Monthly Market Review

"Have you heard? Inversion's the word!"

Economic Highlights

- At the end of March all eyes turned to the seven-day stint when the yield on a 3-Month U.S. Treasury bill exceeded that of a 10-Year U.S. Treasury note. This yield curve inversion often precedes a recession. Despite this warning sign, other measures of market and economic conditions – such as credit spreads and jobless claims – do not portend a recession in the near term.
- As expected, the Federal Reserve (Fed or FOMC) left the federal funds rate unchanged in March at its current target range of 2.25% to 2.50%. Chairman Powell confirmed the Fed's intent to be patient and "on hold" while assessing global economic and financial developments and inflation to determine what future adjustments to short-term rates – up or down – might be warranted.
- The final estimate of U.S. Gross Domestic Product (GDP) showed that growth moderated in the fourth quarter of 2018. The economy expanded at 2.2%, decelerating from 4.2% and 3.4% in the prior two quarters. The biggest headwinds to U.S. growth are from abroad, as vulnerabilities remain in the Eurozone, China, and Japan. Estimates for 2019 growth are in the 2% to 2.5% range, implying slower but steady expansion relative to 2018.
- The March U.S. jobs report showed non-farm payrolls rose by 196,000, rebounding from February's lackluster 33,000 increase. The unemployment rate remained near its multi-decade low at 3.8%. Wage growth slowed a bit.
- U.S. Manufacturing and Consumer Confidence gauges remain positive, but are off their late-2018 highs. While consumer sentiment remains high, the difference between future and current assessments of economic conditions indicates consumers have become less optimistic about the future.
- After weakening for most of 2018, several measures of the housing market have rebounded. Boosted by lower mortgage rates and slowing home price appreciation, new and existing home sales spiked month-over-month by 4.9% and 11.8%, respectively.

Bond Markets

- U.S. Treasury yields rallied across the curve over the month, with maturities beyond one year declining 20 to 30 basis points (0.20% to 0.30%). The result was an even flatter yield curve.
- As a result, returns on longer duration indices dominated their shorter-term counterparts. For example, the 1-year and 2-year constant maturity U.S. Treasury indices returned 0.35% and 0.62%, respectively, while, the 5-Year and 10-Year indices generated 1.49% and 2.84% total return for the month.
- The inversion of the Treasury yield curve, albeit brief, did not change positive investor sentiment. Historically, this inverted relationship has foreshadowed recessions, with only one false positive in the past 45 years. But this event was brief, and other confirming signals such as stock market prices and credit market conditions suggest that a downturn is not imminent.

Equity Markets

- U.S equities continued their strong start to 2019, with the S&P 500 Index advancing 1.9% in March, pushing first quarter returns to 13.6% – the strongest start to a year since 1998. International equity indexes generated strong gains as well.
- The U.S. Dollar Index (DXY), measured against a basket of international currencies, inched higher for the second consecutive month reaching its highest level in over a year.

PFM Outlook

- With the Fed on hold and many investors expecting - a rate cut rather than a rate *hike* as the next move, we recommend no change to our overall strategy which is to minimize interest rate bets and focus on income as the main driver of portfolio returns.
- In an oft-repeated theme, federal agency spreads remain very narrow. In some instances, issues are trading at yields equal to or less than similar maturity Treasuries. Given the flat yield curve, callable structures may offer enhanced return opportunity. Value remains very issue specific.
- Supranational issuance has been lighter than expected, keeping yield spreads narrow and the sector offers little value. Foreign exchange rate dynamics may be a driver, as some new issues have been in currencies other than U.S. dollars.
- Investment-grade (IG) credit was a standout performer in the first quarter as spreads narrowed back to September 2018 levels. Because of this, current value has diminished somewhat but the positively-sloped credit curve continues to support allocations to the sector. With lower yields and a flat Treasury curve, we expect incremental income from corporates to buoy performance in coming quarters.
- Mortgage-backed securities (MBS) also performed well in the quarter, reversing some of the dismal performance of the fourth quarter of 2018. On the positive side, the Fed's recent announcement of an end to their balance sheet wind-down by September should remove one of the headwinds to the sector.
- AAA-rated asset-backed securities (ABS) have been a staple in portfolios over the last several quarters and will remain so. Attractive spreads and lower volatility are key attributes driving our desire to hold healthy allocations.
- Money market investors continue to reap the benefits of short-maturity yields at a decade high. Although yields on commercial paper and bank certificates of deposit have moderated with the outlook for a patient Fed, they remain attractive relative to those in short, or even intermediate-term, government securities.

