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Kiplinger Investing for Income

Strategies to Boost Your Cash Yield

Tales and Guidance From This Resilient Economy

There are times to seek shelter from financial flames, and there are times to fight monetary fire with fire. We assert that this is one of those occasions to stay squarely on offense. Many investment categories that distribute more cash than money market repositories stand to benefit from the moderately inflationary growth trend and high interest rates.

Powerful job and income growth readings and other upbeat data that discomfit bond-market talking heads and quick-draw stock traders are not fundamentally negative for high-income seekers. The Federal Reserve's interest rate pause means the yield curve will stay inverted longer, probably well into 2025. This prolongs your opportunities to vacuum up high yield with little or no duration (the risk of loss of principal from long-term interest rate increases) from such sources as floating-rate loans and short-term high-yield bonds. The inflation-sensitive alliance of commodities, energy and high-yield debt is flourishing, boosted by the end of recession fears, a great demand for yield, and perhaps a fear premium embedded in oil and other commodity markets. Thus (and this requires mental gymnastics to grasp), lower-quality or higher-risk investments are often outperforming staid stuff like Treasury index funds and blue-chip dividend standbys.

Which raises a question: If 2-2-2 percentages of inflation, growth and interest rates were so fruitful for everything from 2009 until the pandemic of 2020, what wins during an extended 3-3-3 regime? We shall examine that prospect through 2024 and for next year. This does not suggest radical portfolio transformation or a rethinking of our 50-50 division between interest payers and dividend dispensaries. But the hotter economy offers more opportunities than if America were tottering toward a downturn, or if interest rates and inflation were at 1970s and 1980s peaks. We asked around for thoughts to accompany or validate our insights.

> **The inflation-sensitive alliance of commodities, energy and high-yield debt is flourishing.**

And the sentiment is fine. Michael Landsberg, a private wealth manager in Florida, deems the higher-rate and elevated-inflation framework, which he expects to persist, as bullish for energy, materials, commodities and other sectors with price-raising power. Greg Wilensky, Janus Henderson's head of U.S. fixed income, speaks of "the highest real [inflation-adjusted] yields in 20 years" and likes high-

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coupon debt such as collateralized mortgage obligations and actively managed multisector (go anywhere) bond and credit funds. David Schassler, portfolio manager of several VanEck ETFs, echoes that the combo of extra inflation and the need for a "yield cushion" favors high-yield bonds, domestic and foreign, plus commodities. Investing in commodities usually involves futures trading, which does not generate regular income. But if you can wait until year-end for an annual dividend, PIT, the VanEck Commodity Strategy ETF, has so far this year returned more than 8% and in December paid a 6.3% dividend as a lump sum to cap its first year in business. Fidelity's FYHTX, the Fidelity Commodity Strategy Fund, is similar and has been around since 2017, if you want to hedge this hedging by splitting your wager. It pays twice a year, in September and again in November.

Another clear beneficiary of current financial conditions is the dollar. The fuel: the Fed's refusal to cut interest rates and potent U.S. growth compared with other major economies. This sounds redundant, but you should keep some money in UUP, the Invesco Dollar Bullish ETF. It is up almost 7% already in 2024 and has had only one down year since 2017. UUP doesn't promise income, but last year it paid a surprise 6.4% dividend. We continue to disagree with the many Wall Street and academic seers who always expect a weakening dollar. What currency, pray tell, will take its place?

Dollar strength is a factor in the general superiority of U.S. securities' returns vs. most foreign ones. However, the dollar's supremacy and robust U.S. growth have some localized international coattails. Mexico and Brazil are in fine economic shape, the former due to relocation of industry from China and other distant places, the latter as a commodities colossus whose best-known exports, coffee and crude oil, are surging (although soybeans, another big Brazilian export business, are down). As a result, says Western Asset Management portfolio manager Kevin Ritter, both countries have falling inflation and interest rates but stable or strengthening currencies—a perfecto for their bonds. Hence, actively managed emerging-markets bond funds that overweight Latin America and oil-and-gas exporters such as Kuwait and Qatar are ripe. Ritter's closed-end EMD, Western Asset Emerging Markets Debt, has rallied from a 15% discount to its net asset value to 10% in a few months, distributes income of 8.1% (11.2% counting returned capital), and has an above-average record for the category, despite the same big losses in 2022 that crossed all frontiers. Don't go overboard on foreign bonds, but if you are curious, we prefer this mix to plain old euro and yen debt. The same is true with international stocks.

