Domestic Investment Grade Fixed Income Market Summary

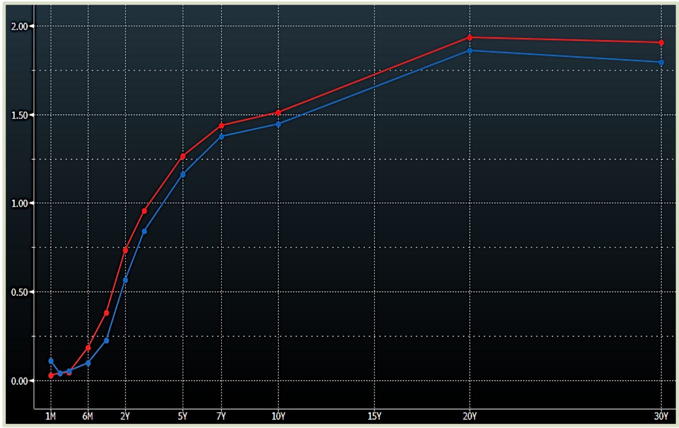
December 2021

Treasury Yield Curve Shifted Higher, Continued to Flatten

- Treasury yields rose, and the curve flattened in December with short-term rates rising on more aggressive Fed policy projections while longer maturity yields increased, but to a lesser extent, from easing COVID-19 concerns and rebounding inflation expectations.
- While the latest COVID-19 variant, omicron, has proved to be highly transmittable, relatively mild symptoms and a more modest increase in hospitalizations eased concerns that economy impacting restrictions would be required to slow the spread.
- The Federal Reserve (Fed) took an increasingly hawkish stance to combat inflation, doubling the monthly bond purchase reduction amount and signaling three rate hikes in 2022.
  - Bond purchases are now expected to conclude in early 2022
- Bureau of Labor Statistics (BLS) reported that 210,000 jobs were created in November, less than half of the projected amount and the fewest since December 2020.
  - Retail trade lost 20,000 jobs, while hospitality and leisure added only 23,000 workers compared to 278,000 the previous two months.
  - Unemployment rate fell to 4.2% (expected: 4.5%)
- Consumer Price Index (CPI) surged by 0.8% in November (expected: 0.7%), broadly impacted by energy, automobiles, food, and shelter.
  - CPI YoY: +6.8% (largest since June 1982)
  - Core CPI MoM: 0.5% (expected: 0.5%)

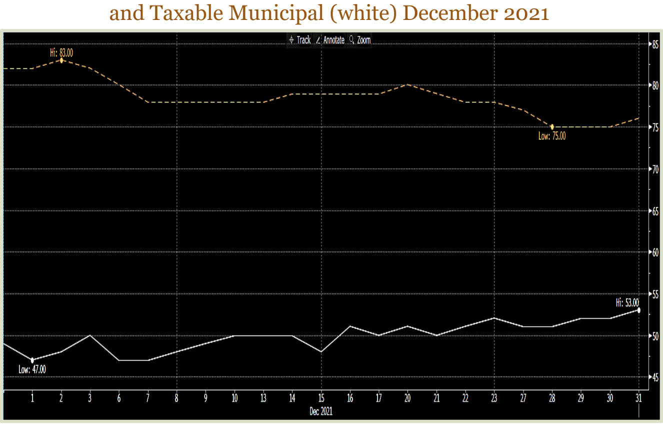
Maturity	11/30/21 Treasury	12/31/21 Treasury	Change
2-year	0.57%	0.73%	+0.16%
5-year	1.16%	1.26%	+0.10%
7-year	1.37%	1.44%	+0.07%
10-year	1.45%	1.51%	+0.06%
30-year	1.79%	1.90%	+0.11%

Treasury Yield Curve: 11/30/21 (blue) vs. 12/31/21 (red)



