# Monthly Market Review

Risk investing is back! A renewed bull market has taken hold as global stock markets recover and the Fed pauses.

## Economic Highlights

- The post-holiday euphoria continued through January as stocks extended their strong rebound. In particular, U.S. markets had their strongest January since 1987. Calmer heads prevailed despite a prolonged partial government shutdown in the U.S., a resounding defeat of Prime Minister Theresa May's Brexit plan in the U.K., and slowing economic momentum in the U.S., Europe and China.
- The Trump administration reluctantly agreed to a three-week truce to end the longest government shutdown in U.S. history (at least through February 15). Although government paychecks are flowing once again, the battle lines over border security funding appear deeply entrenched.
- At its January 2019 meeting, the Federal Reserve (Fed) left rates unchanged, but pivoted monetary policy to a wait-and-see approach as the Committee noted "it will be patient as it determines what future adjustments ... may be appropriate." They also shifted from a somewhat singular focus on U.S. employment and inflation to consider a broader range of "global economic and financial developments." So it appears the Fed is firmly on hold for the indefinite future.
- The U.S. labor market marched ahead unabated, creating 304,000 new jobs in January, far exceeding expectations. Although the unemployment rate ticked up to 4%, it was partially due an increase in the labor participation rate and the government shutdown.
- U.S. economic data appears to confirm a modest slowdown as readings of both consumer and business activity decelerated. Housing, auto sales and factory orders all slowed. Manufacturing gauges also moderated due to weakening global demand, ongoing trade disputes, and the fourth quarter plunge in oil prices.

## Bond Markets

- Bond market volatility subsided. The U.S. Treasury yield curve remained slightly inverted between 2- and 5- year maturities. U.S. Treasury yields were modestly lower, falling two to eight basis points (0.02% to 0.08%) over the month.
- As a result of declining yields across the yield curve in January, fixed income returns were strongly positive, with longer duration indexes outperforming shorter-term ones. For example, the 3-Month and 2-Year Constant Maturity U.S. Treasury Indices returned 0.20% and 0.27%, respectively, while the 5-Year and 10-Year indices generated 0.53% and 0.71% total return for the month.
- The "risk-on" recovery led to a sharp contraction in credit spreads across the ratings spectrum. Returns on corporate indices far outpaced returns on comparable-maturity Treasury indices for the month.

## Equity Markets

- U.S equities rebounded, with the S&P 500 recovering more than half of its fourth quarter losses from 2018's highs. Over the month, the S&P 500 advanced 8.0%, the Dow climbed 7.3%, and the NASDAQ soared 9.8%.
- Cyclical sectors, like industrials and consumer discretionary, outpaced more defensive sectors, like utilities and healthcare.
- The U.S. Dollar Index (DXY) drifted marginally lower over the month, but has generally moved sideways in a relatively tight range since the beginning of the fourth quarter of 2018.

## PFM Outlook

- With the Fed on hold, we now favor duration-neutral portfolio positions relative to benchmarks. We are focusing our efforts on generating income as the primary source of total return.
- Federal agency and supranational supply remained constrained as new issuance was limited. Consequently, agency and supranational yield spreads remain tight, but have begun to inch their way wider. This applies particularly to agency spreads on maturities beyond seven years where relative yields are slowly becoming more attractive. We will continue to look for issue-specific value amidst new issue offerings as we approach the seasonal uptick in issuance.
- Over January, investment-grade (IG) credit spreads reversed the bulk of December's widening. The reversal has reduced the relative value of corporate bonds to the levels experienced before the December blow-out. Fourth quarter returns, depressed by this spread widening, rebounded in January. Consequently, the sector now offers only modest or fair value. With the yield curve flat and spreads near last November's levels, we plan to be more selective, assessing issue-specific value based on issuer quality and maturity.
- Mortgage-backed securities (MBS) have recovered somewhat from their underperformance in December, but they still face uncertainty due to elevated volatility, weakness in the housing market, higher mortgage rates, and the Fed's ongoing wind-down of balance sheet holdings. On balance, however, the underperformance of the mortgage sector over the past several months has created more attractive valuations and some opportunity to selectively add MBS allocations to portfolios.
- AAA-rated asset-backed securities (ABS) proved their worth in the face of heightened late-2018 volatility. We continue to maintain an overweight to high-quality ABS and look forward to a higher-volume issuance season.
- With the Fed on hold, short-term rates may have peaked. However, money market investors continue to reap the benefits of 2.25% rate increase over the past three years, which put short rates near their highest levels in over a decade. Commercial paper, negotiable CDs and even Treasury notes look attractive for ultra-short investors.