U.S. Treasury Yields

Maturity	Mar 31, 2018	Feb 28, 2019	Mar 31, 2019	Monthly Change
3 Month	1.71%	2.44%	2.39%	-0.05%
6 Month	1.92%	2.50%	2.43%	-0.07%
2 Year	2.27%	2.52%	2.26%	-0.26%
5 Year	2.56%	2.51%	2.23%	-0.28%
10 Year	2.74%	2.72%	2.41%	-0.31%
30 Year	2.97%	3.08%	2.82%	-0.26%

Yields by Sector and Maturity as of March 31, 2019

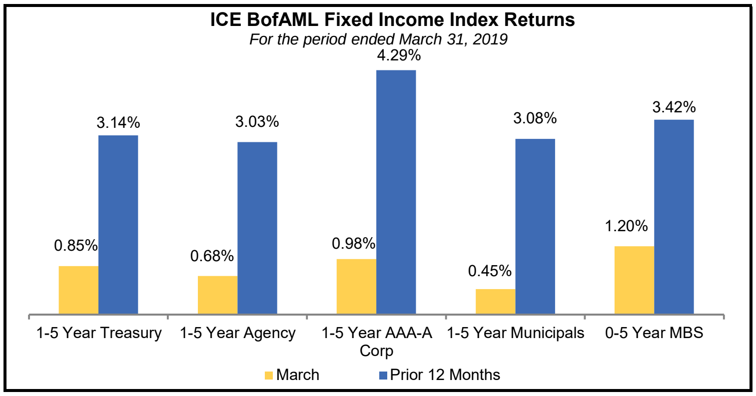
Maturity	U.S. Treasury	Federal Agency	Corporates-A Industrials	AAA Municipals
3 Month	2.39%	2.42%	2.46%	-
6 Month	2.43%	2.40%	2.50%	-
2 Year	2.26%	2.31%	2.64%	1.52%
5 Year	2.23%	2.32%	2.77%	1.67%
10 Year	2.41%	2.68%	3.19%	2.12%
30 Year	2.82%	3.05%	3.95%	2.76%