Segment	December Return	YTD Return
Bloomberg Barclays Intermediate Government Credit Index	-0.13%	-1.44%
ICE BofA 1-10 Year US Treasury Index	-0.30%	-1.65%
ICE BofA 1-10 Year US Inflation-Linked Treasury Index	0.34%	5.67%
ICE BofA 1-10 Year Corporate Index	0.04%	-0.85%
ICE BofA 1-10 Year Taxable Municipal Index	-0.47%	-0.38%

1-10 Year IG Credit Spreads: Corporate (orange) and Taxable Municipal (white) December 2021



Corporate Market Were Calm Despite Hawkish Fed; Strong TIPS Performance Continued

- Increased market volatility in November eased during the final month of the year despite central bank sentiment toward a more aggressive tightening timeline.
- Treasury Inflation Protected Securities (TIPS) once again outperformed nominal Treasuries as CPI prints remain elevated, and inflation expectations moved higher in December.
  - 10-year inflation expectations ended the year at 2.61%, after increasing 8 basis points in December, but slightly lower than the 2021 high of 2.77% reached in mid-November.
  - The inflation break-even rate curve remained inverted with investors projecting average annual inflation of 2.91% for the first five years followed by 2.31% yearly inflation for the subsequent five-year period.
  - The 1-10-year TIPS index outperformed the comparable maturity nominal Treasury index by 7.32% in 2021.
- After widening in November, investment grade corporate bond spreads tightened slightly in December. Meanwhile, taxable municipal risk premiums moved in opposite fashion, holding relatively steady in November but widening slightly in the final month of the year.
  - Generally, investment grade credit spreads are 10 basis points wider than the post-pandemic low reached in June but remain well below historical averages.
  - In the 1-10-year bucket, investment grade corporate and taxable municipal bonds outperformed the comparable Treasury index by 80 basis points and 127 basis points, respectively, in 2021.

Source: Bloomberg; Bureau of Economic Analysis; Federal Reserve; ICE BofA; Veritable, L.P.
All numbers are estimates. See Disclosures for index descriptions and additional information.

Municipal Yields Mostly Unchanged, Outperformed Treasuries Across the Curve

- Municipal yields were essentially unchanged in December with a 0-1 basis point move across the curve.
- Over the final month of the year, municipal rates were subdued despite price volatility in the Treasury market. Municipal supply and demand were in equilibrium, particularly over the final two weeks of the year as new issuance grinded to a halt while investors were in holiday mode.
    - The lack of volatility in the tax-exempt market as Treasury yields rose led to municipal outperformance in all maturities. The strongest relative performance was in shorter maturities, as 1-5-year municipal rates were unchanged versus a 10-16 basis point rise in comparable Treasury yields.
    - While Treasury weakness became more pronounced at month-end, municipal market trading activity slowed heading into the holidays with average daily volume falling to just \$4.7 billion, slightly more than half the 2021 average of \$8.8 billion according to MSRB data.
- The term premium between 2-year and 10-year AAA municipal rates remained at 79 basis points, generally in-line with the 2021 average and 22 basis points above the 2020 year-end spread.
- The 10-year AAA municipal yield was unchanged on a month-over-month basis at 1.03%, outperforming the 6-basis point rise of the 10-year Treasury rate with the yield ratio falling to 68%.

Maturity	11/30/21 Muni	12/31/21 Muni	Change	% of U.S. Govt 12/31/21
2-Year	0.24%	0.24%	0.00%	32.88%
5-Year	0.59%	0.59%	0.00%	46.83%
7-Year	0.86%	0.87%	0.01%	60.42%
10-Year	1.03%	1.03%	0.00%	68.21%
15-Year	1.14%	1.15%	0.01%	74.68%
20-Year	1.29%	1.30%	0.01%	67.01%
30-Year	1.48%	1.49%	0.01%	78.42%

- According to Refinitiv Lipper, weekly reporting municipal bond funds experienced inflows totaling \$3.9 billion in December, recording the 43rd consecutive week of positive net flows.
    - Municipal investors continued to show their affinity for risk, as weekly reporting high yield municipal bond mutual funds pulled in more than \$2.1 billion during the month.
    - Weekly municipal bond fund inflows averaged \$781 million in December, down from November's \$1.2 billion, but gained momentum over the final 2 weeks of the year.
    - With improving credit fundamentals and strong demand for tax shelters, municipal bond mutual funds saw record demand in 2021 with inflows totaling \$101.7 billion.

