April 2019

OREGON STATE TREASURY

Inside the Vault

Local Government Edition

Bond-Related Educational Resources

On April 9, the Municipal Securities Rulemaking Board (MSRB) added to its valuable informational resources by introducing a new podcast series:

The MSRB today announced the launch of the MSRB Podcast, a new series about the regulatory and market structure of the largest source of infrastructure financing in the United States.

The MSRB Podcast, available on MSRB.org and most podcast platforms, consists of a 12- to 30-minute immersion into municipal securities regulation, market data and emerging market topics. Each episode deconstructs—for municipal bond market practitioners and others—a topic, drawing on the expertise of featured subject matter experts.

"Our new podcast program provides easy and convenient access to municipal market information that can inform practitioners and others," said Lynnette Kelly, MSRB President and CEO. "Distilling the complexities and unique characteristics of the municipal market for the public is fundamental to the MSRB's mission."

The first podcast episode, released today, examines municipal market yield curves and indices, including their value to market participants and the attributes that make municipal yield curves distinct from other fixed-income benchmarks. Listen to the MSRB Podcast premiere, A Conversation About Yield Curves.

The MSRB Podcast will periodically release a new episode. Listeners can subscribe and hear new episodes on podcast platforms including Apple Podcasts, Google Podcasts and Spotify, and on the MSRB's website.

In addition to the podcasts, the MSRB web site provides multiple municipal debt–related tools, including an array of existing educational resources such as the MSRB Education Center, On-Demand Webinars, information regarding SEC Rule 15c2-12 amendments (including a transcript of the 2/27/19 webinar and EMMA submission guide), and MSRB MuniPro.

Interest Rates

Average Annualized Yield	
March	2.75%
Interest Rates	
March 1–31	2.75%

Credit Market Review

Economic confusion from the end of last year carried into 2019, as the daily growth outlook becomes dependent on each morning's data release. As Federal Reserve policy risks abated, equity markets began a rally on Christmas Eve to send the S&P 500 a few points under the September 2018 high—a 22% run that at face value is a clear sign that all economic worry is in the rearview mirror. However, the bond market is telling a different story. In late March, yields on the 10-year Treasury fell to 2.368%, a near-term low, breaking under the 3-month Treasury bill yield for the first time since 2007. We call this dynamic an "inverted" yield curve. The Fed identified a "3s & 10s inversion" as the single most accurate predictor of a growth recession and put odds on a slowdown in the next 12 months at 30%.

While bond and equity traders are divided about the direction of the economy, there is unity about who put the collar on *animal spirits* in the fourth quarter of 2018. Fed Chairman Jerome Powell has gone full dove after last year's quantitative tightening, when the Fed delivered four rate hikes and shrunk its balance sheet by $370 billion. The Fed's dot plot, a consensus view by the voting members of the Federal Open Market Committee, pushed back the hiking cycle by calling for no more rate hikes in 2019. As of print, the market is pricing a 20% chance of a lower federal funds rate by June, and President Trump is calling for a return of quantitative easing.

A remedy to U.S. market anxiety is a quick look offshore, where the economic picture is more mixed. Brexit negotiations continue on with little resolution in sight and Eurozone growth and inflation continues to underwhelm. Eurozone GDP posted two consecutive quarters of 1.1% growth and the European Central Bank is on track to usher in a new wave of stimulus sometime this year. The market remains put-off and yields are now negative on 10-year German bunds.

From one set of tariffs to another, the U.S.-China trade negotiations nudge

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Save the Date: LGIP Investor Meeting

As part of our goal to better serve our government customers—and by extension, the public—Treasury hosted the first-ever Local Government Investment Pool investor meeting last summer.

The daylong session included a conversation with State Treasurer Tobias Read, updates from our investment staff including Chief Investment Officer John Skjervem, and an overview of the economy by State Economist Mark McMullen.

The level of interest was so strong—more than 50 finance officers attended from across the state and every spot was filled—that we have decided to host a meeting again, this year.

This year's event will be on Thursday, August 29. Mark your calendar!

To make sure the event is valuable for you and your organization, we are asking for your input on potential agenda items and the location for this year's event. What would you like to learn more about when it comes to the Local Government Investment Pool and the Oregon Short Term Fund? Is there a session from last year's event that you'd like us to repeat, or something new you'd like us to cover? Our online survey will take just a few minutes.

