Market Update

After a relatively calm August, the first week of September brought volatility back to financial markets. Equities saw a sharp three-day sell-off led by big-name tech stocks, while oil took a quick -8% header after Labor Day weekend. The bond market was not immune to the turbulence: instability in longer maturity Treasurys started a few weeks earlier following several large-sized auctions. Meanwhile, the macroeconomic picture showed accelerating recovery with a drop in unemployment from 10.2% to 8.4%. However, this good news was accompanied with a sharp escalation in trade tensions between the U.S. and China.

The pullback in equities follows a shallow breadth market run that began since the March lows, with the Nasdaq composite hitting a low on March 23, 2020, and then going on a 75% rally to September 2. The tech heavy index gave up 10% over the next three trading days. Many commentators have noted the rich valuations of U.S. equities, with the price-earnings ratio of the S&P 500 hitting 28 on September 1—a value not seen since 2002.

On August 4, the yield on the 10-year Treasury hit a summer low of 0.50, a level only exceeded by the intraday low of 0.39 on March 9. Since then, rates took a choppy ride up some 18 basis points as the yield curve steepled. The Federal Reserve’s anchoring of the lower end resulted in the 6-month to 10-year spread increasing by a similar 18 points over the month. The market is getting hit with massive waves of new U.S. paper, often over $100 billion per day with a recent high on September 8 of $249 billion. Buyer’s fatigue is resulting in inconsistent auction results. Corporate bonds and structure product were broadly placid over the month, with spreads mostly steady to the sovereign curve.

After the recent pick-up in inflation expectation, break-evens (the difference between the nominal yield on Treasurys and the yield on inflation indexed bonds) drifted lower over the month. Most early

(Continued on page 2)
indicators of inflation were continuing to power higher. Industrial commodities (copper, iron, timber) all moved higher over the reporting period. In addition, agriculture commodities (grains and livestock) have come off recent lows. The only major commodities bucking the trend are precious metals and oil. Gold is back under $2,000 per ounce, and crude took the aforementioned tumble. In these later two cases, there is market talk of lower overseas demand causing the price declines.

The surprise 2% drop in unemployment would normally spur inflation concerns off wage pressure, but significant slack remains in the labor market. The drop to 8.4% is roughly half of the peak from the COVID-19 economic shutdown. Wages for August were up 4.7% year-over-year, but these figures are misleading given that lower wage jobs were most severely impacted by the shutdown. Last month saw one of the largest pops in low-income job growth, but jobs numbers for this cohort are still 10% to 12% under pre-pandemic levels. Headline labor force participation figures are stagnating around 61%, off by approximately 2% from last year. Adding to the murkiness of the labor picture, permanent layoffs are surging 18% month-over-month against slowing temporary layoffs of -34% month-over-month.

Meanwhile, the Fed continues to expand its balance sheet through Treasury and corporate bond purchases. These actions are anchoring the front-end of the yield curve and hindering lift in corporate spreads.

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EON Security Enhancements Coming in October

Treasury is continuously focused on protecting public funds and our customers’ financial data. As part of these efforts, and in recognition of next month being National Cybersecurity Awareness Month, we are excited to announce three EON security enhancements that will start rolling out to the Local Government Investment Pool in late October.

The first enhancement, multi-factor authentication (MFA), is an industry leading practice for verifying a user’s identity. Once enabled, EON users will be prompted to enter a one-time numeric passcode immediately after entering your user name and password. Users can choose to receive the passcode by email, phone call, or text message. Once you have selected the delivery method, you will receive the passcode and then enter it in EON to complete your login. To prepare for MFA, log in to EON today and verify your contact information by clicking on “Profile Update” at the top of the page.

The second enhancement, the account activity notification center, alerts EON users to key account activities including certain transactions and changes to both ACH/wire instructions and user permissions. Users will receive e-mail notifications based on individual account permissions and subscription preferences.

