Homestead Funds

Quarterly Market Review

Fourth Quarter 2021

Summary

- Stocks resumed their upward march, finishing the year with gains. Consumer demand remained strong as household balance sheets continued to improve and low interest rates supported economic activity. Company earnings have surpassed pre-COVID levels.
- Inflation was higher than expected again in the period. Companies have been successful in passing cost increases along to customers, keeping profit margins intact. The effects are beginning to drive wages higher, with companies budgeting an average wage increase of 3.9% for the coming year. Amid this trend, policymakers are now projecting three interest-rate increases over the course of 2022.
- Bond returns were mixed in the fourth quarter. Medium-term interest rates (for bond maturities in the 2- to 10-year range) climbed higher as the policy outlook changed, pressuring bond prices. Most broad bond benchmarks delivered negative returns for the calendar year thanks to the impact of rising rates.

This commentary was prepared on January 13, 2022, and reflects our view of events at that time. Please visit our website, homesteadfunds.com, for the latest perspectives.

A Rally to Year-End

Stock markets in the U.S. were up in the final quarter. For the calendar year 2021, most broad stock indexes delivered strong performance with double-digit returns. Bond returns were mixed for the fourth quarter, with some indexes posting gains and others declining modestly. For the year, many broad bond benchmarks were down.

Stocks had strong momentum in the first month of the quarter but encountered turbulence from November onward amid reports of persistently higher inflation and resurging COVID-19 cases. Large-cap stocks recovered well and ended the quarter higher, while small-cap stocks delivered more mixed performance by the end of the period.

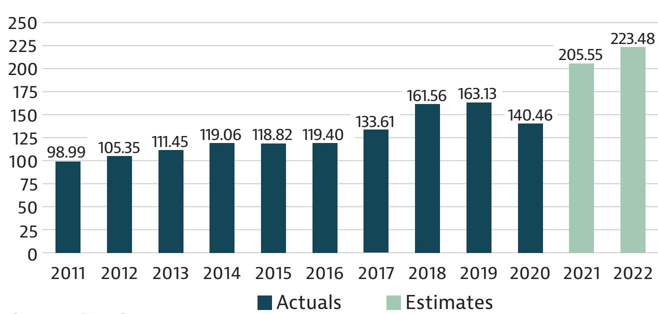
Company Earnings Are Booming

U.S. companies reported robust profits over the course of the year. In the fourth quarter, companies in the S&P 500 Index reported growth of 12.9% for revenue (on a per-share basis) and growth of 21.7% for earnings, compared to the fourth quarter of 2020. For context, the five-year average is 6.5% for revenue growth and 13.7% for earnings growth.

Year-over-year comparisons appear especially high because 2020 revenues and profits were depressed by lockdowns and restricted consumer activity.

Per-Share Profits Surge Past Pre-COVID Levels

(S&P 500 Calendar Year)

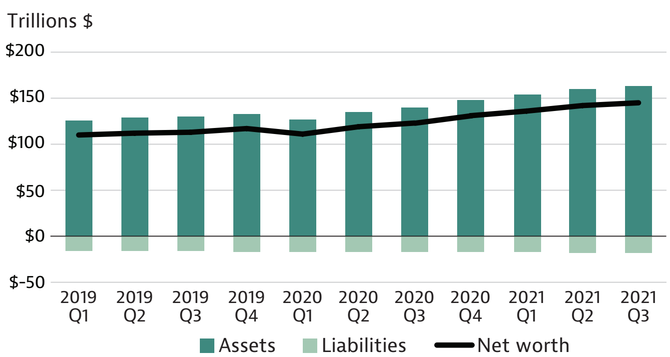


Source: FactSet

Per-share figures are also boosted when companies shrink the pool of publicly held stock by using cash to buyback outstanding shares, which they have been doing at a significant pace. Still, company earnings have clearly recovered to pre-COVID levels — and then some.

Companies are benefiting from continued high demand from consumers. While it's certainly not true for every household, many U.S. consumers have a stronger balance sheet today than they had before the pandemic. After the restrictions on typical spending in 2020, particularly in categories like travel and restaurants, many households stockpiled extra savings. Along with the rise in stock prices and home values, net worth has gone up in aggregate since the spring of 2020. With an improving labor market and a solid balance sheet, consumer confidence measures were high at year-end.

