC and $2.0 billion of committed and other non-fee-paying capital from Napier Park.
* Private equity funds indirectly controlled by Blackstone Inc. and Corsair Capital LLC, as well as certain co-investors, indirectly own a majority stake in First Eagle Investment Management, LLC.

While 2024 was a strong year across most asset classes, uncertainty remains a dominant theme in the investment management industry. Amid an increasingly complex investment backdrop, we remain committed to putting clients first and embarked on several new initiatives designed to meet their evolving needs.

We began 2024 with the introduction of our new High Yield Municipal Credit team, whose strategies have attracted $5 billion in investor assets to date as we bolstered the team's credit research capabilities and distribution support throughout the year.[1] In December, we entered the actively managed exchange-traded fund (ETF) space with two new offerings, further diversifying our lineup of mutual funds, private funds, separately managed accounts, interval funds, a business development company, collective investment trusts, collateralized loan obligations and UCITS funds. We also introduced a new private credit strategy focused on lower middle market direct lending for non-US investors through our exclusive distribution partner.

Our leadership structure also continued to evolve, reflecting our ongoing commitment to strong governance and organizational agility. At year end, we bid farewell to Chris Flynn, whose leadership transformed FEAC into a premier alternative credit platform. Chris co-led FEAC with Chief Investment Officer Jim Fellows throughout 2024 to ensure a smooth leadership transition, and Jim has now assumed the role of president of FEAC. Bob Hickey stepped into Jim's chief investment officer role across FEAC's investment platforms, and Michelle Handy continues to serve as chief investment officer of its Direct Landing platform. In September, we welcomed Michael Constantino as First Eagle's new chief financial officer to help advance our strategic objectives.

First Eagle remains dedicated to positively impacting the communities where we live, work and invest. Financial literacy continued to be a cornerstone of our Corporate Social Responsibility initiatives, and in 2024 we partnered with the Council for Economic Education's FinEd50 coalition to advance financial education and literacy for students across the US. We also continued to focus on educating, empowering and developing the next generation of diverse leaders. We were honored by the Posse Foundation at its New York Power of 10 event and became a gold sponsor of the Association of Asian American Investment Managers. We expanded our annual "Season of Giving" in our New York, Boston and Chicago offices, featuring activities such as administering career panels for teens, granting holiday wishes to underprivileged children, coat drives, preparing care packages and hosting events for gift recipients.

First Eagle strives to cultivate a high-performance culture that attracts, develops and retains a talented, inclusive workforce. We were pleased to again be named among the "Best Places to Work in Money Management" by *Pensions & Investments* for the second consecutive year.[2] Our colleagues—626 strong at the end of the third quarter, up from 612 last year—remain our most valuable asset. We believe our holistic approach to human capital management positions them to do their life's best work on behalf of our clients. To support their growth, we launched First Eagle University to enhance learning and professional growth while also expanding existing programs, such as the employee-led Engagement and Inclusion Council and the leadership training program with Columbia Business School. We also enhanced our benefits programs to support of our colleagues' lives outside of the office.

2022

Acquired Napier Park

Acquisition of $19.5 billion global alternative credit manager significantly broadened our capabilities in the space.

2023

Established High Yield Municipal Credit team

Unique risk/return profile of the asset class broadened our range of differentiated investment solutions and complemented our existing capabilities.

2024

Launched Active ETFs

Offering expanded access to the Global Value team's platform through a flexible, cost-efficient structure.

1. Source: First Eagle Investments; data as of December 31, 2024.
2. Any published third-party rankings, awards or similar groupings have inherent limitations and qualifications, and are not indicative of the experience of any client or investor or of the future performance of any product described herein. **Unless otherwise specified, all awards shown are based on the one-year period immediately preceding the date listed.** First Eagle pays a licensing fee for the right to disclose this information.

In our annual tradition, we asked our colleagues a few questions about their lives outside the office. Here is a selection of their responses:

What’s your favorite way to unwind after a hectic day?

“Reading to my two-year-old daughter.”

