Homestead Funds

Quarterly Market Review

Fourth Quarter 2023

Summary

- The market rally was back on in the fourth quarter as inflation turned a corner and interest rates retreated. On signs that inflation was moderating at a better pace, the Federal Reserve (Fed) opted to pause rate hikes in the period. Markets began to convene around a new consensus viewpoint that hikes are most likely finished, and the Fed may even begin cutting its target rate early in 2024.
- Stocks rallied on the changing interest rate outlook, and the gains were broad-based across sectors. Most stock indexes delivered double-digit gains for 2023.
- The turnaround in rates also drove a historic rally in bonds. Bond prices predictably rose as rates went down, but bonds got an added boost from tightening credit spreads. The yield curve remains inverted. Markets are forecasting about six quarter-point rate cuts over the course of 2024.

This commentary was prepared on January 9, 2024, and reflects our view of events at that time. Please visit our website, homesteadfunds.com, for the latest perspectives.

Markets Deliver a Strong Finish for 2023

Markets delivered a powerful finish to the year, with stocks and bonds both rebounding from the third-quarter pullback to post gains in the last period of 2023. The investment backdrop shifted considerably as the fight against inflation turned a corner. Interest rates retreated, and stocks and bonds both rallied.

While stock performance in the first half of 2023 was dominated by tech names and the momentum of artificial intelligence innovations, investment gains in the fourth quarter were broad-based across sectors, stock styles and market-cap ranges.

Inflation Turns a Corner and Rates Follow

The fourth quarter proved to be a turning point in the trajectory of inflation. In October's monthly report, inflation was lower than expected for prices on core items (excluding volatile food and energy inputs). Later data reinforced the growing consensus that the pandemic-driven price pressures had eased significantly. In response, the Fed paused its rate hikes, leaving rates unchanged throughout the quarter.

In fact, market expectations shifted toward a growing consensus that the rate-hiking cycle is finished. By the end of the year, futures markets were reflecting forecasts of six or so rate cuts to come in 2024, though the Fed has been more conservative in its estimates. In response to the changing outlook, yields fell for most bond maturities and across other market rates, such as mortgages and credit cards.

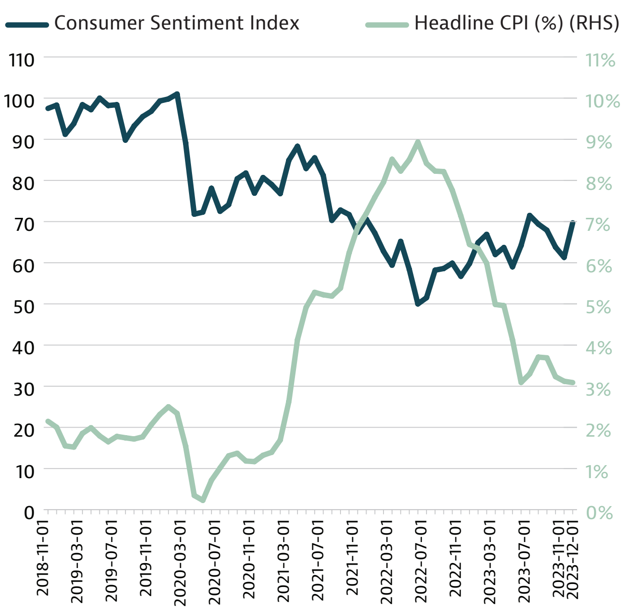
The investment backdrop shifted considerably as the fight against inflation turned a corner.

Lower Inflation Means Happier Consumers

Households felt the boost of easing inflation in real time, and it showed up in rising consumer sentiment numbers in the fourth quarter.

Consumers were generally faring well as 2023 came to a close. The labor market proved to be strong through the year, with ongoing payroll gains in the fourth quarter and job openings continuing at high levels. Unemployment remained low, boosting household finances and confidence levels. Against that backdrop, lower inflation levels had a clear effect on improved consumer sentiment, and people indicated that they also had falling expectations for inflation in the future.

Consumer Sentiment Climbs as Inflation Falls



Source: Federal Reserve Bank of St. Louis

Households felt the boost of easing inflation in real time, and it showed up in rising consumer sentiment numbers in the fourth quarter.