Back stateside, we praise high-yield bonds, floating-rate everything and the enormous cash flows from energy. So far this year, Kiplinger Income 25 member Valero Energy has a 26% return, and 25er ONEOK, a pipeline and storage operator, is ahead 12%. Plus, oil and energy services are at a safe distance from Fed policy and much else that moves the indexes. Energy—all commodities, really—has a 0.4 correlation over 10 years to the S&P 500 and even less linkage to bond prices. And the sector is not even expensive: Eaton Vance notes that at the end of the first quarter, energy's price-earnings ratio of 13 trailed its 10-year average of 16. Only utilities offer a similar discount.

High interest rates and inflation hurt when buying a house or running for political office. But for income portfolios, and even with 5% available at the bank, there are ways to benefit or at least fight back. And that's a comfort.

EDITOR EMERITUS
Knight A. Kiplinger

EDITOR Jeffrey R. Kosnett
MANAGING EDITOR Jim Patterson
COPY EDITOR Frederic Fane Wolfer
ART DIRECTOR Will Tims
DESIGNER Eva Garis

SUBSCRIBER SERVICES
TELEPHONE: 800-544-0155
E-MAIL: KIIservice@kiplinger.com

Send address corrections to *Kiplinger Investing for Income*, P.O. Box 37234, Boone, IA 50037-0234.

REPRINT SERVICE
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The Case for Ultra-Short-Term Bond Funds

Bonds are all about math, so here's a quiz: If cash yields 5%, how much total return for the year through mid April did you need (from something else) to jump that hurdle? The breakeven is 1.43%, and while bonds in general are in the red so far this year, more than 50 ultra-short bond mutual funds and another 50 such exchange-traded funds had outgained that 1.43% threshold through April 19—some of them substantially.

Hence these encouraging words from Western Asset Management co-chief investment officer Mike Buchanan: "Cash might not be king in this current environment." Or, from David Sherman of the RiverPark and CrossingBridge funds: "I want to make more than a Treasury return. A lot more." So far this year, Western's Ultra-Short Income (ARMZX), once managed by Buchanan, and two Sherman funds, CrossingBridge Ultra-Short Duration (CBUDX) and RiverPark Short-Term High Yield (RPHYX), are not merely clearing that 1.43% hurdle. With returns of 1.78%, 1.90% and 1.61%, respectively, each of them is putting the hammer to such alternatives as the Vanguard Short-Term Treasury ETF (VGSH, –0.14%) and the iShares TIPS ETF (TIP, –1.43%). Floating-rate bank loans and high-yield oil and gas debt do have a year-to-date total return edge over the ultra-short bond funds, but no other entries among iBoxx's 50 fixed-income yardsticks are outpacing the iBoxx Liquid Investment Grade Ultrashort Index's 1.68% gain. Indeed, virtually every bond index is negative so far this year.

Yet it is easy to ignore ultra-short funds or deride them as pointlessly risky in the face of the lofty rates on risk-free Treasury bills, money market funds and certificates of deposit. The numbers above indicate that is a mistaken assumption. But why, exactly?

First, bond and credit snippets due to mature in one year or less are often inefficiently priced. That allows research teams and trading desks to turn what looks like a few months of a humdrum 3% or 4% coupon into a heftier return. Sherman's favorite targets are BB-rated bonds that have a few months to mature and below-market coupons, which means they are apt to languish at 90 cents on the dollar. There are two possible outcomes, both favorable for the fund. One, the issuer gets acquired by a firm with a stronger credit rating, so the bonds are repriced forthwith closer to 100. Or, absent a buyout, the fund keeps the debt to maturity and notches a capital gain merely by waiting for the return of the full principal. Two or three such situations can be enough for a fund's total return to outscore the averages.

