Monthly Market Review

Fixed Income | January 2022

Information provided by NLAF's Investment Advisor PFM Asset Management LLC

NEBRASKA LIQUID ASSET FUND

"The Fed's New Year's resolution? A monetary policy diet."

Economic Highlights

► The surge of COVID-19 cases due to the Omicron variant reached an all-time high. Some hospitals are once again running near full capacity, although the death rate held steady at around 1,300 per day in the U.S. Meanwhile, businesses are once again dealing with staffing issues, higher costs and reduced customer traffic.

► Inflation remained in the spotlight. The consumer price index rose 6.8% year-over-year (YOY) in December, a nearly 40-year high. Stripping out food and surging energy prices, the Core CPI rose 4.9% over the same period. Other measures of inflation also ran hot – the PPI rose 9.6% YOY in December, export prices were up 18.2% through November, and the Core PCE was up 4.7% YOY compared to the Federal Reserve's (Fed) 2% average target.

► The U.S. economy added only 199,000 new jobs in December, well below forecast, but the unemployment rate fell to a cycle low of 3.9%. Since 1970, the rate has only been lower once in 2000 and during the 22 months preceding the pandemic. For the year, the economy added 6.4 million jobs. In other signs of strength, average hourly earnings rose 4.7% YOY, job openings remained elevated at 10.6 million, and the quits rate reached a record 4.5 million workers. A remarkable 3% of the U.S. workforce left their job in November.

► In light of the strengthening labor market and elevated inflation pressures, the Fed decided to speed up tapering, implying that their bond purchases would end in March, several months sooner than previously expected. In its updated economic projections, Federal Open Market Committee participants revised their forecast for the unemployment rate lower and inflation higher for the coming year. The market is keenly focused on the timing and pace of potential Fed rate hikes. The median projection for the appropriate level of the federal funds rate now shows three rate hikes occurring during 2022.

► According to Mastercard, retail sales during the holiday shopping season rose 8.5% compared to last year, with online sales surging 11%. Due to supply chain worries, consumers shopped earlier than usual. Apparel and jewelry were the strongest categories.

► Looking ahead, economists expect U.S. real gross domestic product to register a strong 6% for Q4 2021 and an above-trend rate of 3.9% for 2022 before falling back to 2.5% in 2023. Inflation is expected to remain elevated in 2022, with gradual improvement each quarter.

Bond Markets

► U.S. Treasury yields moved higher in December, with 1-5 year yields rising by about 6-16 basis points (0.06%-0.16%). This was the market's reaction to the risk of Fed rate hikes being pulled forward in 2022. Yields moved higher at an even faster pace in the first week of the new year as it became clear the Fed may reduce its balance sheet even more aggressively than their announced tapering plan would indicate.

► As a result of higher yields, Treasury returns were negative for the month. For example, in December the ICE BofA 1-, 5- and 10-year U.S. Treasury indices returned -0.11%, -0.39% and -0.42%, respectively.

Equity Markets

► Despite rising rates and surging COVID-19 cases, equity markets had a strong December. The S&P 500 returned 4.5%, capping a year in which the index returned 28.7%. The Dow Jones Industrial Average charged ahead 5.5% for the month and 21% for the year, while the tech-heavy NASDAQ index advanced just 0.7% in December, but was up 22.2% for all of 2021.

► Most international equity markets also had strong years in local currency terms, but the appreciating U.S. dollar offset 6-10% of those returns. The MSCI ACWI ex-U.S. index rose 4.1% in December and 7.8% for the year. The MSCI Emerging Market Index fell 2.3% on the year.

PFM Strategy Recap

► As the Fed attempts to engineer a pivot from easy policy to supply a pandemic recovery to tighter policy that curbs inflation, markets appear poised for increased volatility. We expect Treasury yields to continue to move higher in lock-step with expectations around Fed rate hikes. However, most of 2022's expected rate increases are arguably already built into today's yield curve. We plan to maintain a modestly defensive duration bias relative to benchmarks.

► Most non-government spread sectors improved, with yield spreads tightening off recent near year-to-date wide levels. As a result, most investment-grade (IG) sectors generated positive excess returns for the month, bucking the broader trend of underperformance from Q4.

► IG corporate spreads ratcheted in to close the year after bouncing wider in October and November. After the late-year widening, selective additions to the sector helped performance to close the year.