Bonds

In the fourth quarter, bonds surged higher amid the changing interest rate dynamics. Rates fell for most bond maturities by a full percentage point from peak levels in late October. The yield curve remains inverted. A possibility of recession lingers, and some economic markers were softer in the fourth quarter compared with the third quarter. For instance, the December reading for the Services Purchasing Manager Index was down to 50.6%, an atypically low level and very close to dipping below the 50 mark, below which is considered a contraction.

The other component of bond yields, the credit spread, compressed in the fourth quarter. Credit spreads measure the difference in yield between corporate bonds and similar-duration Treasuries. After widening sharply during the March failure of Silicon Valley Bank, spreads came back down and spent much of 2023 in a stable zone before compressing further in the fourth quarter. The year-end rally suggests a market that has confidence in both the fundamentals of borrowers and credit conditions.

Performance Attribution for Our Bond Funds

Against this backdrop, the Homestead Short-Term Government Securities Fund (HOSGX) returned 3.23% in the fourth quarter, outperforming its benchmark, the ICE BofA 1-5 Year Treasury Index, which returned 3.10%. The fund's overweight exposure in mortgage-backed security (MBS) passthrough issues and collateralized mortgage obligations (CMOs) aided relative performance. Conversely, an overweight to agencies detracted slightly from fund returns.

The Homestead Short-Term Bond Fund (HOSBX) returned 3.41% in the quarter, outpacing its benchmark, the ICE BofA 1-5 Year Corporate/Government Bond Index, which returned 3.34%. The fund's underweight position in U.S. Treasuries boosted relative performance compared with the benchmark. Exposure to CMOs was also additive. Conversely, positioning in asset-backed securities (ABS) detracted from the fund's relative performance.

The Homestead Intermediate Bond Fund (HOIBX) returned 6.69% in the fourth quarter, trailing its benchmark, the Bloomberg U.S. Aggregate Index, which returned 6.82%. The fund's holdings in ABS detracted from relative returns, as did exposure to bonds from financial issuers and CMOs. Conversely, yield curve positioning and an underweight allocation to U.S. Treasuries helped the fund's performance compared with the benchmark.

Stocks

Stocks rebounded in the fourth quarter, with gains across categories of stocks. Performance was mixed across growth, value, small- and large-cap stocks. On a sector basis, real estate, technology and financials were top performers in the quarter. Energy was the only sector in the S&P 500 Index to record a loss, pressured by continued weakness in oil and commodity prices. More defensive sectors, such as utilities, health care and consumer staples, all posted mid to high single-digit gains for the fourth quarter.

Earnings trends continued to improve modestly, with analysts forecasting marginal year-over-year growth in quarterly earnings. The consensus forecasts project that S&P 500 Index companies will see earnings for companies in the S&P 500 Index up 1.3% on a year-over-year basis. Revenues are expected to grow about 3.1% year over year for the fourth quarter.

Performance Attribution for Our Stock Funds

The Homestead Value Fund (HOVLX) returned 10.63% in the fourth quarter, outpacing its benchmark, the Russell 1000 Value Index, which returned 9.50%. In the period, the fund's underweight allocation to consumer staples boosted relative returns, as did stock selection in holdings in the financials sector. Conversely, a small cash balance detracted from performance compared with the benchmark. Stock selection in the real estate sector and an overweight position in the health care sector also weighed modestly on relative performance.

Compared with the index, the fund holds overweights in industrials, communications services and health care stocks. Its largest underweight allocations continue to be in consumer staples and utilities stocks. With a bottom-up stock-picking process, our portfolio managers note that they consider diversification from a sector perspective but that they also look at company-level factors to balance the portfolio.

The Small-Company Stock Fund (HSCSX) returned 13.23% in the fourth quarter, trailing its benchmark, the Russell 2000 Index, which returned 14.03%. In the period, stock selection in the health care and consumer discretionary sectors detracted from the fund's relative performance. Conversely, stock picks in the industrials and materials sectors boosted returns.

Relative to its benchmark, the Small-Company Stock Fund is most underweight in the consumer staples, utilities and real estate sectors. The portfolio's most significant overweights are in the industrials, information technology and materials sectors. As in the Value Fund, the Small-Company Stock Fund's portfolio managers assemble the portfolio with a bottom-up approach, applying a company-specific approach to diversification.