If you have additional thoughts, contact Kristel on our planning team at kristel.flores@ost.state.or.us. We appreciate your feedback and we look forward to seeing you in August.

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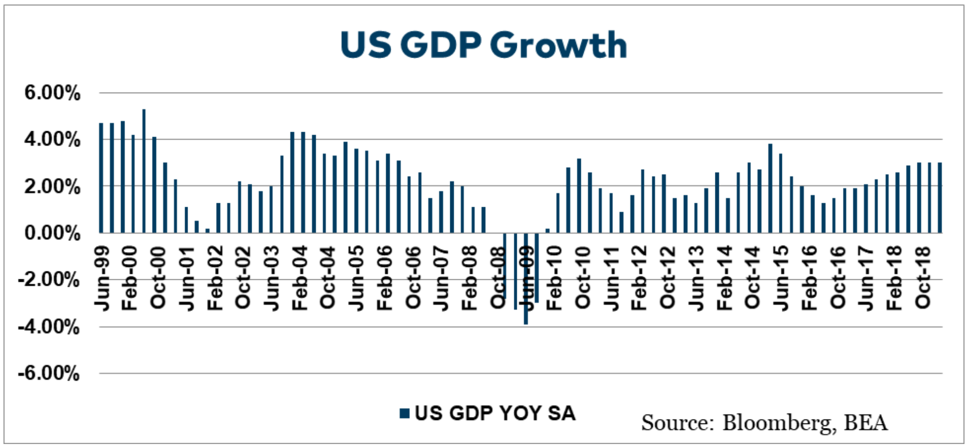
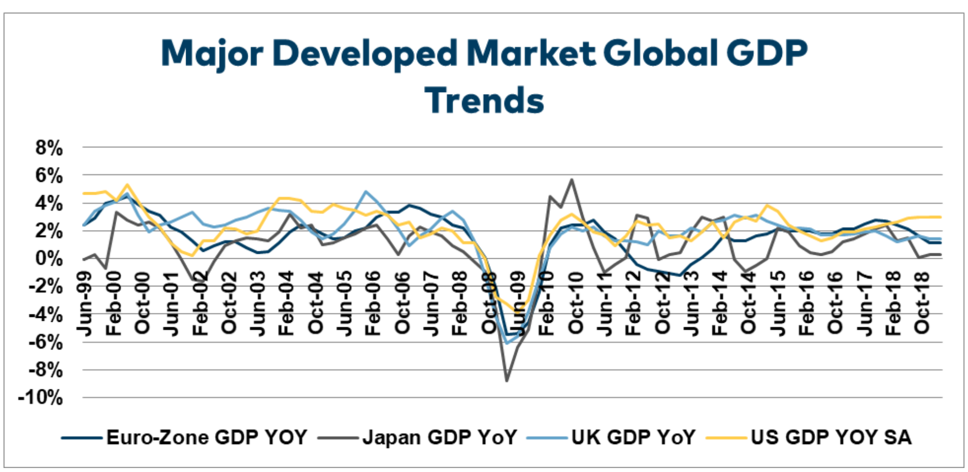
ever closer to a "deal." Both sides need a political win to offset the drag on the economy. Pressure today is on China, where the growth is slowing (even with some recent lift in production numbers). Beijing is planning a $250 billion stimulus package, but questions abound on how effective this program will be. The 2015 stimulus leaned heavily on the banking system, which today may be stretched too thin to push growth through credit stimulus. Current estimates of China's total debt levels are near 300% of GDP.

Unremarkably, the bond market signaling recession and new tariffs at the U.S. border caused the International Monetary Fund to drop forecasts on global trade and growth. There will be day-by-day volatility in the markets until we get enough economic data points to build a better thesis, but for now the market is fully bifurcated between equity bulls and bond market bears and time will soon prove that one side is likely wrong.



The recently released fourth quarter GDP print met expectations and also led to a series of downward revisions to growth forecasts. However, since March, the Atlanta Fed's GDPNow (a contemporaneous estimate of growth) was revised aggressively from 0.2% to 2.3%. While this model is notoriously volatile, the upward drift is reflective of positive data releases on wages, employment, and a trade surplus from energy exports. The rise in oil prices back over $60 per barrel might help U.S. export revenues but raises the specter of inflation.