Marty Loew
First Eagle Alternative Credit

Carl Katerndahl
High Yield Municipal Credit

“Playing padel tennis.”

“Watching *Jeopardy!* with the whole family.”

Idanna Appio
Global Value

Christian Heck
Global Value

“Going to the gym followed by reading a good book.”

“Spending time with my kids—as counterintuitive to “unwind” as that may sound.”

Joe Henrici
First Eagle Alternative Credit

Bill Hench
Small Cap

“I am lucky to be able to walk home from the office; the 24-block stroll is a great way to decompress.”

“I really enjoy a nice sunset walk after work to refresh.”

Stephen McCall
Napier Park

What's your favorite way to spend a weekend?

"Being as active as possible—running, boxing, reading, spending time with friends or trying new restaurants."

Tina Alhani
First Eagle Alternative Credit

Bridget Young
High Yield Municipal Credit

"Taking my daughter to do all her favorite things."

"Going to the beach with my family."

Ross Sylvester
Napier Park

Joseph Dargan
Global Value

"Getting out in the fresh air."

"I've been trying to cook something new for dinner every Sunday, which has been a fun creative outlet."

Jacqueline Crawford
Napier Park

What do you wish you had more time to do?

Elle Sisco
Napier Park

"Travel more with my sisters. We have a tradition of an annual long weekend trip to Europe, and I would love to do more of those!"

"Go to my ranch."

Suzanne Franks
Small Cap

Purva Patel
High Yield Municipal Credit

"Give back to my community by volunteering for a charity or a good cause."

"Mountain climbing."

Adam Mielnik
Small Cap

John Suh
High Yield Municipal Credit

"Everything."

Is there a particular philosophy that guides your decision making?

“Our greatest glory is not in never falling, but in rising every time we fall.”

Ryan McKenna
First Eagle Alternative Credit

Benjamin Bahr
Global Value

“The Golden Rule seems to hold up well.”

“Generosity is the cure for greed.”

Aaron Kirsch
First Eagle Alternative Credit

George Ross
Global Value

“As the Stoics said, focus your actions on things you can control and don’t worry about the rest—and avoid social media!”

“Don’t get lost in your biases and bubbles. Acknowledge them, then actively seek to challenge them so you can develop conviction in your views.”

Joe Riggi
Napier Park

Daniel Schwarz
First Eagle Alternative Credit

“Carpe diem!”

“I’ve always loved this Viktor Frankl quote: “What is to give light must endure burning.””

John Masi
Global Value

Doug Johnston
High Yield Municipal Credit

“Keep going, keep growing. (My wife told me that.)”

The opinions expressed are not necessarily those of the firm. **These materials are provided for informational purposes only.** These opinions are not intended to be a forecast of future events, a guarantee of future results, or investment advice. Any statistics contained herein have been obtained from sources believed to be reliable, but the accuracy of this information cannot be guaranteed. The views expressed herein may change at any time subsequent to the date of issue hereof. The information provided is not to be construed as a recommendation to buy, hold or sell or the solicitation or an offer to buy or sell any fund or security.

Past performance is not indicative of future results.

Risk Disclosures

All investments involve the risk of loss of principal.

There are risks associated with investing in securities of foreign countries, such as erratic market conditions, economic and political instability and fluctuations in currency exchange rates.

A principal risk of investing in value stocks is that the price of the security may not approach its anticipated value or may decline in value. "Value" investments as a category, or entire industries or sectors associated with such investments, may lose favor with investors as compared to those that are more "growth" oriented.

The value and liquidity of portfolio holdings may fluctuate in response to events specific to the companies or markets, as well as economic, political or social events in the US or abroad. During periods of market volatility, the value of individual securities and other investments at times may decline significantly and rapidly. The securities of small and micro-size companies can be more volatile in price than those of larger companies and may be more difficult or expensive to trade.

There are risks associated with investing in foreign investments (including depositary receipts). Foreign investments, which can be denominated in foreign currencies, are susceptible to less politically, economically and socially stable environments; fluctuations in the value of foreign currency and exchange rates; and adverse changes to government regulations.

