Summer 2023

INVESTOR NEWSLETTER

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What happens next for banks?

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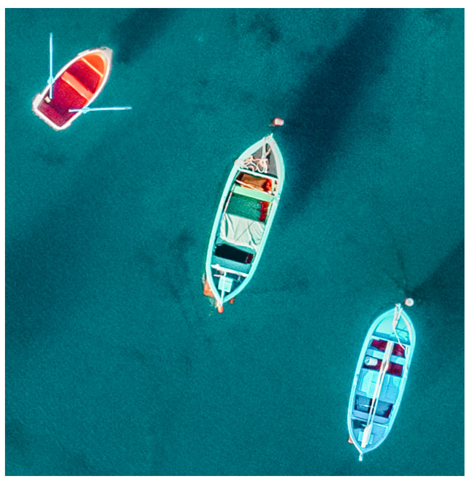

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Columbia Threadneedle Investor Newsletter is published quarterly online and features timely articles covering economic trends, investment strategies and solutions, and service changes.

WHAT HAPPENS NEXT FOR BANKS?

Our CIO and bank analysts consider changes that may be coming for banks in the wake of recent events.

The U.S. government may not like too-big-to-fail financial institutions, but the market is heading in that direction and the big will become bigger.

WILLIAM DAVIES
Global CIO

DICK MANUEL
CFA, Senior Equity Analyst

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Confidence, the bedrock of a functioning financial system, was tested in early March as news of bank failures and questions about liquidity shook depositors and investors. Here are our expectations for the sector.

A rush for safety continues

It is relatively easy to move assets to a large money center bank in the digital/mobile age, and in the current environment many depositors and CFOs perceive them to be less risky. Though it is unnecessary, in the short term, we would not be surprised to see deposits move from regional banks to larger ones. The U.S. government may not like too-big-to-fail financial institutions, but the market is heading in that direction and the big will become bigger. That doesn't mean everything is necessarily rosy for the big banks. While they may be raking in deposits, they'll also be on the hook to fund corresponding deposit insurance. (The Federal Deposit Insurance Corporation is not funded by taxpayers; banks and savings associations pay into the FDIC insurance fund in proportion to their size.)

Regionals get reregulated

In 2018, Congress exempted small banks from the regulatory scrutiny that the big banks still face, such as the Fed's annual CCAR[1] bank stress tests. We expect this to be reimplemented.

The tests, which assess whether a bank has the strength to weather large losses, are likely to be applied more broadly to regional banks, as regulators acknowledge that even banks that are not the largest can still destabilize the financial sector. Capital and liquidity rules that currently only apply to systemically important banks (i.e., large money center, super-regional and trust banks) may also be pushed down to apply to regional banks.

Greater regulation equals increased costs for the regionals. While the application of these rules will likely be phased in over a few years to give the banks sufficient time to comply, they will likely reduce profitability and perhaps bank stock valuations, even while providing investors with more confidence.

We're also likely to see a larger role for regulators generally as they seek to maintain confidence in the financial system. The brokered takeover of Credit Suisse by UBS and First Republic Bank's sale to JP Morgan Chase are good examples of this.

Continued on next page

Depositor insurance protection is not guaranteed

Regulators and policymakers have, on several occasions, demonstrated a willingness to protect depositors in the event of a bank failure, whether the deposit is above the insured $250k official insurance limit or below. But this implicit guarantee differs from an outright, explicit guarantee of all deposits. Such an explicit guarantee would likely calm depositors' concerns and make them less vulnerable to short seller manipulation, but the government has limited ability and appetite to provide such explicit, preemptive deposit guarantee. While an executive order might provide a short-term solution, a long-term expansion of the deposit guarantee would require congressional action.

The rate backdrop remains important

It's only a small subset of banks that are seeing deposits flee, and obviously there are significant implications for those banks from a profitability standpoint — especially if they are backfilling with expensive borrowing or swapping of assets with the new Fed facility. Another subset of banks is worthy of investor attention: those banks that are not seeing any deposits flee, but have a high allocation of "held to maturity" investments and outsized bond losses in their "available for sale" bond portfolios, coupled with other liquidity constraints. We anticipate that many of these banks will seek to rebalance their bond portfolios as quickly as possible, which may mean selling longer duration bonds and buying shorter duration issues.

