Monthly Market Review

Information provided by MILAF+'s Investment Adviser PFM Asset Management LLC

"Hawks...Doves...How about Turkey?"

Economic Highlights

- U.S. economic growth slowed more than expected in the third quarter of 2021, dampened by the delta-variant COVID-19 surge and ongoing supply chain issues. Following a 6.7% pace in the second quarter, U.S. real gross domestic product (GDP) expanded at a 2% annualized rate. The deceleration reflected a sharp slowdown in the pace of personal consumption, especially in durable goods expenditures like autos and appliances. GDP also reflected increases in private inventory investment, state and local government spending, and nonresidential fixed investment that were partly offset by decreases in residential investment, federal government spending, and exports. The implicit price deflator for the third quarter was 5.7%, indicating that reported real GDP was pulled down sharply by higher inflation measures.
- Strong employment gains resumed as the U.S. economy added 531,000 new jobs in October with notable gains in leisure and hospitality, professional and business services, manufacturing, and transportation and warehousing. In addition, the prior two month's readings were revised sharply higher. The unemployment rate fell by 0.2% to a recovery-cycle low of 4.6%. Job openings are plentiful while the labor force participation rate remains depressed and the "quits rate" – one measure of workers' willingness to leave or change jobs – reached a record high. Average hourly earnings rose 4.9% over the past year, reflecting the strong demand for labor.
- Consumer confidence rose for the first time in four months as the COVID-19 surge eased, but higher prices are weighing on Americans' perception of current economic policies. Consumer prices surged again in October, rising 6.2% year-over-year, the largest increase since 1990. High housing prices, continuing material shortages, and surging energy prices this winter will likely keep inflationary pressures higher for longer.
- At its November 3 meeting, the Federal Open Market Committee announced the anticipated tapering of bond purchases, reducing monthly purchases of Treasury securities by $10 billion and agency mortgage-backed securities by $5 billion. Similar reductions are expected on a monthly basis going forward. Federal Reserve (Fed) Chair Jerome Powell was careful to note that the tapering decision does not imply any direct signal regarding future interest rate policy.
- After months of wrangling, Congress passed the $1.2 trillion bipartisan Infrastructure Investment and Jobs Act in early November. In addition to recurring annual appropriations, the bill includes $550 billion in new spending for improvements to roads, bridges, public transit, passenger and freight rail, airports, ports, the power grid, and expanded broadband access.

Bond Markets

- The U.S. Treasury yield curve steepened in October as the belly of the curve (2-7 year maturities) led the charge and moved higher by 15-25 basis points (bps). Meanwhile, the yield on the 30-year Treasury bond actually moved lower, dipping back below 2%.
- The U.S. Treasury Department announced the first reduction in its quarterly sale of longer-term debt since 2016, which reflects lower borrowing needs as pandemic relief spending recedes.
- Treasury total returns retreated for the month at higher rates. The ICE BofA 2- and 5-year maturity indices returned -0.3% and -0.8% in October, respectively. For the year, long-duration strategies have underperformed.

Equity Markets

- U.S. equity markets advanced in October and reached all-time highs, supported by higher-than-expected corporate earnings, as more than 80% of companies beat estimates. The S&P 500 Index rose 7.0%; the Nasdaq jumped 7.3%, while the Dow Jones Industrial Average was up 5.9%.
- Global stocks also rose, with the MSCI ACWI ex-USA Index rising 2.4% in October and is now up 8% year-to-date, while emerging market stocks increased 1.0% over the month but are still negative for the year.
- U.S. Dollar Index (DXY) was relatively flat in October but is up 5.0% since hitting multi-year lows in May.

