Monthly Market Review

Fixed Income | December 2023

pfm asset management

"November rains returns."

Economic Highlights

► November was an about-face to market-wide risk sentiment as a less-hawkish Federal Reserve (Fed) fueled risk-on 'everything.' Bond returns posted multi-year bests and equities approached 12-month highs, as the reality of a soft-landing and the end of an historical rate hiking cycle took focus.

► Following two unchanged rate decisions, Fed minutes from November's Federal Open Market Committee meeting noted that "finances of some households […] were increasingly coming under pressure" and that "while labor market conditions remained tight, they had eased since earlier in the year." As a result, markets inferred a cautious approach to further rate action, removing additional hikes from fed funds futures and pulling the first cut forward to the spring of 2024.

► The November employment report showed non-farm payrolls increasing by 199,000, which was mostly in line with expectations. The unemployment rate ticked down to 3.7% from 3.9% the month prior. The labor force participation rate inched back up to 62.8%, which is the highest rate seen since the pandemic.

► After registering 3.7% in August and September, headline CPI fell to a lower-than-expected 3.2% in October with higher shelter costs offsetting lower gasoline prices. Core inflation, which excludes food and energy, fell from 4.1% to 4.0%, also below forecasts. While both metrics of prices have consistently trended lower over the past several months, inflation is still above the Fed's target of 2%.

► The second estimate of third quarter gross domestic product accelerated to 5.2%, topping the initial 4.9% release. The increase reflected an upturn in most categories, while consumer spending was revised lower to 3.6% from 4%.

► Retail sales (which do not adjust for inflation) decreased in October for the first time in seven months and personal spending rose by the smallest amount in five months. While the consumer remains resilient and a tailwind to economic prospects, minor cracks have started to appear.

Bond Markets

► The bond market had a roaring November as the economy seems poised for a "goldilocks" cooldown. Total returns for the Bloomberg U.S. Aggregate Index were 4.5% in November, the best month since May 1985, and 5.0% for the Bloomberg Global Aggregate Index, the strongest month since December 2008.

► Overall, U.S. Treasury yields rallied substantially as markets now widely accept and expect the Fed has likely reached the peak overnight target of this tightening cycle.

► The benchmark 2-, 5-, and 10-year U.S. Treasury notes finished the month at 4.68%, 4.27%, and 4.33%, moving down -41, -59, and -60 basis points during November, respectively.

► As a result of significantly lower yields, the ICE BofA 2-, 5-, and 10-year U.S. Treasury indices generated strong returns for the month: 0.98%, 2.62%, and 4.78%, respectively.

► In line with the broad risk-on sentiment through November, non-government allocations to portfolios added notable excess return as spreads generally narrowed across sectors.

Equity Markets

► Stocks broke a three-month losing streak while posting their best month in over a year. All three major U.S. stock indexes ended November notably higher, with the Dow Jones Industrial Average setting an all-time high. On a total return basis, the Nasdaq gained 10.8%, the Dow rose 9.2%, and the S&P 500 ended the month up 9.1%.

► International equities, as measured by the MSCI All Countries World ex-U.S. Net Index, kept pace with domestic stock returns, generating 9.0% total return for the month. The U.S. Dollar declined 3% through November as the world hawked a less hawkish Fed.

PFMAM Strategy Recap

► Preference for a defensive duration posture shifted in early November as signals flashed that the Fed's hiking cycle may be complete. As a result, portfolio durations were extended to a near-neutral stance versus benchmarks as we favor minimizing duration mismatch.

► Government alternatives including federal agency, supranational, and municipal debt continues to trade in a narrow and tight range as light issuance has limited attractive buying opportunities.

► Short-term credit (commercial paper and certificates of deposit) spreads tightened along with the broad corporate debt sector. Though not as wide as recent months, short credit remains a solid alternative, especially for maturities beyond six months.

► Investment-grade (IG) corporates outperformed in November as spreads approached summer lows. Good credit fundamentals and a positive economic outlook should be supportive, and we maintain an overweight bias for the sector. While incremental income in the sector remains above historical averages, recent tightening has provided opportunities to trim the most expensive holdings.

