Homestead Funds

Quarterly Market Review

Third Quarter 2022

Summary

- Stocks and bonds both retreated again in the third quarter. Energy prices eased somewhat, though a post-quarter production cut from OPEC+ could drive oil prices higher again. Other sources of inflation remained stubbornly high, leading the Federal Reserve (Fed) to hike interest rates two more times. With continued strength in jobs, markets expect that the Fed will continue its rate-hike campaign in a "higher for longer" trend.
- Though employment remains solid, consumers are feeling the budget crunch of inflation. Savings rates were down and credit card balances were up. A shift toward staples is aggravating the inventory pileup in some retail sectors. Company earnings forecasts softened, with analysts predicting year-over-year growth in earnings for only four of 11 sectors.
- Bonds declined as rates increased. Treasury yields climbed the most for shorter-term bond issues, creating an inverted yield curve for most of the quarter. Inverted yield curves have historically predicted recession.

This commentary was prepared on October 11, 2022, and reflects our view of events at that time. Please visit our website, homesteadfunds.com, for the latest perspectives.

Continued Rate-Hike Stings

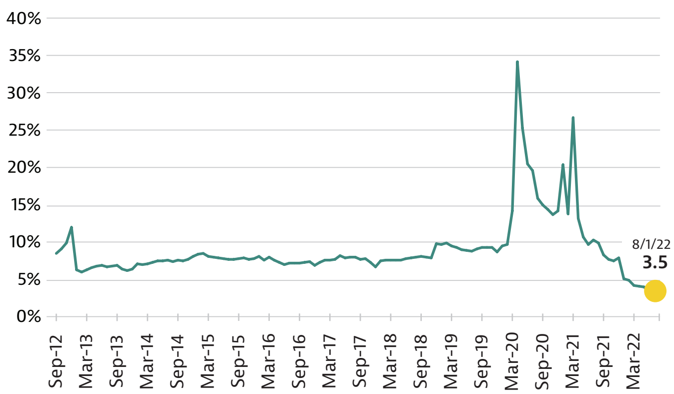
Stocks and bonds both retreated again, marking the third straight quarter of declines for both asset classes. Inflation remained stubbornly high in the face of interest-rate hikes and other monetary policy tightening. The Fed hiked the short-term target interest rate two more times in the period; additional hikes are expected.

Demand softening amid higher prices, rates

Consumers felt the pressures of inflated living costs and higher interest rates. Inflation remained above 8% on a year-over-year basis, as measured by the Consumer Price Index, a basket of goods and services. Shelter, food and medical care were the categories with the biggest impact, according to the August inflation report. Natural gas and electricity prices were also up, but households enjoyed a respite in gasoline prices — though maybe not for long. Just after the quarter ended , OPEC+ announced production cuts, aiming to drive oil prices back up.

Facing Higher Costs, Household Savings Rate Are Down

Personal savings rate (% of disposable income)



Source: U.S. Bureau of Economic Analysis

The pressure on household budgets showed up in lower savings rates. Consumer savings as a percentage of disposable income fell to 3.5% in August. Meanwhile, consumers are also taking on more debt, especially on credit cards, to make ends meet. Between August 2021 and August 2022, total credit card balances climbed 13%.

Retail inventories also reflected the strain on household budgets. With demand easing at the same time as supply-chain backlogs began to resolve, some retailers have reported ballooning inventories.

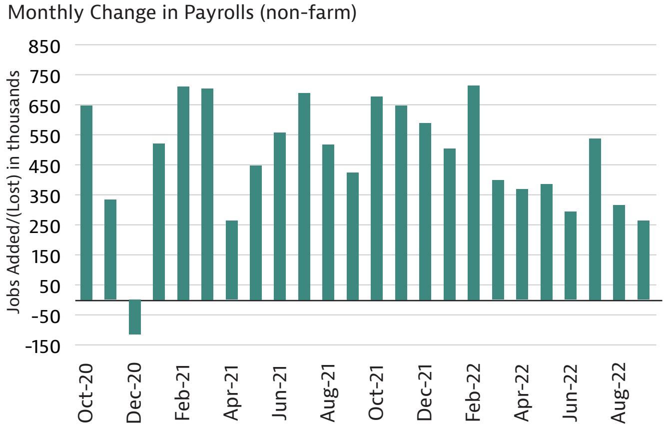
Employment has held up, to date

Though budgets are strained, employment has been a relative bright spot in the mixed economic environment. Unemployment was at a low 3.5% for the September reading. Job creation continued, albeit at a slower pace than in recent months. Non-farm payroll numbers were positive through the quarter.