PFM Strategy Recap

- The U.S. economy is poised to rebound in the fourth quarter, but inflation remains the biggest headline risk. A potential winter COVID-19 surge is also worth monitoring. Interest rate volatility has picked up, the U.S. debt ceiling looms in December, and a wider range of possible growth outcomes leads us to remain cautiously optimistic and set a neutral duration stance.
- Federal agency spreads are low, range-bound and offer little value.
- Investment-grade (IG) corporate spreads widened a touch as yields rose, but valuations are still rich. Healthy profit margins and record cash levels provide a cushion against potential market stresses.
- AAA-rated asset-backed securities spreads were also marginally wider in October, but likewise, remain tight. Collateral performance remains exceptionally strong.
- Mortgage-backed security spreads retreated to their lowest level in six months, even as Fed tapering begins
- The short-term money market yield curve steepened, with 6-12 month maturities offering the potential to earn additional income for funds that do not have to be immediately liquid.

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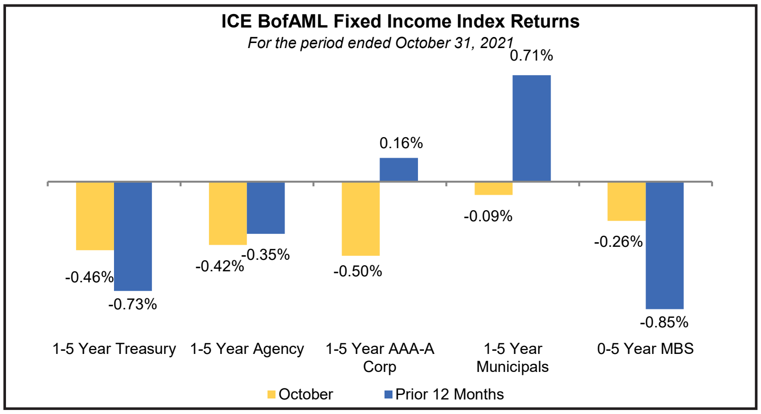
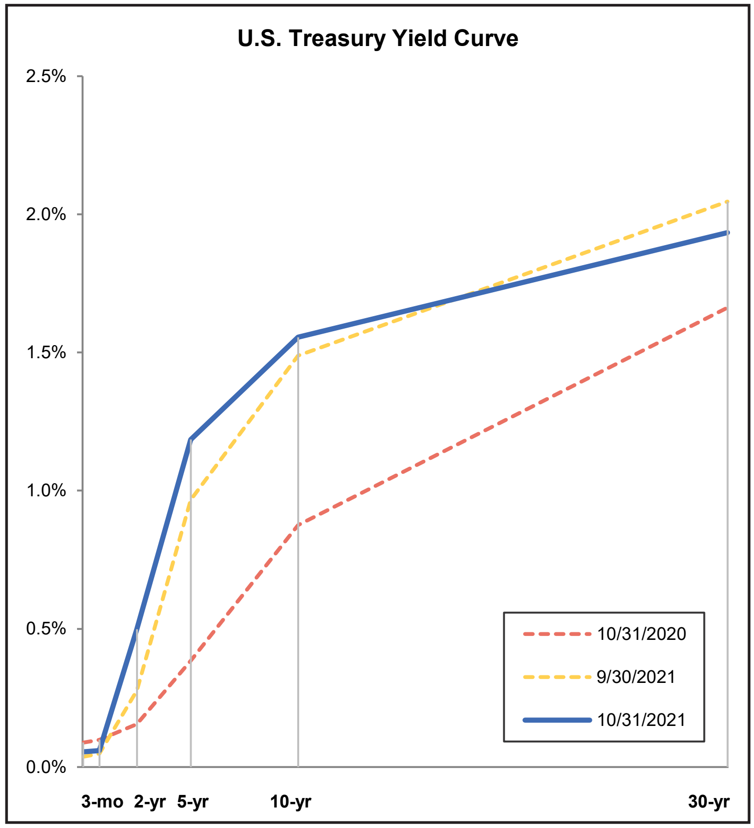
U.S. Treasury Yields				
Duration	Oct 31, 2020	Sep 30, 2021	Oct 31, 2021	Monthly Change
3-Month	0.09%	0.04%	0.06%	0.02%
6-Month	0.10%	0.05%	0.06%	0.01%
2-Year	0.16%	0.28%	0.50%	0.22%
5-Year	0.39%	0.97%	1.19%	0.22%
10-Year	0.88%	1.49%	1.56%	0.07%
30-Year	1.66%	2.05%	1.93%	-0.12%

