

Monthly Market Review



"Here we go again."

Economic Highlights

- New coronavirus cases are once again surging as the Delta variant grips the globe. In the U.S., new cases spiked from a seven-day average of about 13,000 at the end of June to over 78,000 at the end of July, now appearing headed sharply higher. The rise in infections has triggered a wave of new public health restrictions by state and local governments and has the potential to disrupt the U.S. economic recovery.
- The U.S. economy grew at an annualized rate of 6.5% in the second quarter — strong but well short of estimates. Gross domestic product reflected robust consumer spending and outlays for business equipment but was held back by significant decreases in private inventories. They were drawn down as a result of supply shortages, residential investment and federal government spending.
- U.S. job growth was strong in July. The economy added 943,000 jobs, led once again by gains in service sectors. Job growth has averaged 831,000 jobs in the last three months. The unemployment rate fell a full half percent to 5.4%. Wages continued to increase, while the average manufacturing workweek matched the best reading since the onset of the pandemic.
- The ISM Manufacturing Purchasing Managers Index registered an unexpected decrease in July amid conditions where "companies and suppliers continue to struggle to meet increasing demand" and are being "impacted by near record-long raw material lead times, continued shortages of critical basic materials, rising commodities prices and difficulties in transporting products." Meanwhile, the ISM Services Sector PMI grew for the 14th month in a row to an all-time high.
- At the July Federal Open Market Committee (FOMC) meeting, the Federal Reserve (Fed) kept short-term rates near zero and asset purchases at \$120 billion per month. The Fed noted that the economy has made progress toward its employment and inflation goals and continues to view the recent surge in inflation as transitory. Fed Chair Jerome Powell commented that labor market conditions nevertheless remain "some way away" from reaching the central bank's goals for removing policy accommodation.
- U.S. senators unveiled the \$1 trillion bipartisan "Infrastructure Investment and Jobs Act" that includes \$550 billion in new federal spending on America's roads and bridges, clean drinking water and wastewater infrastructure, public transit, high-speed internet, clean energy transmission and electric vehicle infrastructure.

Bond Markets

- Long-term Treasury yields continued to trend lower in July, while short-term yields were largely unchanged, resulting in a flatter yield curve. Yields on the benchmark 2- and 10-year Treasury note fell six and 25 basis points (bps), respectively. The 10-year posted the biggest monthly decline since the onset of the pandemic in March 2020.

- Concerns that the Delta variant could trigger another infection surge, along with some weaker economic data, weigh on the outlook for economic growth and put downward pressure on long-term rates. Bond yields evidence investor sentiment that inflation will not accelerate once pandemic-related disruptions pass.
- Usage of the Fed's Reverse Repo Facility surged to a record \$1.04 trillion, indicating continuing imbalances in short-term markets, partly due to drawdowns of the Treasury's cash account.
- Treasury performance was positive in July as government securities with long tenors continue to rally. The 3-month Treasury index performance was again marginally flat, while the 5- and 10-year Treasury index advanced 1.0% and 2.0%, respectively.
- Investment-grade (IG) corporate bond returns lagged those of Treasuries. Although issuance slowed a bit to \$65.5 billion in July, yield spreads widened marginally.

Equity Markets

- Ignoring concerns about rising coronavirus cases, rising inflation, materials shortages, and supply-chain challenges, U.S. equity markets climbed to new record highs amid solid earnings reports. In July, the S&P 500 rose 2.4%; the Nasdaq rose 1.2%, while the Dow Jones Industrial Average returned 1.3%.
- Developed market equities sold off with the MSCI ACWI ex-U.S. Index down 1.65%. Coronavirus fears are more prevalent outside of the U.S. The U.S. Dollar Index (DXY) was relatively flat in July.

