BOND MARKET REVIEW

A Monthly Review of Fixed Income Markets

CHANDLER ASSET MANAGEMENT

JUNE 2021

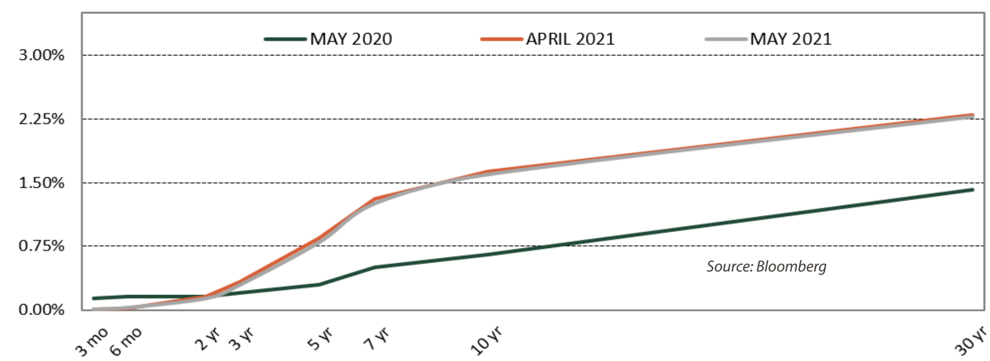
Market Summary

The US economy continues to recover and while some pockets of the economy remain dislocated, real gross domestic product (GDP) is now approaching pre-pandemic levels. The recovery has been fueled by robust fiscal spending, accommodative monetary policy, and a swift vaccine rollout. These factors are beginning to moderate but should continue to provide tailwinds for the economy in the coming quarters. More than 50% of the US population have received at least one dose of a vaccine. Recently, vaccinations have slowed down, but infection rates continue to improve. Some pandemic-related fiscal relief is starting to phase out, but the Biden administration is advocating for large-scale infrastructure spending. We expect some version of an infrastructure spending bill (albeit smaller than the initial White House proposal) to come to fruition later this year. Meanwhile, the Federal Reserve continues to signal that it will look past any near-term uptick in inflation to facilitate continued improvement in the labor market. The Fed has started to unwind the corporate credit facility it established during the pandemic but continues purchase Treasuries and agency mortgage-backed securities each month and has signaled plans to keep the fed funds rate near zero at least through 2023. Estimates for US GDP growth remain strong. The current Bloomberg consensus estimate for 2021 and 2022 US GDP growth are 6.6% and 4.0%, respectively.

The Federal Open Market Committee is scheduled to meet June 15-16, and we expect the Fed to keep monetary policy unchanged. 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. We believe the Fed wants to see a sustained improvement in the employment-to-population and labor participation rates before they start adjusting monetary policy, despite the recent uptick in inflationary pressure. It also remains unclear if rising prices will be temporary. As such, we believe the Fed is likely to wait until at least the fourth quarter of this year to assess the labor market and inflation data to determine if a change in monetary policy is warranted.

The yield curve was little changed on a month-over-month basis in May. So far in June, the yield curve has flattened driven by a decline in longer-term yields. We believe this may reflect, at least in part, a more modest outlook for fiscal spending as negotiations over the infrastructure bill move forward. The yield on 10-year Treasuries has declined roughly 16 basis points since the end of May to 1.43% (as of yesterday's close). Looking ahead, we believe the Treasury yield curve is poised to steepen, which would be consistent with continued improvement in economic activity.

TREASURY YIELD CURVE POISED FOR FURTHER STEEPENING



At the end of May, the treasury yield curve was much steeper on a year-over-year basis. The 3-month T-bill yield was about 12 basis points lower, and the 2-year Treasury yield was about two basis points lower, while the 10-Year Treasury yield was about 94 basis points higher, year-over-year. The Fed has signaled plans to keep the front end of the Treasury yield curve anchored near zero through 2023. We believe longer-term rates still have room to move higher this year.

