



Tom Slefinger  
Market Strategist

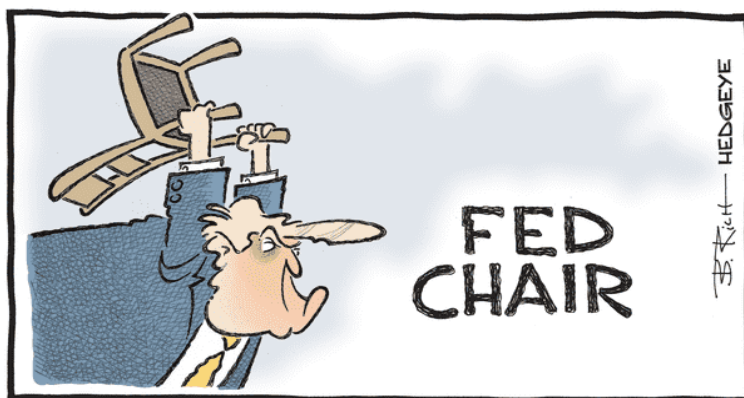
# Weekly Relative Value

WEEK OF MAY 18, 2026

## Baptism of Fire

The Senate narrowly confirmed Kevin Warsh as Chair of the Federal Reserve, setting up the most controversial leadership transition at the U.S. central bank in decades and a test of its independence. The 54-45 vote last Wednesday was the slimmest confirmation margin ever for a head of the central bank, reflecting polarized politics in Congress and Democratic fears that Warsh will bend to President Donald Trump's demands to rapidly lower interest rates.

A politically charged environment is an uncommon start for a Fed Chair. Trump has strongly advocated for significant rate cuts, supported by advisors like Stephen Miran, who has been the lone voice for steep reductions within the Fed. Warsh has not clearly supported immediate rate cuts and pointed out that he made **"no promises"** to Trump about rate policy.



The main question and concern looming over the incoming chair is whether he'll maintain the Fed's tradition of making interest-rate decisions free from political pressure. Elizabeth Warren has been one of his most vocal critics, stating that Trump nominated Warsh to be his **"sock puppet"** in controlling interest rates. During the Senate Banking Committee hearing, Senator John Kennedy pressed him directly, asking if he would be Trump's **"human sock puppet."** Warsh replied, **"Absolutely not."** He emphasized that the president had never asked him to commit to any specific interest rate path, and that he would never agree to such a request.

Historically, Warsh often had a hawkish bias during his time as a Fed governor from 2006 to 2011, especially after the global financial crisis. He faulted the Fed's performance on fighting inflation during the Biden years, suggesting the Fed lost focus on its core mission. Of late, his remarks have leaned in the opposite direction.

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### THIS WEEK

- THE END OF FORWARD GUIDANCE?
- THE BALANCE SHEET AND THE YIELD CURVE
- CONSUMER STRESS BUILDS
- AMERICAN DEBT
- SOMETHING HAS TO GIVE
- SALES IN DEEP FREEZE
- WAR AND INFLATION
- PPI EXPLODES HIGHER
- MARKET OUTLOOK AND PORTFOLIO STRATEGY



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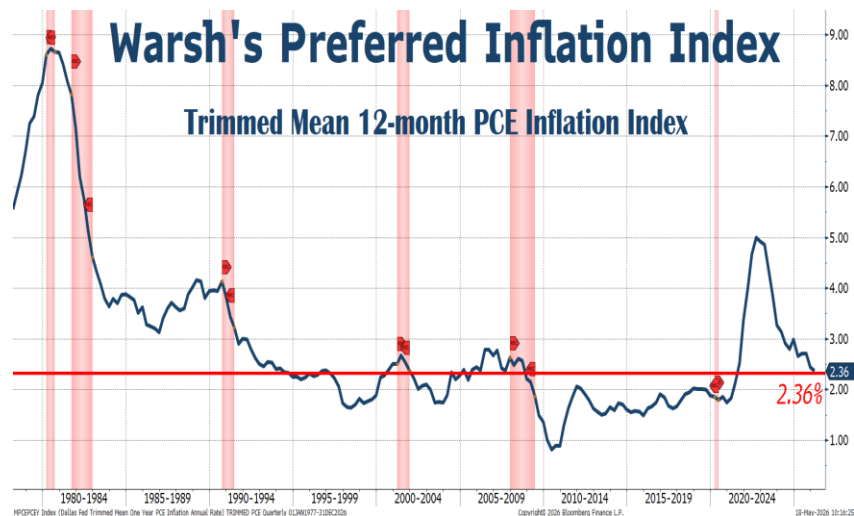


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Warsh has also been critical of the Fed getting too involved in the markets, suggesting he might support a more hands-off approach. Compared to the era under Alan Greenspan, Bernanke and Yellen, markets may find the so-called “Warsh Put” less dependable.

He’s also no “inflationista,” mainly because he believes artificial intelligence (AI) will boost productivity and supply, which could help the economy grow without fueling inflation. That suggests he may support policies aimed at sustaining expansion rather than keeping rates elevated for longer.

He's also doubtful of current measures of inflation, preferring instead trimmed mean or median measures — both of which are running below headline or core Personal Consumption Expenditures (PCE) inflation.



As we are fully aware, Trump lambasted “Too Late” Powell (whom he appointed) repeatedly for not cutting rates fast enough and has made it clear he expects Warsh to lower borrowing costs immediately. So, while appointed by Trump, Warsh will likely still face public criticism from the president if he does not do as he’s told, as others have.