PFM Strategy Recap

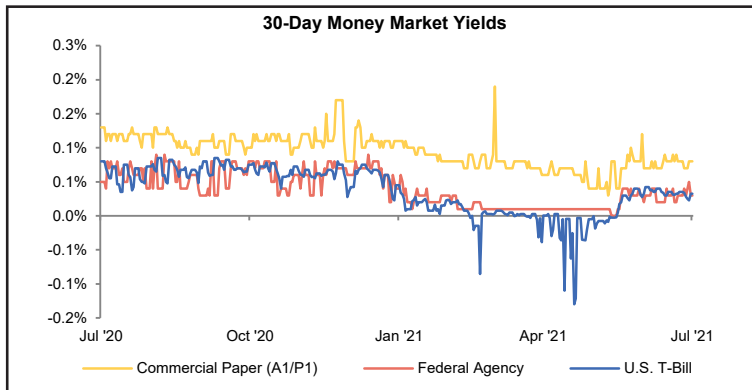
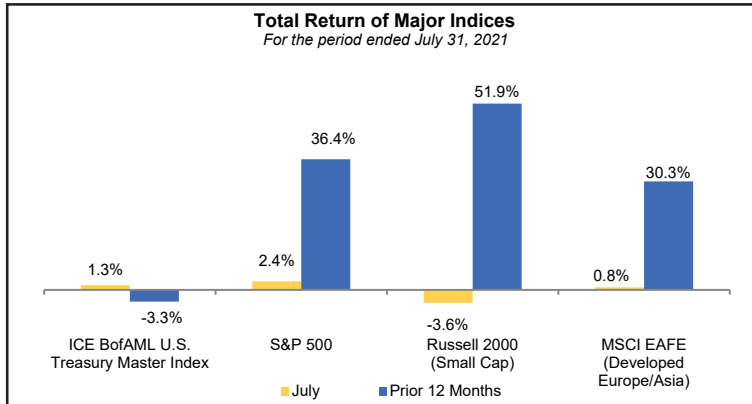
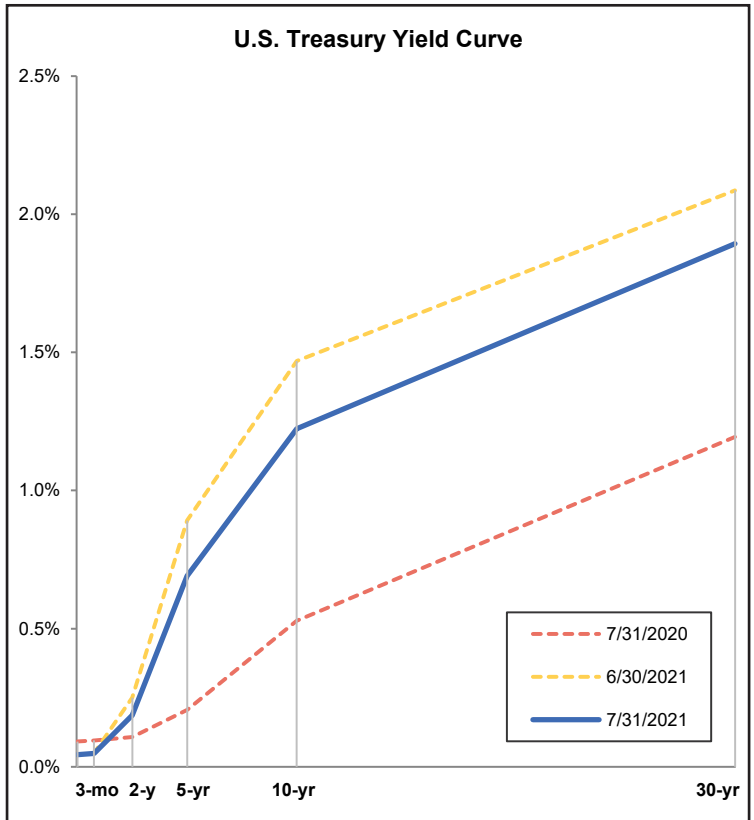
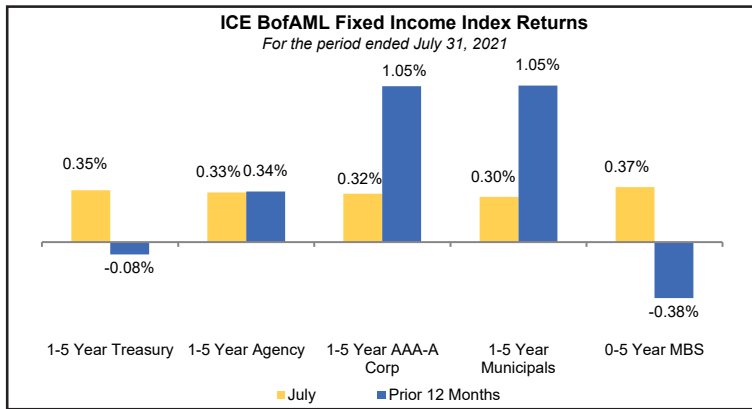
- Economic growth prospects have become less certain, as has the timing of any Fed tapering of bond purchases. Because of this cloudy outlook, along with persistent and surprisingly low long-term yields, our duration stance remains generally neutral to benchmarks.
- Yield spreads on both federal agency and supranational are tight on maturities out to seven years. We have generally been net sellers, awaiting better opportunities in other sectors, maturities, or better-priced new issues.
- IG corporate spreads widened modestly from their extreme tights. While corporate fundamentals and ratings trends are encouraging, valuations remain very rich. Core allocations will remain, with new purchases more selective and skewed toward longer durations where spreads are wider.
- AAA-rated asset-backed securities (ABS) spreads are marginally off record tights. New issue activity remained elevated in July, but demand remains equally robust, and opportunities to add attractive issues are limited.
- Mortgage-backed securities (MBS) spreads widened over the past month but remain tight. With valuations slightly better, the sector may present opportunities, especially in longer duration accounts. Fed tapering of MBS purchases remains a material risk and is expected to weigh on the sector through the balance of the year.