Performance Attribution for Our Balanced Fund

The Rural America Growth & Income Fund (HRRLX) returned 7.29% in the fourth quarter, trailing its custom benchmark, a 60%/40% blend of the Russell 3000 Index and the Bloomberg Intermediate U.S. Government/Credit Bond Index, which returned 9.07% for the same period.

The fund's stock holdings underperformed their benchmark. Stock selection and overweight exposure in the information technology sector detracted from the fund's performance against its benchmark. Stock choices in the industrials sector also underperformed in the quarter. Conversely, stock choices and an overweight allocation in the real estate sector boosted performance, as did stock selection in the health care sector.

The fund's bond allocation performed in-line with its benchmark. The fund's underweight positioning in U.S. Treasuries boosted relative returns, as did holdings in MBS. Conversely, exposure to issues from the financials sector weighed on performance. An overweight to ABS also detracted from fund returns. Compared with its bond benchmark, the fund holds overweights in corporate bonds and agency-issued bonds. It is underweight in U.S. Treasury holdings.

Total Returns as of 12/31/2023

		Average Annual				
	Q4	1-yr	3-yr	5-yr	10-yr	Since fund's inception
Bond Funds						
Short-Term Government Securities Fund (HOSGX)	3.23%	4.68%	-0.72%	1.04%	0.93%	2.70%
ICE BofA 1-5 Year U.S. Treasury Index	3.10%	4.30%	-0.76%	1.21%	1.15%	3.39%
Expense ratio 0.80% (gross) 0.75% (net) (12/31/22)*						
Short-Term Bond Fund (HOSBX)	3.41%	5.40%	-0.58%	1.48%	1.45%	3.78%
ICE BofA 1-5 Year Corp./Gov. Index	3.34%	4.89%	-0.60%	1.55%	1.46%	3.97%
Expense ratio 0.76% (12/31/22)						
Intermediate Bond Fund (HOIBX)**	6.69%	6.35%	-3.06%	NA	NA	0.77%
Bloomberg U.S. Aggregate Index	6.82%	5.53%	-3.31%	1.10%	1.81%	0.55%
Expense ratio 0.87% (gross) 0.80% (net) (12/31/22)*						
Balanced Fund						
Rural America Growth & Income Fund (HRRLX)***	7.29%	6.74%	N/A	NA	NA	-1.59%
Blended Index****	9.07%	17.45%	N/A	NA	NA	2.81%
Expense ratio 2.85% (gross) 1.00% (net) (12/31/22)*						
Equity Funds						
Value Fund (HOVLX)	10.63%	12.86%	10.08%	12.88%	10.20%	10.26%
Russell 1000 Value Index	9.50%	11.46%	8.86%	10.91%	8.40%	9.63%
Expense ratio 0.62% (12/31/22)						
Small-Company Stock Fund (HSCSX)	13.23%	17.09%	5.50%	11.86%	5.83%	8.43%
Russell 2000 Index	14.03%	16.93%	2.22%	9.97%	7.16%	7.31%
Expense ratio 1.05% (12/31/22)						

The total returns shown above represent past performance, which does not guarantee future results. Investment return and principal value of an investment will fluctuate. An investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be higher or lower than the performance data quoted. For performance data current to the most recent month-end, call 800.258.3030 or visit homesteadfunds.com.

The expense ratio shows the percentage of fund assets deducted annually to cover operating expenses. Fund expense ratios shown here do not include acquired fund fees and expenses. If applicable, these additional costs are disclosed in the prospectus. The net expense ratio is the expense ratio minus the portion of expenses waived or reimbursed.

