Monthly Market Review

Fixed Income | February 2025

pfm asset management

One Thing is Certain…Uncertainty

Economic Highlights

► At the January Federal Open Market Committee (FOMC), the Federal Reserve (Fed) maintained the target range for the federal funds rate at 4.25% to 4.50%. In Fed Chair Jerome Powell's post-meeting press conference, he emphasized the Fed is "not in a hurry" to make further policy rate adjustments as the labor market remains "solid" and inflation "somewhat elevated."

► Previously announced tariffs on Mexico and Canada scheduled to go into effect on February 2 were paused for one month while a 10% tariff on Chinese goods went forward. China announced retaliatory tariffs on a small subset of American goods.

► The Consumer Price Index (CPI) and Personal Consumption Expenditures Index (PCE) both increased marginally on a year-over-year basis. Core PCE remained above the Fed's 2% target at 2.8% YoY, although the annualized three- and six-month rates are beginning to show signs of disinflation.

► Non-farm payrolls for January grew 143,000, slightly missing consensus expectations. This was offset by a combined 100,000 upward revision to the already-strong November and December readings, resulting in a 3-month moving average change in nonfarm payrolls at a robust 237,000. The unemployment rate also fell to 4.0%.

► The preliminary advance estimate for Q4 gross domestic product (GDP) came in at 2.3%. While the headline figure came in below expectations due to weak gross private domestic investment, consumer spending increased at the fastest pace in almost two years. Real GDP grew by an estimated 2.8% in 2024, marking the fourth consecutive year the economy grew faster than its estimated long-term growth potential.

► Given the strength of the labor market and limited progress on inflation, the market expects the Fed to pause for at least several months as it continues to "wait and see" the impacts of the new administration's policies.

Bond Markets

► The short end of the U.S. Treasury yield curve was generally unchanged over the month as the expectations for a Fed pause over the next several months affected the shortest U.S. Treasury yields.

► After touching multi-month highs in mid-January, U.S. Treasury yields beyond two years declined notably over the latter half of the month on ebbing inflation fears. Despite the end-of-month rally, the yield on the 10-year U.S. Treasury remains near the higher end of its three-year range, while 2-year yields are closer to the multi-year average.

► Yields on 3-month, 2-year, and 10-year U.S. Treasuries ended the month 3 to 4 basis points lower at 4.28%, 4.20%, and 4.54%, respectively. The yield curve continued to steepen as the spread between the 2-year and 10-year U.S. Treasury reached its highest level in nearly three years. This relationship underscores the recent trend of a steepening curve and expectations this dynamic will continue.

► Fixed income total returns were positive, with longer duration indices outperforming shorter-term strategies. The ICE BofA 3-month, 2-year, and 10-year U.S. Treasury indices returned +0.37%, +0.41%, and +0.66%, respectively.

Equity Markets

► Equity markets experienced some heightened volatility as investors responded to a deluge of earnings results, headline surprises, and a wave of Presidential executive orders. The Dow Jones Industrial Average ended the month up 4.8%, the S&P 500 Index finished up 2.8%, while the NASDAQ gained 1.7%.

► International equities (measured by MSCI ACWI ex U.S. Net Index) rallied for the month, advancing 4.0%. The U.S. Dollar Index ended the month essentially unchanged after whipsawing on rate volatility and tariff uncertainty.

PFMAM Strategy Recap

► We will continue to maintain portfolio durations near 100% of benchmarks given the ongoing rate uncertainty. We continue to prefer a bulleted maturity structure on our expectation that the yield curve will continue to steepen.

► Spreads on federal agencies and supranationals were essentially unchanged and remain quite narrow. No significant changes are expected in the near-term and we will maintain low allocations in favor of other sectors.

► Investment-grade (IG) corporate bond valuations remain rich, with spreads at historically narrow levels with little room to tighten further. Our view is that the combination of heightened market volatility, fiscal policy uncertainty, and Q1 issuance seasonality may create opportunities to increase allocations at more attractive levels while technical strength and favorable fundamentals will likely limit significant spread widening. 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) new issuance levels started the year trailing behind last year's pace. Strong demand for new issues and continued strength in underlying technicals has kept a lid on spreads, leading to spread tightening that produced positive excess returns in January. The consumer's response to prior monetary policy easing remains a key factor for the sector's outlook in the near term. We will therefore seek to maintain allocations via the reinvestment of passive cash flows in new issuance.

