Homestead Funds

Quarterly Market Review

Second Quarter 2023

Summary

- Stocks continued their rally, while bonds trended more negative in the second quarter. Market sentiment was generally upbeat, led by excitement in technology and communications stocks over new artificial intelligence (AI) tools. There were also continued signals that inflation continued to retreat while the job market remained strong. The Federal Reserve (Fed) hiked short-term interest rates another 0.25% and indicated that two additional hikes may be in the cards, depending on market conditions.
- Quarterly company earnings are poised for another year-over-year decline. If earnings come in as expected, it will be the third straight quarter of declines, extending the earnings recession.
- Bonds posted modest declines as interest rates climbed higher across the yield curve in the quarter. The yield curve remains inverted and has even steepened as short-term rates climbed more than long-term rates. Though an inverted yield curve is associated with a coming recession, GDP growth seems to have remained solid in the first half of the year.

This commentary was prepared on July 14, 2023, and reflects our view of events at that time. Please visit our website, homesteadfunds.com, for the latest perspectives.

Rally Continues, Led by Tech Excitement

The second quarter delivered mixed returns for investments. Stocks extended their rally for a third consecutive period, led by gains in large-cap technology and communications services in response to excitement about new AI technology. Bonds were generally negative in the second quarter. The Fed implemented another quarter-point rate hike in May, bringing its target overnight interest rate up to a range of 5% to 5.25%. Policymakers indicated that two more hikes may be needed in the ongoing fight against inflation.

Economy Kept Calm, Carried On

For all the worry about a looming recession, there were plenty of positive trends in the economy in the second quarter. Excitement about new AI technology, such as ChatGPT, helped drive tech and communications stocks higher.

Consumers are feeling a bit more optimistic, according to July data from the University of Michigan Index of Consumer Sentiment. Stability in the labor markets contributed to brightening views, as did the continued retreat of last year's inflation surge. Gas and food prices have moderated, and rents have slowed their ascent.

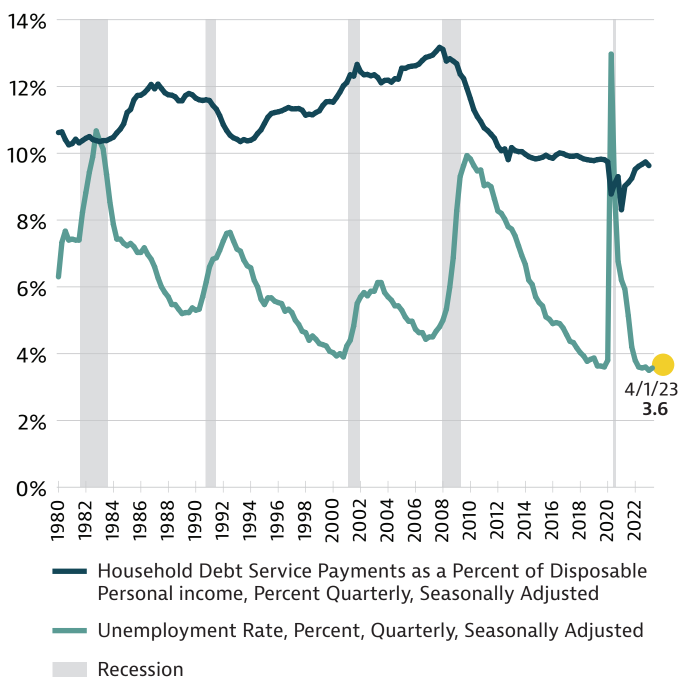
If indeed a recession lies ahead, households are actually in a decent financial position overall. One key measure is the household debt service ratio, which measures monthly debt obligations as a percentage of disposable income.

Stability in the labor markets contributed to brightening views, as did the continued retreat of last year's inflation surge.

Currently, American households have a debt service ratio around 10%, considerably lower than the 13% level before the Great Financial Crisis. Consumers are still benefiting from the extra savings that piled up from stimulus packages and lockdown limits on normal spending.

The employment picture also remains positive. There are only 0.6 unemployed people for every job opening in the United States, while the unemployment rate is at a cyclical low, below 4%.