The buoyancy of U.S. economic growth against a backdrop of recession abroad raises a number of sustainability questions about the expansion. Japan and Germany are seeing a sharp decrease in

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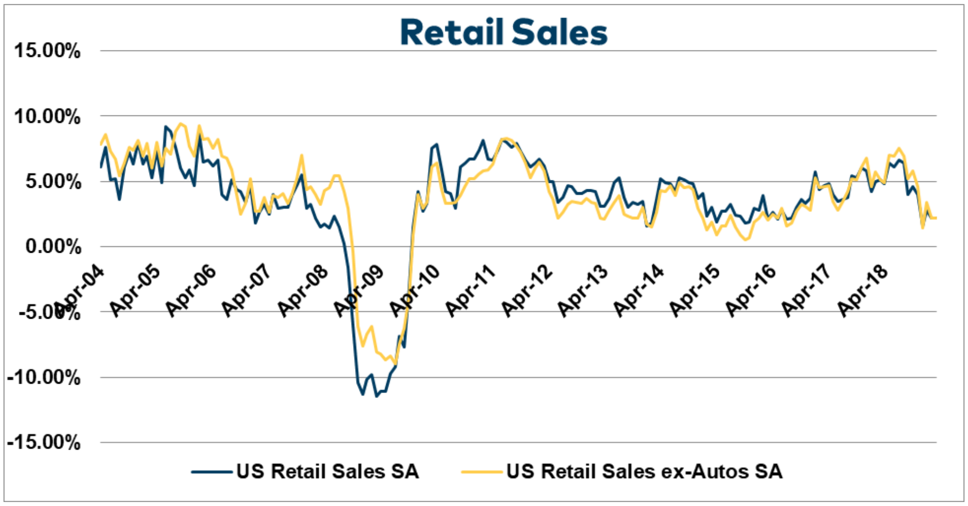
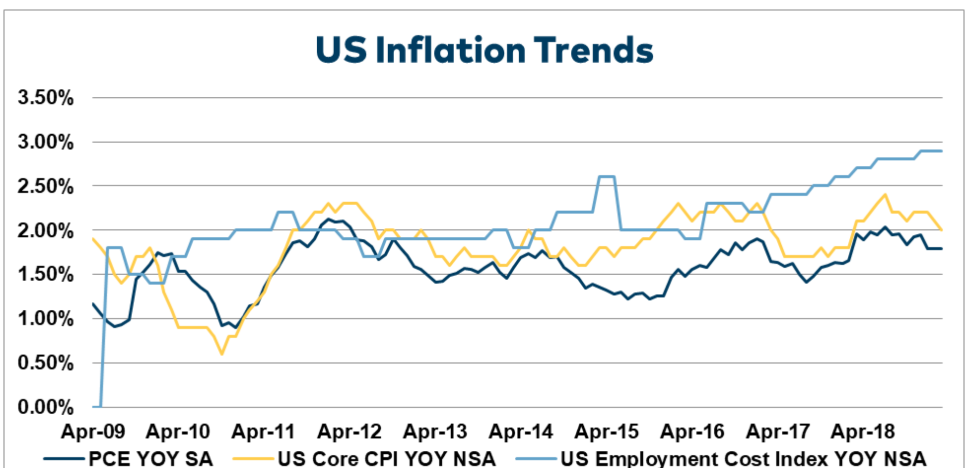
growth related to tech and industrial exports thanks to a downtrend in the global capex cycle. Much of the recent growth spurt in the U.S. economy is attributed to a combination of pro-cyclical fiscal deficit spending, tax breaks, and a push to get U.S. corporates to bring offshore money back into the country. Unfortunately, whether capital repatriation is propping up U.S. growth is more a political debate than a sound data point. Generally, there is a great deal of lag between investment and a return to economic growth, especially in high-tech service companies where research and development can take decades.



A leading cause for the economic pessimism at the end of last year was the sharp drop in retail sales. The decline continued into 2019 albeit with some recent upward revisions to the series that make things appear less dire. While the numbers show a weakening U.S. consumer, which accounts for nearly 70% of the domestic economy, the data is clouded by both the government shutdown at the start of the year and a potential negative wealth effect from the fourth quarter drop in equities. Like much of the general market outlook since October, the best interpretation is "conditionally pessimistic" while waiting for more data points to better assess where the economy is headed.