Household Balance Sheets Continue to Improve



Source: The Federal Reserve

Along with the rise in stock prices and home values, net worth has gone up in aggregate since the spring of 2020.

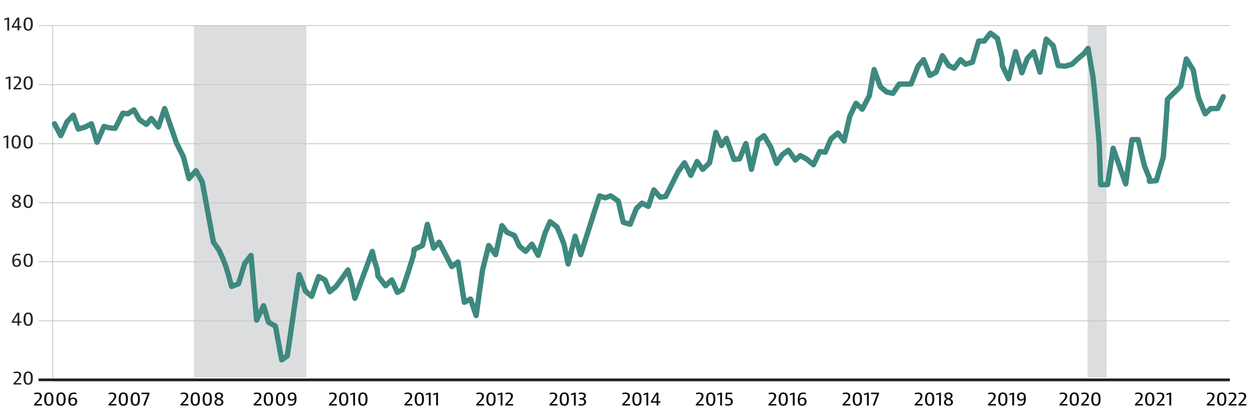
Policymakers Unsettled by Inflation

Inflation continues to be a key topic of interest for investors and policymakers. Monthly readings for the Consumer Price Indicator (CPI) have been coming in higher than 5% year-over-year since May of 2021. The December reading of 7.0% was the highest year-over-year price change since 1982.

Inflation has not been a major problem to date for companies, who seem to be successfully passing cost increases along to customers with higher end-product prices. Profit margins, which measure profits as a percentage of sales, averaged a healthy 11.9% among S&P 500 companies in the fourth quarter, down from recent all-time peaks but still above the long-term average of 11%.

Inflation is a bigger problem for consumers. When living costs increase faster than wages, households lose purchasing power. In recent months, wages have been on the rise, but not at the same pace as inflation. According to the Conference Board, companies are budgeting an average of 3.9% for wage increases in 2022, up from their last estimate of 3% in April but still below inflation.

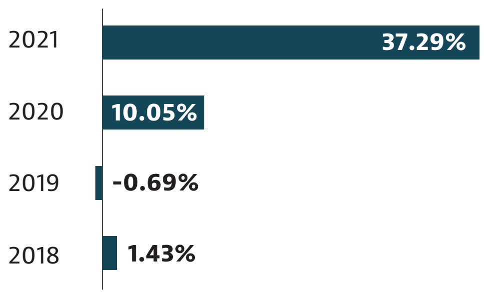
Consumer Confidence Approaching Prior Peaks



Source: The Conference Board, Consumer Confidence Index.
Shaded areas represent recessions.

Meanwhile, the disruptions of the pandemic have continued to affect supply chains and generate pockets of surging prices in some categories. Used cars and trucks, for instance, have experienced extreme inflation, with prices rising more than 30% year-over-year.

Change in Used Car Prices Year-Over-Year



Source: Bloomberg, Homestead Funds' analysis.

Companies are benefiting from continued high demand from consumers. While it's certainly not true for every household, many U.S. consumers have a stronger balance sheet today than they had before the pandemic.

Growth With a Bumpy Ride Ahead

Analysts are currently projecting continued growth in 2022 for company earnings, though at a slower pace than we saw in 2021.