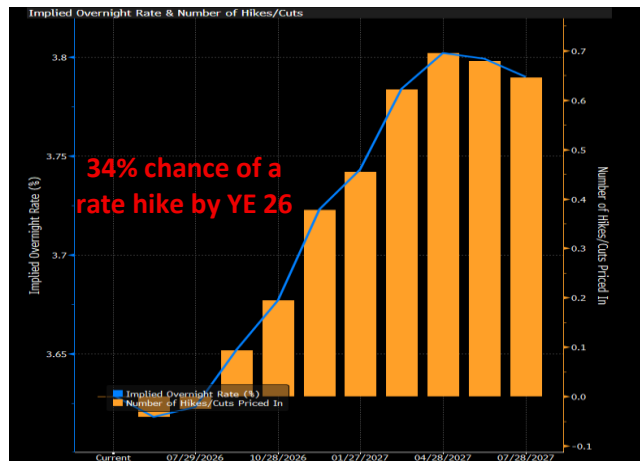
All the while, an increasing number of Fed officials are arguing the Fed should signal explicitly that its next rate move could be either a “cut” or a “hike.” So, even if he succumbs to the president’s whims, convincing his fellow Federal Open Market Committee (FOMC) members may prove trickier.

Powell has said he will remain a Fed governor until he chooses to step down, so Warsh’s appointment to Stephen Miran’s seat can proceed. However, Trump will lose a vote in the process. Meanwhile, a June ruling on Lisa Cook’s governorship and the administration’s effort to remove her could further shape views of Fed independence.

Warsh’s leadership will also face an immediate credibility test, and Powell’s continued presence only adds to the intrigue. Together, these dynamics could make Warsh’s tenure especially volatile for markets, with investors reacting closely to both his decisions and his rhetoric.

Still, it’s impossible to know how exactly Warsh will govern as Fed chair.

Warsh wants lower rates to appease Trump, but the market now thinks the next move is a hike. Warsh will not only be fighting the rest of the FOMC committee. He will be fighting the bond market itself. Good luck with that. Currently, the futures market is pricing in a 34% chance of a hike by year-end, up from just 6% last week.



## THE END OF FORWARD GUIDANCE?

After the global financial crisis, forward guidance became a key tool for the Federal Reserve. By making explicit commitments, the Fed was able to anchor the yield curve, reduce volatility and maintain easy financial conditions even when interest rates were at the zero lower bound.

That said, Warsh has been critical of the Fed's heavy use of forward guidance. He prefers a less predictable approach, favoring flexibility over managed expectations. As such, under Warsh, the Fed would likely avoid firm commitments and rely more on incoming data, resulting in greater meeting-by-meeting changes.

If forward guidance is removed or weakened, uncertainty about the policy path is likely to increase, causing sharper market adjustments during each FOMC meeting.

Kevin Warsh cannot control interest rate policy by himself, but he is likely to stop month-to-month forward guidance.

## THE BALANCE SHEET AND THE YIELD CURVE

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*"The Fed should exit markets outside of crises." — Kevin Warsh*

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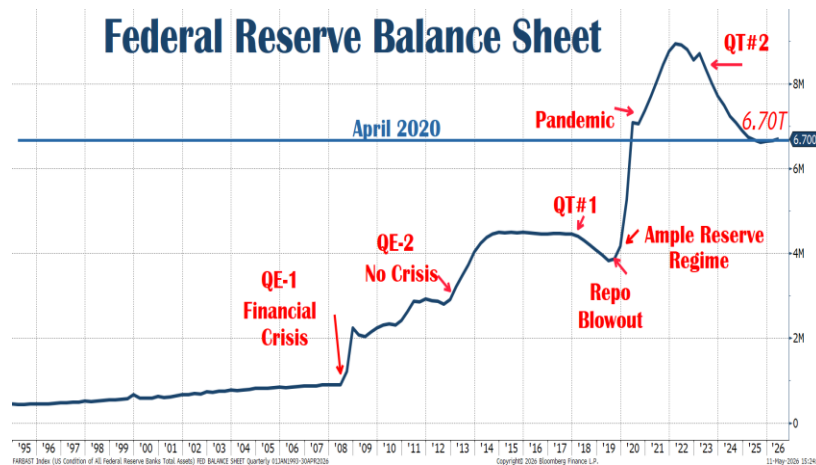
The Fed can impact Treasury yields through interest rates or balance sheet management. Warsh's views on this issue are crystal clear. As he said in his confirmation hearing:

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***"The Fed has an interest rate tool and a balance sheet tool. My view is the interest rate tool gets in the cracks. It's fairer. The balance sheet tool disproportionately helps those with financial assets. The interest rate tool hits the entire economy. So we need a new framework, new tools. [...] Slowly and deliberately, I believe we need a smaller central bank balance sheet."***

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The central bank currently holds about \$4.4 trillion in Treasuries and \$2.0 trillion in mortgage-backed securities (MBS). Both peaked in mid-2022 and are now declining, though Treasury holdings ticked up slightly since November 2025.



Warsh is expected to oppose balance sheet expansion and favor more quantitative tightening, which would likely steepen the yield curve and raise long-term yields. This could conflict with Mr. Trump's "affordability campaign," as higher yields increase mortgage rates and may offset the impact of any policy rate cuts.

**Bottom line:** His prescription is straightforward. Shrink the balance sheet. Take the Fed out of markets unless there's a crisis. In doing so, you reduce the inflation pressure it's been generating. And with lower inflation, you can actually bring interest rates down, which is what the real economy needs.

At the same time, if the Warsh-led Fed resumes balance sheet reductions, this also means less liquidity and the curve is likely to steepen, where short-term yields decline more sharply while long-term rates remain anchored by term premia and subdued demand for U.S. bonds.

Kevin Warsh finds himself in an extraordinarily difficult situation as he begins his tenure as Fed chair. Additionally, Warsh's leadership and communication skills will be tested and may contribute to increased market volatility, as markets continually adjust expectations between forward guidance and actual decisions.

Warsh's baptism of fire is coming right up.

Warsh will NOT deliver a rate cut in June. And the administration will likely react negatively. That much is clear.

Expect fireworks on June 17, the next FOMC meeting. The world will be tuned in.

## CONSUMER STRESS BUILDS

*"We need to fill up the car to get to work, to get the kids to school. We need to eat. These aren't purchases that households can avoid or put off... This really is putting the squeeze on a lot of U.S. households."*

— Sarah House, Senior Economist, Wells Fargo & Co

Trump was elected in part due to Americans' frustrations with high prices, but he has largely focused his attention on foreign wars and White House renovations.