► AAA-rated asset-backed securities (ABS) have also become slightly more attractive, however light issuance limited opportunities in December. We expect the mortgage-backed securities (MBS) sector to face continued headwinds in 2022 and will likely hold lower allocations due to principal attrition.

► In short-term money markets, wider spreads and a steeper yield curve offer value in 6-12 month maturities. This is a welcome development after nearly two years of near-zero short-term rates.

U.S. Treasury Yields

Duration	Dec 31, 2020	Nov 30, 2021	Dec 31, 2021	Monthly Change
3-Month	0.07%	0.05%	0.04%	-0.01%
6-Month	0.09%	0.10%	0.19%	0.09%
2-Year	0.12%	0.57%	0.73%	0.16%
5-Year	0.36%	1.16%	1.26%	0.10%
10-Year	0.92%	1.45%	1.51%	0.06%
30-Year	1.65%	1.79%	1.90%	0.11%

Yields by Sector and Maturity

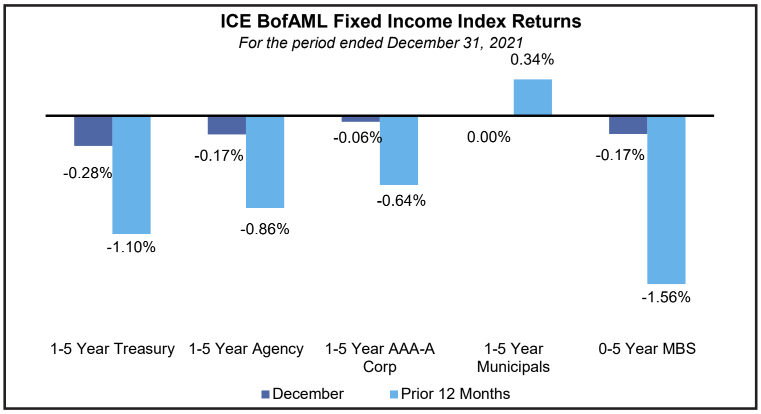
Maturity	U.S. Treasury	Federal Agency	Corporates-A Industrials	AAA Municipals
3-Month	0.04%	0.04%	0.44%	--
6-Month	0.19%	0.09%	0.48%	--
2-Year	0.73%	0.77%	0.86%	0.20%
5-Year	1.26%	1.28%	1.59%	0.56%
10-Year	1.51%	1.67%	2.23%	1.26%
30-Year	1.90%	2.16%	2.87%	1.76%

