CHANDLER ASSET MANAGEMENT

BOND MARKET REVIEW

A Monthly Review of Fixed Income Markets

DECEMBER 2022

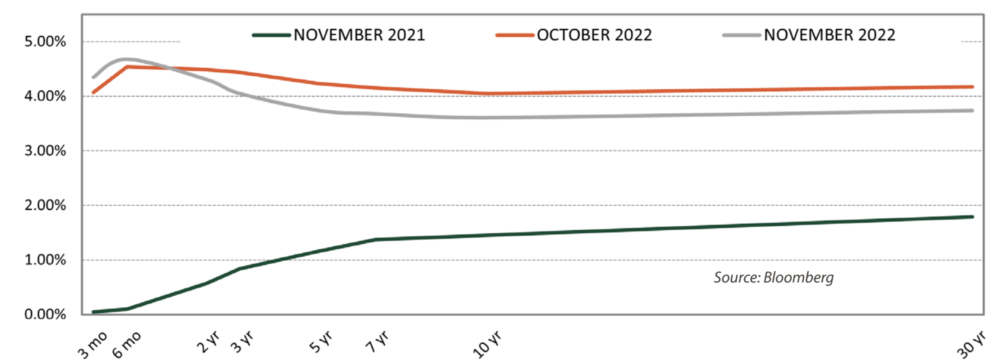
Market Summary

Market volatility has intensified as financial conditions tighten and global central banks pursue monetary policies to combat persistently high inflation and maintain financial market stability. Labor markets remain strong, although the pace of job growth is moderating. Inflation is weighing on consumer sentiment and negatively impacting savings rates. Corporate earnings have generally performed better than expected, but warnings are growing along with wider credit spreads this year. While evidence of slower economic conditions has begun to mount, we expect the Federal Reserve to continue to raise rates to battle inflation, albeit perhaps at a less aggressive pace. Over the near-term, we expect financial market volatility to remain intensified and conditions tighter with persistent inflation, geopolitical risk, and the Fed's hawkish monetary policy.

The Federal Open Market Committee (FOMC) raised the fed funds target rate by 50 basis points, as expected, at their December 14 meeting to a range of 4.25% - 4.50%, the highest level since 2007 and an increase of 425 basis points since the beginning of the year. This is the seventh consecutive rate increase in this cycle, and was a deceleration from the past four rate hikes of 75 basis points each. Federal Reserve Chairman Powell indicated that they expect to see a weakening of financial conditions as they continue to tighten monetary policy. We believe that the Fed will continue to hike in early 2023 but will look to pause if inflationary pressures continue to subside.

In November, yields declined significantly while the yield curve became more inverted. The 2-year Treasury yield declined 17 basis points to 4.31%, the 5-year Treasury yield fell 49 basis points to 3.74%, and the 10-year Treasury yield dropped 44 basis points to 3.61%. The inversion between the 2-year Treasury yield and 10-year Treasury yield widened to -71 basis points while the 3-month and 10-year treasuries widened to -74 basis points in November.

Treasury Yields Fell in November



Although yields on Treasury securities fell in November, they remain significantly higher from a year ago. The 2-year Treasury yield was 374 basis points higher, and the 10-Year Treasury yield was about 216 basis points higher, year-over-year. The inversion between the 2-year Treasury yield and 10-year Treasury yield widened to -71 basis points at November month-end versus -44 basis points at October month-end. The average historical spread (since 2003) is about +130 basis points. The inversion between 3-month and 10-year treasuries widened to -74 basis points in November from -2 basis points in October. The shape of the yield curve indicates that the probability of recession is increasing.

TREASURY YIELDS	Trend (▲/▼)	11/30/2022	10/31/2022	Change
3-Month	▲	4.35	4.07	0.28
2-Year	▼	4.31	4.49	-0.17
3-Year	▼	4.05	4.44	-0.39
5-Year	▼	3.74	4.23	-0.49
7-Year	▼	3.68	4.15	-0.46
10-Year	▼	3.61	4.05	-0.44
30-Year	▼	3.74	4.17	-0.43

Source: Bloomberg

Market Data

World Stock Market Indices
data as of 11/30/2022

	Change (10/31/2022)	%CHG
S&P 500		
4,080.11	208.13	5.38%
NASDAQ		
11,468.00	479.85	4.37%
DOW JONES		
34,589.77	1,856.82	5.67%
FTSE (UK)		
7,573.05	478.52	6.74%
DAX (Germany)		
14,397.04	1,143.30	8.63%
Hang Seng (Hong Kong)		
18,597.23	3,910.21	26.62%
Nikkei (Japan)		
27,968.99	381.53	1.38%

Source: Bloomberg. Please see descriptions of indices on Page 2.

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Since 1988, Chandler Asset Management has specialized in providing fixed income investment solutions to risk-averse public agencies and institutions. Chandler's mission is to provide fully customizable client-centered portfolio management that preserves principal, mitigates risk, and generates income in our clients' portfolios.