Pressed about the impact of the war on American consumers, this was the exchange between a reporter and Trump:

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**Reporter:** *What extent are Americans' financial situation motivating you to make a deal?*  
**Trump:** *Not even a little bit. I don't think about Americans' financial situation.*

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Republican strategist Alex Conant said it was important for the White House to show they are focused on the issue, arguing that the:

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*"Cost of living is the number one issue for voters; it better be the number one issue for Trump."*

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And then we have this little ditty from the *Financial Times*: **"US taxpayers foot \$25bn bill as Iran conflict weighs heavily on economy."** This is just the running war tab for Uncle Sam. What about the American consumer? Well, the cost to households has now reached \$35 billion and is rising each day the Strait is closed. That may not sound like a whole lot, but it amounts to nearly \$270 per household, which is the cost of a week's groceries. But don't worry, the boom in credit card usage will surely save the day.

This is not a data point, but it says a whole lot about the current state of the U.S. consumer, which was on full display on the front-page article of *The New York Times* titled **"Consumers Lean on a 'Hamster Wheel' of Credit to Manage Rising Costs"** with more evidence of contracting real wages and a household sector feeding off credit card usage to make ends meet. The tagline just says it all:

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*"As prices increase for gas, groceries and other staples, more and more households are borrowing to get by."*

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**Bottom line:** The average person is not really getting ahead. The U.S. consumer is on an increasingly fragile footing, and the current status quo (with an extremely low savings rate,) is completely unsustainable.

## AMERICAN DEBT

I was watching CNBC last week and a consumer credit expert from one of the big U.S. banks was being interviewed. She waxed on and on about this recent acceleration in credit card growth and what terrific news that is. Credit card debt hit \$1.25 trillion in Q1 2026 up 5.9% year over year. She stopped before adding that it is the bank that will be the one doing great from this development, and why not, with credit card interest rates at 21%?

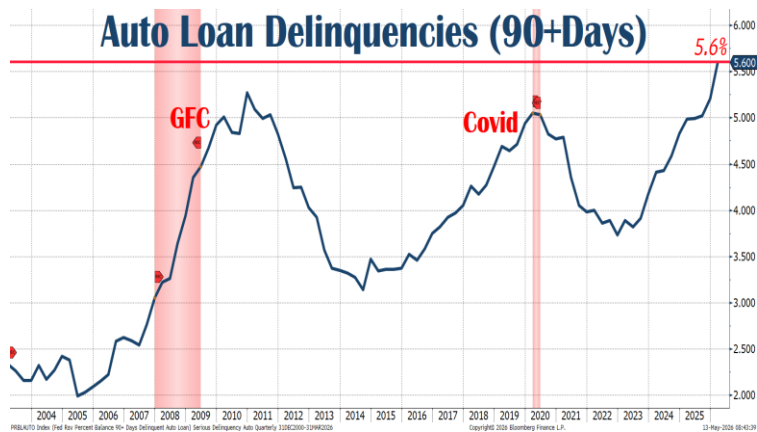
Here's a little secret. Nobody is taking on credit card growth at these sky-high rates because they feel good. They are doing it to subsist. Currently, 27 million Americans can only afford the minimum payment each month, and consumers paid \$160 billion in interest charges in 2024 alone, up from \$105 billion in 2022.

Had I been on that CNBC segment, I would have asked if this bank rep was aware that there is a historical (going back thirty years) -60% inverse correlation between credit card usage and consumer sentiment? It's a classic contra-cyclical move.

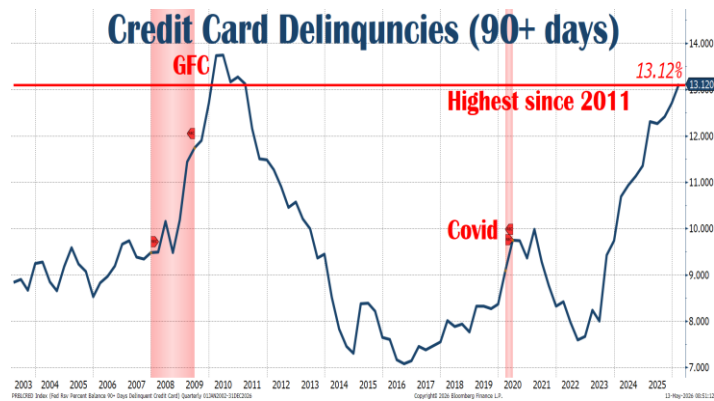


The deterioration was broad-based across every major consumer credit category:

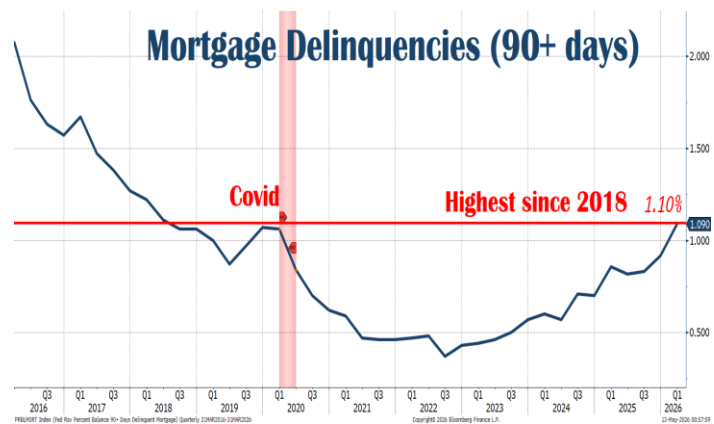
- Auto loan delinquency has risen to an all-time high of 5.6% of the balance. That’s higher than the peaks after the great financial crisis or the pandemic. The jump in a single quarter was +0.4 %, the largest one-quarter increase since Q4 2010.