Supply chain issues arising from pandemic-induced labor interruptions are also still an ongoing headwind for companies. The Federal Reserve Bank of New York recently announced a new index that measures global supply chain pressure. The latest readings suggest that supply-chain backlogs may have peaked in late 2021, but it remains to be seen. Future variant waves could cause considerable disruption in the year ahead as well. The last two years have shown just how difficult it is to predict what comes next in a pandemic.

Bonds

Bond returns were mixed in the fourth quarter. Interest rates climbed, particularly for bond maturities in the 2- to 10-year range. Rates for 30-year Treasuries and short-term issues under one year were essentially unchanged. Higher-than-expected inflation readings prompted expectations for a tighter, less accommodative monetary policy in 2022 and beyond, driving interest rates higher for the medium-term segment of the market.

Credit spreads — the difference in yield for corporate bond issues compared to similar-duration Treasuries — trended slightly wider but remained in a stable, healthy zone. We believe corporate balance sheets are strong and the likelihood of default among corporate issuers is low.

With increasing concerns about an overheating economy, policymakers at the Federal Reserve Bank (Fed) indicated a faster timeline for removing accommodative measures. They have begun to taper the asset purchasing program and markets are forecasting about three interest-rate increases in 2022.

Performance Attribution for Our Bond Funds

Against this backdrop, the Homestead Short-Term Government Securities Fund (HOSGX) returned -0.66% in the fourth quarter, in-line with its benchmark, the ICE BofAML 1-5 Year Treasury Index, which returned -0.68%. The fund's yield curve positioning boosted relative performance slightly thanks to an underweight around the 2-year maturity segment.

The Homestead Short-Term Bond Fund (HOSBX) returned -0.88% in the quarter, trailing its benchmark, the ICE BofAML 1-5 Year Corporate/Government Bond Index, which returned -0.69%. The fund's overweight in higher-quality holdings, relative to its benchmark, detracted from performance. However, yield curve positioning boosted returns.

The Homestead Intermediate Bond Fund (HOIBX) returned -0.24% in the fourth quarter, trailing its benchmark, the Bloomberg Barclays Aggregate Bond Index, which rose 0.01%. Widening credit spreads weighed on fund performance, particularly among issues in the financial and industrial sectors. Asset-backed securities also detracted from returns. However, yield curve positioning in Treasuries helped fund performance.

Stocks

Stocks resumed their rally, finishing the year with gains. Performance was mixed among benchmarks. Large-cap stocks generally outperformed small caps, but there was no clear trend in terms of growth- versus value-style benchmarks. On a sector basis, performance varied across different segments of the market, but real estate stocks were a standout leader and communications services stocks lagged.

Companies posted another strong quarter for earnings, closing out the year with about 45% growth in earnings-per-share overall in 2021. Supply chain issues continue to impact company sales in some instances. Stock valuations remained at higher-than-average levels on a price-to-earnings (P/E ratio) basis. M&A activity in the U.S. nearly doubled from 2020 levels to reach $2.61 trillion in deals.

Performance Attribution for Our Stock Funds

The Homestead Value Fund (HOVLX) returned 8.51% in the fourth quarter, outperforming its benchmark, the Russell 1000 Value Index, which rose 7.77%. In the period, stock selection in communications services and health care holdings contributed to fund performance. Conversely, stock choices in the financials sector detracted from relative returns.

Compared to the index, the fund holds significant overweights in industrials 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) rose 6.08% in the fourth quarter, outperforming its benchmark, the Russell 2000 Index, which returned 2.14%. In the period, stock choices in the materials sector contributed to out-performance. Our overweight position and stock selection in the industrials sector was also additive. Conversely, our underweight in the real estate sector and lack of holdings in the utilities sector detracted from relative returns.

Relative to its benchmark, the Small-Company Stock Fund continues to be notably underweight in the energy and consumer discretionary 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 4.58% in the fourth quarter, trailing its custom benchmark, a 60%/40% blend of the Russell 3000 Index and the Bloomberg Barclays Government-Credit Index, which returned 5.31% for the same period.