Investment in gold and gold-related investments present certain risks, including political and economic risks affecting the price of gold and other precious metals, like changes in US or foreign tax, currency or mining laws; increased environmental costs; international monetary and political policies; economic conditions within an individual country; trade imbalances; and trade or currency restrictions between countries. The price of gold, in turn, is likely to affect the market prices of securities of companies mining or processing gold and, accordingly, the value of investments in such securities may also be affected. Gold-related investments as a group have not performed as well as the stock market in general during periods when the US dollar is strong, inflation is low and general economic conditions are stable. In addition, returns on gold-related investments have traditionally been more volatile than investments in broader equity or debt markets. Investment in gold and gold-related investments may be speculative and may be subject to greater price volatility than investments in other assets and types of companies.

Municipal bonds are subject to credit risk, interest rate risk, liquidity risk and call risk. However, the obligations of some municipal issuers may not be enforceable through the exercise of traditional creditors' rights. The reorganization under federal bankruptcy laws of a municipal bond issuer may result in the bonds being cancelled without payment or repaid only in part or in delays in collecting principal and interest.

The information is not intended to provide and should not be relied on for accounting or tax advice. Any tax information presented is not intended to constitute an analysis of all tax considerations.

Diversification does not guarantee investment returns and does not eliminate the risk of loss.

Alternative Investment Risks

Alternative investments can be speculative and are not suitable for all investors. Investing in alternative investments is only intended for experienced and sophisticated investors who are willing and able to bear the high economic risks associated with such an investment. Investors should carefully review and consider potential risks before investing. Certain of these risks include:

- Loss of all or a substantial portion of the investment;
- Lack of liquidity in that there may be no secondary market or interest in the strategy and none is expected to develop;
- Volatility of returns;
- Interest rate risk;
- Restrictions on transferring interests in a private investment strategy;
- Potential lack of diversification and resulting higher risk due to concentration within one or more sectors, industries, countries or regions;
- Absence of information regarding valuations and pricing;
- Complex tax structures and delays in tax reporting;
- Less regulation and higher fees than mutual funds;
- Use of leverage, which magnifies the potential for gain or loss on amounts invested and is generally considered a speculative investment technique and increases the risks associated with investing in the strategy;
- Carried interest, which may cause the strategy to make more speculative, higher-risk investments than would be the case in absence of such arrangements; and
- Below investment grade loans, which may default and adversely affect returns.

Indexes are unmanaged and one cannot invest directly in an index.

Bloomberg Municipal Bond Index (Gross/Total) measures the performance of the US municipal tax-exempt investment grade bond market. A total-return index tracks price changes and reinvestment of distribution income.

Bloomberg US Aggregate Bond Index (Gross/Total) measures the performance of the investment grade, US dollar-denominated, fixed-rate taxable bond market in the US, including Treasuries, government-related and corporate securities, fixed-rate agency MBS (agency fixed-rate and hybrid ARM passthroughs), ABS and CMBS. A total-return index tracks price changes and reinvestment of distribution income.

Bloomberg US Corporate Bond Index (Gross/Total) measures the performance of investment grade, fixed-rate, taxable corporate bond market. It includes US dollar denominated securities publicly issued by US and non-US industrial, utility and financial issuers. A total-return index tracks price changes and reinvestment of distribution income.

Bloomberg US Corporate High Yield Bond Index (Gross/Total) measures the US dollar-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below. A total-return index tracks price changes and reinvestment of distribution income.

Cliffwater Direct Lending Index (Gross/Total) is an asset-weighted index of US middle-market direct loans. A total-return index tracks price changes and reinvestment of distribution income.

Consumer price index (CPI) (Price) measures inflation as experienced by consumers in their day-to-day living expenses by capturing the average change over time in the prices paid for a representative basket of consumer goods and services. A price-return index only measures price changes.

Fannie Mae Home Purchase Sentiment Index distills consumer responses to Fannie Mae's monthly National Housing Survey into a single indicator designed to provide signals on future housing outcomes.