► Valuations in both the agency mortgage-backed securities (MBS) and agency commercial MBS (CMBS) sectors are stretched as spreads remain narrow and rate volatility is expected to pick up in the face of wider domestic uncertainty. As a result, we will seek to actively reduce allocations in longer duration strategies.

U.S. Treasury Yields

Maturity	Jan 31, 2024	Dec 31, 2024	Jan 31, 2025	Monthly Change
3-Month	5.37%	4.32%	4.29%	-0.03%
6-Month	5.20%	4.27%	4.30%	0.03%
2-Year	4.21%	4.24%	4.20%	-0.04%
5-Year	3.84%	4.38%	4.33%	-0.05%
10-Year	3.91%	4.57%	4.54%	-0.03%
30-Year	4.17%	4.78%	4.79%	0.01%

Yields by Sector and Maturity

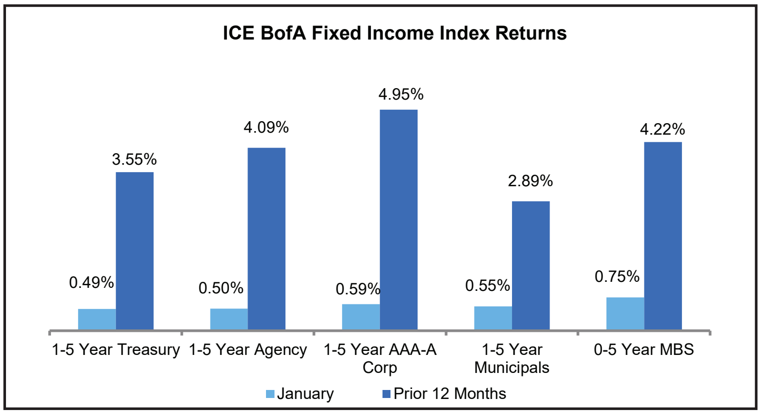
Maturity	U.S. Treasury	Federal Agency	Corporates-AA-A Industrials	AAA Municipals
3-Month	4.29%	4.30%	4.49%	-
6-Month	4.30%	4.30%	4.60%	-
2-Year	4.20%	4.21%	4.48%	2.89%
5-Year	4.33%	4.34%	4.85%	2.90%
10-Year	4.54%	4.60%	5.23%	3.12%
30-Year	4.79%	-	5.70%	3.26%

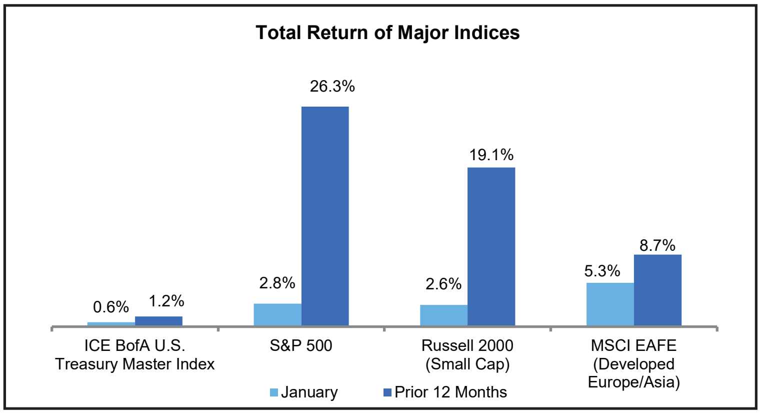
Spot Prices and Benchmark Rates

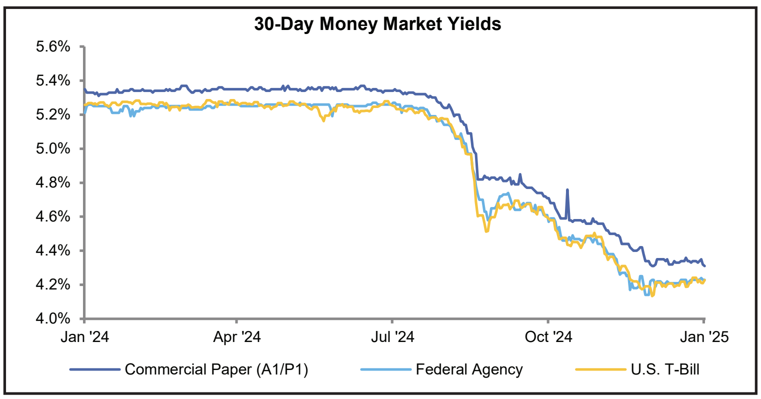
Index	Jan 31, 2024	Dec 31, 2024	Jan 31, 2025	Monthly Change
1-Month LIBOR	5.33%	4.33%	4.31%	-0.02%
3-Month LIBOR	5.32%	4.31%	4.30%	-0.01%
Effective Fed Funds Rate	5.33%	4.33%	4.33%	0.00%
Fed Funds Target Rate	5.50%	4.50%	4.50%	0.00%
Gold ($/oz)	$2,048	$2,641	$2,813	$172
Crude Oil ($/Barrel)	$75.85	$71.72	$72.53	$0.81
U.S. Dollars per Euro	$1.08	$1.04	$1.04	$0.00