Source: Bloomberg, Bureau of Economic Analysis, Bureau of Labor

For the past 18 months, inflation (CPI-yellow & PCE-dark blue) remained muted while employment costs (light blue) continued to accelerate. The wage-inflation gap creates major difficulties for both the market and policy makers. Increasingly, both sides of the issues are bracing for lower inflation and slower wage growth.

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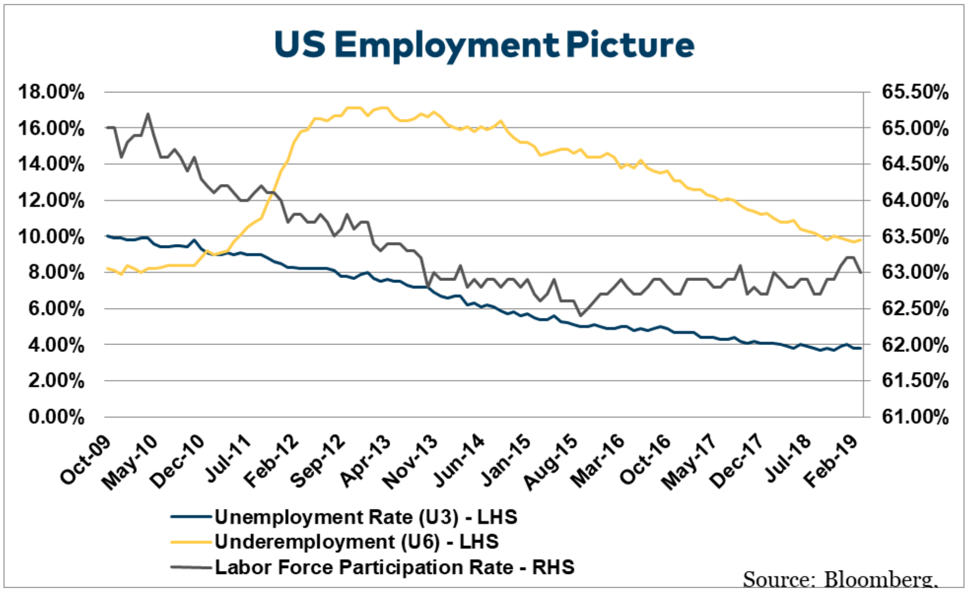
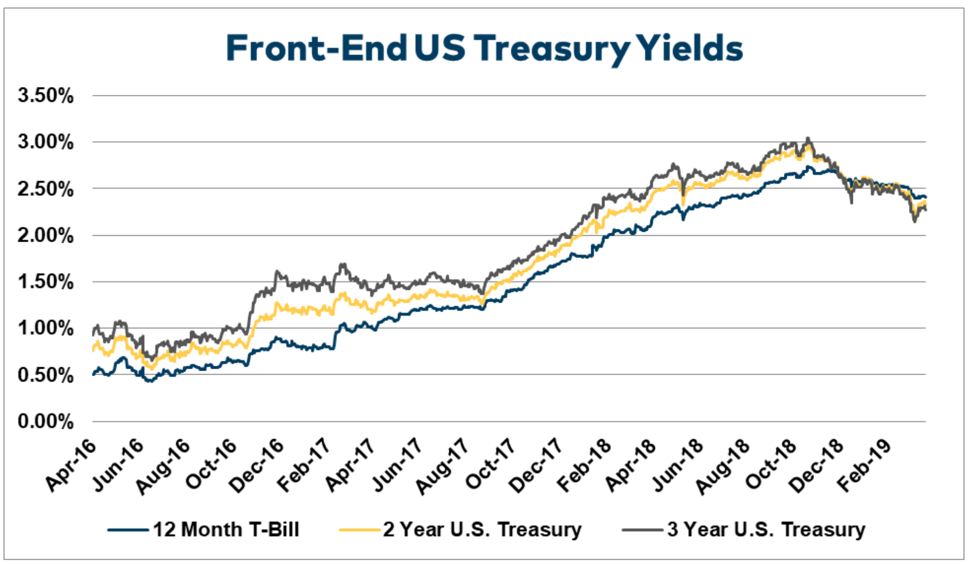
With the drop in consumer spending, and a large percentage of U.S. workers in retail, the current market temperament is that wages are at the cusp of a cooling phase.