The third enhancement, updated password complexity requirements, will require users to use passwords that meet current industry best practices. If a user’s existing password does not meet the new requirements, the user will be prompted to create a new password when logging in. As the user types the new password, EON will list the requirements and indicate which are met or unmet. A user’s new password must meet all requirements before EON will accept the new password.

More information about these security enhancements will soon be available within EON, and we hope you join Treasury in recognizing the value of these security enhancements.
depressed yield in fixed income contributed to the summer rally in equities, but the overall impact of monetary policy continues to lose strength. Money velocity, or the ratio of money growth to economic output, collapsed over the summer by 41%, meaning the burden of future stimulus will lean on fiscal measures.

With the next round of spending stalled in Congress, and continued policy uncertainty running into the November election, a volatile market seems somewhat inevitable through the back half of the year. Furthermore, the U.S. and China trade dispute continues to escalate. The import purchasing mandates by China from the first round of trade negotiations will not be met and, over the past month, the Trump administration targeted sanctions on specific Chinese tech and agriculture companies. Moreover, last month saw the forced closure of two consulates from increasing political tit for tat. In a normal year, these events would cause massive swings in financial markets, but 2020 is far from normal. The long-term impact of the diplomatic deterioration between the world’s two largest economies becomes yet another major issue that depends on the outcome of the November election.

In July, the OSTF paid rate was lowered from 1.3% to 1.0%, which remains over what the market is currently paying on OSTF’s investable universe. As higher yielding securities reach maturity, reinvestment under current market conditions will continue to put downward pressure on the paid rate.

Treasury and PFM Asset Management have maintained normal operations and participants remain able to perform all transactions as normal. We remain focused on functioning in an open and transparent manner and, should you have any questions, please contact our Fixed Income Team at 503.431.7900.

**Impact on Markets in August 2020**

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<tr>
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<th>8/1/20</th>
<th>8/31/20</th>
<th>Delta</th>
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<tbody>
<tr>
<td>S&amp;P 500</td>
<td>3,294.61</td>
<td>3,500.31</td>
<td>+6.2%</td>
<td>S&amp;P 500 intraday low at 3,284 on 8/3</td>
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<tr>
<td>30-Year Treasury</td>
<td>1.233%</td>
<td>1.476%</td>
<td>+24.3 bps</td>
<td>30-Year Bond intraday low at 1.179% on 8/4</td>
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<tr>
<td>10-Year Treasury</td>
<td>0.556%</td>
<td>0.706%</td>
<td>+15.0 bps</td>
<td>10-Year Note intraday low at 0.502% on 8/6</td>
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<tr>
<td>2-Year Treasury</td>
<td>0.111%</td>
<td>0.132%</td>
<td>+2.1 bps</td>
<td>2-Year Note intraday low at 0.105% on 8/4</td>
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<tr>
<td>3-Month Bills</td>
<td>0.085%</td>
<td>0.101%</td>
<td>+1.6 bps</td>
<td>3-Month Bill intraday low at 0.066% on 8/7</td>
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*Treasury yields represent closing bid side levels

**New Debt Management Director**

This month we welcomed Jacqueline Knights as our next Director of Debt Management. Jacqueline arrives at Treasury with decades of experience in municipal finance and may be familiar to some of you through work she has done within Oregon during her career. Prior to joining Treasury, Jacqueline worked for the Williams Capital Group, Jackson Securities, Bear Stearns, and JP Morgan during which she worked on infrastructure, transportation, public utilities, and other municipal sectors. Jacqueline has a Master of Business Administration from Columbia and bachelor’s degree in economics from the Wharton School of Business. Jacqueline is replacing Laura Lockwood-McCall who, after more than a decade of service to the State of Oregon, will be headed toward a well-earned retirement. Please help us both welcome Jacqueline and thank Laura for her service.
Oregon Short Term Fund Analysis

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 respectively) bank certificates of deposit and are quoted on a CD equivalent yield basis.

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