Monthly Market Review

Fixed Income | March 2025

Information provided by VA SNAP's Program Administrator PFM Asset Management, a division of U.S. Bancorp Asset Management, Inc.

Virginia State SNAP® Non-Arbitrage Program

Uncertainty Taking a Toll

Economic Highlights

► Market sentiment shifted towards the end of February as several survey-based measures showed consumers becoming increasingly nervous about the future trajectory of the economy. The potential for federal job cuts and the looming threat of tariffs were top of mind for consumers.

► Tariffs on Mexico and Canada went into effect in early March with a one-month exemption for autos and any items covered under the United States-Mexico-Canada Trade Agreement ("USMCA"). An additional 10% tariff was levied on China, and a 25% tariff on steel and aluminum is set to take effect on March 12. The market is also focusing on the potential for reciprocal tariffs to be announced in early April, which may be met by retaliatory tariffs.

► Minutes from the January Federal Open Market Committee (FOMC) meeting showed that the Federal Reserve (Fed) is willing to keep the federal funds rate unchanged as long as the labor market remains strong. Participants noted additional upside risks to inflation from proposed trade and immigration policy, although policymakers were unsure if the new policies would lead to a persistent or more temporary increase in inflation.

► The month-over-month change in the Core Personal Consumption Expenditures Index (PCE), which is the Fed's preferred measure of inflation, increased to its highest level since October on higher goods prices. Core PCE, which omits volatile food and energy prices, slowed to 2.6% year-over-year mainly on favorable base effects.

► Consumer spending for the month of January fell by -0.5% on an inflation-adjusted basis, marking the weakest print since February 2021. While this came on the heels of a strong 2024 holiday shopping season, there is increasing concern that consumers are becoming more cautious with their spending.

► In February, nonfarm payrolls grew 151,000, slightly missing expectations, but continuing to show solid growth. The unemployment rate also missed expectations and rose to 4.1%. Initial jobless claims for federal workers will be a focus going forward as markets look for the first signs of the potential impact of federal job cuts.

Bond Markets

► The short end of the U.S. Treasury yield curve was unchanged in February as expectations for a Fed pause over the next several months held yields on the short end of the curve steady.

► U.S. Treasury yields beyond one year declined notably over the latter half of the month on fears related to inflation and its impact on the consumer and growth. The yield on the 10-year U.S. Treasury remains firmly above its two-year average while 2-year yields have now moved below their two-year average.

► Yields on 2-year and 10-year Treasuries declined 20 basis points (bps) and 33 bps, respectively, underscoring uncertainty in the market surrounding geopolitical tensions, inflation expectations, and labor market conditions. This resulted in the yield curve inverting again in February as yields on 3-month, 2-year, and 10-year U.S. Treasuries ended the month at 4.29%, 3.99%, and 4.21%, respectively.

► The move lower in yields resulted in positive total returns for fixed income for the month, with longer duration indices outperforming shorter-term strategies. The ICE BofA 3-month, 2-year, and 10-year U.S. Treasury indices returned +0.32%, +0.68%, and +3.09%, respectively.

Equity Markets

► Equity markets retreated in February as the "Magnificent Seven" stocks fell over 11% since peaking in mid-December. The Dow Jones Industrial Average ended the month down 1.4%, the S&P 500 Index finished down 1.3%, and the NASDAQ fell 3.9%.

► International equities (measured by MSCI ACWI ex-U.S. Net Index) advanced 1.4% as investors trimmed domestic profits and diversified holdings globally. The U.S. Dollar Index ended the month 1% weaker.

PFMAM Strategy Recap

► We will continue to maintain portfolio durations near 100% of benchmarks given the ongoing rate and policy uncertainty and the attractive level of absolute yields. For longer duration strategies, we continue to prefer a bulleted yield curve structure as we expect the yield curve to steepen further.