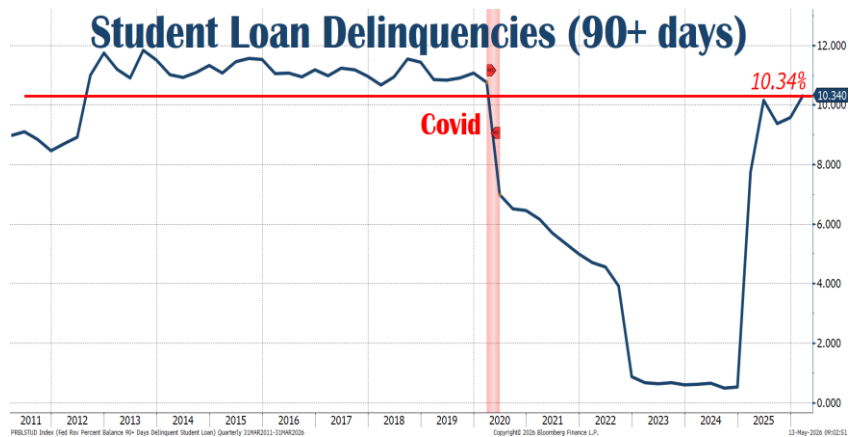
- Credit card delinquency jumped from 12.7% to 13.1% and is the highest since Q1 2011 after the end of the global financial crisis. Even as credit card delinquency rates have soared to 15-year highs and the average interest rate is 21%, applications for more cards just hit the highest level in four years.



- Mortgage loan delinquency increased from 0.9% to 1.1%, the highest since Q2 2018.



- Student loan delinquency increased from 9.6% to 10.3%, the highest since Q1 2020 (when various relief measures came in). This is more bad news for the apartment rental market.



And finally, all of this is happening at a time when personal bankruptcies (Chapter 13) have surged ~17% over the year to March to the highest level since the depths of pandemic despair back in the winter of 2020.

**Bottom line:** Taken together, this data strongly suggests that consumers will increasingly be forced to retrench discretionary spending and redirect more of their income toward debt servicing and essential purchases. This, in turn, will be a headwind against the economy.

**SALES IN DEEP FREEZE**

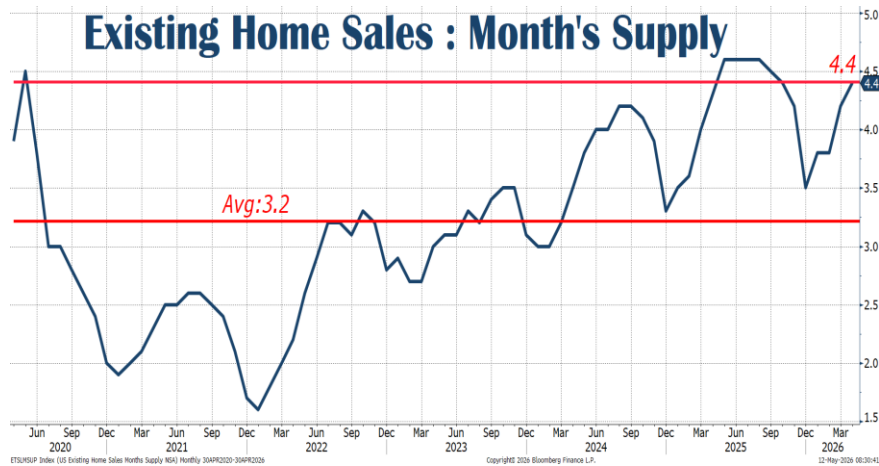
With the spring selling season already in tatters, existing home sales were expected to rebound in April very modestly (+2.0% month over month) off recent record lows. However, the rebound was far less than expected, up just 0.2% month over month, which left sales of existing homes unchanged year over year.

As depicted below, total existing home sales annualized hovers at just above four million homes near the very bottom of the deep freeze range that has existed for the past three and a half years. **It really says something that existing home sales over the first four months of 2026 are actually -6% lower today than they were in September 2008, the month that Lehman collapsed and the great financial crisis entered an ominous chapter.**

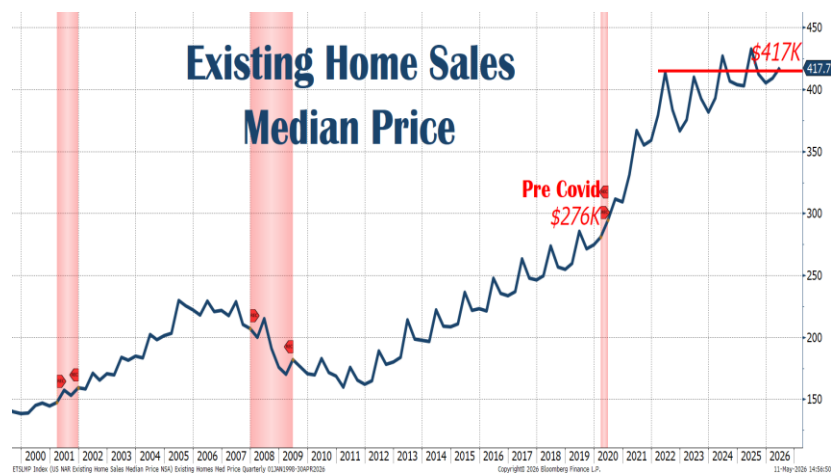


Meanwhile, the inventory of previously owned homes increased from a year ago to 1.47 million, the most for any April since 2019. This is equivalent to 4.4 months of supply (inventory/sales) based on the current sales rate. And while still well below the highs seen in the 2008 crash, it's increasing every year as the housing market continues to normalize. Also, this is national data. If you were to break out the South and West, they would be well above pre-pandemic supply while the Northeast/Midwest are still constrained.

There are now 630,000 more sellers than buyers — the largest gap ever. Currently, there are 1.46 sellers for each buyer, a reversal from 2014-2019 when buyers outnumbered sellers and prices stayed high. This shift began in 2022 and is now at its most extreme. When supply far exceeds demand, prices drop. Since most Americans' wealth is tied to home equity, this trend has broad implications beyond housing.



