1Q 2021

Investment Highlights

Oregon Local Government Intermediate Fund

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	Portfolio	Index**
1Q21 Performance*	-0.94%	-0.57%

As of 31 Mar 21
**Performance is gross of fees*
*** Bloomberg Barclays 1-5 Year US Government/Credit Bond Index*

Performance Review

During the first quarter of 2021 the portfolio underperformed its benchmark, the Bloomberg Barclays 1-5 Year US Government/Credit Bond Index, by 36 basis points (bps) on a gross basis.

Optimism over the global outlook rose throughout the quarter against a backdrop of slowing COVID-19 case counts, increased vaccination efforts and the anticipation of the eventual reopening of economies. The US experienced significant declines in new Covid cases from the peak December and January numbers, and restrictions were eased or lifted in certain regions. The greatest contributor to performance during the quarter was TIPS exposure, contributing 2 bps as breakeven inflation rates rose. Long US duration positioning detracted to performance as yields rose. Yield-curve positioning was also a detractor over the quarter as the curve steepened.

Investment Outlook

The US economy behaved much as we expected in 1Q21, and contrasts in the statuses of various industries have sharpened. That is, output levels in manufacturing and construction have largely caught up with aggregate demand in those sectors, so we think it is likely that growth in these sectors will actually slow in the months ahead. There have been some signs of such slowing recently, as factory orders slipped a bit in February, and, more importantly, new-home sales and housing starts appear to have gone flat in recent months. Consensus opinion has blamed these slowdowns on a winter blizzard that shut down Texas power supplies for a few days in February. Those power shutdowns could indeed have suppressed homebuilding and manufacturing activity, but we think there is more to the recent slowdowns there than merely weather, especially as new-home sales have been flat to down for the last six months. Then again, March payroll data showed strong job growth in both these sectors. Prior to March, while output had recovered nicely, staffing levels were still markedly depressed from pre-Covid levels. So, it will be interesting to see whether the March job gains signal further output growth in manufacturing and homebuilding or merely a catching up of staffing levels with output levels already attained.

Meanwhile, for the service sectors where essentially all the remaining "slack" in the US economy resides, any reopening has so far been only halting, and growth there has been accordingly sluggish. Restaurants had reopened to something like 25% indoor capacity in California, and entertainment venues are only now reaching these levels. The new administration has not yet announced any timetables for a more complete reopening of these sectors.

Absent a complete full-capacity reopening of restaurants, hotels, airports, theaters, etc. and with manufacturing and homebuilding already having fully recovered, we are inclined to think that realized US growth will fall short of the expectations that seem built into market pricing, given how sharply term yields have risen in recent months. Finally, as might be inferred from the previous remarks, we are skeptical that there is any substantial economic stimulus in the bills that have been passed by Washington recently.

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