One catalyst that would bring rapid relief to the bond portfolio situation: lower rates. The Fed's rapid increases after many years of zero interest rates created liquidity mismatches, and any reduction in rates would take the pressure off and allow banks to shorten their duration. So, by extension, any relief found in the inflation data will eventually translate into a better backdrop for banks.

Banks must balance long-term investments in a short-term-minded market

Banks take in deposits and lend them out to companies that want to expand (e.g., buy equipment and hire employees). In the past, banks could rely on these deposits to remain for years, so they felt comfortable lending money to companies for these long-term investments. Deposit outflows in recent weeks occurred as market participants began to question the valuation of long-term loans and investments that were meant to be held for years, which resulted in concerns over bank viability. Banks need to be able to diligently provide long-term capital to growth-minded borrowers without fear of short-term factors inhibiting their ability to do so. Policymakers should focus on the root causes of how we got here and help figure out a path forward.

As one reads about bank failures and sees volatility in bank share prices, it is natural to be concerned and wonder about the stability of the system. While the government has not explicitly guaranteed all deposits, their past actions speak loudly, especially when one considers how hard it is for the government to explicitly guarantee all deposits. At the system level, while banks will face earnings pressure, we observe that the vast majority of deposits in the U.S. sit in banks that have very strong balance sheets, with diverse asset and liability bases, and significantly more capital than required by their regulators.

[1] Comprehensive Capital Analysis and Review

SECURE 2.0

New opportunities for 529 beneficiaries

Legislation enacted at the end of 2022 brings positive changes for 529 education savings plans.

529 plans: How do they work?

529 plans are designed to encourage saving for education costs. For investors, the benefits include a way to grow assets on a tax-deferred basis. These tax-deferred earnings may then be used tax-free to pay for qualified higher education expenses like tuition, apprenticeship programs, student loan repayments, mandatory student fees, on-campus room and board, off-campus housing (with limits) and equipment (e.g., computers, software and other items required for coursework).

529 plans are also an effective estate and legacy planning tool, given their unique gifting and funding capabilities. Contributions qualify as completed gifts, thus removing the balance of the 529 account from the owner's estate, all while the owner maintains control and access to the account.

Saving for retirement with a 529 account

The recently passed SECURE 2.0 Act of 2022 introduces a new provision that allows "leftover" assets in a beneficiary's 529 plan to be rolled over to a Roth IRA. This rollover to Roth IRA eligibility helps address long-standing concerns about having to pay taxes or other penalties on "overfunded" 529 accounts. It also provides a long-awaited alternative for those who have chosen to make college savings a priority.

These new provisions are also subject to certain conditions, including the "15-and-5 rule" — meaning rollovers must come from an account that has been established for 15 years or longer, and eligible assets must have been in the account for at least 5 years. The qualifying rollover must be made to a Roth IRA account owned by the designated beneficiary of the 529 and is subject to the annual Roth funding limit (currently $6,500 for individuals under 50 years old), with a lifetime maximum of $35,000. However, Roth IRA income limits do not apply to rollovers from 529 plans, making this a unique opportunity for those with higher incomes.

Hypothetical grandparents' journey

A set of grandparents makes a one-time contribution this year of $100,000 to a 529 account naming their eight-year-old grandchild as beneficiary. This account, if compounded at 6% over 10 years, could grow to a balance of nearly $180,000. Suppose this grandchild attends college at an average cost of $39,000 per year over four years. Qualified distributions totaling approximately $157,000 are taken tax-free from the 529 account to cover the cost. Assuming the 529 account remains invested over this period and continues earning 6% annually, when their grandchild graduates the 529 account would have a remaining balance of approximately $44,000.

With the new SECURE 2.0 provision, that balance can be rolled over to a Roth IRA through distributions over the subsequent six years until the maximum eligible amount of $35,000 is reached.

Even if their grandchild never makes another contribution to the Roth IRA account, assuming a 7% annual rate of return, this Roth IRA could grow to approximately $550,000 by the time their grandchild reaches age 65.