TREASURY YIELDS	Trend (▲/▼)	5/31/2021	4/30/2021	Change
3-Month	-	0.01	0.01	0.00
2-Year	▼	0.14	0.16	-0.02
3-Year	▼	0.30	0.33	-0.03
5-Year	▼	0.80	0.85	-0.05
7-Year	▼	1.26	1.31	-0.05
10-Year	▼	1.60	1.63	-0.03
30-Year	▼	2.28	2.30	-0.02

Source: Bloomberg

Market Data

World Stock Market Indices
data as of 5/31/2021

		Change (4/30/21)	%CHG
S&P 500	**4,204.11**	22.94	0.55%
NASDAQ	**13,748.74**	-213.94	-1.53%
DOW JONES	**34,529.45**	654.60	1.93%
FTSE (UK)	**7,022.61**	52.80	0.76%
DAX (Germany)	**15,421.13**	285.22	1.88%
Hang Seng (Hong Kong)	**29,151.80**	426.92	1.49%
Nikkei (Japan)	**28,860.08**	47.45	0.16%

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 Tightened Slightly in May

CREDIT SPREADS	Spread to Treasuries (%)	One Month Ago (%)	Change
3-month top rated commercial paper	0.04	0.06	(0.02)
2-year A corporate note	0.15	0.19	(0.04)
5-year A corporate note	0.36	0.39	(0.03)
5-year Agency note	0.01	0.02	(0.01)

Source: Bloomberg Data as of 5/31/2021

The Economy Continues to Recover

ECONOMIC INDICATOR	Current Release	Prior Release	One Year Ago
Trade Balance	(68.90) $Bln APR 21	(75.03) $Bln MAR 21	(52.96) $Bln APR 20
Gross Domestic Product	6.40% MAR 21	4.30% DEC 20	(5.00%) MAR 20
Unemployment Rate	5.80% MAY 21	6.10% APR 21	13.30%MAY 20
Prime Rate	3.25% MAY 21	3.25% APR 21	3.25% MAY 20
Commodity Research Bureau Index	205.70 MAY 21	199.76 APR 21	132.24 MAY 20
Oil (West Texas Int.)	$66.32 MAY 21	$63.58 APR 21	$35.49 MAY 20
Consumer Price Index (y/o/y)	5.00% MAY 21	4.20% APR 21	0.10% MAY 20
Producer Price Index (y/o/y)	9.50% APR 21	5.90 MAR 21	(5.30%) APR 20
Dollar/Euro	1.22 MAY 21	1.20 APR 21	1.11 MAY 20

Source: Bloomberg

Economic Roundup

Consumer Prices

The Consumer Price Index (CPI) was up 5.0% year-over-year in May versus up 4.2% in April. The increase was driven in part by a continued surge in used vehicle prices. Core CPI (CPI less food and energy) was up 3.8% year-over-year in May, versus up 3.0% in April. The Personal Consumption Expenditures (PCE) index was up 3.6% year-over-year in April, versus up 2.4% year-over-year in March. Core PCE was up 3.1% year-over-year in April versus the consensus estimate of 3.0%, up from 1.9% year-over-year in March. As expected, inflation has started to heat up, but we believe the Fed is looking through the near-term inflation data. The Fed expects "base effects" (i.e., comparing current prices to prices at the early stage of the pandemic when prices were under pressure), bottlenecks, and ongoing supply chain disruptions to cause near-term pricing pressures, but the Fed still believes these factors will be temporary.

Retail Sales

On a year-over-year basis, retail sales were up 51.2% in April versus up 29.0% in March. The year-over-year gains are distorted by the drop-off in spending and activity at the early stage of the pandemic last year. On a month-over-month basis, retail sales were flat in April, following a strong 10.7% increase in March. March sales were likely boosted by federal stimulus as well as pent-up demand following severe winter storms in February. Excluding autos and gas, retail sales declined 0.8% in April on a month-over-month basis. Overall, we believe consumer spending remains consistent with an ongoing recovery in economic activity.

Labor Market

Job growth was modestly below expectations in May. U.S. nonfarm payrolls increased by 559,000, versus the Bloomberg consensus forecast of 675,000. April payrolls were revised up by 12,000 to 278,000. On a trailing 3-month and 6-month basis, payrolls increased by an average of 541,000 and 348,000 per month, respectively. The leisure and hospitality sector continue to drive the job gains and increased by 292,000 in May. Notably, the construction sector lost 20,000 payrolls in May, likely due to materials shortages and project delays. The labor participation rate declined to 61.6% from 61.7%, which will surely catch the attention of Fed policymakers. The unemployment rate declined to 5.8% in May from 6.1% in April. 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 10.2% in May from 10.4% in April. Still, more than 9.3 million people remained unemployed in May.

Housing Starts

Total housing starts declined 9.5% in April to an annual pace of 1,569,000. Single-family starts fell 13.4% in April while multi-family starts were up 0.8%. On a year-over-year basis, housing starts were up 67.3% in April, due in part to the steep decline in activity in April 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.