Taken in isolation, current jobs market data is one of the strongest on record. U.S. unemployment is currently below 4% versus 8% in the Eurozone. Meanwhile, the broader underemployment measure is trending downward and labor force participation is growing. The lack of a Philip's curve, or a positive relationship between high employment and inflation, should be a boon for consumption as real wages grow (contrary to recent retail sales numbers). Taken as a whole, the market and the Fed are discounting the labor data in light of weakness in inflation, retail sales, and the yield curve inversion.



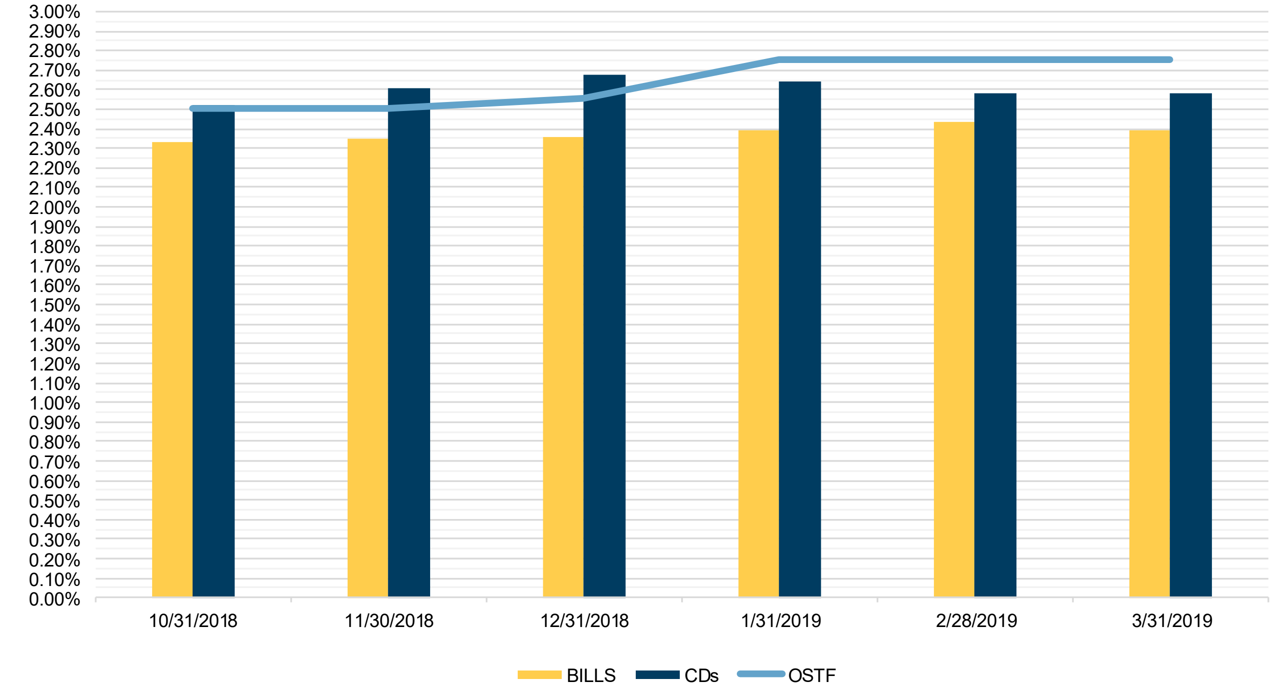
The short end of the yield curve inverted in December (two- and three-year bond yields trading under 12-month bill yields) and sustained a negative spread through March. Yield compression seemed to concentrate on two-year treasuries with a 0.26% drop, while Treasury bills were flat to moderately higher over the quarter. Front-end credit spreads, as measured by the 1-3 year Bloomberg Barclays Corporate Index, rallied strongly and fully reversed the selloff from the fourth quarter of 2018.

FY18 Overlapping Debt Report Request Deadline

Treasury's Debt Management Division is conducting the annual process of updating our Bond Tracker database with the current Real Market Values of local taxing districts' data obtained from the Oregon Department of Revenue. This process will be completed no later than June 30, 2019. Once the data is verified, Bond Tracker records will be permanently altered and we will no longer be able to generate FY2018 Overlapping Debt reports. As these reports are often required for financial reporting and other disclosure purposes, we highly recommend that you request and save an electronic copy of your Overlapping Debt Report for FY2018 at this time. There is no fee for Overlapping Debt Reports.

If you would like to receive a copy of your district's Overlapping Debt Report, submit a request before **Friday, June 14**. After that date, we will no longer be able to provide the FY2018 report for your use. As we receive so many requests during this process, please be patient while we work through all the requests. If you have any questions, contact Debt Management at 503.378.4930 or dmd@ost.state.or.us.

