Monthly Market Review

"New Year, New Beginning?"

Economic Highlights

- 2020 was a seminal and tragic year. The coronavirus pandemic ravaged the global economy infecting over 85 million people and killing nearly two million. Governments implemented lockdown measures and injected – alongside their central banks – unprecedented monetary and fiscal stimulus to try to immunize their pandemic-plagued economies. Fueled by monetary and fiscal support, financial markets demonstrated impressive resilience. Though the pandemic has ruptured the fabric of normalcy, optimism in the new year hinges on the success of a global vaccination program.
- While the results of the presidential election are now sealed, the violence on capitol hill has thrown the current political environment even deeper into turmoil.
- After months of significant recovery, the U.S. labor market weakened substantially as the U.S. economy lost 140,000 jobs in December. Driven by COVID-19-induced losses in leisure and hospitality, the unemployment rate held at 6.7%. There were nearly nine million fewer people employed in December than a year ago, and 24% of those employed worked remotely or worked from home during the month.
- American consumers cut back spending on both goods and services in November. Meanwhile, personal income was dragged down as government loan programs ended and unemployment insurance and other social programs expired. With income falling more than spending, the savings rate slipped to 12.9% in November, from 13.6% in the prior month, albeit still notably elevated from a historical perspective.
- After months of wrangling, Congress finally passed a $900 billion economic relief package, including new individual taxpayer stimulus payments, expanded unemployment benefits, support for small businesses and schools, and resources for vaccine efforts.
- The Federal Reserve (Fed) ended the year by affirming its zero-rate monetary policy and its commitment that monetary policy will continue to support the economy. That support will continue until the recovery is complete and the economy achieves maximum employment and inflation consistent with the Fed's new 2% average over time. Market indicators are for short-term interest rates to stay near zero for the foreseeable future.

Bond Markets

- The U.S. Treasury yield curve steepened modestly in December as rates on 10- and 30-year maturities rose by seven to eight basis points (bps), while shorter-term rates remained anchored near zero.
- As a result, muted returns of shorter-maturity U.S. Treasuries exceeded the negative returns of those U.S. Treasuries with longer maturities. In December, the 3-month and 2-year Treasury benchmarks generated returns of 0.01% and 0.07%, respectively, while the 10-year Treasury benchmark posted a return of -0.58%.
- Corporate, asset-backed and supranational issuance was quiet in December as issuers closed their books for the year. Nevertheless, corporate issuers enjoyed low borrowing rates during 2020, resulting in the largest issuance year on record.

Equity Markets

- Equity markets closed the curtain on 2020 with an impressive yearly gain despite the COVID-19 related plunge in the first quarter. In December, the S&P 500 gained 3.8%, lifting the year's performance to 18.4%. The Dow Jones Industrial Average rose 3.4%, boosting its full-year performance to 9.7%, and the Nasdaq increased 5.7% for a remarkable annual performance of 45.1%. Tech stocks, benefiting from public health restrictions and work-from-home policies, led the charge, while small-caps played catch-up on renewed small business stimulus. Global equities had noteworthy gains with the MSCI Developed Market Index up 10.55% and the World Index up 15.90% for the year.
- The U.S. dollar fell during the second half of 2020 as the ongoing pandemic threatened global funding conditions and economic growth. December extended that trend as the currency depreciated 2.1%, closing the year at a two-and-a-half-year low.

PFM Strategy Recap

- The economic outlook remains uncertain, as the pace and efficacy of the global vaccine battles a major resurgence of virus cases headlining 2021 unknowns; political turmoil in the U.S. adds to the unpredictability. Remarkably, the markets have largely discounted the downside. Underlying the recent low market volatility is confidence in the Fed and global central banks that have supported economic stability and expansion.
- Our recent portfolio strategy themes are likely to roll over into the new year: maintain core allocations in most sectors, match benchmark durations and carefully manage risk.
- Yield spreads in all sectors – federal agencies, corporates, supranationals, asset- and mortgage-backed securities remain tight, in many cases at or tighter than pre-pandemic levels. After increasing allocations in most sectors at wider spreads throughout the second and third quarters, we will likely hold the bulk of these positions to earn their incremental income, and only add to positions selectively.
- New issue supply is expected to pick up in January across all fixed income sectors. New issues are likely to be the best opportunity to add corporates and asset-backed securities in the new year.
- In short-term markets, rates are expected to remain low for the next several years. In the near term, short-term rates may be affected by the scale of Treasury issuance necessary to fund the 2021 federal budget deficit. While the deficit will require trillions of dollars of new Treasury issuance, the focus will be on longer-maturity securities and the Treasury bill supply is likely to decline, pressuring short-term rates lower.

