BOND MARKET REVIEW

A Monthly Review of Fixed Income Markets

CHANDLER ASSET MANAGEMENT

AUGUST 2021

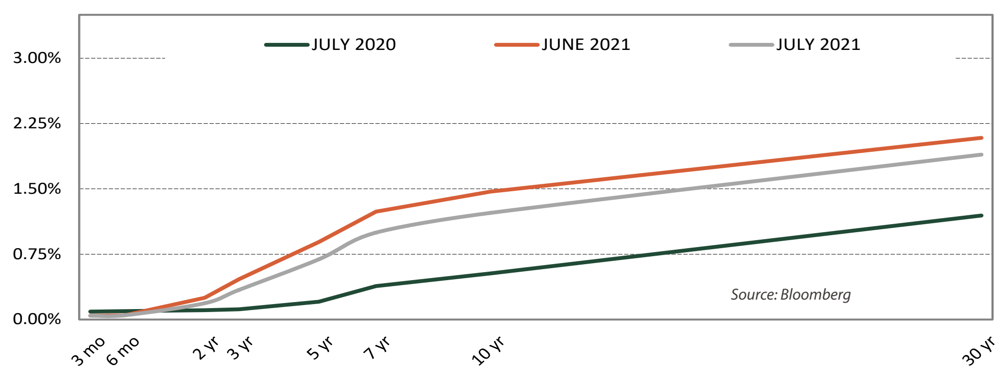
Market Summary

While some pockets of the economy remain dislocated, US real gross domestic product (GDP) has recovered to pre-pandemic levels. The recovery has been fueled by robust fiscal spending, accommodative monetary policy, and vaccinations. These factors are beginning to moderate but should continue to provide tailwinds for the economy in the coming quarters. COVID-19 infection rates in the US have reaccelerated up but remain well below their peak. Nevertheless, the surge in infection rates will likely disrupt expectations for a full economic reopening this fall. Some pandemic-related fiscal relief has started to phase out, but an infrastructure spending plan is likely on the horizon. Meanwhile, the Federal Reserve remains accommodative and continues to facilitate further improvement in the labor market. Estimates for US GDP growth remain strong. The current Bloomberg consensus estimates for 2021 and 2022 US GDP growth are 6.5% and 4.2%, respectively.

The Federal Open Market Committee (FOMC) kept monetary policy unchanged in July. The fed funds target rate remains in the range of 0.0% to 0.25%, and the Fed continues to purchase $80 billion of Treasuries per month, and $40 billion of agency mortgage-backed securities per month. The FOMC has not committed to any specific timeline for tapering asset purchases but signaled that tapering is likely the next step if the economy continues to make significant progress toward their employment and inflation goals, and they will continue to discuss it at upcoming meetings. Fed Chair Powell said that another surge in COVID-19 infections may cause some disruption to the economy and labor market but noted with each successive wave of the virus there tends to be less of an economic impact. The Fed seems to be inching toward a path of policy normalization, and the FOMC's most recent dot plot in June suggested that the Fed may start to raise interest rates in 2023, but the path and timing of monetary policy remains uncertain. As such, we expect financial market volatility may be elevated through year-end.

The yield curve continued to flatten in July. The 2-year Treasury yield declined nearly seven basis points while the 10-year Treasury yield declined almost 25 basis points. We believe multiple factors influenced Treasury rates in the month including rising concerns about the Delta COVID-19 variant, market technicals, and uneven global vaccination and economic recovery rates. Nevertheless, we believe longer-term Treasury yields are poised to move higher this year and the Treasury yield curve is likely to steepen in the intermediate-term.

TREASURY YIELD CURVE POISED TO STEEPEN



The treasury yield curve is steeper on a year-over-year basis. The 3-month T-bill yield was about four basis points lower, while the 2-year Treasury yield was about eight basis points higher, and the 10-Year Treasury yield was about 69 basis points higher, year-over-year, as of July month-end. The Fed has signaled plans to keep the front end of the Treasury yield curve anchored near zero until 2023. The 10-year Treasury yield is roughly 40 basis points lower from late March 2021, but we believe longer-term Treasury yields are poised to move higher.

TREASURY YIELDS	Trend (▲/▼)	7/31/2021	6/30/2021	Change
3-Month	-	0.04	0.04	0.00
2-Year	▼	0.19	0.25	-0.06
3-Year	▼	0.34	0.46	-0.12
5-Year	▼	0.69	0.89	-0.20
7-Year	▼	1.00	1.24	-0.24
10-Year	▼	1.22	1.47	-0.25
30-Year	▼	1.89	2.09	-0.19

Source: Bloomberg

Market Data

World Stock Market Indices
data as of 7/31/2021

	Change (6/30/21)	%CHG
S&P 500		
4,395.26	97.76	2.27%
NASDAQ		
14,672.68	168.73	1.16%
DOW JONES		
34,935.47	432.96	1.25%
FTSE (UK)		
7,032.30	-5.17	-0.07%
DAX (Germany)		
15,544.39	13.35	0.09%
Hang Seng (Hong Kong)		
25,961.03	-2,866.92	-9.94%
Nikkei (Japan)		
27,283.59	-1,507.94	-5.24%

Source: Bloomberg. Please see descriptions of indices on Page 2.

