Domestic Investment Grade Fixed Income Market Summary

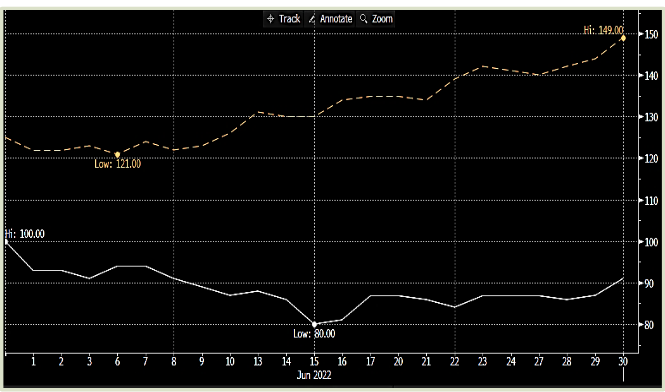
June 2022

Treasury Rates Increased, and the Yield Curve Flattened

- Treasury yields moved sharply higher around mid-month on Fed rate hike expectations following the Consumer Price Index (CPI) report. Rates trended lower thereafter, but 5-30 year Treasury yields were still 14-22 basis points (bps) higher for the month, while the 2-year rate rose 40 bps.
    - After steepening the previous two months, the Treasury curve bear flattened in June due to expectations for more aggressive Fed tightening.
- In its largest hike in 28 years, the Fed raised the funds rate 75 bps to a 1.50% - 1.75% range during its mid-June meeting and stated that the central bank is committed to bringing inflation back down to the 2% target.
    - At the beginning of June, market participants confidently priced in a 50 bp rate hike; however, expectations shifted sharply after CPI data released a few days prior to the Fed meeting showed greater-than-expected pricing pressures.
    - Updated Fed member projections indicate a median expectation for an additional 175 bps of rate hikes this year, essentially matching Fed fund futures pricing.
- Bureau of Labor Statistics released another solid labor market report with 390,000 jobs added (expected: 318,000) in May, the unemployment rate unchanged at 3.6%, and less-than-expected wage pressure (hourly earnings: +0.3% vs. +0.4% estimate).
- CPI for May was much stronger-than-expected, increasing 1.0% (expected: 0.7% / year-over-year: 8.6%) with broad price pressures led by energy, shelter, and food prices.

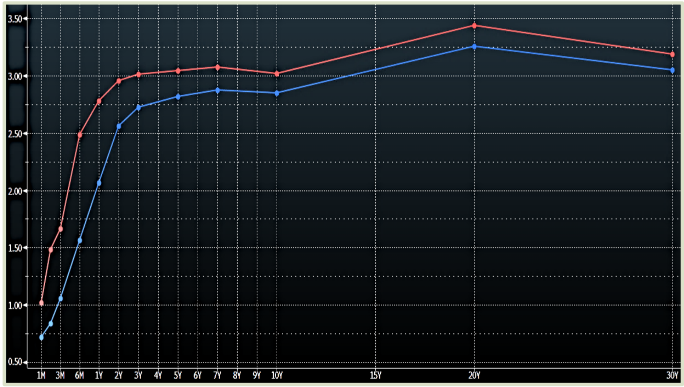
Segment	June Return	2022 Return
Bloomberg Barclays Intermediate Government Credit Index	-1.11%	-6.77%
ICE BofA 1-10 Year US Treasury Index	-0.64%	-5.55%
ICE BofA 1-10 Year US Inflation-Linked Treasury Index	-2.39%	-4.95%
ICE BofA 1-10 Year Corporate Index	-1.71%	-9.08%
ICE BofA 1-10 Year Taxable Municipal Index	-0.24%	-7.45%

1-10 Year IG Credit Spreads: Corporate (orange) and Taxable Municipal (white) June 2022



Maturity	5/31/22 Treasury	6/30/22 Treasury	Change
2-year	2.56%	2.96%	+0.40%
5-year	2.82%	3.04%	+0.22%
7-year	2.87%	3.07%	+0.20%
10-year	2.85%	3.02%	+0.17%
30-year	3.05%	3.19%	+0.14%

Treasury Yield Curve: 5/31/22 (blue) vs. 6/30/22 (red)



TIPS Performed Poorly Again; Credit Markets Were Mixed

- For the second consecutive month, Treasury Inflation Protected Securities (TIPS) underperformed nominal Treasury bonds as 1-10-year issues lagged by 185 bps on a duration-adjusted basis in June, the worst monthly relative performance since June 2013 excluding the March 2020 pandemic-induced sell-off.
    - The Fed's accelerated tightening timeline and their pledge to bring inflation down have pulled inflation expectations lower and outweighed the benefit of continued high CPI prints.
    - Despite initially rising, the 10-year TIPS inflation break-even rate fell 31 bps to 2.34% in June, while the 5-year break-even rate declined 34 bps to 2.60%.
- Investment grade corporate bonds meaningfully lagged Treasuries and taxable municipal bonds in June as 1-10 year issues posted their worst monthly performance relative to government bonds since January 2016, excluding March 2020 pandemic weakness.
    - A late May risk rally that caused corporate bond credit spreads to tighten lost momentum as risk premiums rose in June due to more aggressive Fed tightening coupled with increasing recession risks.
- After lagging badly last month, taxable municipal bonds performed well in June, outpacing Treasuries despite the general risk-off sentiment in financial markets.
    - 1-10 year taxable municipal bonds provided 49 bps of duration-adjusted excess return over government bonds during the month, offsetting weakness in May.