There are early signs of hiring freezes and even layoffs in some industries. Still, the bigger picture for jobs was solid in September. Labor-market participation has inched higher in 2022 but remained below pre-COVID-19 levels; the supply of workers has not fully recovered. Wages climbed at a pace of about 5%, according to the most recent report.

Job Creation Continued in Third Quarter

Monthly Change in Payrolls (non-farm)



Source: Bureau of Labor Statistics

All eyes on Fed policy moves

With high inflation continuing, Fed policy remained in focus for markets. If inflation is coupled with a strong job market, the Fed is more likely to continue hiking interest rates and keep them higher for longer, aiming to cool prices. If job markets falter more, the Fed could potentially take a less-aggressive stance — but weak labor markets are difficult in other ways.

In the third quarter, relative strength in economic data prompted more aggressive Fed policy steps, which took a toll on stocks and bonds. Still, household balance sheets and company finances are both in good condition, overall.

Bonds

Interest rates once again climbed higher across all maturities, driving negative performance for bonds in the third quarter. The change in rates was most pronounced for shorter maturities. With still-higher-than-expected inflation numbers, markets adjusted expectations to include more aggressive interest-rate moves for the year. The Fed raised interest rates by 0.75% in July and again in September, for a year-to-date increase of 3% in the target short-term rate. Markets expect policymakers to raise rates by another 1.25% or so before year end.

Though interest rate changes have a big impact on bond performance, the "price of risk" was essentially stable. Credit spreads, which measure the difference in yield between corporate bonds and similar-duration Treasuries, expanded mid-quarter but finished the period around the same level as they started. When credit spreads widen, corporate bonds tend to underperform. With spreads largely unchanged, corporate bonds slightly outperformed Treasuries.

It is atypical for bonds and stocks to underperform in lockstep, as they have in recent months. It is also atypical for the Fed to be hiking interest rates in a moment where the economy is in or poised for a slowdown. The yield curve was inverted, meaning that two-year yields were higher than 10-year yields, for the whole quarter. Recessions have historically been preceded by inverted yield curves. Still, companies remain in healthy condition with strong balance sheets and decent earnings performance. The likelihood of default among corporate issuers remained low.

Performance Attribution for Our Bond Funds

Against this backdrop, the Homestead Short-Term Government Securities Fund (HOSGX) returned -2.07% in the third quarter, outperforming its benchmark, the ICE BofA 1-5 Year Treasury Index, which returned -2.28%. The fund's overweight to agencies boosted performance in the period, as did a small cash position in the fund. Yield curve positioning in Treasuries weighed slightly on returns.

The Homestead Short-Term Bond Fund (HOSBX) returned -1.96% in the quarter, outperforming its benchmark, the ICE BofA 1-5 Year Corporate/Government Bond Index, which returned -2.21%. The fund's holdings in asset-backed securities (ABS) aided performance, as did a small cash balance. Yield curve positioning in Treasuries weighed on returns.

The Homestead Intermediate Bond Fund (HOIBX) returned -4.40% in the third quarter, outperforming its benchmark, the Bloomberg Barclays Aggregate Bond Index, which fell -4.75%. Overweight positioning in ABS and financial institutions boosted performance, as did a small cash position in the fund. Conversely, yield curve positioning in Treasuries detracted from performance.

Stocks

Stocks fell for a third straight quarter. Growth stocks fared slightly better than value stocks, and small caps outperformed large caps. On a sector basis, most sectors delivered losses in the quarter. Real estate and communications services stocks performed the worst. Energy and consumer discretionary stocks fared best, as did some health care stocks.

Analyst expectations for third-quarter earnings have retreated significantly since earlier in the year, but the consensus forecasts still project that S&P 500 Index companies will grow earnings 2% to 3% year over year. After making a significant shift in the prior quarter, the price-to-earnings ratio remained below average.

Performance Attribution for Our Stock Funds

The Homestead Value Fund (HOVLX) declined -4.74% in the third quarter, outperforming its benchmark, the Russell 1000 Value Index, which returned -5.62%. In the period, the fund's stock choices in the consumer discretionary sector boosted performance, as did an underweight allocation to communications services. Conversely, stock choices in financials and health care detracted from relative performance.

Compared with the index, the fund holds significant overweights in industrials, health care and materials stocks. Its largest underweight allocations are 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) declined -5.40% in the third quarter, lagging its benchmark, the Russell 2000 Index, which returned -2.19%. In the period , stock selection in the health care and industrials sectors detracted from performance. The fund's lack of holdings in consumer staples contributed to returns, as did stock choices in the information technology sector.