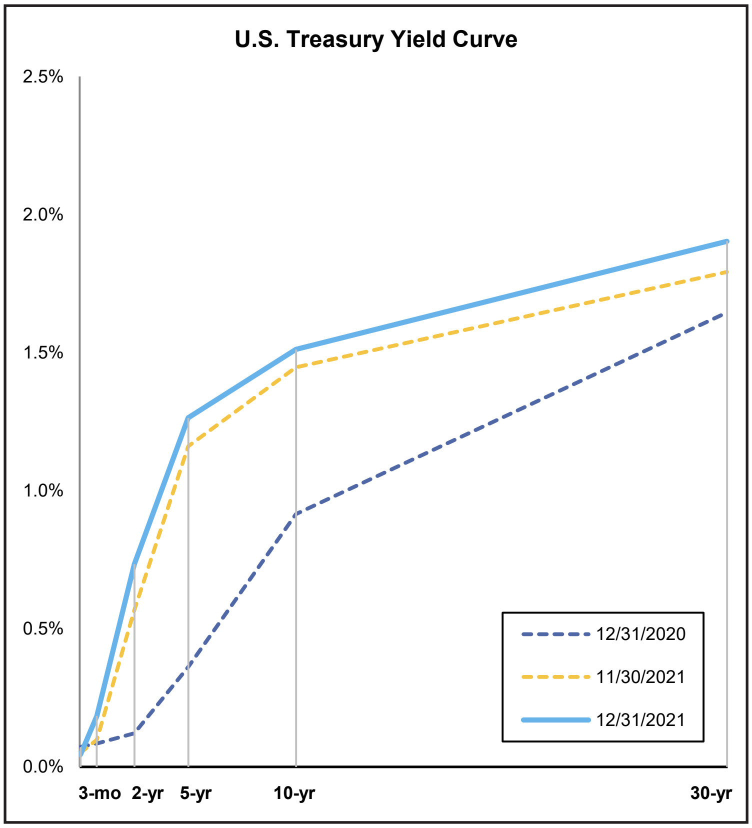
Spot Prices and Benchmark Rates

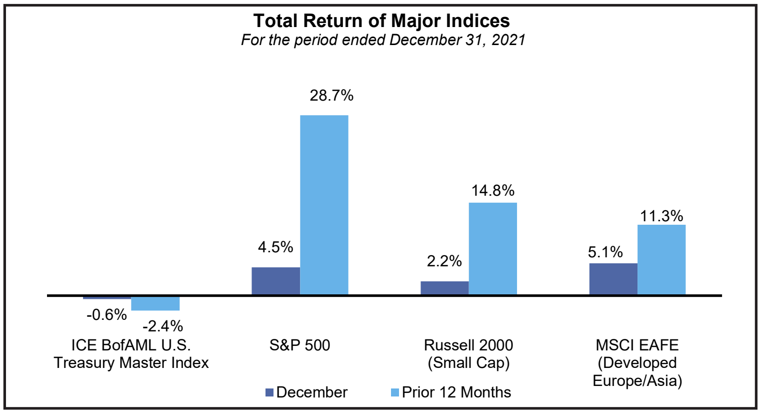
Index	Dec 31, 2020	Nov 30, 2021	Dec 31, 2021	Monthly Change
1-Month LIBOR	0.14%	0.09%	0.10%	0.01%
3-Month LIBOR	0.24%	0.17%	0.21%	0.04%
Effective Fed Funds Rate	0.09%	0.07%	0.07%	0.00%
Fed Funds Target Rate	0.25%	0.25%	0.25%	0.00%
Gold ($/oz)	$1,895	$1,774	$1,829	$55
Crude Oil ($/Barrel)	$48.52	$66.18	$75.21	$9.03
U.S. Dollars per Euro	$1.22	$1.13	$1.14	$0.01

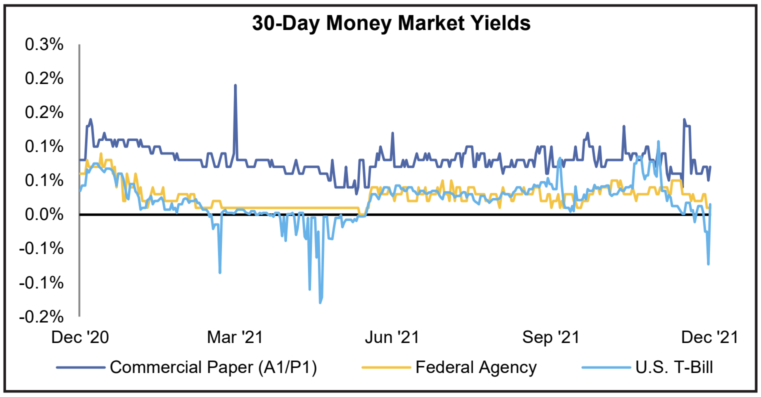
Key Economic Indicators

Indicator	Release Date	Period	Actual	Survey (Median)
Retail Sales Advance MoM	15-Dec	Nov	0.3%	0.8%
GDP Annualized QoQ	22-Dec	3Q T	2.3%	2.1%
PCE Core Deflator YoY	23-Dec	Nov	4.7%	4.5%
Consumer Confidence	22-Dec	Dec	115.8	111.0
ISM Manufacturing	4-Jan	Dec	58.7	60.0
Change in Nonfarm Payrolls	7-Jan	Dec	199k	450k
Unemployment Rate	7-Jan	Dec	3.9%	4.1%









Source: Bloomberg. Data as of December 31, 2021, unless otherwise noted.

The views expressed constitute the perspective of PFM Asset Management LLC at the time of distribution and are subject to change. The content is based on sources generally believed to be reliable and available to the public; however, PFMAM cannot guarantee its accuracy, completeness or suitability. This material is for general information purposes only and is not intended to provide specific advice or a specific recommendation.

PFM Asset Management LLC ("PFMAM") is an investment adviser registered with the U.S. Securities and Exchange Commission and a subsidiary of U.S. Bancorp Asset Management, Inc. ("USBAM"). USBAM is a subsidiary of U.S. Bank National Association ("U.S. Bank"). U.S. Bank is a separate entity and subsidiary of U.S. Bancorp. U.S. Bank is not responsible for and does not guarantee the products, services or performance of PFMAM.

NOT FDIC INSURED : NO BANK GUARANTEE : MAY LOSE VALUE