ICE BofA AA-BBB US Fixed Rate Automobile ABS Index (Gross/Total) measures the performance of asset-backed securities collateralized by automobile loans with a middle rating in a range of AA/Aa to BBB/Baa as measured Moody's, Fitch and S&P. A total-return index tracks price changes and reinvestment of distribution income.

ICE BofA AA-BBB US Floating Rate Credit Card ABS Index (Gross/Total) measures the performance of asset-backed securities collateralized by credit card loans with a middle rating in a range of AA/Aa to BBB/Baa as measured Moody's, Fitch and S&P. A total-return index tracks price changes and reinvestment of distribution income.

ICE BofA AA-BBB US Floating Rate Student Loan ABS Index (Gross/Total) measures the performance of asset-backed securities collateralized by student loans with a middle rating in a range of AA/Aa to BBB/Baa as measured Moody's, Fitch and S&P. A total-return index tracks price changes and reinvestment of distribution income.

ICE BofA Current 10-Year US Treasury Index (Gross/Total) measures the performance of US Treasury securities with a remaining maturity exceeding seven years and less than or equal to 10 years. A total-return index tracks price changes and reinvestment of distribution income.

Morningstar LSTA US Leveraged Loan Index (Gross/Total) is a market value-weighted index that measures the performance of the US leveraged loan market. A total-return index tracks price changes and reinvestment of distribution income.

MSCI China Index (Net) measures the performance of large and midcap representation across China A shares, H shares, B shares, Red chips, P chips and foreign listings. A net-return index tracks price changes and reinvestment of distribution income net of withholding taxes.

MSCI World Index (Net) measures the performance of large and midcap equities across developed markets. A net-return index tracks price changes and reinvestment of distribution income net of withholding taxes.

Palmer Square CLO AAA Index (Gross/Total) is a subindex of the Palmer Square CLO Debt Index that tracks only CLOs originally rated AAA. A total-return index tracks price changes and reinvestment of distribution income.

Palmer Square CLO BBB Index (Gross/Total) is a subindex of the Palmer Square CLO Debt Index that tracks only CLOs originally rated BBB. A total-return index tracks price changes and reinvestment of distribution income.

Russell 2000® Index (Gross/Total) measures the performance of the small cap segment of the US equity universe. It includes approximately 2,000 of the smallest securities based on a combination of their market cap and current index membership. A total-return index tracks price changes and reinvestment of distribution income.

S&P 500 Index (Gross/Total) measures the performance of 500 of the top companies in the leading industries of the US economy and is widely recognized as a proxy for the US market as a whole. A total-return index tracks price changes and reinvestment of distribution income.

S&P Municipal Bond High Yield Index (Gross/Total) measures the performance of bonds in the S&P Municipal Bond Index that are not rated or whose ratings are below investment grade. A total-return index tracks price changes and reinvestment of distribution income.

S&P Municipal Yield Index (Gross/Total) measures the performance of high yield and investment grade municipal bonds. A total-return index tracks price changes and reinvestment of distribution income.

Definitions

A **10-year Treasury note** is a debt obligation of the US government with a maturity of 10 years upon issuance.

AA credit rating—as used by S&P Global Ratings and Fitch Ratings—is an investment grade rating on a bond considered to have a very strong capacity to meet its financial commitments. The equivalent rating from Moody's Investors Service is Aa.

AAA credit rating—as used by S&P Global Ratings and Fitch Ratings—is an investment grade rating on a bond considered to have an extremely strong capacity to meet its financial commitments. The equivalent rating from Moody's Investors Service is Aaa.

Asset-based lending (ABL) is corporate borrowing supported by specific assets of the borrower rather than its cash flows.

BBB credit rating—as used by S&P Global Ratings and Fitch Ratings—is an investment grade rating on a bond considered to have adequate capacity to meet its financial commitments but that is more susceptible to adverse business, financial and economic conditions. The equivalent rating from Moody's Investors Service is Baa.