Second, ultra-short funds are connoisseurs of variable-rate short-term asset-backed securities. Rising interest rates are a plus not only when the rates reset quickly but also when a debt's term expires, because the fund can usually find similar paper that pays more. (Ask yourself what your bank is charging for lines of credit now compared with last year.) Consequently, this is a rare case of a bond fund's net asset value increasing in the face of rising interest rates. Northern Ultra-Short Fixed Income (NUSFX, year-to-date return 1.81%) has a duration of 0.50 and yet (in all seriousness) informs its prospective shareholders that it seeks capital appreciation alongside high yield. So far in 2024, its NAV is up from $10.20 to $10.24, which is not much by long-term bond fund standards but contributes a few ticks to overall performance. More importantly, in the first three months of this year, NUSFX distributed a total of $0.1208 a share, which is 8% more than the $0.1120 it paid in the fourth quarter of 2023. A typical bank or utility has not raised dividends 8% of late—and NUSFX is not done adding to its payout.

In no way are we advising you to ditch money market funds or CDs, although these are CD-like: going all the way back to its initial offering at $10 in 2009, NUSFX's net asset value has never closed lower than $9.92, which is remarkable. We checked, and as a rule, all of these funds' only noticeable NAV dips came during the 2008 financial crisis, and they recovered sharply in 2009. But in general, wherever a well-managed credit or bond fund offers a current yield several percentage points greater than its duration, you certainly have a low-risk winner. The aforementioned Northern and RiverPark entries not only have sweet 2024 numbers but also boast five-year total return edges over both that Vanguard short-term Treasury fund and LQD, a giant, investment-grade corporate ETF. That aphorism about tortoises and hares sometimes applies where you least expect it.

Follow the Dollars (Gas Pump Edition)

In the 2000s and early 2010s, when crude oil surpassed $100 a barrel and American gasoline first hit $4 per gallon, Kiplinger semi-seriously suggested you accumulate shares of an oil trust, cash the dividend checks and put the money in your car to buy fuel. Our favorite back in the day was BPT, the BP Prudhoe Bay Royalty Trust, an unmanaged trust created in 1989 to pass through a percentage of the variable proceeds from BP Alaska oil production. Not only did high crude prices boost BPT's dividend yield above 12%, but the trust units, initially offered for $25, quadrupled from 2004 to 2010 and peaked at $131. Motorists thus equipped could ignore the national discontent about then-unimaginable pump prices. Today, inflation-adjusted fuel costs less, but the discount is narrowing. And crude oil prices are surging again on heavy demand and traders' bets on ever-higher prices due to international conflict. Wars are energy hogs; global military oil usage is growing faster than civilian consumption.

What has not kept pace, though, is the value of BPT shares. BPT closed April 19 at $2.27 (yes, two bucks and change). The trust is 35 years old and has stopped paying dividends as revenue dwindles, and so it finally looks set to end, a decade or more after the initial indications of its demise. Older oil fields are often unsuitable for additional drilling or revived production.

However, BPT is not one of a kind. If you want to collect oil dividends to fill your tank, other royalty trusts are expanding. The Permian Basin Royalty Trust (PBT), which yields 9.2% based on its two latest dividends, plans to drill 95 new wells on its West Texas acreage this year, compared with the 77 that it completed last year. Unlike some Texas and New Mexico onshore trusts, PBT is much more an oil than a natural gas revenue source; 88% of its income comes from oil. And while the share price is down 13% so far this year, it is the same as it was three years ago. Sabine Royalty Trust (SBR) yields 10.2% on a revenue stream that is two-thirds oil, mostly from Texas and Oklahoma, and one-third natural gas. It also reports more drilling and increased proven reserves. (All royalty trusts publish annual projections of production and reserves, but those depend on the price and demand for their production. Nothing is assured.) Sabine's shares, trading near $64, are down 6% this year, but in April, the monthly distribution grew from 41 cents to 54.

Granted, royalty trust share prices and dividends are unpredictable and by no means constitute a complete energy-income strategy. Once crude oil leaves the ground, it must pass through a series of value-adding steps before it goes into your car. All offer additional opportunities to profit or defray the high cost of retail fuel. Refiners such as Valero and Marathon don't pay high dividends, but their earnings and share prices benefit from robust demand and tight refining capacity. And while pipeline and storage operators are usually identified with natural gas, they also earn big tolls from moving gasoline and other refined fuels. ONEOK, which acquired prime gasoline carrier Magellan Midstream Partners last year, and Sunoco LP, a giant gasoline transporter and marketer, put you in the driver's seat here. Sunoco has a precious monopoly on service-plaza sales along the New Jersey Turnpike, America's busiest toll road. OKE is priced to yield 5%, while SUN pays 6.7%. Both stocks are way up over the past year, but if anything, business is better now.