Household Debt Ratios Remain Low and Employment is Still Strong



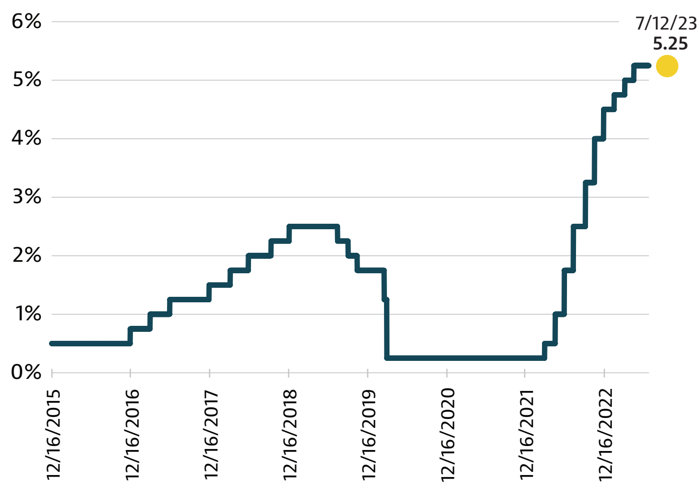
Source: St. Louis Federal Reserve

Though Inflation Cooled, Fed Remains Ready

The Fed's campaign to stifle inflation has been successful to date, with topline inflation falling to an annual rate of 3% in the June reading. As policymakers say that it takes 12 to 18 months for interest rate hikes to "work through the system," it's difficult to gauge in the short term how many hikes will be needed. Since late 2021, the Fed has hiked its short-term target rate from a 0% to 0.25% range up to a 5% to 5.25% range. These moves make financial conditions tighter, especially for consumers who use loans to fund mortgages, auto purchases and credit card balances.

Though markets had previously anticipated the likelihood of rate cuts later in 2023, expectations have shifted to match the Fed's language, which has been reiterating the possibility of one or two more rate increases before the effort is finished.

Federal Funds Target Interest Rate



Source: U.S. Federal Reserve

Bonds

Bond returns trended negative in the second quarter, while interest rates rose over the period. The Fed's additional rate hike drove short-term rates higher, but longer-term rates also climbed incrementally as the outlook for economic growth strengthened incrementally. Inflation continued to retreat but the prospect of recession remains unresolved, with mixed signals from economic indicators.

The other component of bond yields, the credit spread, remained steady during the second quarter. Credit spreads measure the difference in yield between corporate bonds and similar-duration Treasuries. Though spreads widened sharply during the March failure of Silicon Valley Bank, they have since come back down and even tightened modestly from the start of the year. Tighter spreads tend to reflect a positive market environment. Spreads, like rates, have an inverse movement with bond prices. When spreads get higher, corporate bond prices go lower, and vice versa.

The yield curve remained inverted for the whole quarter, meaning that the yield on short-term Treasuries was higher than the yield on long-term Treasuries.

Inflation continued to retreat but the prospect of recession remains unresolved, with mixed signals from economic indicators.

Performance Attribution for Our Bond Funds

Against this backdrop, the Homestead Short-Term Government Securities Fund (HOSGX) returned -0.83% in the second quarter, in line with its benchmark, the ICE BofA 1-5 Year Treasury Index, which returned -0.86%. The fund's overweight to agencies boosted performance in the period, as did exposure to asset-backed securities (ABS).

The Homestead Short-Term Bond Fund (HOSBX) returned -0.48% in the quarter, outperforming its benchmark, the ICE BofA 1-5 Year Corporate/Government Bond Index, which returned -0.57%. The fund's holdings in ABS, industrials and financials bonds boosted returns in the period relative to the benchmark.

The Homestead Intermediate Bond Fund (HOIBX) returned -0.74% in the second quarter, outperforming its benchmark, the Bloomberg U.S. Aggregate Index, which returned -0.84%. The fund's holdings in ABS boosted performance, as did its underweight position in U.S. Treasuries compared to the benchmark. Holdings in industrials and collateralized mortgage obligations (CMOs) were also additive. The portfolio team has continued to add to mortgage-backed securities positions as an area of opportunity in recent quarters.

Stocks

Stocks largely rose again in the second quarter, with positive performance across most categories of stocks. Growth stocks outperformed value stocks, and large caps outperformed small caps. Thus, large-cap growth was the top-performing category while small-cap value was the lowest performer.

Earnings showed signs of further softening in the quarter, with analysts forecasting a third consecutive year-over-year decline in quarterly earnings. The consensus forecasts project that S&P 500 Index companies will see earnings down -6.8% on a year-over-year basis. Revenues are also expected to contract about -0.4%. As stock prices generally rose while forward earnings expectations declined in the period, the price-to-earnings ratio, a measure of stock valuation, ticked higher.

