Investment Highlights

Oregon Local Government Intermediate Fund

WESTERN ASSET

Oregon Local Government Intermediate Fund

	Portfolio (gross)	Portfolio (net)	Index*
4Q22 Performance	1.47%	1.45%	1.20%

As of 31 Dec 22.
**Bloomberg 1-5 Year US Government/Credit Bond Index*
Past investment results are not indicative of future investment results. *Gross-of-fees returns are presented before management fees, but after all trading expenses. Net-of-Fees performance returns are an estimate of time-weighted rate of return. The effective fee, based on a fee schedule, is deducted from the monthly gross return.*

Performance Review

During the fourth quarter of 2022 the portfolio outperformed its benchmark, the Bloomberg 1-5 Year US Government/Credit Bond Index, by 27 basis points (bps) on a gross basis.

During the fourth quarter of 2022, risk assets and bond yields traded in a wide range, but ultimately risk assets rose and bond yields were mostly higher as the Federal Reserve (Fed) continued to hike rates. Risk sentiment was boosted by lower-than-expected inflation prints as well as prospects for a slower pace of rate hikes and an eventual rate pause in 2023. Oil prices fluctuated as global growth expectations adjusted while credit spreads tightened and the S&P 500 rose.

Investment Outlook

Western Asset believes the effects of Federal Reserve (Fed) rate hikes to date are accumulating, albeit remarkably slowly and diffusely. Inflation is moderating across the economy, most clearly in goods prices, but also in services prices and in housing costs (home prices and rents); the latter effects, however, have yet to show up in the Consumer Price Index (CPI) for technical reasons. We expect this moderation to continue. We think month-to-month inflation will be within the Fed's target ranges before the middle of 2023. While year-over-year (YoY) measures won't show this improvement as quickly, the "perception lags" arising from looking at YoY measures are well understood by any trained economist, and we believe the Fed will be astute enough to make this deduction as well.

The US construction industry has been in recession for some time, even while construction companies continue to replenish staffing. Lately, we are seeing similar developments in manufacturing, where both production and production hours worked have begun to decline, even as factory worker counts continue to recover. Understaffing is most acute in service industries, but even there job growth has slowed substantially except in those industries that were hardest hit by Covid restrictions (and where job counts are hundreds of thousands below pre-Covid levels). Even as service jobs continue to rebound, service-related workweeks are being cut enough that total production hours worked are decelerating or even declining.

Western Asset takes these trends as clear evidence that either Fed rate hikes are taking their toll or that economic growth is slowing on its own, even while residual understaffing in the wake of Covid restrictions has meant further job growth. With these conditions, and given the progress made on inflation, it makes little sense and is likely counterproductive for the Fed to continue to tighten aggressively, and we think a change in its policy slant will be coming soon.

For more information on Western Asset, visit westernasset.com.