Timely Tactic of the Month

In trolling the list of downtrodden and oversold REITs, we were surprised to find **Easterly Government Properties (DEA, $11.60)** trading at or a couple of pennies above its 52-week low. As an office landlord, some of the distress makes sense, but Easterly owns only government offices and laboratories whose federal and state tenants are always good for the rent and unlikely to move. The dividend yield is a hefty 8.9% and the shares are discounted from the properties' net asset value, which is more than $15. The symbol DEA refers to one of the tenants. Regulators rejected FBI when the trust went public in 2015.

Kiplinger 25 for Income

Sellers and profit-takers appeared in April and trimmed first-quarter gains all around the 25. Federal Reserve warnings about rapid growth and sticky inflation indexes also scratched the numbers, sending the likes of Annaly Capital and Brookfield Infrastructure to the lower ends of their trading ranges. But more striking was the number of selections whose share prices or net asset values stood still: Suburban Propane "rose" from $19.41 to $19.42, and Welltower, Franklin U.S. Low Volatility and Valero all moved a handful of pennies. Bond funds lost about 2% of their principal, however, and the redoubtable Pimco Corporate & Income Strategy cheapened to a 13% premium over NAV from the 20% it had reached in March. None of this strikes us as anything but normal difficulties during a month when ordinary stock and bond indexes sustained moderate losses. Nobody cut dividends, and rising energy prices offset weaknesses in real estate and banking. On we go as the inflation and interest rate picture stays murky.

Utility stocks		Price	Yield	Frequency
American Electric Power (AEP)	Traditional electric company serving 11 eastern and southern states	$84.20	4.2%	quarterly
AT&T (T)	Wireless-service giant that grew out of the former SBC	16.51	6.7	quarterly
American Water (AWK)	Largest investor-owned water utility, serving 16 states	118.52	2.4	quarterly
High-yielding open-end bond funds				
Baird Core Plus Bond (BCOSX)	A rare general bond fund that usually beats its benchmarks handily	$10.32	3.7	quarterly
Dodge & Cox Global Bond (DODLX)	A mix of domestic and foreign corporate bonds, mostly denominated in U.S. dollars	10.54	3.6	quarterly
Fidelity Capital & Income (FAGIX)	Creative and aggressive junk bond fund	9.66	5.2	monthly
Hotchkis & Wiley High Yield (HWHAX)	Boutique high-yield fund that concentrates on small companies	10.20	6.1	monthly
Payden Corporate Bond (PYACX)	Actively managed fund emphasizing BBB-rated U.S. corporate debt	9.48	4.3	monthly
TCW Emerging Markets (TGEIX)	A higher-quality approach to emerging markets, with all debt in hard currency	6.37	5.5	monthly
Closed-end mutual funds and ETFs				
AllianceBernstein Global High Income (AWF)	High-yield corporate bonds and government bonds from emerging markets	$10.05	7.8	monthly
BNY Mellon Muni Bond Infrastructure *(DMB)*	*A leveraged closed-end fund that likes transportation and hospital bonds*	9.99	3.6	*monthly*
Franklin U.S. Low Vol High Div Index (LVHD)	High-yield stock fund with moderate sensitivity to daily market index swings	35.75	4.0	monthly
Global X Nasdaq 100 Covered Call ETF (QYLD)	High distributions from writing options on Nasdaq stocks	17.28	12.1	monthly
iShares U.S. Preferred ETF (PFF)	This exchange-traded index fund spreads your money in more than 301 preferred stocks	30.90	6.8	monthly
Nuveen Credit Strategies Income (JQC)	A leveraged floating-rate fund that also has some junk bonds	5.41	12.0	monthly
Nuveen Municipal Value *(NUV)*	*This non-leveraged closed-end is an alternative to the BNY Mellon Infrastructure fund*	8.51	4.1	*monthly*
Pimco Corporate & Income Strategy (PCN)	An unusual mixture of high-yield corporate, muni and foreign bonds	12.85	10.5	monthly
Real estate investment trusts				
Annaly Capital Management (NLY)	Borrows cheaply to reinvest in government-guaranteed mortgage securities	$18.23	14.2	quarterly
Digital Realty Trust (DLR)	Developer and operator of data centers in the U.S., Canada, Europe and Asia	136.83	3.6	quarterly
Realty Income (O)	Landlord to chain stores and restaurants, also known for 50 years of monthly dividends	53.04	5.9	monthly
Welltower (WELL)	Develops and owns assisted-living facilities, hospitals and medical labs	91.32	2.7	quarterly
Energy investments and partnerships				
Brookfield Infrastructure Partners (BIP)*	Owns toll highways, ports and transmission lines	$27.16	6.0	quarterly
ONEOK (OKE)	Major diversified energy infrastructure former partnership	79.63	5.0	quarterly
Suburban Propane Partners (SPH)*	Propane distributor normally yields substantially more than junk bonds	19.42	6.7	quarterly
Valero Energy (VLO)	World's largest independent refiner	163.89	2.6	quarterly