Beta is a measure of an investment's price volatility relative to that of the overall market.

A **bull market** is generally defined as a period during which a securities market index rises by 20% or more.

A **business development company** is a closed-end investment vehicle that invests in early stage and/or distressed small and medium-sized companies.

Collateralized loan obligations (CLO) are financial instruments collateralized by a pool of corporate loans.

Collective investment funds (CIFs), also known as collective investment trusts (CITs), are bank-administered trusts that hold commingled assets.

A **credit rating** is an assessment provided by a nationally recognized statistical rating organization (NRSRO) of the creditworthiness of an issuer with respect to debt obligations, including specific securities, money market instruments or other bonds. Ratings are measured on a scale that generally ranges from AAA/Aaa (highest) to D/RD (lowest); ratings are subject to change without notice. Not rated (NR) indicates that the debtor was not rated and should not be interpreted as indicating low quality.

Credit-risk transfer (CRT) securities are synthetic securitizations that reference the credit risk of a designated group of mortgage loans guaranteed by Fannie Mae or Freddie Mac.

Currency debasement refers to the reduction of a currency's purchasing power.

Direct lending refers to a loan agreement between a borrower and single lender or small group of lenders. Direct lending can also be referred to as "private credit" or "private lending."

Exchange-traded funds (ETFs) are listed investment vehicles that seek to provide exposure to a benchmark, index or actively managed strategy.

Federal funds rate is the interest rate at which depository institutions (banks and credit unions) lend reserve balances to other depository institutions overnight on an uncollateralized basis.

General obligation bonds are municipal securities in which payments are backed by the full faith and credit of the issuer and by extension its ability to tax its residents.

A **Goldilocks** economic scenario refers to a level of growth that is neither strong enough to promote inflation pressures nor weak enough to suggest recession may be near.

Government-sponsored enterprises (GSEs) were established and chartered by the US federal government for public policy purposes. They are private companies, and their securities are not backed by the full faith and credit of the federal government.

High yield municipal bonds are debt securities issued by states, cities, counties and other public entities that offer a higher rate of interest due to their perceived higher risk of default.

An **interval fund** is a pooled investment vehicle that offers investors periodic liquidity at an interval specified in its prospectus.

Moody's Investors Service is a nationally recognized statistical rating organization (NRSRO) of the creditworthiness of an issuer with respect to debt obligations, including specific securities, money market instruments or other bonds. Ratings are measured on a scale that generally ranges from Aaa (highest) to RD (lowest); ratings are subject to change without notice.

Mortgage-backed securities (MBS) are debt securities whose payments of principal and interest are backed by the cash flow generated by pools of mortgage loans.

Net orderly liquidation value (NOLV) is the estimated proceeds from selling a borrower's collateral assets in an orderly manner, including a reasonable amount of time to find a buyer, after all costs related to the sale.

Not rated (NR) indicates that the debtor was not rated and should not be interpreted as indicating low quality.

A **private fund** is a pooled investment vehicle that is not required to be registered or regulated as an investment company under the Investment Company Act of 1940, as amended.

Revenue bonds are municipal securities whose payments are backed not by a government's taxing power but by revenues from a specific project or source, such as highway tolls or lease fees.

Secured Overnight Financing Rate (SOFR) is a broad measure of the cost of borrowing cash overnight collateralized by Treasury securities.

A **separately managed account (SMA)** is a portfolio of securities that is managed by a professional investment firm.

A **soft landing** refers to a gradual economic slowdown that comes to an end without triggering a recession.

Sovereign debt refers to debt obligations issued by a country's government as a means to borrow capital.

S&P Global Ratings is a nationally recognized statistical rating organization (NRSRO) of the creditworthiness of an issuer with respect to debt obligations, including specific securities, money market instruments, or other bonds. Ratings are measured on a scale that generally ranges from AAA (highest) to D (lowest); ratings are subject to change without notice.

A **tranche** is a portion of a security issue with its own unique risk/reward characteristics and credit rating.