Credit Spreads tightened in November

CREDIT SPREADS	Spread to Treasuries (%)	One Month Ago (%)	Change
3-month top rated commercial paper	0.22	0.37	(0.15)
2-year A corporate note	0.37	0.56	(0.19)
5-year A corporate note	0.92	0.98	(0.06)
5-year Agency note	0.29	0.20	0.08

Source: Bloomberg

Data as of 11/30/2022

Inflation Remains Above the Federal Reserve's Target but has Receded from its Recent Highs

ECONOMIC INDICATOR	Current Release	Prior Release	One Year Ago
Trade Balance	(78.20) $Bln OCT 22	(74.13) $Bln SEP 22	(68.16) $Bln OCT 21
Gross Domestic Product	(2.90%) SEP 22	(0.60%) JUN 22	2.70% SEP 21
Unemployment Rate	3.70% NOV 22	3.70% OCT 22	4.20% NOV 21
Prime Rate	7.00% NOV 22	6.25% OCT 22	3.25% NOV 21
Refinitiv/CoreCommodity CRB Index	279.76 NOV 22	274.13 OCT 22	219.19 NOV 21
Oil (West Texas Int.)	$80.55 NOV 22	$86.53 OCT 22	$66.18 NOV 21
Consumer Price Index (y/o/y)	7.10% NOV 22	7.70% OCT 22	6.80% NOV 21
Producer Price Index (y/o/y)	10.60% NOV 22	11.20% OCT 22	13.30% NOV 21
Euro/Dollar	1.04 NOV 22	0.99 OCT 22	1.13 NOV 21

Economic Roundup

Consumer Prices

The Consumer Price Index (CPI) increased less than expected in November, up 7.1% year-over-year versus consensus expectations for 7.3%, and down from 7.7% from the October release. The Core CPI, which excludes volatile food and energy components, rose 6.0% year-over-year, down from a 6.3% increase in October. Food and shelter costs continued to rise but were offset by broad price declines in energy along with prices of used cars and trucks. The Personal Consumption Expenditures (PCE) index rose 6.0% year-over-year in October, versus an upwardly revised 6.3% year-over-year in September. Core PCE increased 5.0% year-over-year in October versus 5.2% year-over-year in September. Although the pace of inflation is below its recent highs, levels remain well above the Fed's target of around 2%, which is likely to keep the Federal Reserve on the path of tightening monetary policy. If inflation trends continue to decline consistently, the Fed may tighten at a less aggressive pace.

Retail Sales

Advance retail sales fell 0.6% in November, mostly due to declines in auto sales, after surging 1.3% in October. This equates to +6.5% year-over-year, continuing the trend of slower growth as headwinds from higher interest rates combined with elevated prices took a toll on consumer spending. The Conference Board's Consumer Confidence Index dropped 2 points to 100.2 in November as views of current conditions, the future outlook for the economy, and income expectations all declined. The US savings rate dipped to 2.3% in October, the lowest level since 2005, as consumers continue to be squeezed by higher prices and financing rates. Demand for goods and services going into the holiday season was strong as shoppers took advantage of Black Friday and Cyber Monday discounts from retailers looking to move excess inventory.

Labor Market

The U.S. economy added 263,000 jobs in November, surpassing market expectations of 200,000, while gains were revised downward by 23,000 for the prior two months. Trends in employment remain strong, with the three-month moving average payrolls at 272,000 and the six-month moving average at 323,000. Gains were broad-based, led by leisure and hospitality followed by healthcare and government. The unemployment rate was unchanged at 3.7%, and the labor participation rate dipped to 62.1% in November from 62.2% in October. The U-6 underemployment rate, which includes those who are marginally attached to the labor force and employed part time for economic reasons eased to 6.7% from 6.8% last month. Average hourly earnings rose 5.1% year-over-year in November compared to 4.9% year-over-year in October. While the pace of job growth is moderating, the report demonstrates a strong demand for labor and provides the Fed further support for continued rate hikes.

Housing Starts

Total housing starts declined 4.2% to an annual rate of 1,425,000 in October, after an upward revision to 1,488,000 units in September. Single-family home starts fell 6.1%, whereas multi-family starts declined by a more modest 1.2% month-over-month. On a year-over-year basis, total housing starts decreased 8.8% reflecting a shift from single-family units to more affordable multi-family units as homebuyers struggle with a combination of elevated prices and higher mortgage rates. Mortgage rates for a 30-year fixed-rate loan remain at a decade high, though rates receded to 6.39% by the end of November. According to the Case-Shiller 20-City Home Price Index, the year-over-year increase continued its declining rate of gain to +10.4% in September from +13.1% in August, clearly displaying the impact of higher mortgage rates which have reduced demand for homebuying as affordability has declined.

World Stock Market Index Descriptions

S&P 500– The S&P 500 is a market value-weighted index of 500 large-capitalization stocks. The 500 companies included in the index capture approximately 80% of available US market capitalization. NASDAQ–The NASDAQ Composite Index is the market capitalization-weighted index of over 3.300 common stocks listed on the NASDAQ stock exchange. Dow Jones–The Dow Jones Industrial Average is an index that tracks 30 large, publicly-owned companies trading on the New York Stock Exchange and the NASDAQ. The Financial Times Stock Exchange Group (FTSE)– The FTSE is a share index of the 100 companies listed on the London Stock Exchange with the highest market capitalization. DAX–The Deutscher Aktienindex (DAX) is a blue chip stock market index consisting of the 30 major German companies trading on the Frankfurt Stock Exchange. Hang Seng–The Hang Seng Index is a freefloat-adjusted market-capitalization-weighted stock market index in Hong Kong. It is used to record and monitor daily changes of the largest companies of the Hong Kong stock market and is the main indicator of overall market performance in Hong Kong. Nikkei–Japan's Nikkei 225 Stock Average is a price-weighted index composed of Japan's top 225 blue-chip companies traded on the Tokyo Stock Exchange.