Bottom line

The new rollover provision is an important development that could help address ongoing client concerns about overfunding 529 plans and participants or beneficiaries being subject to taxes and penalties when accessing the leftover funds. Given some of the complexities, financial advisors can help investors maximize the benefits of contributions to 529 plans for college and beyond.

Rollover to Roth IRA provision is effective for distribution beginning on or after January 1, 2024.

A thoughtful approach to investing in real estate

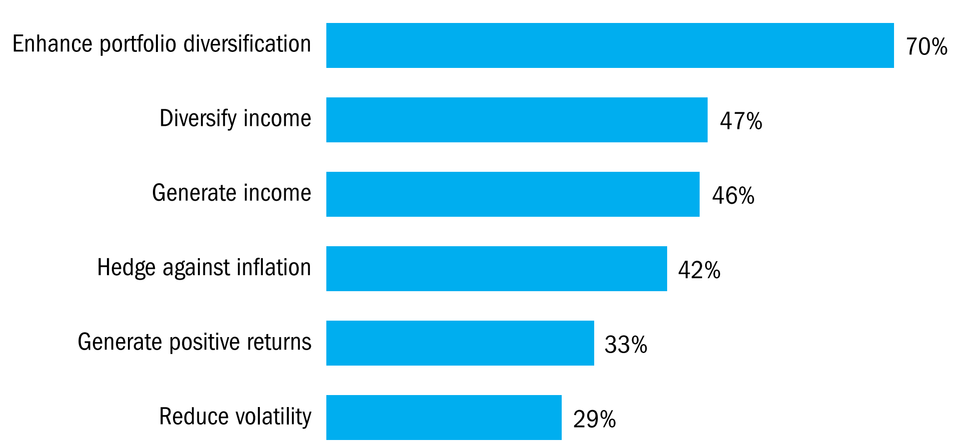
For long-term investors, real estate can serve as a portfolio diversifier while offering long-term growth and income. But investing in this asset class comes with some challenges. Products tracking broad equity benchmarks offer limited exposure to real estate. At the same time, many passive real estate investment trust (REIT) products use a traditional market-cap-weighted methodology and are not designed to meet investor goals. How can clients incorporate real estate into their portfolios?

We conducted an online survey of advisors[1] that provided important insights into the main considerations and challenges they face in seeking exposure to this asset class. Here's what we found.

The "why" to invest in real estate is clear

Our survey clearly indicated the importance of real estate as a driver of diversification, both in terms of return and risk. Real estate is also acknowledged for its ability to generate income and for its role in hedging against inflation.

REASONS ADVISORS ALLOCATE TO REAL ESTATE



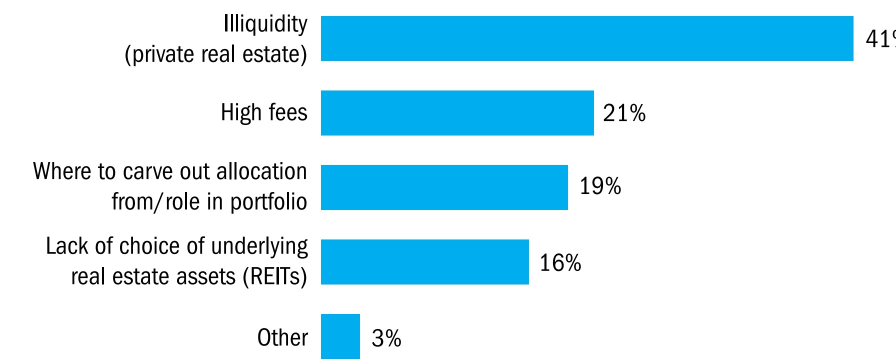
Source: Columbia Threadneedle Investments

The "how" to invest in real estate is a more challenging question

There are many ways to invest in real estate, including direct investment, REITs, mutual funds and exchange traded funds (ETFs), each with their own benefits and drawbacks.

For example, if an investor has a shorter time horizon, a direct investment in real estate — which is less liquid — might not be the most appropriate way to gain access to the asset class. When we asked about considerations for investing in real estate, our survey found that illiquidity and high fees were the biggest concerns.

