# The Return to Normalcy

## Are we already there and don’t know it?
## Is it still a ways off?

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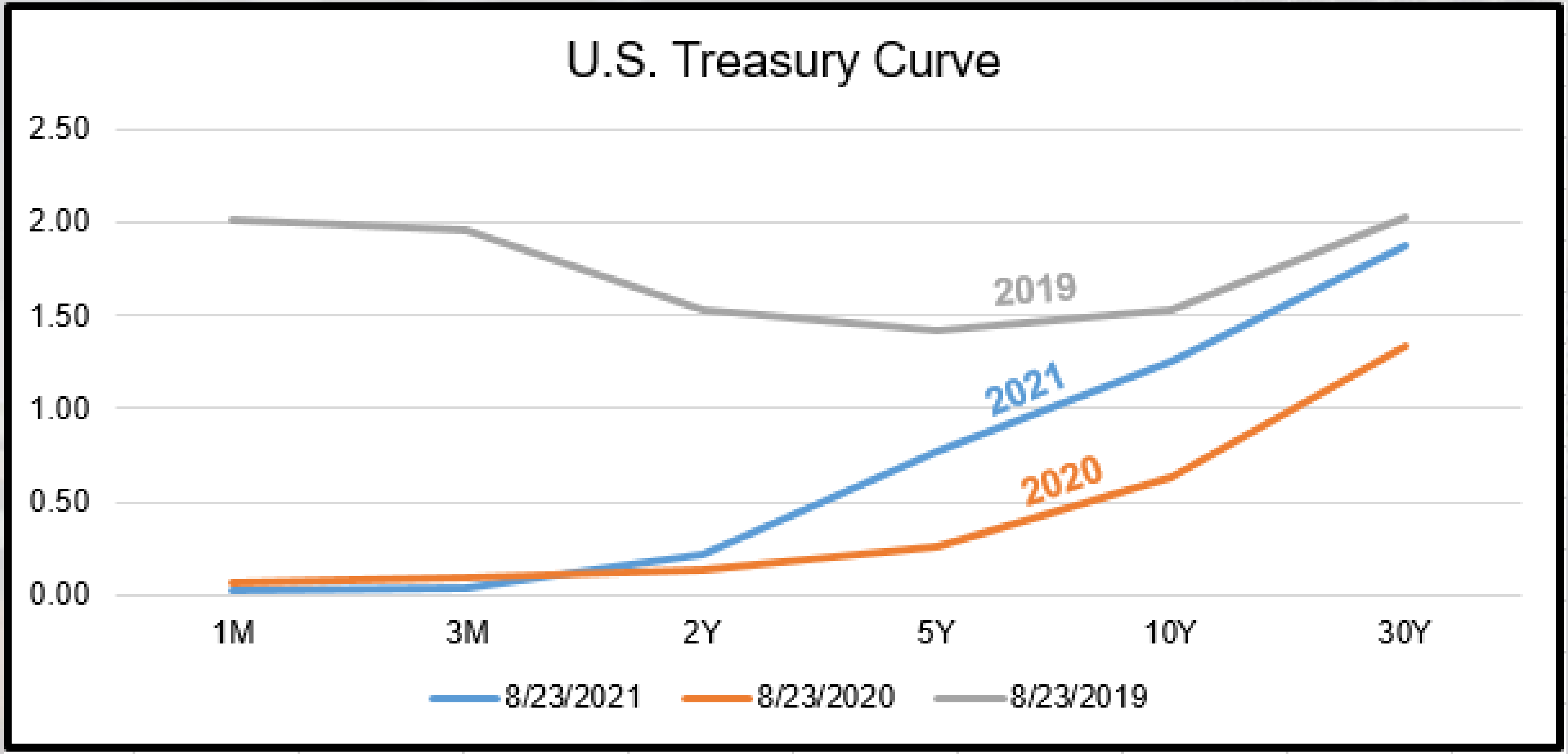
# Overview

- A look back on the current cycle
- Current market threats and opportunities
- Fed Outlook
- Bank Balance Sheets
- How to position the bond portfolio