Undertakings for Collective Investment in Transferable Securities (UCITs) are pooled investment vehicles registered in countries in the European Union.

Volatility represents the degree to which an investment's price has deviated from its average over time.

A **yield curve** is a graphical representation of interest rates on debt of equal credit quality across a range of maturities.

FEF Distributors, LLC (“FEFD”) (SIPC), a limited purpose broker-dealer, distributes certain First Eagle products. FEFD does not provide services to any investor, but rather provides services to its First Eagle affiliates. As such, when FEFD presents a fund, strategy or other product to a prospective investor, FEFD and its representatives do not determine whether an investment in the fund, strategy or other product is in the best interests of, or is otherwise beneficial or suitable for, the investor. No statement by FEFD should be construed as a recommendation. Investors should exercise their own judgment and/or consult with a financial professional to determine whether it is advisable for the investor to invest in any First Eagle fund, strategy, or product.

Important Information for Non-US Residents

This material and the information contained herein is provided for informational purposes only, do not constitute and is not intended to constitute an offer of securities, and accordingly should not be construed as such. Any funds or other products or services referenced in this material may not be licensed in all jurisdictions and unless otherwise indicated, no regulator or government authority has reviewed this material or the merits of the products and services referenced herein. This material and the information contained herein has been made available in accordance with the restrictions and/or limitations implemented by any applicable laws and regulations. This material is directed at and intended for institutional investors (as such term is defined in any applicable jurisdiction). This material is provided on a confidential basis for informational purposes only and may not be reproduced in any form. This material is for general information only and is not intended as investment advice or any other specific recommendation as to any particular course of action or inaction. The information in this material does not take into account the specific investment objectives, financial situation, tax situation or particular needs of the recipient. Before acting on any information in this material, prospective investors should inform themselves of and observe all applicable laws, rules and regulations of any relevant jurisdictions and obtain independent advice if required. This material is for the use of the named addressee only and should not be given, forwarded or shown to any other person (other than employees, agents or consultants in connection with the addressee’s consideration thereof).

Important Information for Residents in the Abu Dhabi Global Market (ADGM)

This material constitutes an Exempt Communication or is not otherwise subject to the financial promotion restriction in accordance with the Financial Services and Markets Regulation of the ADGM. It must not be delivered to, or relied on by, any other person. The ADGM does not accept any responsibility for the content of the information included in this material, including the accuracy or completeness of such information. The ADGM has also not assessed the suitability of the products or services to which this material relates to any particular investor or type of investor. If you do not understand the contents of this material or are unsure whether the products or services to which this material relates are suitable for your individual investment objectives and circumstances, you should consult an authorised financial adviser.

Important Information for Residents of Australia

This communication is exclusively directed and intended for wholesale clients (as such term is defined in Australian Corporations Act 2001 (Cth) only and, by receiving it, each prospective investor is deemed to represent and warrant that it is a wholesale client. The information contained herein is provided for informational purposes only and should not be considered a solicitation or offering of investment services, nor a solicitation to sell or buy any shares of any securities (nor shall any such securities be offered or sold to any person) in any jurisdiction where such solicitation or offering would be unlawful under the applicable laws of such jurisdiction. Unless otherwise indicated, no regulator or government authority has reviewed this material or the merits of the products and services referenced herein. This material and the information contained herein has been made available in accordance with the restrictions and/or limitations implemented by any applicable laws and regulations. This material is provided on a confidential basis for informational purposes only and may not be reproduced in any form. Before acting on any information in this material, prospective investors should inform themselves of and observe all applicable laws, rules and regulations of any relevant jurisdictions and obtain independent advice if required. This material should not be relied upon as investment advice and is not a recommendation to adopt any investment strategy. This material is for the use of the named addressee only and should not be given, forwarded or shown to any other person (other than employees, agents or consultants in connection with the addressee’s consideration thereof). First Eagle Investment Management, LLC is exempt from the requirement to hold an Australian financial services licence under the Corporations Act 2001 (Cth) in respect of the financial services it provides to wholesale clients in Australia and is regulated by the US Securities and Exchange Commission under US laws, which differ from Australian laws.