Median prices edged up month over month by 0.9% to \$417,700 last month but remain flat year over year and are down 3.5% from the cycle peak.



While the national median price is an interesting data point from an overall economics perspective, it is irrelevant for people buying or selling homes. What matters to buyers and sellers are local markets. As shown below, since mid-2022, prices of single-family homes have dropped in some cities, and in some other cities, prices of single-family homes have continued to rise:

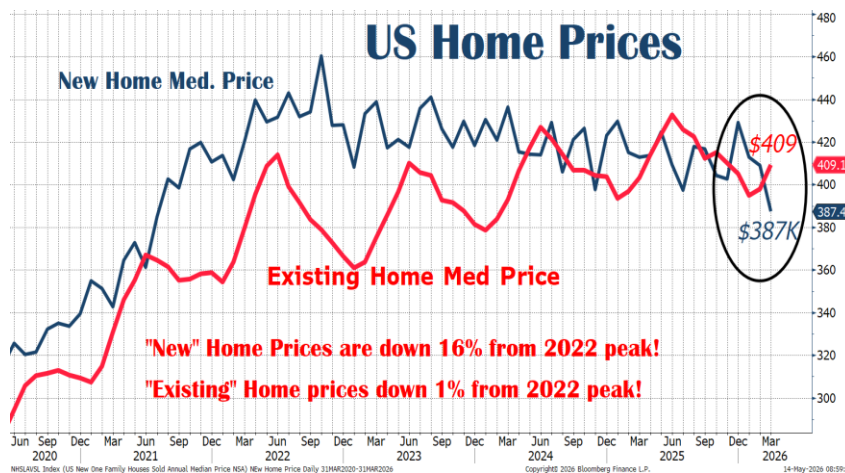
City	Price Change (%) Since 2022 Peak
Oakland	-25%
Austin	-24%
New Orleans	-20%
Fort Myers	-15%
New York City	+5.3%
Milwaukee	+3.7%

In terms of who's buying and who's not, the housing industry is another example of the K-shaped economy. For homes priced at \$1 million plus, sales are up 9.3% year over year. Not because prices are growing, but because the buyer mix is shifting to wealthy people selling to wealthy people. Meanwhile, sales volumes for cheaper houses are dropping, not because prices are rising, but because fewer low-to middle-income Americans are buying. You can see the bifurcation in sales volume on this table from the National Association of Realtors:

**Regional Sales by Price  
Existing Homes Sales  
April 2026**

% Change in Sales from 1 Year Ago						
Region	\$0-100K	\$100-250K	\$250-500K	\$500-750K	\$750K-1M	\$1M+
Northeast	-16.1%	-14.8%	-8.3%	-4.1%	-1.3%	4.9%
Midwest	-11.8%	-2.5%	4.9%	13.9%	8.4%	18.1%
South	7.2%	2.1%	4.9%	7.4%	9.9%	14.2%
West	-12.6%	14.2%	6.6%	5.9%	1.1%	5.8%
U.S.	-5.9%	-1.3%	3.6%	6.0%	4.5%	9.3%

Also worth highlighting is that new houses are now cheaper than existing houses, a first in U.S. housing market history. Normally, builder homes are 15% more expensive than existing homes. Builders have reacted to the market and are showing you where the market needs to head. Existing owners have not.

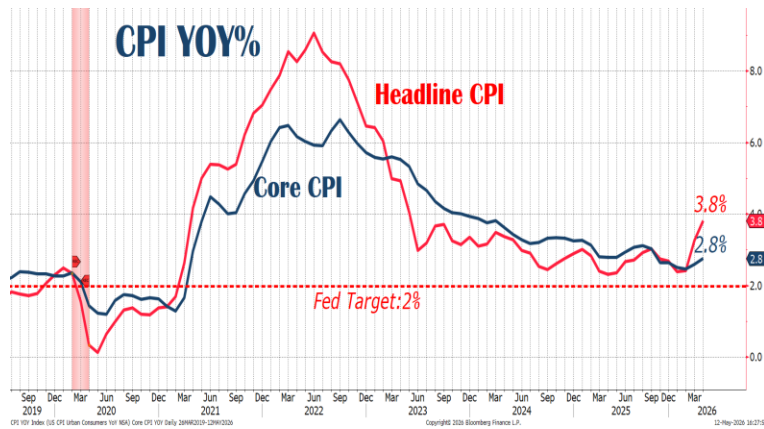


**Bottom line:** Buyers continue to exit the U.S. housing market because they don't want to pay today's sky-high prices or can't afford to, making this the fourth straight year of recession-level home sales.

Builders have already shown us what needs to happen in housing. They've cut prices by over 20% inclusive of mortgage rate buydowns. And they got their sales volumes back to normal. That is what needs to happen in the existing market.

## WAR AND INFLATION

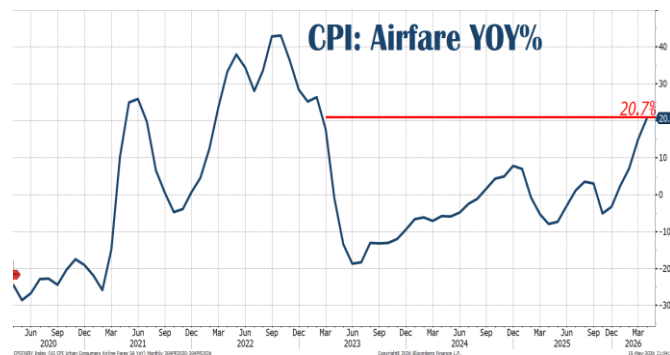
The much-anticipated April Consumer Price Index (CPI) report came out last week, and the headline was as expected at +0.6% month over month, taking the inflation rate up to +3.8% from +3.3%. The key was the core, and it was a disappointment — rising +0.4% and taking the year-over-year core inflation rate further away from the Fed’s target — to +2.8% from +2.6% in March.