Relative to its benchmark, the Small-Company Stock Fund continues to be notably underweight in the energy and consumer staples sectors. The portfolio's most significant overweights are in the industrials 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 -3.05% in the third quarter, outperforming its custom benchmark, a 60%/40% blend of the Russell 3000 Index and the Bloomberg Barclays Government-Credit Index, which returned -3.78% for the same period.

The fund's stock holdings outperformed their benchmark. Stock selection in the information technology and industrials sectors boosted relative returns. Conversely, the fund's stock choices and overweight allocation in the real estate sector weighed on performance, as did stock choices in the health care sector. The fund holds its biggest sector overweights in industrials and real estate, compared with its equity benchmark. The fund's largest underweights are in communication services and energy stocks.

The fund's bond allocation outperformed its benchmark. The fund's overweight positioning in industrials and financials helped performance, as corporate issues generally outperformed government issues. A small cash balance also boosted performance in the quarter. 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 9/30/2022

		Average Annual				
	Q3	1-yr	3-yr	5-yr	10-yr	Since fund's inception
Bond Funds						
Short-Term Government Securities Fund (HOSGX)	-2.07%	-6.64%	-1.05%	0.17%	0.35%	2.63%
ICE BofA 1-5 Year U.S. Treasury Index	-2.28%	-6.78%	-0.97%	0.39%	0.62%	3.35%
Expense ratio 0.79% (gross) 0.75% (net) (12/31/21)*						
Short-Term Bond Fund (HOSBX)	-1.96%	-7.56%	-0.86%	0.55%	1.04%	3.72%
ICE BofA 1-5 Year Corp./Gov. Index	-2.21%	-7.32%	-0.90%	0.57%	0.91%	3.93%
Expense ratio 0.79% (12/31/21)						
Intermediate Bond Fund (HOIBX)**	-4.40%	-14.76%	-2.77%	NA	NA	-1.15%
Bloomberg U.S. Aggregate Index	-4.75%	-14.60%	-3.26%	-0.27%	0.89%	-1.37%
Expense ratio 0.91% (gross) 0.80% (net) (12/31/21)*						
Balanced Fund						
Rural America Growth & Income Fund (HRRLX)***	-3.05%	-13.96%	NA	NA	NA	-10.04%
Blended Index	-3.78%	-14.36%	NA	NA	NA	-12.70%
Expense ratio 5.12% (gross) 1.00% (net) (12/31/21)*						
Equity Funds						
Value Fund (HOVLX)	-4.74%	-11.22%	6.68%	7.30%	10.90%	9.77%
Russell 1000 Value Index	-5.62%	-11.36%	4.36%	5.29%	9.17%	NA
Expense ratio 0.63% (12/31/21)						
Small-Company Stock Fund (HSCSX)	-5.40%	-19.78%	5.76%	0.99%	7.02%	7.77%
Russell 2000 Index	-2.19%	-23.50%	4.29%	3.55%	8.55%	6.75%
Expense ratio 1.06% (12/31/21)						

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.

*Homestead Advisers has contractually agreed, through at least April 30, 2023, to limit the funds' 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). This waiver agreement will terminate immediately upon termination of the fund's Management Agreement and may be terminated by the fund or Homestead Advisers with one year's notice.

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

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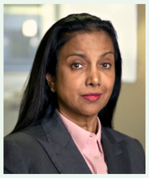
Equity Fund Management



Prabha Carpenter, CFA®
Senior Equity Portfolio Manager

Prabha co-manages Homestead Advisers' equity strategies. She is a graduate of the University of Madras, where she received a BA in economics. She received her BS in business economics and an MBA with distinction in finance from American University. Prabha holds the Chartered Financial Analyst designation.

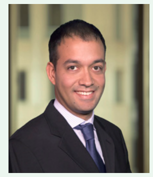
Mark Iong, CFA®
Equity Portfolio Manager

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

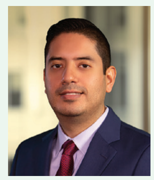
Jim co-manages Homestead Advisers' equity strategies. He is a graduate of Colby College, where he received a Bachelor of Arts degree in English. He received his MBA from the Olin Graduate School of Business at Babson College. Jim holds the Chartered Financial Analyst designation.

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: October 11, 2022 | Updated: December 5, 2022

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. 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. Equity securities generally have greater price volatility than fixed-income securities and are subject to issuer risk and market risk. Value stocks are subject to the risk that returns on stocks within the style category will trail returns on stocks representing other styles or the market overall. Securities of small and medium-sized companies tend to be riskier than those of larger companies.

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 500 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.

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 800.258.3030 or download a PDF at homesteadfunds.com.

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