Important Information for Residents of Brazil

First Eagle Investment Management, LLC is not accredited with the Brazilian Securities Commission - CVM to perform investment management services. The investment management services may not be publicly offered or sold to the public in Brazil. Documents relating to the investment management services as well as the information contained therein may not be supplied to the public in Brazil.

Important Information for Residents of Canada

This material does not constitute investment advice or an offer or solicitation to sell or a solicitation of an offer to buy any product or service or any securities (nor shall any product or service or any securities be offered or sold to any person until such time as such offer and sale is permitted under applicable securities laws.) Any products or services or any securities referenced in this material may not be licensed in all jurisdictions, and unless otherwise indicated, no securities commission or similar authority in Canada has reviewed this material or the merits of the products and services referenced herein. If you receive a copy of this material, you should note that there may be restrictions or limitations to whom these materials may be made available. This material is private and confidential and is directed at and intended for institutional investors and is only being provided to “permitted clients” as defined under the Canadian Securities Administrators’ National Instrument 31-103 – Registration Requirements, Exemptions and Ongoing Registrant Obligations. This material is for informational purposes only. This material does not constitute investment advice and should not be relied upon as such. Before acting on any information in this material, prospective clients should inform themselves of and observe all applicable laws and regulations of Canada. Prospective clients should inform themselves as to the legal requirements and tax consequences within the countries of their citizenship, residence, domicile and place of business with respect to the acquisition, holding or disposal of shares or the ongoing provision of services, and any foreign exchange restrictions that may be relevant thereto. First Eagle Investment Management, LLC is not authorized to provide investment advice and/or management money in Canada.

Important Information for Residents of Dubai

This material and the information contained herein is provided for informational purposes only, does not constitute and is not intended to constitute an offer of securities, and accordingly should not be construed as such. Any funds or other products or services referenced in this material may not be licensed in all jurisdictions and unless otherwise indicated, no regulator or government authority has reviewed this document or the merits of the products and services referenced herein. This material and the information contained herein has been made available in accordance with the restrictions and/or limitations implemented by any applicable laws and regulations. This material is directed at and intended for institutional investors (as such term is defined in any applicable jurisdiction). This material is provided on a confidential basis for informational purposes only and may not be reproduced in any form. Before acting on any information in this material, prospective investors should inform themselves of and observe all applicable laws, rules and regulations of any relevant jurisdictions and obtain independent advice if required. This material is for the use of the named addressee only and should not be given, forwarded or shown to any other person (other than employees, agents or consultants in connection with the addressee’s consideration thereof).

Important Information for Residents of the State of Kuwait

The Capital Markets Authority and all other Regulatory Bodies in Kuwait assume no responsibility whatsoever for the contents of this material and do not approve the contents thereof or verify their validity and accuracy. The Capital Markets Authority and all other Regulatory Bodies in Kuwait assume no responsibility whatsoever for any damages that may result from relying on the contents of this material either wholly or partially. It is recommended to seek the advice of an investment advisor.

Important Information for Residents of the State of Qatar

Any funds, products or services referenced in this material may not be licensed in all jurisdictions, including the State of Qatar ("Qatar"), and unless otherwise indicated, no regulator or government authority, including the Qatar Financial Markets Authority (QFMA), has reviewed this material or the merits of the products and services referenced herein. If you receive a copy of this material, you may not treat this as constituting an offer, and you should note that there may be restrictions or limitations as to whom these materials may be made available. This material is directed at and intended for a limited number of "qualified" investors (as such term is defined under the laws of Qatar). This material is provided on a confidential basis for informational purposes only and may not be reproduced in any form. Before acting on any information in this material, prospective clients should inform themselves of and observe all applicable laws and regulations of any relevant jurisdictions, including any laws of Qatar. This material is for the use of the named addressee only and should not be given, forwarded or shown to any other person (other than employees, agents or consultants in connection with the addressee's consideration thereof). Any entity responsible for forwarding this material to other parties takes responsibility for ensuring compliance with applicable securities laws.