The fund's stock allocation slightly lagged its benchmark, with stock selection in the information technology weighing on performance. Conversely, stock choices in the industrials and health care sectors aided fund returns. The fund holds its biggest sector overweights in real estate and industrials, compared to its equity benchmark, while the fund's largest underweights are in communication services and energy stocks.

The fund's bond allocation lagged its benchmark in the quarter. Holdings in the agency and municipal sectors detracted from relative performance, while holdings in asset-backed securities (ABS) contributed to returns. Compared to its bond benchmark, the fund holds overweights in corporate bonds and agency-issued bonds and is underweight in U.S. Treasury holdings.

Total Returns as of 12/31/2021

	Q4	Average Annual 1-yr	3-yr	5-yr	10-yr	Since fund's inception
Bond Funds						
Short-Term Government Securities Fund (HOSGX)	-0.66%	-1.18%	2.08%	1.66%	1.11%	2.94%
ICE BofA ML 1-5 Year U.S. Treasury Index	-0.68%	-1.10%	2.42%	1.88%	1.34%	3.70%
Expense ratio 0.81% (gross) 0.75% (net) (12/31/20)*						
Short-Term Bond Fund (HOSBX)	-0.88%	-1.11%	2.70%	2.29%	2.13%	4.06%
ICE BofA ML 1-5 Year Corp./Gov. Index	-0.69%	-0.87%	2.92%	2.28%	1.84%	4.27%
Expense ratio 0.78% (12/31/20)						
Intermediate Bond Fund (HOIBX)**	-0.24%	-1.12%	NA	NA	NA	4.51%
Bloomberg Barclays U.S. Aggregate Index	0.01%	-1.54%	4.79%	3.57%	2.90%	4.25%
Expense ratio 1.13% (gross) 0.80% (net) (12/31/20)*						
Balanced Fund						
Rural America Growth & Income Fund (HRRLX)***	4.58%	NA	NA	NA	NA	NA
Blended Index	5.31%	NA	NA	NA	NA	NA
Expense ratio 2.26% (gross) 1.00% (net) (5/01/21)*						
Equity Funds						
Value Fund (HOVLX)	8.51%	25.07%	19.78%	14.48%	14.32%	10.73%
Russell 1000 Value Index	7.77%	25.16%	17.64%	11.16%	12.97%	NA
Expense ratio 0.65% (12/31/20)						
Small-Company Stock Fund (HSCSX)	6.08%	20.68%	21.64%	8.27%	11.46%	9.29%
Russell 2000 Index	2.14%	14.82%	20.02%	12.02%	13.23%	8.28%
Expense ratio 1.12% (12/31/20)						

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.

*RE Advisers has contractually agreed, through at least May 1, 2022, 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 RE Advisers with one year's notice.

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

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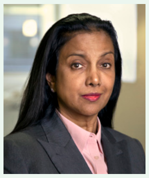
Equity Fund Management



Prabha Carpenter, CFA®
Senior Equity Portfolio Manager

Prabha co-manages the Value, Small-Company Stock and Rural America Growth & Income funds. She is a graduate of the University of Madras, where she received a BA in economics. She received her BS degree in business economics and an MBA with distinction in finance from American University. Prabha holds the Chartered Financial Analyst designation.

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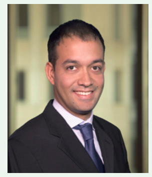
Jim Polk, CFA®
Head of Equity Investments

Jim co-manages the Value, Small-Company Stock and Rural America Growth & Income funds. He received a BA in English from Colby College and an MBA from the Olin Graduate School of Business at Babson College. Jim holds the Chartered Financial Analyst designation.

Bond Fund Management



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Mauricio co-manages the Short-Term Government Securities. Short-Term Bond, Intermediate Bond and Rural America Growth & Income funds. 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.

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Diversification does not guarantee a profit or protect against a loss in a declining market. It is a method used to help manage investment risk.

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 of 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 Merrill Lynch 1-5 Year U.S. Treasury Index** measures the performance of short-term U.S. Treasury securities. The **ICE BofA Merrill Lynch 1-5 Year Corp./Gov. Index** measures the performance of U.S. government and investment-grade corporate debt. The **Bloomberg Barclays U.S. Aggregate Bond 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 Barclays 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 Barclays 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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