## U.S. Treasury Yields

| Maturity | Jan 31, 2018 | Dec 31, 2018 | Jan 31, 2019 | Monthly Change |
|---|---|---|---|---|
| 3-Month | 1.46% | 2.36% | 2.39% | 0.03% |
| 6-Month | 1.65% | 2.48% | 2.46% | -0.02% |
| 2-Year | 2.14% | 2.49% | 2.46% | -0.03% |
| 5-Year | 2.52% | 2.51% | 2.44% | -0.07% |
| 10-Year | 2.71% | 2.69% | 2.63% | -0.06% |
| 30-Year | 2.94% | 3.02% | 3.00% | -0.02% |

## Yields by Sector and Maturity as of January 31, 2019

| Maturity | U.S. Treasury | Federal Agency | Corporates-A Industrials | AAA Municipals |
|---|---|---|---|---|
| 3-Month | 2.39% | 2.37% | 2.56% | - |
| 6-Month | 2.46% | 2.44% | 2.61% | - |
| 2-Year | 2.46% | 2.51% | 2.89% | 1.70% |
| 5-Year | 2.44% | 2.60% | 3.06% | 1.93% |
| 10-Year | 2.63% | 3.00% | 3.46% | 2.43% |
| 30-Year | 3.00% | 3.35% | 4.16% | 3.11% |

## Spot Prices and Benchmark Rates

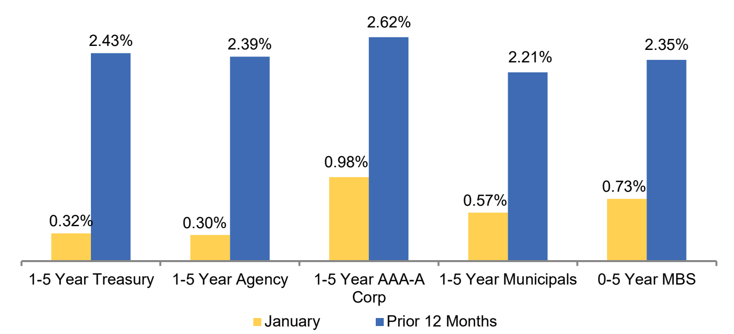
| Index | Jan 31, 2018 | Dec 31, 2018 | Jan 31, 2019 | Monthly Change |
|---|---|---|---|---|
| 1-Month LIBOR | 1.58% | 2.50% | 2.51% | 0.01% |
| 3-Month LIBOR | 1.78% | 2.81% | 2.74% | -0.07% |
| Effective Fed Funds Rate | 1.34% | 2.40% | 2.40% | 0.00% |
| Fed Funds Target Rate | 1.50% | 2.50% | 2.50% | 0.00% |
| Gold ($/oz) | $1,339 | $1,281 | $1,320 | $38 |
| Crude Oil ($/Barrel) | $64.73 | $45.41 | $53.79 | $8.38 |
| U.S. Dollars per Euro | $1.24 | $1.15 | $1.14 | -$0.01 |