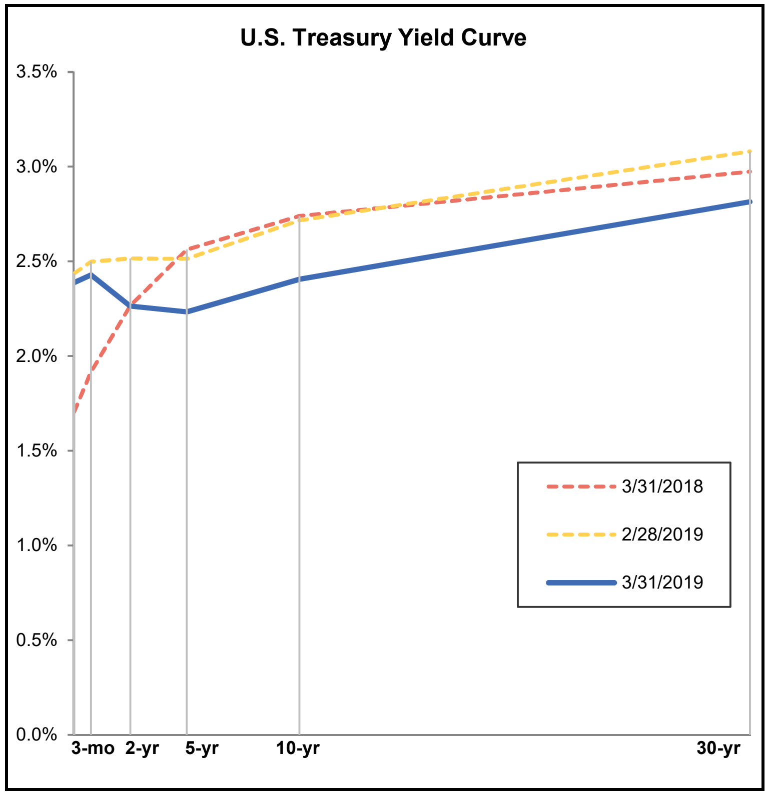
Spot Prices and Benchmark Rates

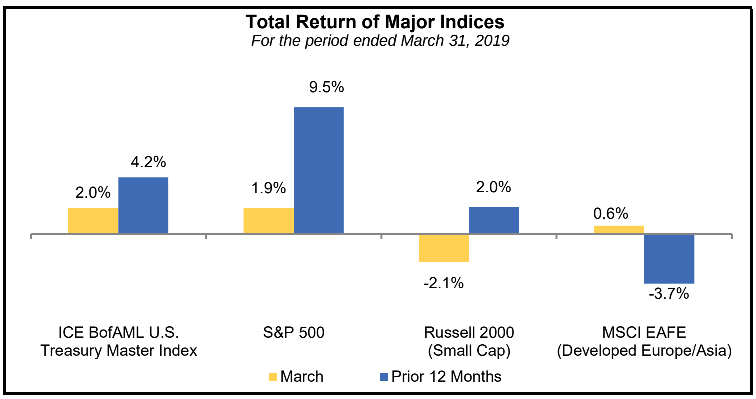
Index	Mar 31, 2018	Feb 28, 2019	Mar 31, 2019	Monthly Change
1-Month LIBOR	1.88%	2.49%	2.49%	0.00%
3-Month LIBOR	2.31%	2.62%	2.60%	-0.02%
Effective Fed Funds Rate	1.67%	2.40%	2.43%	0.03%
Fed Funds Target Rate	1.75%	2.50%	2.50%	0.00%
Gold ($/oz)	$1,323	$1,316	$1,293	-$23
Crude Oil ($/Barrel)	$64.94	$57.22	$60.14	$2.92
U.S. Dollars per Euro	$1.23	$1.14	$1.12	-$0.02

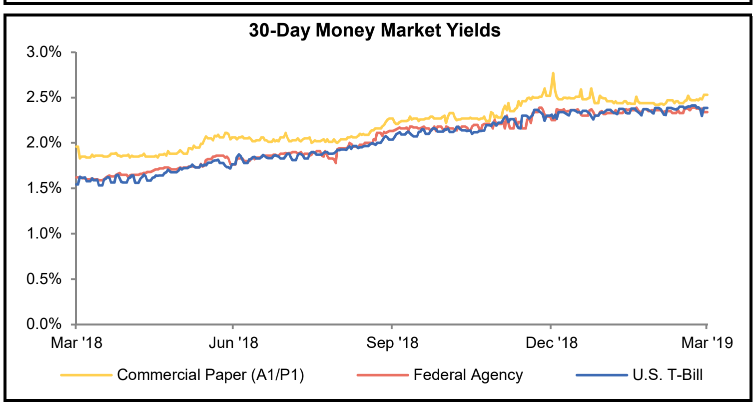
Economic Indicators

Indicator	Release Date	Period	Actual	Survey (Median)
FOMC Rate Dec. (Upper)	20-Mar	Mar	2.50%	2.50%
Existing Home Sales MoM	22-Mar	Feb	11.8%	3.2%
Consumer Confidence	26-Mar	Mar	124.1	132.5
GDP Annualized QoQ	28-Mar	4Q T	2.2%	2.3%
New Home Sales MoM	29-Mar	Feb	4.9%	2.1%
Retail Sales MoM	1-Apr	Feb	-0.2%	0.2%
Nonfarm Payrolls	5-Apr	Mar	196k	177k









Source: Bloomberg. Data as of March 31, 2019, unless otherwise noted.