CAVANAL HILL

Fourth Quarter 2023

Cavanal Hill Strategic Enhanced Yield Fund Quarterly Commentary

AAEMX, APENX, AIENX

Market Overview

After the slight reality check in the third quarter, the last three months of the year saw strong returns across most major asset classes. Growing excitement that central banks will cut interest rates sooner in 2024 than previously expected resulted in an "almost everything rally". Coming into the final quarter of 2023, the market was comfortable that central banks had finished hiking but cautious about how long rates would remain at restrictive levels. A series of softer inflation prints in the U.S. and Europe, however, was enough to remove those fears as investors shifted to expect preemptive cuts from the central banks. This view was compounded at the December Federal Open Market Committee meeting, where the latest projections suggested three cuts during 2024.

While the predominant view among many is still to call for some type of recession later this year, others believe it's still possible to have a type of "Goldilocks" scenario, where the economy continues to grow, the job market doesn't soften significantly, and inflation subsides. As with all things lately, no significant data or trend has been established to help determine which scenario is more likely. The yield on the 10-year Treasury began the quarter at 4.57% and rose in October to a multi-year high of 5.02% intraday before reversing hard and fast for the rest of the year to finish much lower at 3.88%. The U.S. dollar finished much weaker this quarter in anticipation of a monetary policy pivot.

Tightening spreads also helped credit markets this quarter. Spreads on high yield and emerging market debt fell as the funding risk posed by "higher for longer" U.S. rates for emerging market economies and riskier companies faded. With the credit subsectors, industrials and utilities outperformed financials this quarter as the financial sector's shorter duration could not keep up with the total return of the longer-duration sectors.

Longer-term securities in both the Treasury and corporate space significantly outperformed shorter ones as the yield curve's shape flattened bullishly. The U.S. Treasury (+5.66%) and government agency securities (+3.68%) sectors underperformed the broader Barclays U.S. Aggregate Bond Index's quarterly return of +6.82%. The high yield (+7.16%), emerging market debt (+8.10%), corporate (+8.50%), non-dollar (+9.21%) and mortgage-backed securities (MBS) (+7.48%) sectors outperformed the broader index's return.

Positioning the Fund

Portfolio composition is subject to change

The Fund maintained a shorter duration following a quarter of still-rising rates. As rates stopped increasing, we lengthened duration but still under a defensive stand. We maintained our sector allocation while overweight U.S. investment grade corporates and emerging market debt. Allocation to MBS remained slightly underweight along with Treasuries, with changes to allocation in response to market volatility during the quarter.

Notable Portfolio Changes

Other than increasing the Fund's Treasury sector allocation, we have no immediate plans to change allocations to other sectors.

Why should investors consider investing in this fund?

Expected returns are higher than they have been in many years. With economic growth slowing and an aggressive Federal Reserve working to bring inflation down, high quality fixed income should be an attractive asset class. This fund's conservative positioning should be beneficial in a more risk-averse environment.

If you'd like additional information about this or any of the Cavanal Hill Funds, please contact Craig McQueen at 303.355.2799, CraigMcQueen@cavanalhill.com, or cavanalhillfunds.com.

Disclosures

An investor should consider a fund's investment objectives, risks and charges and expenses carefully before investing or sending money This and other important information about an investment company can be found in the fund's prospectus. To obtain a Cavanal Hill Funds prospectus or summary prospectus, please call 800-762-7085 or visit us at www.cavanalhillfunds.com. Please read it carefully before investing.

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Investment Risks

Fixed income securities are subject to interest rate risks. The principal value of a bond falls when interest rates rise and rise when interest rates fall. During periods of rising interest rates, the value of a bond investment is at greater risk than during periods of stable or falling rates. Bond funds will tend to experience smaller fluctuations in value than stock funds. However, investors in any bond fund should anticipate fluctuations in prices, especially for longer-term issues and in environments of changing interest rates.

If you'd like additional information about this or any of the Cavanal Hill Funds, please contact Craig McQueen at 303.355.2799, CraigMcQueen@cavanalhill.com, or cavanalhillfunds.com.