► Asset-backed security (ABS) spreads tightened in November, but not quite to the extent as IG corporates, reflecting to an extent the market view of shifting consumer risks. Nevertheless, the sector generated positive excess returns for the month and light issuance expectations for the balance of the year is supportive. Fundamentals remain within our expectations and spreads remain attractive.

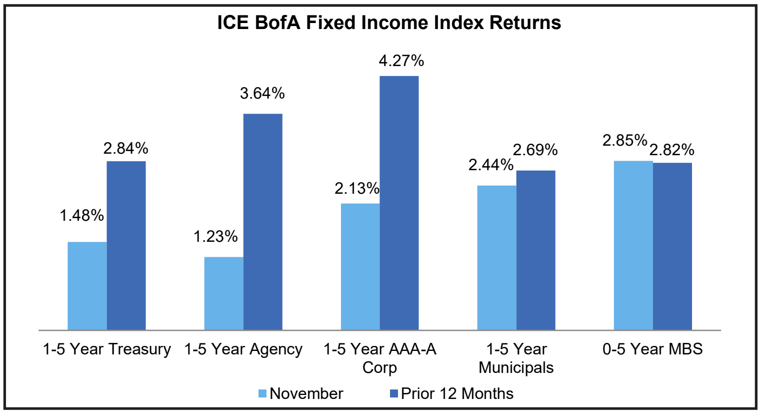
► The mortgage-backed securities (MBS) sector underscored the about-face of risk sentiment during the month as outperformance more than offset the substantially poor performance from October. While spreads narrowed significantly from recent wides, the sector remains elevated relative to 12-month averages. We continue to look for opportunities to add exposure through new issuance in particular.

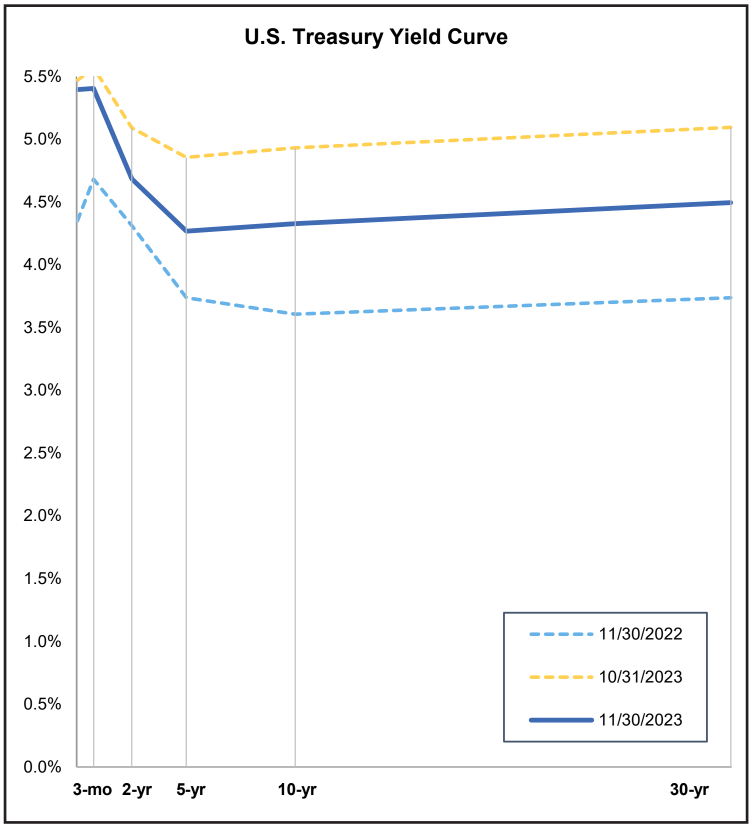
U.S. Treasury Yields				
Duration	**Nov 30, 2022**	**Oct 31, 2023**	**Nov 30, 2023**	**Monthly Change**
3-Month	4.35%	5.47%	5.39%	-0.08%
6-Month	4.68%	5.57%	5.40%	-0.17%
2-Year	4.31%	5.09%	4.68%	-0.41%
5-Year	3.74%	4.86%	4.27%	-0.59%
10-Year	3.61%	4.93%	4.33%	-0.60%
30-Year	3.74%	5.10%	4.50%	-0.60%