U.S. Treasury Yields

Duration	Dec 31, 2019	Nov 30, 2020	Dec 31, 2020	Monthly Change
3-Month	1.55%	0.08%	0.07%	-0.01%
6-Month	1.59%	0.09%	0.09%	0.00%
2-Year	1.57%	0.15%	0.12%	-0.03%
5-Year	1.69%	0.36%	0.36%	0.00%
10-Year	1.92%	0.84%	0.92%	0.08%
30-Year	2.39%	1.57%	1.65%	0.08%

Yields by Sector and Maturity as of December 31, 2020

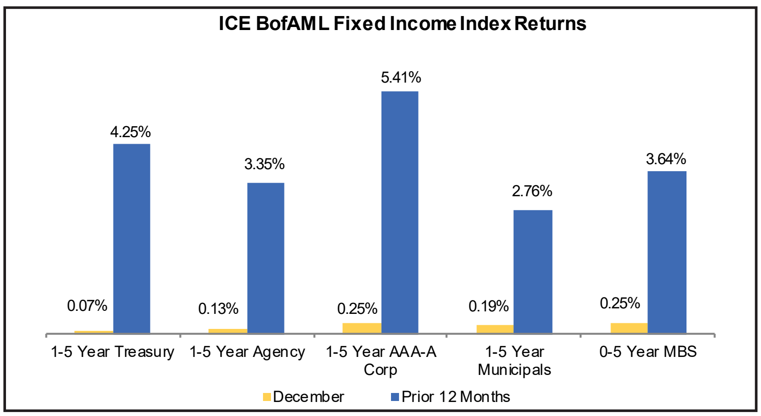
Maturity	U.S. Treasury	Federal Agency	Corporates-A Industrials	AAA Municipals
3-Month	0.07%	0.06%	0.18%	--
6-Month	0.09%	0.06%	0.21%	--
2-Year	0.12%	0.13%	0.29%	0.27%
5-Year	0.36%	0.42%	0.70%	0.51%
10-Year	0.92%	1.10%	1.51%	1.09%
30-Year	1.65%	1.76%	2.52%	1.63%