CHALLENGES WHEN ALLOCATING TO REAL ESTATE

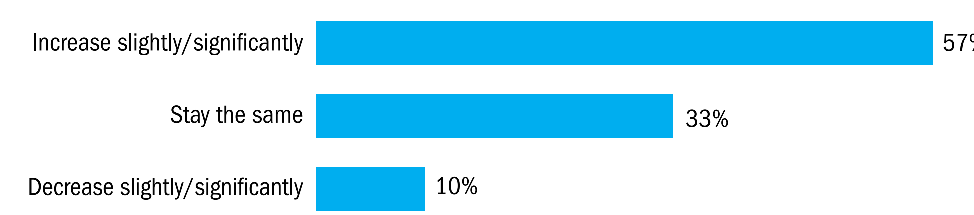


Source: Columbia Threadneedle Investments

ETFs look to be a vehicle of choice

Vehicles like REIT ETFs and mutual funds are favored because they offer broad exposure to the real estate market at lower costs. ETFs generally offer lower fees relative to other vehicles. They also offer meaningful diversification by providing access to different types of real estate, including commercial, residential and office, across different geographies. Other benefits for investing in real estate ETFs over other vehicles include tax efficiency (ETFs typically have lower capital gains distributions than mutual funds) and liquidity. These benefits help explain why over half of existing REIT ETF investors are expected to increase their allocations within the next one to two years.

HOW ALLOCATIONS TO REAL ESTATE MAY CHANGE IN THE NEXT 12-24 MONTHS



Source: Columbia Threadneedle Investments

It's necessary to navigate a variety of approaches when investing in real estate. But the enhanced diversification and return potential make the effort worthwhile.

[1] Online surveys via Connecting Advisors fielded February 27, 2023–March 3, 2023.

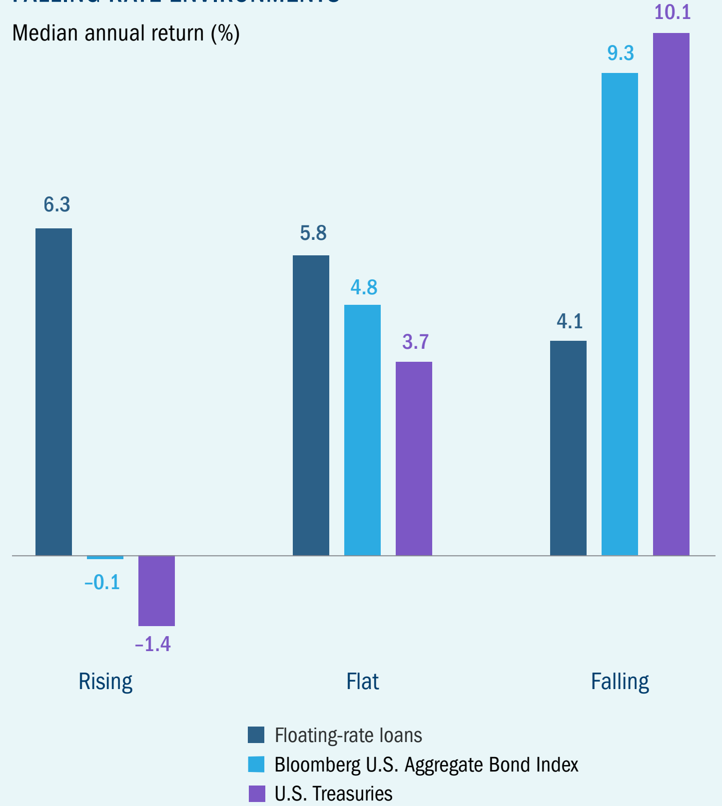
WHY FLOATING-RATE FUNDS IN TODAY'S MARKET

The appeal of floating-rate loans usually peaks when interest rates are rising. But they may help diversify portfolios in any environment.

Floating-rate loans are known by many names, including bank loans, senior loans and leveraged loans. They're typically extended to companies with higher levels of debt relative to cash flow, and because of this, they carry greater credit risk than investment-grade bonds. But unlike traditional bonds, floating-rate loans don't make a fixed-interest payment, or coupon, each period. Instead, their coupons reset every 30 or 90 days, floating up or down with the changes in prevailing interest rates. This floating feature makes loan prices less sensitive to shifts in interest rates, so flows into floating-rate loan funds tend to increase when the Federal Reserve is actively raising rates in response to a growing economy and improved labor market. And, as you can guess, this trend tends to reverse when rates are falling.