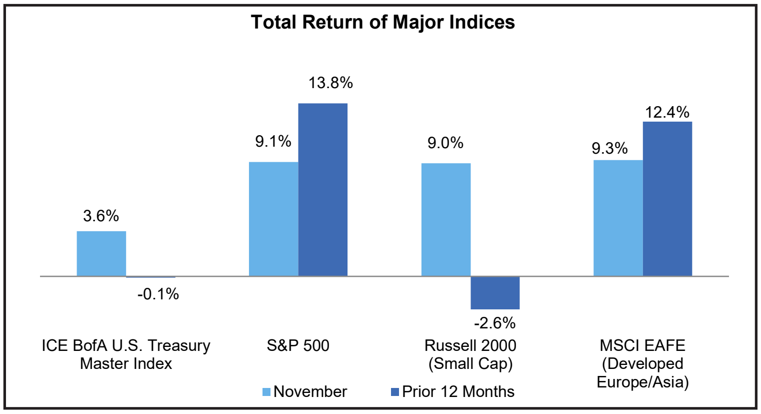
Yields by Sector and Maturity				
Maturity	**U.S. Treasury**	**Federal Agency**	**Corporates-A Industrials**	**AAA Municipals**
3-Month	5.39%	5.32%	5.38%	-
6-Month	5.40%	5.37%	5.38%	-
2-Year	4.68%	4.78%	5.06%	2.88%
5-Year	4.27%	4.43%	4.85%	2.61%
10-Year	4.33%	4.65%	5.09%	2.84%
30-Year	4.50%	5.00%	5.46%	3.44%

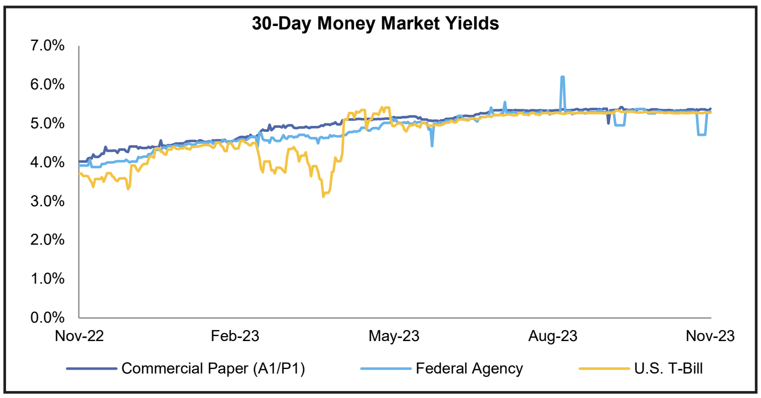
Spot Prices and Benchmark Rates				
Index	**Nov 30, 2022**	**Oct 31, 2023**	**Nov 30, 2023**	**Monthly Change**
1-Month LIBOR	4.14%	5.43%	5.46%	0.03%
3-Month LIBOR	4.78%	5.64%	5.63%	-0.01%
Effective Fed Funds Rate	3.83%	5.33%	5.33%	0.00%
Fed Funds Target Rate	4.00%	5.50%	5.50%	0.00%
Gold ($/oz)	$1,746	$1,994	$2,038	$44
Crude Oil ($/Barrel)	$80.55	$81.02	$75.96	-$5.06
U.S. Dollars per Euro	$1.04	$1.06	$1.09	$0.03

Economic Indicators				
Indicator	**Release Date**	**Period**	**Actual**	**Survey (Median)**
Change in Nonfarm Payrolls	3-Nov	Oct	150K	180K
CPI YoY	14-Nov	Oct	3.20%	3.30%
Retail Sales Advance MoM	15-Nov	Oct	-0.10%	-0.30%
U. of Mich. Consumer Sentiment	22-Nov	Nov F	61.3	61
GDP Annualized QoQ	29-Nov	3QS	5.20%	5.00%
PCE Core Deflator YoY	30-Nov	Oct	3.50%	3.50%
ISM Manufacturing	1-Dec	Nov	46.7	47.8









Source: Bloomberg. Data as of November 30, 2023, unless otherwise noted.

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