Funds in italics pay tax-exempt income. Investments with an asterisk (*) are partnerships. Prices and yields as of April 19, 2024. SOURCES: Fund companies, Morningstar Inc., Yahoo.

Ask Jeff

Readers are invited to send questions about income investments to jkosnett@kiplinger.com. I'll answer you personally if there's no space here for a published reply.

Dear Jeff:
I heard that the strategy behind buy-write ETFs, such as QYLD, Global X's Nasdaq 100 options fund, forces the gradual and inevitable erosion of the share price. For that reason, am I right that these funds are not recommended for long-term buy and hold?
Bill

Dear Bill:
An absolute price decline is not inevitable. But when share prices grow, which is most of the time, the NAV of a call-options-writing fund will lag the underlying stock index because exercised options preclude some capital gains. In a bear market, the profits from writing calls drop, so buy-write funds struggle to generate income. A sideways market works best. Still, a reasonable expectation over several trading cycles is for the share price to stay flat or wander slightly higher. Although QYLD's original $25 NAV in 2013 now sits at $18, almost all the drop occurred in 2022; otherwise, it stays generally steady. More typically, XYLD, a Global X ETF that writes calls on the S&P 500, debuted at $40 and after 11 years changes hands at $40.50. But the rationale for these funds is not capital appreciation or preservation, and they are not a substitute even for low-volatility non-option funds. A buy-write fund's purpose is to pay consistently more monthly income than a BBB-rated corporate bond fund or a collection of preferred stocks. Both QYLD and XYLD meet that standard.

Dear Jeff:
In 2021, when PFD, the closed-end Flaherty & Crumrine Preferred Stock fund, traded around $16, you called it a rare buying opportunity. It has been languishing around $10 since 2022, and it has swung from a premium over net asset value to a substantial discount. Is this a reaction to higher interest rates, or has this fund's management skill or outlook fundamentally changed?
Ron

Dear Ron:
PFD did bounce to $19 soon after we wrote that, but it sank during the bear market of 2022 and the bank failures of early 2023. Interest rates added to the pressure, but the real pain derives from how traders soured on the category and saddled PFD with its first sustained discounts in ages. The NAV is edging higher and is closing in on $12, but the fund "can only speculate why the relationship between the share price and NAV hasn't been closer." There is little asset turnover, and the fund avoids credit risk, so we can't point to any poor portfolio decision-making. CEF managers have no direct influence on discounts and premiums, except in that fine long-term outperformance (as F&C has had over the years) can attract aggressive buying, which bids up the premiums. At any rate, for PFD, what is past is past. Its collection of large banks and insurers distributes 6.8% and is priced around par value. $10 seems like a favorable entry point. There is upside once the interest rate situation settles.