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Since 1988, Chandler Asset Management has specialized in providing fixed income investment solutions to risk-averse public agencies and institutions. Chandler's mission is to provide fully customizable, client-centered portfolio management that preserves principal, mitigates risk and generates income in our clients' portfolios.

Credit Spreads Widened in July

CREDIT SPREADS	Spread to Treasuries (%)	One Month Ago (%)	Change
3-month top rated commercial paper	0.08	0.12	(0.04)
2-year A corporate note	0.15	0.14	0.01
5-year A corporate note	0.37	0.31	0.07
5-year Agency note	0.03	0.00	0.03

Source: Bloomberg

Data as of 7/31/2021

Economy Continues to Grow at an Above-Trend Pace

ECONOMIC INDICATOR	Current Release	Prior Release	One Year Ago
Trade Balance	(75.75) $Bln JUN 21	(70.99) $Bln MAY 21	(50.68) $Bln JUN 20
Gross Domestic Product	6.50% JUN 21	6.30% MAR 21	(31.20%) JUN 20
Unemployment Rate	5.40% JUL 21	5.90% JUN 21	10.20% JUL 20
Prime Rate	3.25% JUL 21	3.25% JUN 21	3.25% JUL 20
Commodity Research Bureau Index	218.08 JUL 21	213.39 JUN 21	143.69 JUL 20
Oil (West Texas Int.)	$73.95 JUL 21	$73.47 JUN 21	$40.27 JUL 20
Consumer Price Index (y/o/y)	5.40% JUL 21	5.40% JUN 21	1.00% JUL 20
Producer Price Index (y/o/y)	9.40% JUN 21	8.70% MAY 21	(2.30%) JUN 20
Euro/Dollar	1.19 JUL 21	1.19 JUN 21	1.18 JUL 20

Source: Bloomberg

Economic Roundup

Consumer Prices

The Consumer Price Index (CPI) was up 5.4% year-over-year in July, unchanged on a year-over-year basis from June. Core CPI (CPI less food and energy) was up 4.3% year-over-year in July, versus up 4.5% in June. The Personal Consumption Expenditures (PCE) index was up 4.0% year-over-year in June, unchanged from May. Core PCE was up 3.5% year-over-year in June, versus up 3.4% year-over-year in May. Current inflation readings are running well above the Fed's longer-run target of around 2.0% but the Fed believes many of the factors fueling higher inflation will be temporary.

Retail Sales

On a year-over-year basis, retail sales were up 18.0% in June versus up 27.6% in May. Year-over-year gains were fueled in part by the drop-off in spending and activity during the pandemic last year. On a month-over-month basis, retail sales increased 0.6% in June (exceeding expectations), following a 1.7% decline in May. Retail sales have been somewhat uneven on a monthly basis due to the timing of fiscal stimulus and economic reopening. Overall, we believe ongoing fiscal support, an improving labor market, and further progress on vaccinations should continue to support consumer spending.

Labor Market

Job growth was stronger than expected in July. U.S. nonfarm payrolls increased by 943,000, versus the consensus forecast of 870,000. On a trailing 3-month and 6-month basis, payrolls increased by an average of 832,000 and 681,000 per month, respectively. The leisure and hospitality sectors continue to drive the job gains in July and increased by 380,000. Government payrolls also posted another solid increase, up by 240,000 in July. The labor participation rate increased slightly to 61.7% from 61.6% but remains lower than the pre-pandemic level of 63.4%. The employment-population ratio increased to 58.4% from 58.0%, but also remains below the pre-pandemic level of 61.1%. The unemployment rate declined to 5.4% in July from 5.9% in June and remains well above the pre-pandemic low of 3.5% in February 2020. The U-6 underemployment rate, which includes those who are marginally attached to the labor force and employed part time for economic reasons, declined to 9.2% in July from 9.8% in June (versus 7.0% in February 2020). Annualized average hourly earnings were up by 4.0% in July versus 3.7% in June, reflecting a solid increase in wages.

Housing Starts

Total housing starts rose 6.3% in June to an annual pace of 1,643,000, in line with expectations. Single-family starts rose 6.3% in June while multi-family starts were up 6.2%. On a year-over-year basis, housing starts were up 29.1% in June, due in part to a decline in activity due to the pandemic last year.

World Stock Market Index Descriptions
S&P 500– The S&P 500 is a market value weighted index of 500 large-capitalization stocks. The 500 companies included in the index capture approximately 80% of available US market capitalization. NASDAQ–The NASDAQ Composite Index is the market capitalization-weighted index of over 3.300 common stocks listed on the NASDAQ stock exchange. Dow Jones–The Dow Jones Industrial Average is an index that tracks 30 large, publicly-owned companies trading on the New York Stock Exchange and the NASDAQ. The Financial Times Stock Exchange Group (FTSE)– The FTSE is a share index of the 100 companies listed on the London Stock Exchange with the highest market capitalization. DAX–The Deutscher Aktienindex (DAX) is a blue chip stock market index consisting of the 30 major German companies trading on the Frankfurt Stock Exchange. Hang Seng–The Hang Seng Index is a freefloat-adjusted market-capitalization-weighted stock market index in Hong Kong. It is used to record and monitor daily changes of the largest companies of the Hong Kong stock market and is the main indicator of overall market performance in Hong Kong. Nikkei–Japan's Nikkei 225 Stock Average is a price-weighted index composed of Japan's top 225 blue-chip companies traded on the Tokyo Stock Exchange.