Oregon Short Term Fund Analysis



	10/31/2018	11/30/2018	12/31/2018	1/31/2019	2/28/2019	3/31/2019
LGIP AV DOLLARS INVESTED (MM)	6,602	9,377	10,030	9,236	9,016	8,969
STATE AGENCY AV DOLLARS INVESTED (MM)	10,795	10,936	10,903	10,844	10,922	10,833
TOTAL OSTF AV DOLLARS INVESTED (MM)	17,397	20,313	20,933	20,080	19,938	19,802
OST ANNUAL YIELD (ACT/ACT)	2.50	2.50	2.56	2.75	2.75	2.75
3-MO UST BILLS (BOND EQ YLD)	2.33	2.35	2.36	2.39	2.44	2.39
3-MO US CD (ACT/360)*	2.52	2.61	2.68	2.64	2.58	2.58

NOTE: The OST ANNUAL YIELD represents the average annualized yield paid to account holders during the month. Since interest accrues to accounts on a daily basis and the rate paid changes during the month, this average rate is not the exact rate earned by each account.

3-MO UST BILLS yield is the yield for the Treasury Bill Issue maturing closest to 3 months from month end. 3-MO US CD rates are obtained from Bloomberg and represent a composite of broker dealer quotes on highly rated (A1+/P1/F1+ from Standard & Poor's Ratings Services, Moody's Investors Service and Fitch Ratings respectivley) bank certificates of deposit and are quoted on a CD equivalent yield basis.

This material is available in alternative format and media upon request.

Market Data Table

	3/31/2019	1 Month	3 Months	12 Months
7-Day Agency Discount Note**	2.26	2.32	2.26	1.57
30-Day Agy Nt Disc**	2.34	2.36	2.29	1.62
90-Day Agy Nt Disc**	2.41	2.40	2.31	1.70
180-Day Agy Nt Disc**	2.37	2.42	2.43	1.86
360-Day Agy Nt Disc**	2.30	2.44	2.49	2.00
30-Day Treasury Bill**	2.38	2.38	2.30	1.54
60-Day Treasury Bill**	2.36	2.38	2.35	1.64
90-Day Treasury Bill**	2.37	2.40	2.36	1.71
6-Month Treasury Yield**	2.43	2.51	2.47	1.92
1-Year Treasury Yield**	2.39	2.55	2.58	2.09
2-Year Treasury Yield**	2.26	2.56	2.52	2.27
3-Year Treasury Yield**	2.21	2.53	2.50	2.38
1-Month LIBOR**	2.49	2.48	2.52	1.88
3-Month LIBOR**	2.60	2.60	2.80	2.31
6-Month LIBOR**	2.66	2.68	2.87	2.45
12-Month LIBOR**	2.71	2.88	3.01	2.66
Sources: *Bloomberg Index Services, **Bloomberg				

	3/31/2019	1 Month	3 Months	12 Months
Bloomberg Barclays 1-3 Year Corporate YTW*	2.77	3.06	3.28	2.88
Bloomberg Barclays 1-3 Year Corporate OAS*	0.55	0.57	0.86	0.67
Bloomberg Barclays 1-3 Year Corporate Modified Duration*	1.91	1.94	1.86	1.95
7-Day Muni VRDN Yield**	1.50	1.74	1.71	1.58
O/N GGC Repo Yield**	2.62	2.46	2.57	2.10
US 1 Year Inflation Break-Even**	4.29	2.90	(2.73)	2.24
US 2 Year Inflation Break-Even**	1.83	1.74	0.67	1.98
US 3 Year Inflation Break-Even**	1.77	1.80	1.15	2.00
1-Day CP (A1/P1)**	2.45	2.36	2.36	2.40
7-Day CP (A1/P1)**	2.47	2.40	2.39	2.26
30-Day CP (A1/P1)**	2.53	2.42	2.52	1.96
30-Day CD (A1/P1)**	2.49	2.45	2.43	1.65
90-Day CD (A1/P1)**	2.58	2.56	2.70	2.06
6-Month CD (A1/P1)**	2.63	2.65	2.88	2.37
1-Year CD (A1/P1)**	2.78	2.77	3.02	2.59

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- Statutory Requirements
- Service Provider Issues
- General Program Inquiries

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