Fourth Quarter 2021

Bond Market Commentary

Beginning 2009, 2-year Treasury Note yields have been below 1.00% in 10 of the last 13 years. According to Bloomberg, the average yield for that period was 0.87%. This historically low period was not free-market induced, it was orchestrated by the Federal Reserve.

Initiated under emergency powers to prevent a financial melt-down caused by the mortgage crisis of 2008, this artificial manipulation of interest rates has long ago served its purpose. It is difficult to understand how the Fed could build a case that the emergency has remained in place for over 13 years.

The impact on bond investors has been enormous. Income produced from portfolios during that period have declined to historical lows. Baby Boomers, the largest generation in history, have faced retirement without the benefit of obtaining a real return from safe assets. As a result, investors have been forced into purchasing riskier assets to obtain any real return on their investments. Many investors are not in position to understand or accept this additional risk.

Bloomberg indicates that the S&P Index returned an annual equivalent 15.96% return during the same 13-year period, assuming dividends were reinvested into the index. It is difficult to understand how the Fed could believe we have remained under the same conditions as the financial melt-down for this long and sustained such low interest rates.

It appears that this is about to change. The Fed has indicated that they will be reversing their bond buying and raising the possibility of short-term rate increases in 2022. Inflation has been rapidly rising, employment is reaching capacity and household wealth is near all time highs. Should the Fed begin the transition to higher interest rates, many investors will be entering a new frontier.

Thirty-year interest rates peaked in 1981 at 14.67% and following a 40-year decline, bottomed in 2020 at 1.42%. For reference, had you invested $100,000 dollars into the 14.67% 30-year bond, you would have received $440,100 of interest income, over 4 times your original investment. Investing that same $100,00 in the 30-year bond in 2020 would offer you only $42,600 of income for the same period.

Inflation only complicates the situation as the future purchasing power of the annual income evaporates. Low interest rates together with rising inflation is an investor's nightmare.

What can be done? Investors in bonds will ultimately benefit from higher interest rates. It will take time, however reinvesting income and principal as current bonds mature will lead to higher income and returns. As such, we have maintained relatively short-term portfolios which will allow us to increase annual income sooner than later. While longer-term bonds will drop in market value, holding the issues to their maturity will provide the income and return as purchased. The goals of bond investing are to provide income and manage volatility. A properly structured bond portfolio will produce increasing income with low relative volatility.

Index Returns As of 12/31/21	Performance Period		
Index	3 Month	6 Month	1 Year
Bloomberg US Treasury Intermediate	-0.57	-1.76	-1.72
Bloomberg Govt/Credit Intermediate	-0.57	-0.36	-1.44
Bloomberg Intermediate Aggregate	-0.51	-0.41	-1.29
Bloomberg US Treasury	0.18	-2.96	-2.32
Bloomberg Govt/Credit	0.18	-0.17	-1.75
Bloomberg Aggregate	0.01	-0.27	-1.54
Bloomberg US Treasury 20+ Year	3.52	-7.14	-4.37
Bloomberg Corporate	0.23	3.54	-1.04
Bloomberg Corporate Intermediate	-0.56	2.08	-1.00
Bloomberg Corporate High Yield	0.71	17.22	5.28
Bloomberg Credit AAA	1.12	0.26	-2.26
Bloomberg Credit AA	0.59	1.07	-1.46
Bloomberg Credit A	0.13	1.39	-1.93
Bloomberg Credit BAA	0.23	5.84	-0.22
Bloomberg MBS	-0.37	-0.69	-1.04
Bloomberg TIPS	2.36	10.94	5.96
Bloomberg Inter-Short Muni	0.10	2.31	0.43