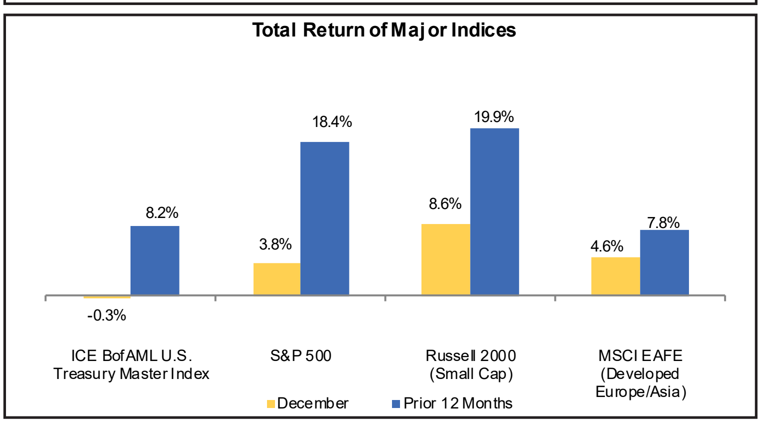
Spot Prices and Benchmark Rates

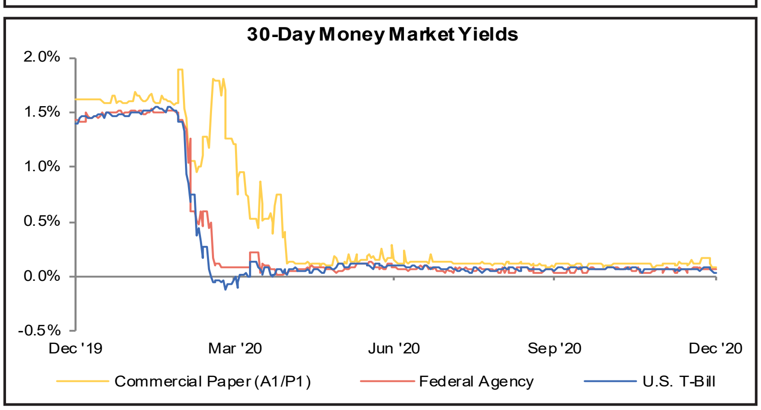
Index	Dec 31, 2019	Nov 30, 2020	Dec 31, 2020	Monthly Change
1-Month LIBOR	1.76%	0.15%	0.14%	-0.01%
3-Month LIBOR	1.91%	0.23%	0.24%	0.01%
Effective Fed Funds Rate	1.55%	0.09%	0.09%	0.00%
Fed Funds Target Rate	1.75%	0.25%	0.25%	0.00%
Gold ($/oz)	$1,523	$1,776	$1,895	$119
Crude Oil ($/Barrel)	$61.06	$45.34	$48.52	$3.18
U.S. Dollars per Euro	$1.12	$1.19	$1.22	$0.03

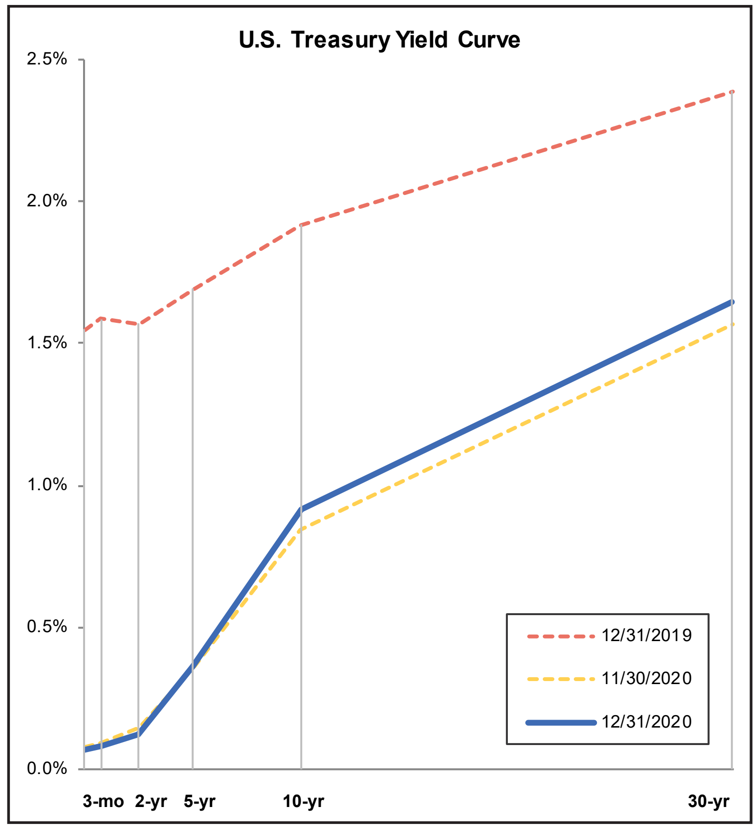
Economic Indicators

Indicator	Release Date	Period	Actual	Survey (Median)
Retail Sales Advance MoM	16-Dec	Nov	-1.1%	-0.3%
Consumer Confidence	22-Dec	Dec	88.6	97.0
GDP Annualized QoQ	22-Dec	3Q T	33.4%	33.1%
PCE Core Deflator YoY	23-Dec	Nov	1.4%	1.4%
ISM Manufacturing	5-Jan	Dec	60.7	56.8
Change in Nonfarm Payrolls	8-Jan	Dec	-140k	50k
Unemployment Rate	8-Jan	Dec	6.7%	6.8%









Source: Bloomberg. Data as of December 31, 2020, unless otherwise noted.