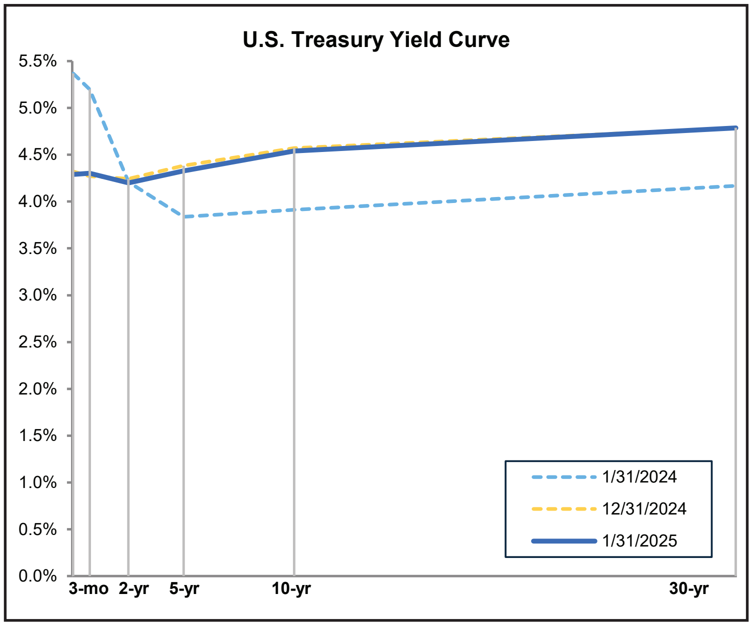
Economic Indicators

Indicator	Release Date	Period	Actual	Survey (Median)
ISM Manufacturing	3-Jan	Dec	49.3	48.2
Retail Sales Advance MoM	16-Jan	Dec	0.40%	0.60%
Existing Home Sales MoM	24-Jan	Dec	2.20%	1.20%
U. of Mich. Consumer Sentiment	24-Jan	Jan F	71.1	73.2
FOMC Rate Decision	29-Jan	Jan	4.50%	4.50%
GDP Annualized QoQ	30-Jan	4Q A	2.30%	2.60%
PCE YoY	31-Jan	Dec	2.80%	2.80%









Source: Bloomberg. Data as of January 31, 2025, unless otherwise noted.

Indices shown are not available for investment. The index data reference herein is the property of the index provider and/or its licensors. The index provider assumes no liability in connections with its use and does not sponsor, endorse or recommend the products or services contained herein. Index returns do not reflect payment of any sales charges or fees an investor would pay to purchase the securities they represent. The imposition of these fees and charges would cause investment performance to be lower than the performance shown.

The views expressed within this material constitute the perspective and judgment of U.S. Bancorp Asset Management, Inc. at the time of distribution and are subject to change. Any forecast, projection, or prediction of the market, the economy, economic trends, and equity or fixed-income markets are based upon current opinion as of the date of issue and are also subject to change. Opinions and data presented are not necessarily indicative of future events or expected performance. Information contained herein is based on data obtained from recognized statistical services, issuer reports or communications, or other sources, believed to be reliable. No representation is made as to its accuracy or completeness.

PFM Asset Management serves clients in the public sector and is a division of U.S. Bancorp Asset Management, Inc., which is the legal entity providing investment advisory services. U.S. Bancorp Asset Management, Inc. is a registered investment adviser, a direct subsidiary of U.S. Bank N.A. and an indirect subsidiary of U.S. Bancorp. U.S. Bank N.A. is not responsible for and does not guarantee the products, services, or performance of U.S. Bancorp Asset Management, Inc.

NOT FDIC INSURED : NO BANK GUARANTEE : MAY LOSE VALUE