Dear Jeff:
I own UTG, Reaves Utility Income, for dividends, but the latest several monthly payments included a return of capital. Is that a sell signal? I wonder if utilities are struggling to maintain dividends, and if so, could the fund's action reflect that?
James

Dear James:
In 2023, Reaves boasted that it had never paid a return of capital since it began the fund in 2004. It supplemented dividend income with ample realized capital gains. But recently, utilities and holdings like cell-tower REITs are in the red, so Reaves is reaching into its substantial surplus to keep its 19-cent monthly distribution. Because it does not habitually do this, and the fund's assets still greatly exceed its liabilities, it is in no danger of returning so much capital that it kneecaps potential returns once utilities and REITs recover. I am thus inclined to give Reaves a pass. But when it comes to returns of capital, every situation is different. There are many cases in which the sudden appearance of one would be concerning.

PHOTO BY BOB CROSLIN

What's New in Cash

Bombs bursting in air? Markets simply do not care. Once again, this time because of Iran and Israel, we must push back against the discredited doctrine that "geopolitical" risk and conflicts—let us simply call them wars—harm everyday U.S. investors' fortunes. What does matter, and this is clear from two straight unexpectedly heavy CPI reports, is that the true market influencers are inflation, economic growth, employment, earnings, Federal Reserve inaction and posturing, and sometimes congressional budget fights that raise the terrifying possibility of a Treasury default. The one linkage between bombs and markets we trust is that the dollar inevitably benefits from global turmoil. UUP, the Invesco exchange-rate ETF, which we watch as a referendum on the dollar, is up another 2% over the past month and ahead just shy of 7% for the year to date.

The beating heart of dividends. Right on cue after our March article pointing to a looming revival of dividends, several old-school companies came through with fat dividend increases: Costco, 14%; Constellation Brands, 13.5%; TJX, 13%; Carpenter Tech, 11%; and JP Morgan, 9.5%. Morgan had raised dividends by a total of only 5% since mid 2021. Bank of America strategists now forecast dividend growth to pick up after five quarters of decelerating increases. We hope they are right this time; the same bank forecast big dividend growth in 2022 and 2023 that did not appear.

Utilities on the mend? We remain concerned that high interest rates and investor frustration are conspiring against utility shares, but in the week ending April 19, the sector gained 2%, by far the best showing among all 11 S&P 500 industry groups. Shareholders are evidently content with a series of generous recent dividend increases, such as 10.2% by NextEra Energy, 7.3% by PPL and 6.4% by Ameren. Utilities are no longer so expensive on price-to-book, dividend yield and other markers. XLU, the sector's primary index ETF, closed April 19 at a four-month high. We continue to prefer individual stocks to the index fund, which yields just 3% due to some dividend laggards like Duke Energy and Southern Company. But it is a fair signal of reviving sentiment around the sector.

Flashback

Inflation was marching toward 7% in May of 2022, so we presented "Investments for Fighting Inflation." Depending on the index, the monthly inflation pace over the past year runs from 2.8% to 5.0%. But while it is generally easing, it remains high enough to influence investment tactics and results. And its emergence a few years ago bred some instant solutions. In January 2021, the fund firm Horizon Kinetics hatched INFL, a stock-picking ETF aiming to "benefit from rising prices of real assets." INFL has a cumulative return of 40.3% since its birth, dead even with the S&P 500. INFL, whose largest holdings include basic materials and energy, is up 3.5% in 2024, which is decent. But it is no magical price-slayer. That crown belongs to energy infrastructure firms, pools of commodity investments, and high- and floating-rate creditors. Their returns since 2021 outpace INFL and embarrass IVOL, the Quadratic Interest Rate Volatility and Inflation Hedge ETF. Since the start of 2021, IVOL has melted $1 into 73 cents while MLPX, the Global X MLP and Energy Infrastructure ETF, turned $1 into $2.06.

In that vein, we said in May 2022 to fight inflation by favoring several hard-asset sectors: farmland, high-yield business lending, energy infrastructure and commodities. (We do not cover gold because there is no income, but we note its recent success.)

The pair of farmland REITs, Gladstone Land and Farmland Partners, suffered from high interest rates because farmland returns are historically more closely correlated with Treasury bonds than with the S&P 500 or economic growth. Gladstone reports that the rents it charges lessees rose only 0.6% in 2022 and fell in 2023. Its cash flow and dividends per share have been flat for eight years. Swing and a miss.