Source: Bloomberg

Daily Generic Municipal Bond Yields as of 12/31/21

Term	Maturity	AAA	AA	A	BAA
1 Yr.	2023	0.17	0.30	0.36	1.26
2 Yr.	2024	0.22	0.37	0.43	1.27
3 Yr.	2025	0.32	0.48	0.54	1.34
4 Yr.	2026	0.43	0.60	0.68	1.49
5 Yr.	2027	0.57	0.75	0.85	1.64
7 Yr.	2029	0.84	0.99	1.13	1.92
9 Yr.	2031	1.01	1.15	1.32	2.16
10 Yr.	2032	1.04	1.18	1.36	2.32
12 Yr.	2034	1.09	1.23	1.44	2.34
14 Yr.	2036	1.14	1.31	1.53	2.43
15 Yr.	2037	1.16	1.35	1.58	2.48
17 Yr.	2039	1.23	1.40	1.64	2.53
19 Yr.	2041	1.29	1.47	1.70	2.60
20 Yr.	2042	1.30	1.49	1.71	2.62
25 Yr.	2047	1.44	1.65	1.84	2.78
30 Yr.	2052	1.48	1.72	1.89	2.84

Source: Bloomberg

Index Descriptions:

Bloomberg US Intermediate Treasury Index Unmanaged index includes all publicly issued, US Treasury securities that have a remaining maturity of greater than or equal to 1 year and less than 10 years, are rated investment grade, and have $250 million or more of outstanding face value.

Bloomberg Intermediate Government/Credit Index: Is an unmanaged index based on all publicly issued intermediate government and corporate debt securities with maturities of 1-10 years. This index represents asset types which are subject to risk, including loss of principal.

Bloomberg U.S. Treasury Bond Index: Is part of Bloomberg global family of government bonds indices. The index measures the performance of the U.S. Treasury bond market, using market capitalization weighting and a standard rule based inclusion methodology.

Bloomberg Government/Credit Bond Index Unmanaged index that tracks the performance of US Government and corporate bonds rated investment grade or better, with maturities of at least one year.

Bloomberg Intermediate Aggregate Index: Is an unmanaged index that consists of 1-10 year Governments, 1-10 year Corporates, all Mortgages, and all Asset-Backed securities within the Aggregate Index (i.e. the Aggregate Index less the Long Government/Corporate Index).

Bloomberg U.S. Aggregate Bond Index: Is an unmanaged index composed of securities from the Bloomberg Government/Corporate Bond Index, Mortgage-Backed Securities Index and the Asset-Backed Securities Index. Total return comprises price appreciation/depreciation and income as a percentage of the original investment. Indices are rebalanced monthly by market capitalization.

Bloomberg U.S. Credit Index: Is composed of all publicly issued, fixed-rate, nonconvertible, investment-grade corporate debt. Issues are rated at least Baa by Moody's Investors Service or BBB by Standard & Poor's, if unrated by Moody's. Collateralized Mortgage Obligations (CMOs) are not included. Total return comprises price appreciation/depreciation and income as a percentage of the original investment.

Bloomberg U.S. Intermediate Credit Index: Measures the investment-grade, U.S. dollar-denominated, fixed-rate, taxable corporate and government-related bond markets. The index only includes securities with maturity between one and ten years. It is composed of the Bloomberg U.S. Corporate Index and a non-corporate component that includes foreign agencies, sovereigns, supranationals and local authorities.

Bloomberg U.S. Corporate High Yield Index: Is an unmanaged index that is comprised of issues that meet the following criteria: at least $150 million par value outstanding, maximum credit rating of Ba1 (including defaulted issues) and at least one year to maturity.

Bloomberg U.S. Mortgage-Backed Securities Index: Is an unmanaged index that tracks agency mortgage backed pass-through securities (both fixed-rate and hybrid ARM) guaranteed by GNMA, FNMA, and FHLM.

Bloomberg U.S. Treasury Inflation-Protected Securities (TIPS) Index: Represents securities that protect against adverse inflation and provide a minimum level of real return. To be included in this index, bonds must have cash flows linked to an inflation index, be sovereign issues denominated in U.S. currency, and have more than one year to maturity, and, as a portion of the index, total a minimum amount outstanding of 100 million U.S. dollars. An individual cannot invest directly in an index.

Bloomberg Municipal Bond Inter-Short 1-10 Year Index: Is an unmanaged index of municipal bonds traded in the U.S. with maturities ranging from 1-10 years.