U.S. Treasury Yields				
Duration	Jul 31, 2020	Jun 30, 2021	Jul 31, 2021	Monthly Change
3-Month	0.09%	0.04%	0.04%	0.00%
6-Month	0.10%	0.05%	0.05%	0.00%
2-Year	0.11%	0.25%	0.19%	-0.06%
5-Year	0.21%	0.89%	0.69%	-0.20%
10-Year	0.53%	1.47%	1.22%	-0.25%
30-Year	1.19%	2.09%	1.89%	-0.20%

Yields by Sector and Maturity as of July 31, 2021				
Maturity	U.S. Treasury	Federal Agency	Corporates-A Industrials	AAA Municipals
3-Month	0.04%	0.04%	0.14%	--
6-Month	0.05%	0.03%	0.16%	--
2-Year	0.19%	0.18%	0.30%	0.09%
5-Year	0.69%	0.72%	1.01%	0.38%
10-Year	1.22%	1.33%	1.86%	1.07%
30-Year	1.89%	1.85%	2.74%	1.62%

Spot Prices and Benchmark Rates				
Index	Jul 31, 2020	Jun 30, 2021	Jul 31, 2021	Monthly Change
1-Month LIBOR	0.15%	0.10%	0.09%	-0.01%
3-Month LIBOR	0.25%	0.15%	0.12%	-0.03%
Effective Fed Funds Rate	0.10%	0.08%	0.07%	-0.01%
Fed Funds Target Rate	0.25%	0.25%	0.25%	0.00%
Gold (\$/oz)	\$1,963	\$1,772	\$1,813	\$41
Crude Oil (\$/Barrel)	\$40.27	\$73.47	\$73.95	\$0.48
U.S. Dollars per Euro	\$1.18	\$1.19	\$1.19	\$0.00

Economic Indicators				
Indicator	Release Date	Period	Actual	Survey (Median)
Retail Sales Advance MoM	16-Jul	Jun	0.6%	-0.3%
Consumer Confidence	27-Jul	Jul	129.1	123.9
GDP Annualized QoQ	29-Jul	2Q A	6.5%	8.4%
PCE Core Deflator YoY	30-Jul	Jun	3.5%	3.7%
ISM Manufacturing	2-Aug	Jul	59.5	61.0
Change in Non-Farm Payrolls	6-Aug	Jul	943k	870k
Unemployment Rate	6-Aug	Jul	5.4%	5.7%



Source: Bloomberg. Data as of July 31, 2021, unless otherwise noted. The views expressed constitute the perspective of PFM Asset Management LLC at the time of distribution and are subject to change. The content is based on sources generally believed to be reliable and available to the public; however, PFM cannot guarantee its accuracy, completeness or suitability. This material is for general information purposes only and is not intended to provide specific advice or a specific recommendation. PFM is the marketing name for a group of affiliated companies providing a range of services. All services are provided through separate agreements with each company. Investment advisory services are provided by PFM Asset Management LLC, which is registered with the SEC under the Investment Advisers Act of 1940. For more information regarding PFM's services or entities, please visit www.pfm.com.