To little surprise, energy prices surged 3.8% during the month, accounting for more than 40% of the headline increase, while food and apparel prices rose 0.5% and 0.6%, respectively. On a year-over-year basis, energy inflation accelerated to 17.9%, while food and apparel rose 3.2% and 4.2%.



There was also oil follow-through into air fares, which rose by +2.8% month over month after a similar increase in March, and are now up +20.7% on a year-over-year basis.



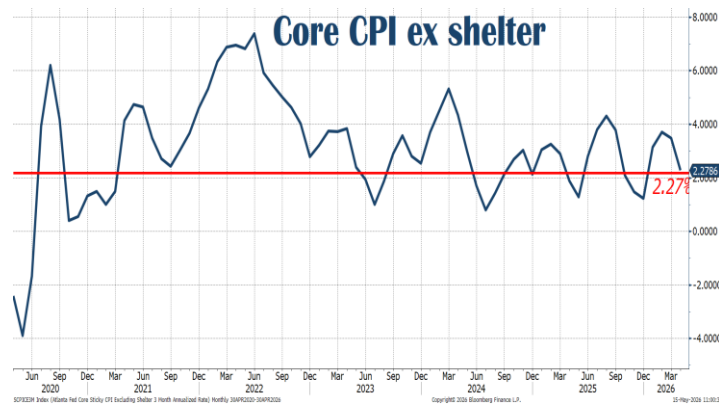
Same for delivery services (think FedEx and UPS), which posted outsized increases of +4.3% month over month, and that came on the heels of a +3.1% spike in March. The year-over-year trend is running at +13.7%. These are the energy-sensitive sectors we would expect to be feeding into the core index.

Another culprit was financial services, where prices soared +8.5% — are brokers and traders raising their fees, as the public takes an even greater leap into the booming stock market? After all, that was a record increase in the CPI financial services component.

What was completely bizarre was shelter inflation, which rose 0.6% after moderating in prior months. This was a bit of a shocker, seeing as we know in real time that rental rates are still deflating and national home prices are cooling off in a major way. Indeed, the Bureau of Labor Statistics (BLS) noted that this figure is misleading due to the government shutdown in 2025. During the shutdown, BLS shelter data collection in October 2025 was suspended. As a result, the BLS was forced to use carry-forward imputation methods that temporarily masked underlying rent increases.

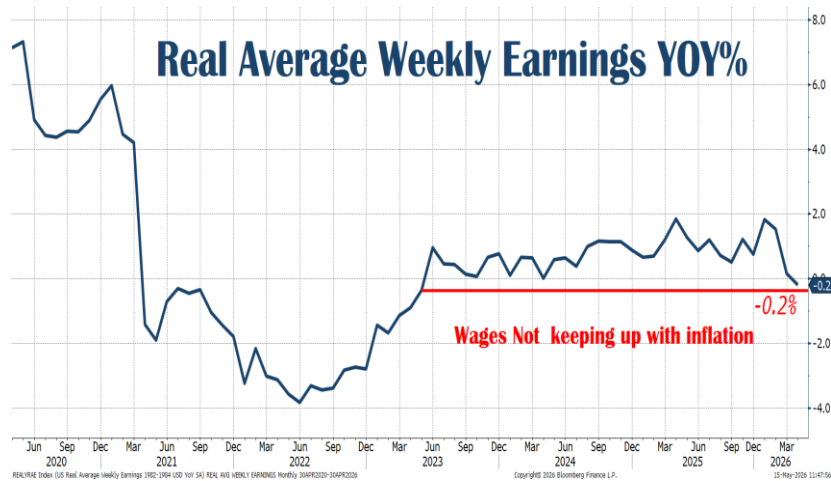
This means the April 2026 rent and owners’ equivalent rent (OER) figures effectively represented a statistical “catch-up,” compressing roughly 12 months of rental inflation into a six-month reporting period rather than reflecting a normal monthly increase. In other words, this is inflation that already happened months ago and is just now being accounted for. In other words, dismiss these outsized +0.5% shelter figures. That knocks around -0.1% off the +0.4% month-over-month change in core inflation.

The core CPI stripping out the clear anomaly of higher shelter costs came in at a tame +0.2%, and this marks the third straight month of a reading like this or lower. The year-over-year trend on this metric stayed at +2.3%, and the three-month pace is running near target at a +2.2% annual rate.



**What this tells me is that the underlying inflation pulse remains far less alarming than the headline would suggest.**

Finally, the real story here for the economy is that real average weekly earnings fell by -0.2% month over month in April as wages have not kept up with inflation. This is what a +115,000 increase in non-farm payrolls (until it gets revised down) managed to generate, on top of a -0.9% slide in March. On a year-over-year basis, real work-based pay has gone from +1.9% a year ago to -0.2% currently. There has been no growth since Trump took office. How is that for a “solid” economy?



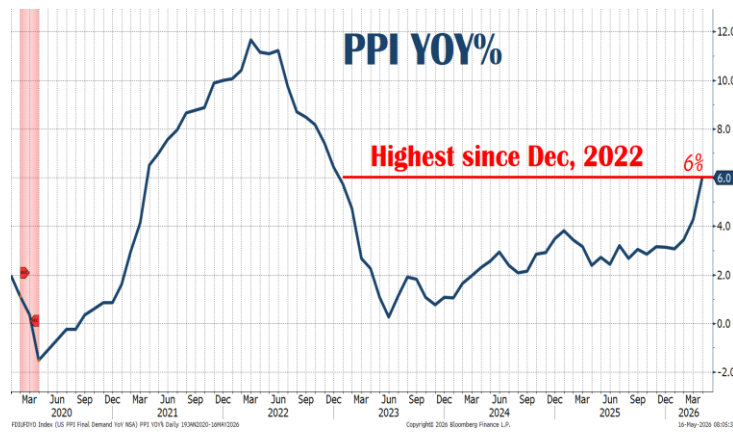
The longer-term story is even more disturbing. While nominal wages have risen by 37% since the pandemic, real inflation adjusted wages have increased by ONLY 3%.