Important Information for Residents of the Kingdom of Saudi Arabia

The information contained herein is provided for informational purposes only and should not be considered a solicitation or offering of investment services, nor a solicitation to sell or buy any shares of any securities (nor shall any such securities be offered or sold to any person) in any jurisdiction where such solicitation or offering would be unlawful under the applicable laws of such jurisdiction. Unless otherwise indicated, no regulator or government authority has reviewed this material or the merits of the products and services referenced herein, including the Saudi Arabian Capital Market Authority. This material and the information contained herein has been made available in accordance with the restrictions and/or limitations implemented by any applicable laws and regulations. This material is directed at and intended for institutional investors (as such term is defined under the laws of the Kingdom of Saudi Arabia). This material is provided on a confidential basis for informational purposes only and may not be reproduced in any form. Before acting on any information in this material, prospective investors should inform themselves of and observe all applicable laws, rules and regulations of any relevant jurisdictions and obtain independent advice if required. This material should not be relied upon as investment advice and is not a recommendation to adopt any investment strategy. This material is for the use of the named addressee only and should not be given, forwarded or shown to any other person (other than employees, agents or consultants in connection with the addressee's consideration thereof).

Important Information for Residents of Taiwan

First Eagle Investment Management, LLC is not licensed to engage in an investment management or investment advisory business in Taiwan and the services described herein are not permitted to be provided in Taiwan. However, such services may be provided outside Taiwan to Taiwan resident clients.

Important Information for Residents of United Arab Emirates (Abu Dhabi)

The offering of the products and/or services described herein have not been approved or licensed by the UAE Central Bank, the UAE Securities and Commodities Authority (SCA), the Dubai Financial Services Authority (DFSA) or any other relevant licensing authorities in the UAE, and accordingly does not constitute a public offer in the UAE in accordance with the commercial companies law, Federal Law No. 2 of 2015 (as amended), SCA Board of Directors' Decision No. (13/Chairman) of 2021 on the Regulations Manual of the Financial Activities and Status Regularization Mechanisms or otherwise. Accordingly, this material is not offered to the public in the UAE (including the Dubai International Financial Centre (DIFC)). This material is strictly private and confidential and is being issued to a limited number of institutional and individual clients: a) who meet the criteria of a Professional Investor as defined in SCA Board of Directors' Decision No. (13/Chairman) of 2021 on the Regulations Manual of the Financial Activities and Status Regularization Mechanisms or who otherwise qualify as sophisticated clients; b) upon their request and confirmation that they understand that the products and/or services described in this material have not been approved or licensed by or registered with the UAE Central Bank, the SCA, DFSA or any other relevant licensing authorities or governmental agencies in the UAE; and c) must not be provided to any person other than the original recipient and may not be reproduced or used for any other purpose.

Important Information for Residents of United Kingdom

This material is issued by First Eagle Investment Management, LLC and is lawfully distributed in the United Kingdom by First Eagle Investment Management, Ltd. First Eagle Investment Management, Ltd is authorised and regulated by the Financial Conduct Authority (FRN: 798029) in the United Kingdom. This material is directed only at persons in the United Kingdom who qualify as "professional investors."
This material is not directed at any persons in the United Kingdom who would qualify as "retail investors" within the meaning of the UK Alternative Investment Fund Managers Regulations 2013 (S.I. 2013/1773) or the EU Packaged Retail and Insurance-based Investment Products Regulation (No 1286/2014), the UK PRIIPs Regulation, and such persons may not act or rely on the information in this material.

First Eagle Investments is the brand name for First Eagle Investment Management, LLC and its subsidiary investment advisers. First Eagle Alternative Credit and Napier Park are brand names for the two subsidiary investment advisers engaged in the alternative credit business.

E-BR-NPD-REFL22-P-L

First Eagle Investments

First Eagle Investments

Equities

Fixed Income & Currencies

Alternative Credit

Real Assets