## Economic Indicators

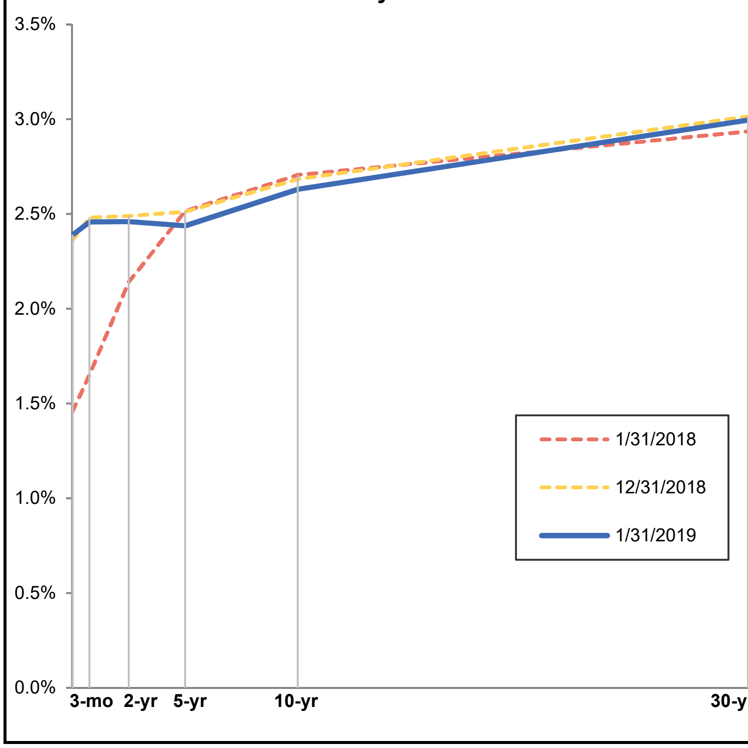
| Indicator | Release Date | Period | Actual | Survey (Median) |
|---|---|---|---|---|
| Nonfarm Payrolls | 1-Feb | Jan | 304k | 165k |
| CPI ExFood&Energy YoY | 11-Jan | Dec | 2.2% | 2.2% |
| New Home Sales MoM | 31-Jan | Nov | 16.9% | 4.8% |
| Consumer Confidence | 29-Jan | Jan | 120.2 | 124.0 |
| Unemployment Rate | 1-Feb | Jan | 4.0% | 3.9% |
| ISM Manufacturing | 1-Feb | Jan | 56.6 | 54.0 |
| FOMC Rate Dec. (Upper) | 30-Jan | Jan | 2.50% | 2.50% |

### ICE BofAML Fixed Income Index Returns

*For the period ended January 31, 2019*

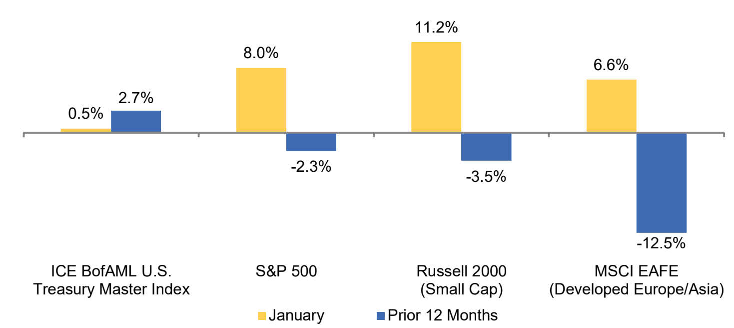



### U.S. Treasury Yield Curve

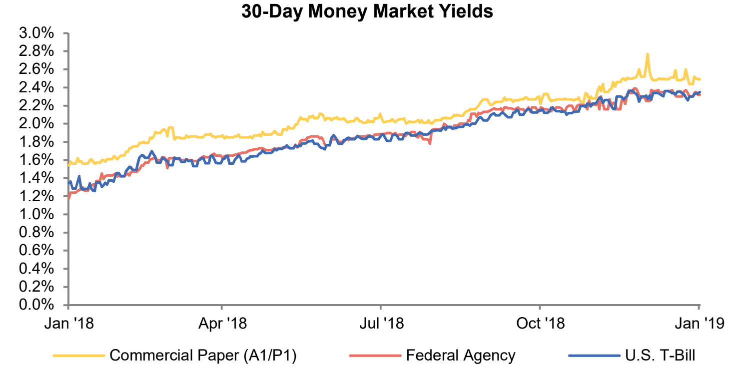



### Total Return of Major Indices

*For the period ended January 31, 2019*




### 30-Day Money Market Yields




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

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