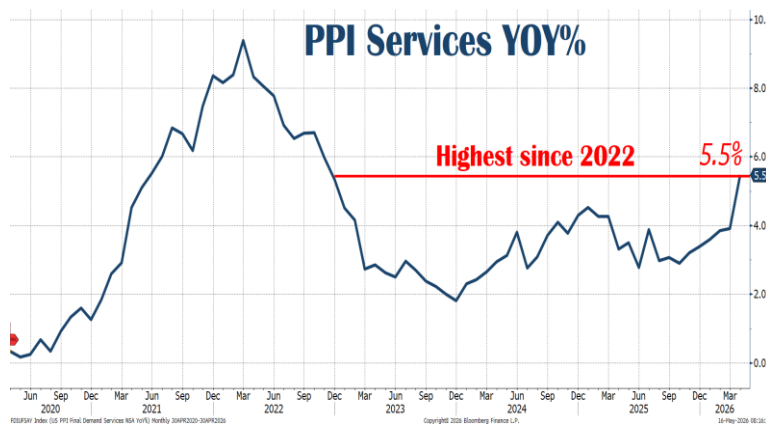
**Bottom line:** If it feels like you are not getting ahead, it is because you aren't. Chalk this up to another in the long list of K-shapes in this economy — over +20% in S&P 500 profits and no growth in real wages. Something tells me the mean-reversion process may well commence at this November's midterm elections.

**PPI EXPLODES HIGHER**

The Producer Price Index final demand (PPI), which tracks inflation in prices that companies pay each other, spiked by 1.40% in April from March (+17.8% annualized), the worst since the historic one-month spike in March 2022, driven by services and energy. Year over year, it spiked by 6.0%, the worst since December 2022.



The shocker is the spike in services, and services dominate the PPI. The services PPI weighs 68% of the overall PPI, and it completely blew out — that was in addition to the spike in energy prices, and it also shows how some of the energy price increases have moved into other parts of the economy. The services PPI spiked by 1.18% (+15.1% annualized) in April from March. Year over year, the services PPI jumped by 5.5%, the worst since November 2022.



- Trade services (19% in overall PPI) spiked a huge +2.7% month to month in April from March.
- Transportation and warehousing services (4.9% in overall PPI) exploded by 5.0% in April from March.
- But “other services” (38% in overall PPI) ticked up only +0.1%, after no change in the prior month.

This is a massive amount of inflation in prices that companies pay each other and are trying to pass on to each other. And some of that will seep into consumer price inflation measures, such as the CPI and PCE price index.

**MARKET OUTLOOK AND PORTFOLIO STRATEGY**

*“I’m still quite attentive to concerns about what’s going to happen with the labor market, but to me the risk is much higher right now that inflation will not behave.” — Michael Barr, Federal Reserve Governor*

Given Trump’s tariff and Mideast policies, both contributing to inflation, bond yields took center stage last week, and for good reason: Driven by a 3–4% surge in oil prices, with Brent hitting \$109 inflation concerns are intensifying, and consequently, yields on government bonds are soaring.

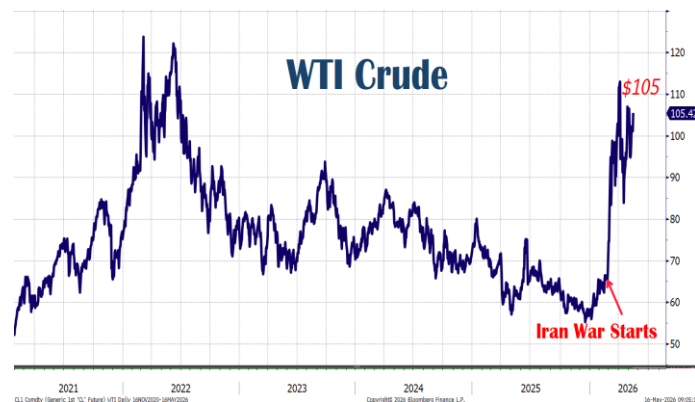
The long bond yield is near a 20-year high.



Since the war with Iran started, the benchmark 10-year Treasury yield has spiked by 59 basis points to 4.59%.



One of the main sources of worry, of course, is that there is still no resolution in sight for the Strait of Hormuz. The market's optimistic and wishful scenarios have so far been proven wrong, and markets will also be wary of another large spike in crude oil prices from already high levels.

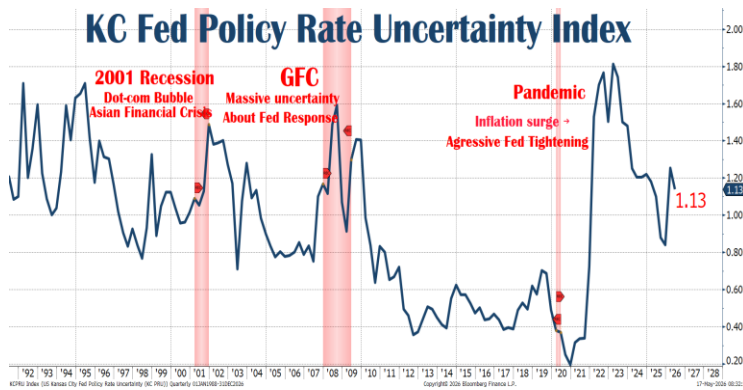


Given the energy crisis and a new Fed regime, the market is increasing doubt over what the Fed will do and by how much.

The Kansas City Fed’s Measure of Policy Rate Uncertainty is a daily measure of market-based uncertainty regarding where short-term U.S. interest rates will be one year in the future.

One percentage point roughly means the market expects the one-year-ahead rate to be within about ±1 percentage point with 68% confidence, similar to how VIX works for stocks. Policy rate uncertainty rises sharply during economic stress, major Fed pivots, or when inflation is unpredictable.

The 2022 peak stands out as the highest in 35+ years, reflecting the unusual combination of post-pandemic inflation shock plus the fastest hiking cycle in decades.