*Homestead Advisers has contractually agreed, through at least April 30, 2024, to limit the fund's operating expenses to an amount not to exceed 0.75% (Short-Term Government Securities Fund), 0.80% (Intermediate Bond Fund) or 1.00% (Rural America Growth & Income Fund) of the Fund's average daily net assets. Operating expenses exclude interest; taxes; brokerage commissions; other expenditures that are capitalized in accordance with generally accepted accounting principles; other extraordinary expenses not incurred in the ordinary course of the Fund's business; and acquired fund fees and expenses such as the fees and expenses associated with an investment in (i) an investment company or (ii) any company that would be an investment company under Section 3(a) of the Investment Company Act of 1940, as amended (the "1940 Act"), but for the exceptions to that definition provided for in Sections 3(c)(1) and 3(c)(7) of the 1940 Act. This waiver agreement will terminate immediately upon termination of the Fund's Management Agreement and may be terminated by the Fund upon 60 days' notice.

**The inception date of this fund is May 1, 2019.

***The inception date of this fund is May 1, 2021.

****The Fund's Blended Index is a 60%/40% blend of the Russell 3000 Index and the Bloomberg Intermediate U.S. Government/Credit Bond Index.

Equity Fund Management

Mark Iong, CFA®
Equity Portfolio Manager

Mark co-manages Rural America Growth & Income Fund and Homestead Advisers' large-cap strategies. Mark is a graduate of Cornell University, where he received a BS in operations research and information engineering. He holds the Chartered Financial Analyst designation.

Jim Polk, CFA®
Head of Equity Investments

Jim co-manages Homestead Advisers' equity strategies. He is a graduate of Colby College, where he received a Bachelor of Arts degree in English. He received his MBA from the Olin Graduate School of Business at Babson College. Jim holds the Chartered Financial Analyst designation.

Bond Fund Management

Mauricio Agudelo, CFA®
Head of Fixed-Income Investments

Mauricio co-manages Homestead Advisers' fixed-income strategies. He received a BS in finance from the University of Maryland, Robert H. Smith School of Business. He minored in business culture and language, with a concentration in Spanish. He holds the Chartered Financial Analyst designation.

Ivan Naranjo, CFA®, FRM®
Fixed-Income Portfolio Manager

Ivan co-manages Homestead Advisers' fixed-income strategies. Ivan received a BS in finance from the University of Maryland, Robert H. Smith School of Business. He holds the Chartered Financial Analyst and Financial Risk Manager designations.

Prepared: January 9, 2024

This material represents an assessment of the market and economic environment at a specific point in time and is not intended to be a forecast of future events, or a guarantee of future results. Forward-looking statements are subject to certain risks and uncertainties. Actual results, performance or achievements may differ materially from those expressed or implied. Information is based on data gathered from what we believe are reliable sources. It is not guaranteed as to accuracy, does not purport to be complete and is not intended to be used as a primary basis for investment decisions. It should also not be construed as advice meeting the particular investment needs of any investor.

Neither asset allocation nor diversification guarantee a profit or protect against a loss in a declining market. They are methods used to help manage investment risk.

The standard definition of a recession offered by the National Bureau of Economic Research (NBER) is two consecutive quarters of declining economic growth.

Debt securities are subject to interest rate risk, credit risk, extension risk, income risk, issuer risk and market risk. The value of U.S. Government securities can decrease due to changes in interest rates or changes to the financial condition or credit rating of the U.S. Government. Investments in asset-backed and mortgage-backed securities are also subject to prepayment risk as well as increased susceptibility to adverse economic developments. High-yield, lower-rated, securities involve greater risk than higher-rated securities.

Equity securities generally have greater price volatility than fixed-income securities. The market price of equity securities may go up or down, sometimes rapidly or unpredictably. Equity securities may decline in value due to factors affecting the issuer or equity securities markets generally.

Loans are subject to risks involving the enforceability of security interests and loan transactions, inadequate collateral, liabilities relating to collateral securing obligations, and the liquidity of the loans.

Growth and value stocks are subject to the risk that returns on stocks within the style category will trail returns of stocks representing other styles or the market overall over any period of time and may shift in and out of favor with investors generally, sometimes rapidly, depending on changes in market, economic, and other factors. Growth stocks can be volatile, as these companies usually invest a high portion of earnings in their business and therefore may lack the dividends of value stocks that can cushion stock prices in a falling market. Also, earnings disappointments often lead to sharply falling prices because investors buy growth stocks in anticipation of superior earnings growth. Investments in value securities may be subject to risks that (1) the issuer's potential business prospects will not be realized; (2) their potential values will never be recognized by the market; and (3) their value was appropriately priced when acquired and they do not perform as anticipated.