Historically, floating-rate loans have outperformed in rising and flat interest-rate environments. When rates are rising, the median annual return for floating-rate loans, as gauged by the Credit Suisse Leveraged Loan Index, has exceeded the return on U.S. Treasuries and the Bloomberg U.S. Aggregate Bond Index by more than six percentage points since 1993. But what's possibly overlooked is that floating-rate loans have also delivered attractive absolute and relative performance regardless of the broader interest-rate environment. Because yield is a significant component of total return, floating-rate loans also have outperformed U.S. Treasuries and the Bloomberg U.S. Aggregate Bond Index when rates are flat. It's only when rates fall that we have seen floating-rate loans underperform.

FLOATING-RATE LOANS IN RISING, FLAT AND FALLING RATE ENVIRONMENTS



Source: Credit Suisse and Bloomberg Indices. "Rising" indicated by an increase of more than 50 bps. "Falling" indicated by a decrease of more than 50 bps. Data reflects rolling 12-month periods from 01/31/93 through 12/21/22. Past performance is not a guarantee of future results.

Diversification potential in any rate environment.

Although their interest-rate-related characteristics are what drive investors' flows into and out of the asset class, floating-rate loans can help diversify a portfolio at any time — and this benefit can be overlooked. Most of the return in floating-rate loans comes from their exposure to credit risk (exposure to corporations), while the Bloomberg U.S. Aggregate Bond Index gets most of its return from duration risk (interest-rate sensitivity). So, historically they've had low correlation to each other and behave differently in different market environments.

Bottom line

Floating-rate loans tend to be popular when interest rates are rising, but they may have diversification benefits in any interest rate environment.

Diversification does not assure a profit or protect against loss.

Floating rate loans typically present greater risk than other fixed-income investments as they are generally subject to legal or contractual resale restrictions, may trade less frequently and experience value impairments during liquidation.

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The Bloomberg U.S. Aggregate Bond Index is a market-value-weighted index that tracks the daily price, coupon, pay-downs and total return performance of fixed-rate, publicly placed, dollar-denominated and non-convertible investment-grade debt issues with at least $250 million par amount outstanding and with at least one year to final maturity.

The Credit Suisse Leveraged Loan Index tracks the investable market of the U.S.-dollar- denominated leveraged loan market. It consists of issues rated "5B" or lower, meaning that the highest rated issues included in this index are Moody's/S&P ratings of Baa1/ BB+ or a1/BBB+. All loans are funded term loans with a tenor of at least one year and are made by issuers domiciled in developed countries.

Indices shown are unmanaged and do not reflect the impact of fees. It is not possible to invest directly in an index.

REFINITIV LIPPER FUND AWARDS
2023 WINNER
UNITED STATES

Two Columbia Threadneedle funds earn prestigious Lipper Fund Awards

Columbia Threadneedle Investments is pleased to announce that Columbia Dividend Income Fund and Columbia Global Technology Growth Fund have received prestigious 2023 U.S. Refinitiv Lipper Fund Awards as high-performing mutual funds in their respective Lipper classifications. The awards recognize funds for outperformance versus their peers. These Columbia funds were recognized as top funds, with Columbia Global Technology Growth Fund winning for a fifth consecutive year. The award-winning Columbia funds showcase the firm's consistent performance, deep knowledge and expertise.

Please click the fund names below to visit our website and learn more about these award-winning funds.

U.S. LIPPER FUND AWARDS (for the period ending 11/30/22)

Columbia Dividend Income Fund
Best in 10-year performance
Institutional 3 Class shares
Equity Income Funds category
82 funds

Columbia Global Technology Growth Fund
Best in 10-year performance
Institutional 2 Class shares
Science & Technology Funds category
34 funds

Investors should carefully consider the investment objectives, risks, charges and expenses of a fund before investing. To obtain a prospectus containing this and other important information, please visit columbiathreadneedleus.com to view or download a prospectus. Read the prospectus carefully before investing.