► Investment-grade (IG) corporate bond valuations remain expensive. Our view is that the combination of preliminary Q4 earnings data releases, heightened market volatility, and fiscal policy uncertainty may create opportunities to increase allocations at more attractive levels. We also believe strong technicals and favorable fundamentals may limit spread widening. As a result, we will look to tactically reduce allocations in the sector to make room for future opportunities, with a focus on industry and credit quality-specific selectivity.

► Asset-backed securities (ABS) spreads widened marginally over the month and market demand remains robust. The consumer's response to prior monetary policy easing remains a key factor for the sector's outlook in the near term.

► Valuations in most agency-backed mortgage-related sectors are stretched as spreads remain narrow. Rate volatility has increased modestly over recent weeks due to heightened domestic policy uncertainty. We expect this trend to continue, which may put pressure on total return potential.

► The supply of U.S. Treasury Bills is expected to decline as the U.S. Treasury approaches the limit of its extraordinary measures, which may put downward pressure on the money market yield curve.

U.S. Treasury Yields

Maturity	Feb 29, 2024	Jan 31, 2025	Feb 28, 2025	Monthly Change
3-Month	5.38%	4.29%	4.30%	0.01%
6-Month	5.33%	4.30%	4.28%	-0.02%
2-Year	4.62%	4.20%	3.99%	-0.21%
5-Year	4.25%	4.33%	4.02%	-0.31%
10-Year	4.25%	4.54%	4.21%	-0.33%
30-Year	4.38%	4.79%	4.49%	-0.30%

Yields by Sector and Maturity

Maturity	U.S. Treasury	Federal Agency	Corporates-AA-A Industrials	AAA Municipals
3-Month	4.30%	4.31%	4.49%	-
6-Month	4.28%	4.28%	4.58%	-
2-Year	3.99%	4.00%	4.35%	2.63%
5-Year	4.02%	4.03%	4.61%	2.71%
10-Year	4.21%	4.27%	4.96%	2.96%
30-Year	4.49%	-	5.47%	3.48%

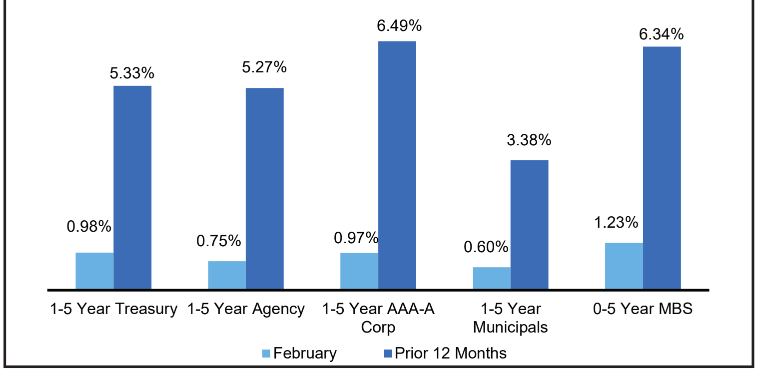
Spot Prices and Benchmark Rates

Index	Feb 29, 2024	Jan 31, 2025	Feb 28, 2025	Monthly Change
1-Month SOFR	5.32%	4.31%	4.32%	0.01%
3-Month SOFR	5.33%	4.30%	4.32%	0.02%
Effective Fed Funds Rate	5.33%	4.33%	4.33%	0.00%
Fed Funds Target Rate	5.50%	4.50%	4.50%	0.00%
Gold ($/oz)	$2,055	$2,813	$2,849	$36
Crude Oil ($/Barrel)	$78.26	$72.53	$69.76	-$2.77
U.S. Dollars per Euro	$1.08	$1.04	$1.04	$0.00