10-Year AAA Municipal-to-Treasury Yield Ratio: 2016-2021

- A stagnant tax-exempt market compared to Treasury price weakness pulled the 10-year relative valuation down to 68%, consistent with the average for 2021 but below the 89% historical average over the past five years.
- As relative valuations sank to near-record lows in shorter-term maturities, crossover opportunities remained an attractive option for traditional tax-exempt investors who prefer the safety of the front-end of the curve.
- The ongoing supportive technical environment appears poised to persist in the early months of 2022 as January and February are projected to generated negative net supply according to JP Morgan data before moving to equilibrium levels in March through May.
    - Note that the net supply projections assume 100% reinvestment of coupon income and principal payments, so a downshift in expected demand could lead to supply pressures and a corresponding rate rise.
    - West Virginia Senator Joe Manchin's lack of support for President Biden's signature \$1.75 trillion Build Back Better spending plan effectively shut down near-term speculation regarding tax reform, but investors continue to monitor developments out of Washington D.C.
- Is the tax-exempt market due for a trend reversal in terms of breaking the cycle of positive fund flows? Catalysts include less-than-anticipated tax hikes as well as a sharp rise in municipal yields (e.g., tax-exempts play catch-up to the increase in Treasury rates).
- With yields generally unchanged on a month-over-month basis, coupon income resulted in the ICE BofA 1-12 Year Municipal Securities Index producing a slightly positive +0.06% total return in December (+0.59% total return for 2021).

Source: Bloomberg; JP Morgan; Refinitiv; Veritable, L.P.
All numbers are estimates. See Disclosures for index descriptions and additional information.

Disclosures

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Index Descriptions *(Investors cannot invest directly in an index)*

Bloomberg Barclays Intermediate Government Credit Index is a total returns index of U.S. dollar denominated U.S. Treasuries, government-related securities, and investment grade U.S. corporate securities that have a remaining maturity of greater than or equal to 1 year and less than 10 years. Securities must have $250 million or more of outstanding face value and must be fixed rate and non-convertible.

ICE BofA 1-10 Year US Treasury Index is a subset of ICE BofA Treasury Index including all securities with a remaining term to final maturity greater than or equal to 1 year and less than 10 years.

ICE BofA 1-10 Year US Inflation-Linked Treasury Index is a subset of ICE BofA US Inflation-Linked Treasury Index including all securities with a remaining term to final maturity greater than or equal to 1 year and less than 10 years.

ICE BofA 1-10 Year Corporate Index measures the performance of investment grade corporate bonds of both U.S. and non-U.S. issuers that are U.S. dollar-denominated and publicly issued in the U.S. domestic market with a remaining term to final maturity greater than or equal to 1 year and less than 10 years.

ICE BofA 1-10 Year Taxable Municipal Index is designed to track the performance of U.S. dollar-denominated taxable municipal debt publicly issued by U.S. states and territories, and their political subdivisions, in the U.S. market with a remaining term to final maturity greater than or equal to 1 year and less than 10 years.

ICE BofA 1-12 Year Municipal Securities Ind*ex* is a subset of ICE BofA Municipal Securities Index including all securities with a remaining term to final maturity less than 12 years. The ICE BofA Municipal Securities Index is market capitalization weighted and tracks the performance of U.S. dollar denominated investment grade tax-exempt debt publicly issued by U.S. states and territories, and their political subdivisions, in the U.S. domestic market. Qualifying securities must have at least one-year remaining term to final maturity, at least 18 months to final maturity at the time of issuance, a fixed coupon schedule and an investment grade rating (based on an average of Moody’s, S&P and Fitch).

Consumer Price Index (CPI) is a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services. The yearly (or monthly) growth rates represent the inflation rate. The CPI is published by the US Bureau of Labor Statistics on a monthly basis.

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