Past performance is not a guarantee of future results.

The Lipper Fund Awards are based on the Lipper Leader for Consistent Return rating, which is a risk-adjusted performance measure calculated over 36, 60 and 120 months. The highest Lipper Leader® for Consistent Return (Effective Return) value within each eligible classification determines the fund classification winner over three, five or 10 years. For a detailed explanation, please review the Lipper Leaders methodology document.

NEW GENERATION, NEW RETIREMENT

A look at recent trends underscores the importance of goal-based advice and financial planning

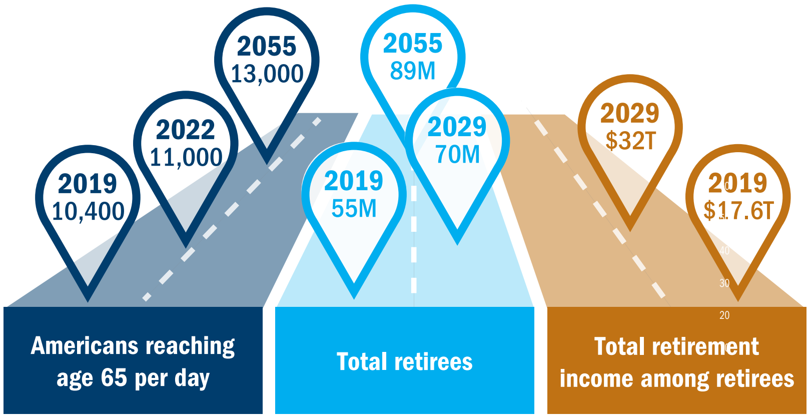
In a research study, we learned that saving for retirement is a top focus for clients.[1] Changes in the retirement landscape indicate that financial planning will take on even greater importance for younger generations.

The charts below illustrate the meaningful shifts related to retirement. The COVID-19 pandemic brought on early retirements and mass layoffs. Recent market volatility has created uncertainty among investors, and expenses like health care and long-term care continue to increase. A look at current trends underscores the importance of planning — not only to save for retirement but also to create lasting income during retirement years.[2]

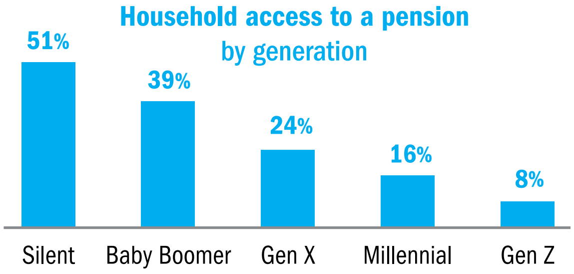
As individuals approach retirement, it's important they effectively manage their savings to create lasting income. **Yet more than 60% of households don't have a formal plan to manage assets, income and expenses in retirement.**

Based on our research, engaging in goal-based advice and financial planning relationships are more important than ever.

The number of retirees increases in the U.S. over the next several decades.



While pensions are currently a top source of retirement income, they're largely phasing out as a retirement savings vehicle. Younger generations will have to prepare for retirement using methods other than pensions.



[1] Financial Goals Quick Poll Study, November 2022, Ameriprise Strategic Insights.

[2] LIMRA Fact Book on Retirement Income, 2022. Includes those with $100,000-plus of annual retirement income.

Investing smarter for the world you want

Columbia Threadneedle Investments offers investment solutions to make a difference in your world, and the wider world. Millions of people rely on the firm to manage their money and invest for their future; together they entrust the firm with $608/€559 billion. Columbia Threadneedle is globally connected with a team of over 650 investment professionals providing diverse expertise, spanning almost every asset class and market. The firm is intense about research, believing that original independent research makes investment decisions smarter.

Columbia Threadneedle has a responsible ethos as investment decisions today help define the future we all seek. Every day the firm looks for opportunities to improve how it invests and what clients experience; a focus on continuous improvement means that Columbia Threadneedle never stands still. Whatever world you want, Columbia Threadneedle's purpose is to help you achieve it.

Source: Columbia Threadneedle Investments as of March 31, 2023.

To find out more, call 800.426.3750
or visit columbiathreadneedle.com

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