**High uncertainty periods often coincide with volatile bond markets.**

As uncertainty rises at the front end, yields are being pressured higher on concerns that the Fed’s next move may be to raise, rather than cut the fed funds rate. I should highlight that the 2-year Treasury yield typically leads the fed funds rate.

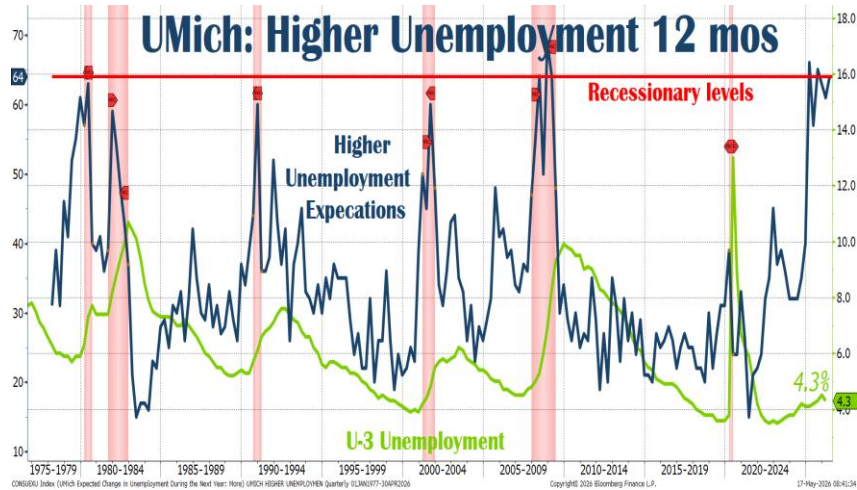
In my view, it’s not possible to cut interest rates when the 2-year Treasury is almost 50 basis points higher than the fed funds rate.



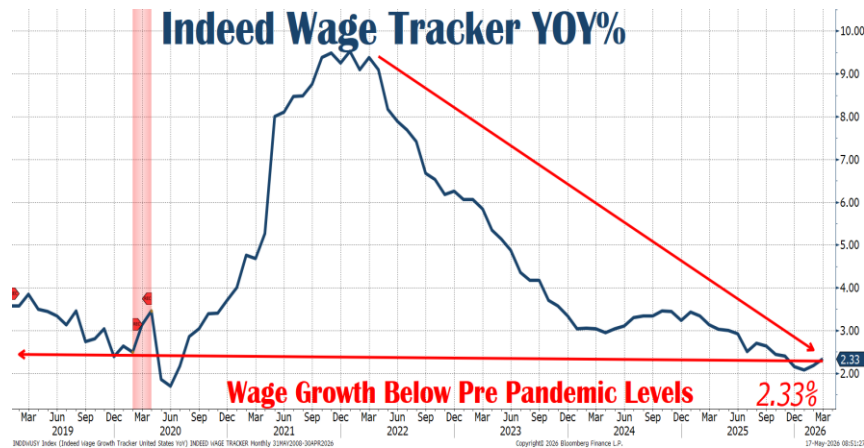
Unquestionably, surging oil prices bleed into U.S. inflation reports. This suggests that the recent upward trend will continue near term and rate-hike probabilities are rising.

**However, the question the bond market must answer is how monetary policy can address a supply-shock-driven inflation problem. Higher rates will not lower oil and energy prices.**

Meanwhile, the labor market may be softening faster than many appreciate, with unemployment expectations already approaching recessionary territory.



Unemployment expectations are already at a recessionary level, and workers who fear losing their jobs generally don't push for raises. Barely more than 40% of Americans expect a pay increase in the next year. The median expected wage gain is just 0.6%, and the Indeed Wage Tracker is back near 2%. This is not what an inflationary labor market looks like. What is more important than labor?



Moreover, the Fed keeps reacting to the headline payroll numbers, which is a bit bizarre because over 90% of the time since January 2025, these numbers have been revised down by 1.1 million. Yet, we've got people that think that we have a healthy labor market on our hands.

Moving on. As recently discussed in this space in the past two years, 92% of the economic growth in the U.S. economy came from productivity. 8% came from labor input. How does anybody think that 92% of the contribution to the economy of productivity... is inflationary?

It's not simply that inflation is slowing. It's that this is no longer an economy where labor has enough leverage to generate the kind of wage inflation the Fed still seems worried about. The same is true of tariffs, which are primarily a price shock, not a self-sustaining inflationary cycle. Without wages chasing higher prices, inflationary spikes tend not to become self-reinforcing. At least not without wages following along.

Finally, shelter costs, including rents and owners' equivalent rent, make up roughly 30% of CPI and nearly 40% of core CPI. Real-time housing data already show new lease rents falling, vacancy rates near cycle highs, and home prices cooling. The problem is that the BLS shelter calculation lags reality by 12-18 months. That means the disinflationary impulse is still slowly working its way into the official inflation data and should continue doing so for some time.

Despite the near-term energy price shock and the potential for still higher inflation prints, my base case is that bonds will eventually benefit from the major disinflation in the pipeline from reduced wage pressure and a sustained slowdown in residential rents. At the same time, the tariff impact should subside.

**That said, patience will be required! With so much near-term uncertainty, I would continue to overweight the front end of the curve due to concerns over fiscal recklessness and a rising term premium on the long end of the curve.**

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## MORE INFORMATION

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As Alloya's Market Strategist, **Tom Slefinger** leverages nearly 40 years of investment strategy expertise to deliver insightful commentary on the economy and market events to optimize balance sheet performance at the credit union level. With thousands of subscribers, Tom's daily and weekly publications are widely read amongst credit union executives.

Prior to becoming the corporate's Market Strategist, Tom served as the Senior Vice President of Institutional Fixed Income Sales at Alloya Investment Services, a division of Alloya Solutions, LLC. In this role, Tom developed and managed operations associated with institutional fixed income sales in addition to developing investment portfolio strategies, identifying appropriate sectors and securities, and optimizing portfolio performance at the credit union level.

Tom holds a B.S. in business administration from the University of Maine. In addition, he holds a Series 7 and 63 through ISI.

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