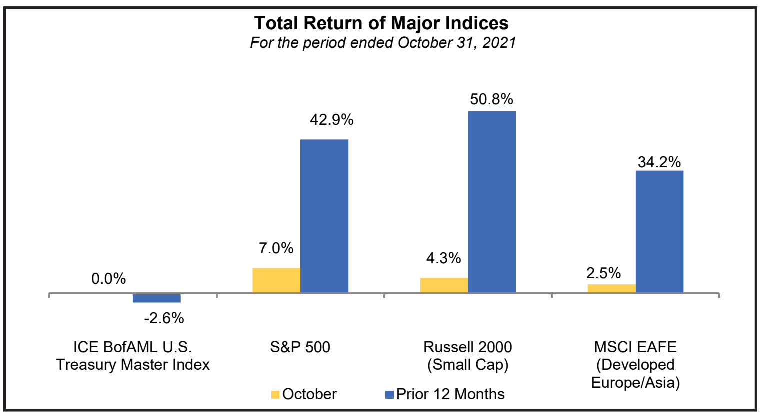
Yields by Sector and Maturity as of October 31, 2021				
Maturity	U.S. Treasury	Federal Agency	Corporates-A Industrials	AAA Municipals
3-Month	0.06%	0.04%	0.32%	--
6-Month	0.06%	0.04%	0.34%	--
2-Year	0.50%	0.47%	0.61%	0.24%
5-Year	1.19%	1.19%	1.43%	0.63%
10-Year	1.56%	1.69%	2.18%	1.38%
30-Year	1.93%	2.17%	2.83%	1.92%

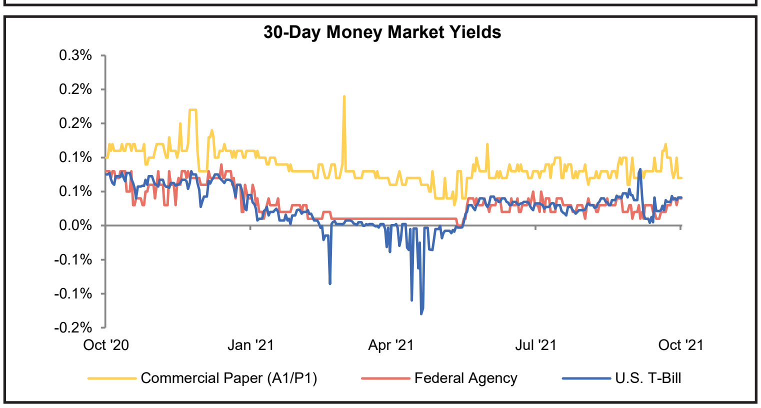
Spot Prices and Benchmark Rates				
Index	Oct 31, 2020	Sep 30, 2021	Oct 31, 2021	Monthly Change
1-Month LIBOR	0.14%	0.08%	0.09%	0.01%
3-Month LIBOR	0.22%	0.13%	0.13%	0.00%
Effective Fed Funds Rate	0.09%	0.06%	0.07%	0.01%
Fed Funds Target Rate	0.25%	0.25%	0.25%	0.00%
Gold ($/oz)	$1,880	$1,755	$1,784	$29
Crude Oil ($/Barrel)	$35.79	$75.03	$83.57	$8.54
U.S. Dollars per Euro	$1.16	$1.16	$1.16	$0.00

Economic Indicators				
Indicator	Release Date	Period	Actual	Survey (Median)
Retail Sales Advance MoM	15-Oct	Sep	0.7%	-0.2%
Consumer Confidence	26-Oct	Oct	113.8	108.0
GDP Annualized QoQ	28-Oct	3Q A	2.0%	2.6%
PCE Core Deflator YoY	29-Oct	Sep	3.6%	3.7%
ISM Manufacturing	1-Nov	Oct	60.8	60.5
Change in Nonfarm Payrolls	5-Nov	Oct	531k	450k
Unemployment Rate	5-Nov	Oct	4.6%	4.7%









Source: Bloomberg. Data as of October 31, 2021, unless otherwise noted.

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