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.

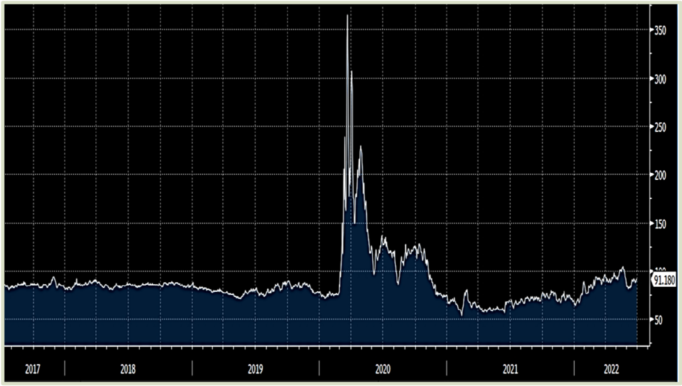
Returning Treasury Market Volatility Resulted in Municipal Performance Turning Negative in June

- Municipal yields climbed higher with Treasuries through mid-June, nearly reaching the multi-year highs observed in May before rallying to end the month in a flight to quality.
- Tax-exempt rates rose by 12-37 bps, and the municipal curve bear steepened.
- Demand from defensive investors via June 1st reinvestments kept front-end yields from gapping higher like their taxable counterparts, but longer-dated yields were more vulnerable to the Treasury volatility.
- During the mid-month peak in yields, 1-3 year tax-exempt rates were higher by roughly 15-20 bps while similar-maturity Treasury rates were higher by 80-96 bps.
- As Treasury market volatility subsided and taxable yields rallied into month-end, tax-exempt yields were pulled lower as well, though not to the same degree as demand remained relatively soft.
- From the mid-June yield peak through month-end, the 10-year AAA municipal yield declined 19 bps compared to a 46 bp decline in the corresponding Treasury yield.
- For the month, the 10-year AAA municipal yield rose 25 bps to 2.72%.
- The term premium between 2-year and 10-year AAA municipal rates rose 13 bps to 77 bps, above the 64 bp historical average over the past five years.

Maturity	5/31/22 Muni	6/30/22 Muni	Change	% of U.S. Govt 6/30/22
2-Year	1.83%	1.95%	0.12%	65.88%
5-Year	2.09%	2.22%	0.13%	73.03%
7-Year	2.31%	2.48%	0.17%	80.78%
10-Year	2.47%	2.72%	0.25%	90.07%
15-Year	2.59%	2.91%	0.32%	96.68%
20-Year	2.68%	3.04%	0.36%	88.37%
30-Year	2.81%	3.18%	0.37%	99.69%

- According to Refinitiv Lipper, weekly-reporting municipal bond fund outflows resumed in earnest in June following a brief reversal to close May as investors negatively reacted to Treasury market volatility.
  - Weekly-reporting municipal bond funds experienced outflows of $10.6 billion for June including a $5.6 billion weekly loss, the third largest on record.
  - Through the end of June, weekly-reporting municipal bond funds have experienced outflows in 22 of the last 24 weeks.
  - After declining to $1.5 billion in May, the average weekly outflow ticked higher to $2.7 billion in June.

10-Year AAA Municipal-to-Treasury Yield Ratio: 2017-2022



- The less-pronounced rally in tax-exempt debt to close the month compared to Treasuries resulted in the 10-year relative valuation rising to 90%, above the five-year average of 88%.
- Weary of Treasury volatility, investors continued to favor the short-end of the municipal curve.
  - The 2-year AAA municipal-to-Treasury yield ratio ended the month at an expensive 66% (5-year historical average: 88%).
- Municipal net supply turned sharply negative in June with redemptions ($53.0 billion) exceeding new issuance ($35.5 billion) by $17.5 billion.
  - June traditionally represents the start of summer reinvestment season, a period of technical strength for tax-exempt debt, wherein expected demand from principal and interest payments outstrips new supply.
  - JP Morgan estimates that net supply in July and August will dip to -$30 billion, a potential performance tailwind that could be strengthened if a period of rate stability leads to healthy demand. On the other hand, rate volatility could partially limit the amount of redemption proceeds that are recycled back into tax-exempts (net supply projections assume 100% reinvestment of coupon and principal payments), potentially creating more supply-demand dislocations than would otherwise occur under normal circumstances.
- With attractive nominal rates, longer-term relative valuations, and curve steepness, investors can take this opportunity to build back portfolio duration while mindful of the ongoing risks that could lead to more rate volatility including unexpected Fed actions, higher-than-expected inflation, as well as heavy fund outflows due to tepid retail demand.
- With Treasury market volatility surging once again in June and the outflow cycle continuing, the ICE BofA 1-12 Year Municipal Securities Index produced a -0.58% loss in June, its fifth loss in six months to start 2022.

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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