Our other ideas, from lenders Ladder Capital and Ares Capital, to the MLPs Plains All-America Pipeline and Energy Transfer Partners, to DBC, the Invesco Commodity Tracking ETF, fared well. Whether due to inflation or economic vigor, in two years this quintet has an equal-weighted return of 31%, despite small losses by Ladder and some ups and downs by the commodity fund. DBC pays a distribution only once a year, but as a bet on metals- and food-exporting countries, it pairs well with UUP, Invesco's indomitable dollar-index fund. We do not expect inflation to reignite, but energy and high-yield credit are keepers.

Model Portfolio: Tax-Exempt Income

You can't see it from these numbers, but tax-exempt bonds are enduring the bond world's struggles of 2024 much better than Treasuries, mortgages or investment-grade corporate debt. This tracks with longstanding findings that municipals are the major bond category that's least sensitive to interest rate hikes and Federal Reserve goings-on. This relative calm owes much to the reality that many individual investors refuse to pay taxes on interest income, even when cash or high-coupon corporate bonds might net more after the IRS bite. So our collection treaded water between December 15 and April 19. We hoped for better, but the portfolio generated $1,088 of tax-free income while losing $825 of capital. It could have been much worse.

Hence our observation that municipals are steely stuff, and long-term patience is mandatory. You may recall that November 2023, just before this measuring period, was one of the best months ever for tax-exempts, while the middle of 2023 was awful. November was enough to restore our nine funds' one-year total returns to the green after we printed several issues in which we had to report 12-month losses as deep as 9%.

The best performer during this current period was our closed-end selection, Nuveen Municipal High-Income Opportunity. The Nuveen fund's share price rallied from $10.02 to $10.18 as it advanced from an 11% discount to net asset value to 7%. Nuveen also raised its monthly distribution by 12% starting in March, more than restoring what it had trimmed last fall. And so far in 2024, NMZ's return on its portfolio assets is in the top 15% of the category. The fund's borrowing (leverage) cost it dearly in 2022, but that borrowing is now a plus. Our two other exemplars are the pair most driven by their managers' decision-making excellence: Baird Strategic and MainStay MacKay Strategic. Baird keeps maturities and durations shorter than MacKay, but both are confident enough in their analysis to put 20% of the fund into nonrated issues, which typically pay higher interest rates than debt rated A and AA. Active and creative management works as well with municipals as it does with junk. And while the ratings agencies are spectators to the issuance of unrated municipals, they have been unambiguously positive on the creditworthiness of most tax-free borrowers. As the pros know (and you should too if you shop for individual municipals): Stay away from poor or shrinking jurisdictions, speculative nursing home and long-term-care developments, and private colleges with falling enrollment. Their troubles inflate the total count of defaults, but they are not representative of what is a profoundly healthy sector. No changes to the fund listings.

SHORT-TERM: 15%. Despite an interest rate bump, the taxable-equivalent yields here still fall short of likely net proceeds from T-bills and taxable money market funds, so stay underweight in this segment.
$7,500 T. Rowe Price Tax-Free Short-Intermediate (PRFSX). Yield, 2.3%. One-year total return, 2.2%.
$7,500 VanEck Vectors AMT-Free Short-Muni ETF (SMB). Yield, 2.4%. One-year return, 2.5%.

INTERMEDIATE-TERM: 45%. These funds complement one another, with Baird the most active and adventurous and Fidelity the most cautious and traditional.
$15,000 Baird Strategic Municipal Bond (BSNSX). Yield, 3.3%. One-year return, 3.8%.
$15,000 Fidelity Intermediate Municipal Income (FLTMX). Yield, 2.5%. One-year return, 2.6%.
$15,000 Schwab Tax-Free Bond (SWNTX). Yield, 3.3%. One-year return, 2.8%.

LONG-TERM: 40%. More yield, and more risk; the three open-end funds all lost between 1% and 2% of their NAV in this period, but so did their rivals.
$10,000 MainStay MacKay Strategic Municipal Allocation Fund (MTFDX). Yield, 3.5%. One-year return, 3.3%
$10,000 Nuveen Municipal High-Income Opportunity (NMZ). Distribution, 5.4%. One-year return, 2.3%.
$10,000 Vanguard California Long-Term Tax Exempt (VCITX). Yield, 3.2%. One-year return, 3.8%.
$10,000 Vanguard Long-Term Tax Exempt (VWLTX). Yield, 3.3%. One-year return, 3.7%.