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Neuberger Berman Tax-Exempt Limited Maturity Fixed Income Portfolio

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Performance Highlights

The Tax-Exempt Limited Maturity Fixed Income Portfolio posted a positive return (before and net of fees) in the third quarter of 2025 but lagged the benchmark.

Market Environment

In September, U.S. and global investment grade (IG) fixed income delivered positive total returns of 1.09% and 0.74%, respectively, as measured by the Bloomberg U.S. Aggregate Index and Bloomberg Global Aggregate Index (USD hedged). For 3Q 2025, the Bloomberg U.S. Aggregate Index and Bloomberg Global Aggregate Index (USD hedged returned 2.03% and 1.21%, respectively. Risk assets outperformed in September and the third quarter as investor demand remained robust, fundamentals stayed broadly stable, the Fed cuts policy rates and economic data continued to be resilient. Across global fixed income markets, spread sectors saw robust returns for the month, which also boosted returns for the quarter.

Quarter

U.S. government yields moved lower across the curve in the third quarter of 2025. The 2-year yield decreased by 11 bps to 3.61%, the 5-year yield fell by 6 bps to 3.74%, and the 10-year yield declined by 8 bps to 4.15%. The 30-year yield was down 5 bps to 4.73%. The 10-year TIPS yield dropped by 15 bps, closing at 1.80%. These shifts reflect ongoing adjustments to expectations regarding inflation, economic growth, and the fiscal outlook. Yields across other major developed countries were mixed but more showed increases in the third quarter.

Overall, demand for fixed income remained robust, with investor interest supported by stable fundamentals and the search for yield, despite ongoing uncertainty.

U.S. Economy

- Nonfarm payrolls for August increased by 22k, significantly below consensus expectations of 75k and the prior month's 73k. The unemployment rate for August was 4.3%, up slightly from 4.2% in the prior month and matching consensus expectations.
- Average hourly earnings for August rose by 0.3% MoM, in line with consensus and unchanged from the prior month.
- U.S. headline CPI for August was 2.9% YoY, with core CPI at 3.1%, both matching consensus survey estimates and slightly higher than July's headline CPI of 2.7%. The impact of tariffs remains mostly limited to goods, with little immediate effect on core services.
- Headline retail sales (MoM) increased by just 0.6% in August, up from 0.5% in July and well above consensus of 0.2%.

U.S. economic activity remains resilient but is showing signs of slowing in some areas, with job growth coming in well below expectations. Consumer spending growth is still positive, but labor market gains have softened, inflation is contained but still above the Fed's target, and ongoing policy and geopolitical risks continue to weigh on the outlook. Further Fed cuts are still expected over the remainder of 2025 and into early 2026.

Investment grade U.S. municipal bond performance, as measured by the ICE BofA Municipal Securities Index, delivered a strong return of 3.08% during the second quarter. For the quarter, 1-3 year munis generated a return of 1.18% and the 3-7 year part of the curve returned 2.36%. Longer maturities, in the 22+ year range, outperformed shorter bonds with a return of 3.85%. The Bloomberg Taxable Municipal Index underperformed tax-exempts with a return of 2.51%. Per Bloomberg, total municipal issuance (tax-exempt only) for the quarter was $161 billion or 7% higher than it was for the same quarter a year earlier. With regard to credit, BBB rated securities slightly underperformed higher rated securities during the quarter. Revenue bonds and general obligations had similar performance during the quarter. Within the revenue bond sector, hospital bonds outperformed while electric utilities underperformed.

Portfolio Review

The Tax-Exempt Limited Maturity Fixed Income Portfolio posted a positive return (before and net of fees) in the third quarter of 2025 but lagged the benchmark. The strategy benefited from its overall duration overweight but that was overshadowed by its curve positioning, and security selection.

Outlook

We believe tight credit spreads and rapid policy change make active security selection crucial in today's municipal market.

The municipal bond market posted strong results in the third quarter, continuing to validate our view that the post-Liberation Day sell-off in April was a buying opportunity and not the start of a sea change in market fundamentals. High absolute yields, relative value versus Treasuries, and increasing confidence that the Federal Reserve would resume its easing cycle contributed to market strength. The rally was especially impressive given the supply backdrop, which remained heavy and should lead to record new issuance volume for the year.

Yield-curve dynamics were noteworthy during the quarter, with the "belly" of the curve (four- to seven-year maturities) outperforming longer bonds in July and August 1. In our view, the primary driver of that strength was the market's belief that the Fed's renewed rate-cutting would be more rapid than expected—a belief reinforced by weaker labor market data and inflation readings that were in line with expectations. In September, we started to see curve-flattening as investors felt more comfortable buying longer-dated issues to take advantage of their higher yields. Lower-rated bonds slightly underperformed for the quarter. In our view, they lagged high-grade bonds, not because of cracks in the credit story, but more because of the narrow yield advantage they offered over highly rated bonds. Fund inflows, mostly from exchange-traded funds, were a tailwind as the quarter progressed.

Looking forward, technical factors related to issuance and maturing bonds should lead to increased net supply in October, potentially causing municipals to cheapen somewhat versus Treasuries. However, we would view any pockets of weakness as a potential buying opportunity, especially given the Fed's easing campaign. With tighter valuations on credit and a host of policy changes from the federal government, we believe that active security selection will take on greater importance going forward. At the same time, should a backup in rates materialize, it should provide a window to tax-loss harvesting when opportunities arise.

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Through December 31, 2023, the Index consists of 40% ICE BofA 1-3 Year US Municipal Securities Index and 60% ICE BofA 3-7 Year US Municipal Securities Index. From January 1, 2024 and onward, the Index consists of ICE BofA 1-10 Year Municipal Securities Index.
ICE BofA 1-10 Year Municipal Securities Index is a subset of ICE BofA US Municipal Securities Index including all securities with a remaining term to final maturity less than 10 years. ICE BofA US Municipal Securities Index tracks the performance of US dollar denominated investment grade tax-exempt debt publicly issued by US states and territories, and their political subdivisions, in the US domestic market. Qualifying securities must have at least one year remaining term to final maturity, at least 18 months to final maturity at the time of issuance, a fixed coupon schedule and an investment grade rating (based on an average of Moody's, S&P and Fitch). Minimum size requirements vary based on the initial term to final maturity at time of issuance. The index is rebalanced on the last calendar day of the month, based on information available up to and including the third business day before the last business day of the month.

The benchmark is an unmanaged index. NBIA advises according to the Portfolio characteristics which may differ from those of the benchmark. Additional disclosures for complete benchmark descriptions are available upon request.

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