Performance Attribution for Our Stock Funds

The Homestead Value Fund (HOVLX) rose 4.75% in the second quarter, outpacing its benchmark, the Russell 1000 Value Index, which returned 4.07%. In the period, the fund's stock choices and overweight exposure in information technology holdings boosted relative performance, as did stock selection in the communications services sector. Conversely, stock selection in the consumer discretionary and health care sectors detracted from returns.

Compared to the Russell 1000 Value 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) returned 4.77% in the second quarter, trailing its benchmark, the Russell 2000 Index, which returned 5.21%. In the period, stock selection in the information technology sector weighed on relative performance. Positioning in the health care sector also detracted. Conversely, stock choices in materials and energy sectors boosted the fund's performance.

Relative to its benchmark, the Small-Company Stock Fund is notably underweight in the health care, consumer staples and utilities 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 1.60% in the second 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 4.68% for the same period.

The fund's stock holdings underperformed its benchmark. Stock selection and underweight exposure in the information technology sector detracted from relative returns. Stock choices and overweight positioning in the real estate sector also weighed on performance. Conversely, stock choices in the health care and materials sectors boosted the fund's returns.

The fund's bond allocation outperformed its benchmark. The fund's underweight in Treasuries aided performance. Exposure to agency bonds and industrials bonds also boosted relative returns. Compared to its bond benchmark, the fund holds overweights in corporate bonds and agency-issued bonds. It is underweight in U.S. Treasury holdings.

As stock prices generally rose while forward earnings expectations declined in the period, the price-to-earnings ratio, a measure of stock valuation, ticked higher.

Total Returns as of 6/30/2023

	Q2	Average Annual 1-yr	3-yr	5-yr	10-yr	Since fund's inception
Bond Funds						
Short-Term Government Securities Fund (HOSGX)	-0.83%	-0.34%	-1.69%	0.57%	0.58%	2.62%
ICE BofA 1-5 Year U.S. Treasury Index	-0.86%	-0.43%	-1.79%	0.90%	0.85%	3.33%
Expense ratio 0.80% (gross) 0.75% (net) (12/31/22)*						
Short-Term Bond Fund (HOSBX)	-0.48%	0.79%	-1.36%	0.98%	1.16%	3.72%
ICE BofA 1-5 Year Corp./Gov. Index	-0.57%	0.18%	-1.52%	1.17%	1.18%	3.91%
Expense ratio 0.76% (12/31/22)						
Intermediate Bond Fund (HOIBX)**	-0.74%	-0.49%	-3.48%	NA	NA	0.01%
Bloomberg U.S. Aggregate Index	-0.84%	-0.94%	-3.96%	0.77%	1.52%	-0.19%
Expense ratio 0.87% (gross) 0.80% (net) (12/31/22)*						
Balanced Fund						
Rural America Growth & Income Fund (HRRLX)***	1.60%	4.59%	N/A	NA	NA	-3.37%
Blended Index****	4.68%	11.33%	N/A	NA	NA	0.46%
Expense ratio 2.85% (gross) 1.00% (net) (12/31/22)*						
Equity Funds						
Value Fund (HOVLX)	4.75%	13.85%	14.15%	9.97%	10.77%	10.13%
Russell 1000 Value Index	4.07%	11.54%	14.30%	8.11%	9.22%	9.59%
Expense ratio 0.62% (12/31/22)						
Small-Company Stock Fund (HSCSX)	4.77%	14.27%	13.41%	4.31%	6.91%	8.33%
Russell 2000 Index	5.21%	12.31%	10.82%	4.21%	8.26%	7.13%
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

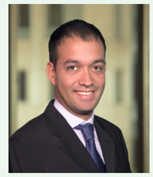
Mark Iong, CFA®
Equity Portfolio Manager

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

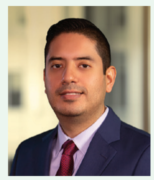
Jim co-manages Homestead Advisers' equity strategies. He is a graduate of Colby College, where he received a Bachelor of Arts degree in English. He received his MBA from the Olin Graduate School of Business at Babson College. Jim holds the Chartered Financial Analyst designation.

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.

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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.

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. 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 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. The **University of Michigan Consumer Sentiment Index** is a consumer confidence index published monthly by the University of Michigan.

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.

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