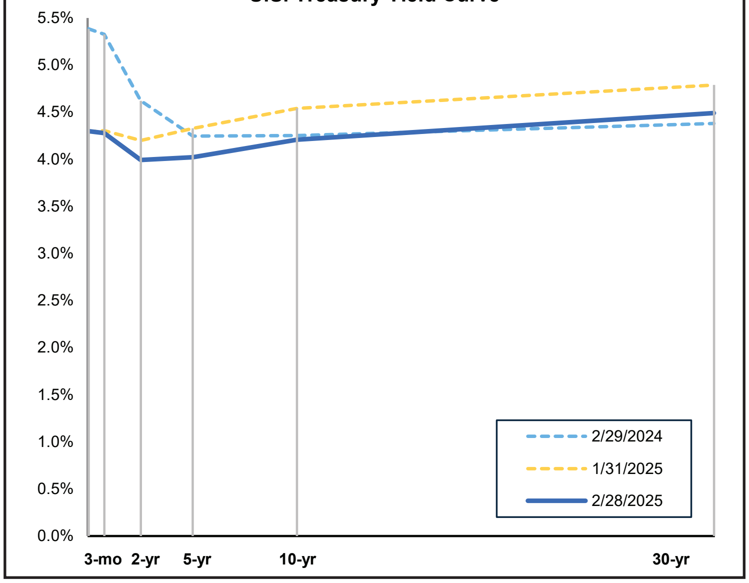
Economic Indicators

Indicator	Release Date	Period	Actual	Survey (Median)
ISM Manufacturing	3-Feb	Jan	50.9	51.2
Change in Nonfarm Payrolls	7-Feb	Jan	143K	175K
Retail Sales Advance MoM	14-Feb	Jan	-0.90%	-0.20%
U. of Mich. Consumer Sentiment	21-Feb	Feb F	64.7	67.8
Existing Home Sales MoM	21-Feb	Jan	-4.90%	-2.60%
GDP Annualized QoQ	27-Feb	4Q S	2.30%	2.30%
PCE YoY	28-Feb	Jan	2.60%	2.60%

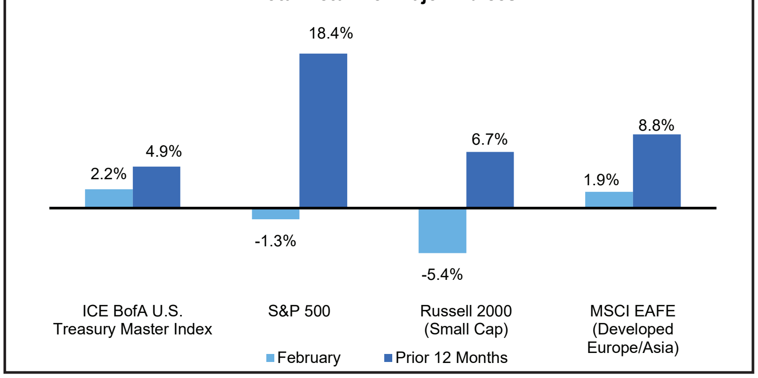
ICE BofA Fixed Income Index Returns



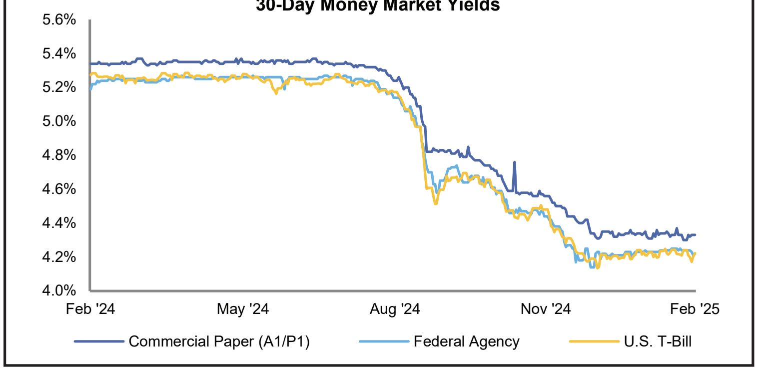
U.S. Treasury Yield Curve



Total Return of Major Indices



30-Day Money Market Yields



Source: Bloomberg. Data as of February 28, 2025, unless otherwise noted.

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