Securities of small and medium-sized companies tend to be riskier than those of larger companies. Compared to large companies, small and medium-sized companies may face greater business risks because they lack the management depth or experience, financial resources, product diversification or competitive strengths of larger companies, and they may be more adversely affected by poor economic conditions. There may be less publicly available information about smaller companies than larger companies. In addition, these companies may have been recently organized and may have little or no track record of success.

Index Definitions: The **ICE BofA 1-5 Year U.S. Treasury Index** measures the performance of short-term U.S. Treasury securities. The **ICE BofA 1-5 Year Corp./Gov. Index** measures the performance of U.S. government and investment-grade corporate debt. The **Bloomberg U.S. Aggregate Index** is a broad-based benchmark that measures the investment-grade, U.S. dollar-denominated, fixed-rate taxable bond market. The **Blended Index** is composed of the Russell 3000 and the Bloomberg Intermediate U.S. Government/Credit Bond Index in a static 60/40 allocation. The Russell 3000 is a market capitalization-weighted benchmark index made up of the 3000 largest U.S. stocks, which represent about 98% of the U.S. equity market. The Bloomberg Intermediate U.S. Government/Credit Bond Index is a broad-based flagship benchmark that measures the non-securitized component of the U.S. Aggregate Index with less than 10 years to maturity. Indices are unmanaged and investors cannot invest directly in an index. The **Dow Jones Industrial Average** measures the stock price performance of 30 actively traded, blue chip companies. The **ISM Manufacturing Index** is an indicator of recent U.S. economic activity based on a survey of purchasing managers at manufacturing firms. The **MSCI EAFE Index** represents the performance of large- and mid-cap securities across 21 developed markets, including countries in Europe, Australasia and the Far East, excluding the U.S. and Canada. The **MSCI Emerging Markets Index** represents the performance of large- and mid-cap securities in emerging market countries, including China, South Korea, Taiwan, India and Brazil. The **Russell 1000 Index** is a subset of the Russell 3000 Index and measures the performance of the 1,000 largest companies in the Russell 3000 Index. The **Russell 2000 Index** is a subset of the Russell 3000 Index and measures the performance of the 2,000 largest companies in the Russell 3000 Index. The **Russell 1000 Growth Index** measures the performance of those Russell 1000 companies with higher price-to-book ratios and higher forecasted growth values. The **Russell 2000 Growth Index** measures the performance of those Russell 2000 companies with higher price-to-book ratios and higher forecasted growth values. The **Russell 1000 Value Index** measures the performance of those Russell 1000 companies with lower price-to-book ratios and lower forecasted growth values. The **Russell 2000 Value Index** measures the performance of those Russell 2000 companies with lower price-to-book ratios and lower forecasted growth values. The **Standard & Poor's Stock Index** is a broad-based measure of U.S. stock market performance and includes 500 widely held common stocks. The **Standard & Poor's 500 Value Index** is a subset of the S&P 500 Index and consists of those stocks in the S&P 500 Index exhibiting the strongest value characteristics. Indices are unmanaged and investors cannot invest directly in an index. Unless otherwise noted, index performance does not account for any fees, commissions or other expenses that would be incurred. Index returns do not include reinvested dividends. The **Consumer Confidence Index** is an indication of future developments of households' consumption and saving, based upon answers regarding their expected financial situation, their sentiment about the general economic situation, unemployment and capability of savings. The **University of Michigan Consumer Sentiment Index** is a consumer confidence index published monthly by the University of Michigan. The **Services Purchasing Manager Index** tracks economic activity in the services sector.

Investing in mutual funds involves risk, including the possible loss of principal. **Past performance does not guarantee future results.**

Investors should carefully consider fund objectives, risks, charges and expenses before investing. The prospectus contains this and other information about the funds and should be read carefully before investing. To obtain a prospectus, call 1-800-258-3030 or visit homesteadfunds.com.

Homestead Funds' investment advisor and/or administrator, Homestead Advisers Corp., and distributor, Homestead Financial Services Corp., are indirect, wholly owned subsidiaries of NRECA. Homestead Financial Services Corp., Distributor. 1/2024