# The past few years…




*Source: Bloomberg, L.P.*

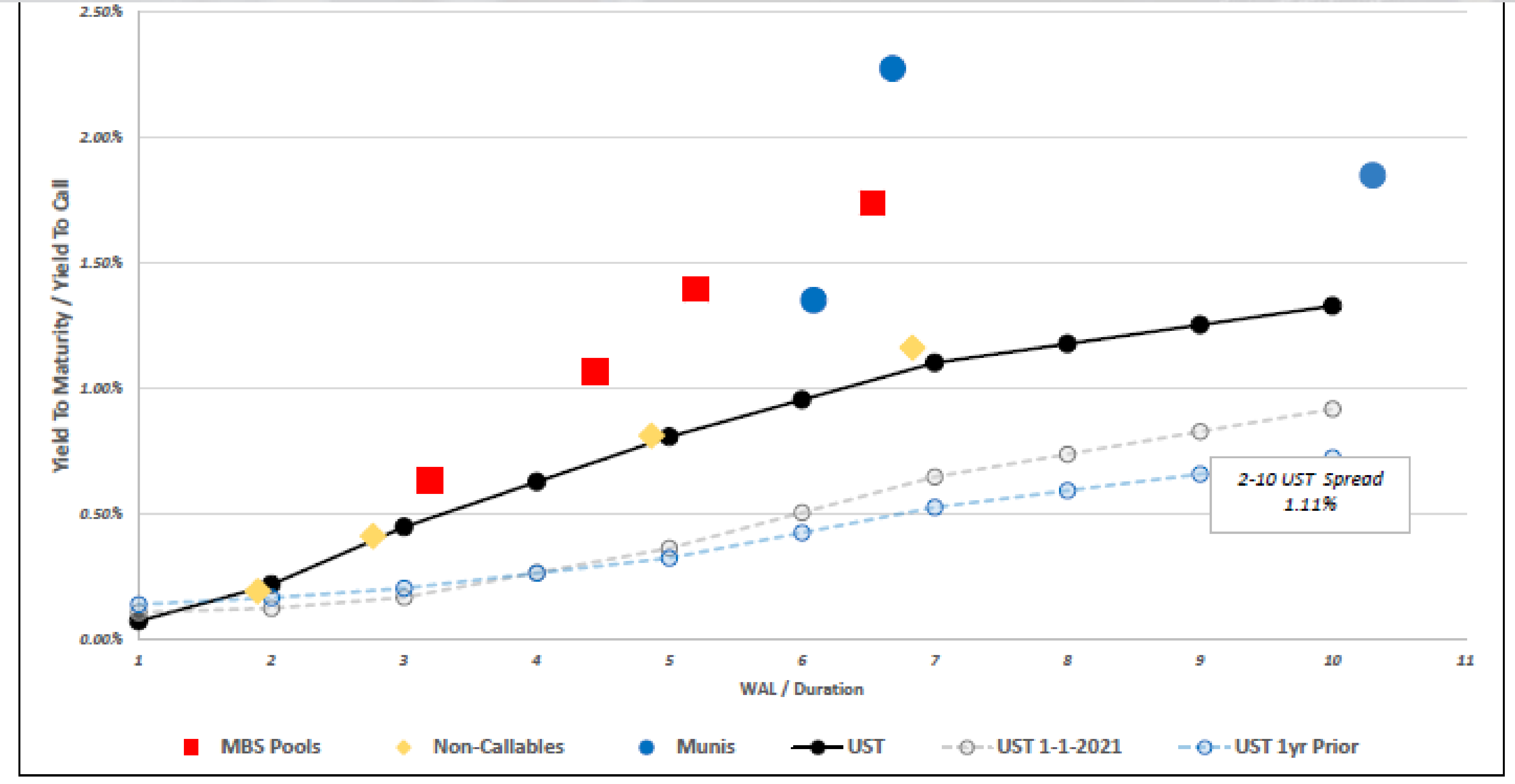
**Vaxwell**
@_AWat_

My fall plans The delta variant


8:25 PM · Aug 11, 2021

18.4K See the latest COVID-19 info...

# Fixed Income Sector Snapshot




*Source: Bloomberg, L.P.*

# Impacts on our market

- Delta Variant
- Herd Immunity
- U.S. Debt
- Fed Bond Buying and Tapering
- Jobs: Unemployment and Job Growth
- Inflation (CPI)

**EUROPEAN OUT-OF-OFFICE:**

I'M AWAY CAMPING FOR THE SUMMER. PLEASE EMAIL BACK IN SEPTEMBER.

**AMERICAN OUT-OF-OFFICE:**

I HAVE LEFT THE OFFICE FOR TWO HOURS TO UNDERGO KIDNEY SURGERY BUT YOU CAN REACH ME ON MY CELL ANY TIME.

# Yellen endorses Powell for another term


*Source: US Federal Reserve | Reuters*

# The Zoom's continue

## Jackson Hole Fed Meeting
## Now Virtual This Week

*How and when will they begin to wind down the multi-phased Quantitative Easing bond-buying program?*

**Stay tuned Friday for a word from Powell**

# Reading between the (yellow) lines…

## July 28, 2021

The Federal Reserve is committed to using its full range of tools to support the U.S. economy in this challenging time, thereby promoting its maximum employment and price stability goals.

With progress on vaccinations and strong policy support, indicators of economic activity and employment have continued to strengthen. The sectors most adversely affected by the pandemic have shown improvement but have not fully recovered. Inflation has risen, largely reflecting transitory factors. Overall financial conditions remain accommodative, in part reflecting policy measures to support the economy and the flow of credit to U.S. households and businesses.

The path of the economy continues to depend on the course of the virus. Progress on vaccinations will likely continue to reduce the effects of the public health crisis on the economy, but risks to the economic outlook remain.

The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. With inflation having run persistently below this longer-run goal, the Committee will aim to achieve inflation moderately above 2 percent for some time so that inflation averages 2 percent over time and longer-term inflation expectations remain well anchored at 2 percent. The Committee expects to maintain an accommodative stance of monetary policy until these outcomes are achieved. The Committee decided to keep the target range for the federal funds rate at 0 to 1/4 percent and expects it will be appropriate to maintain this target range until labor market conditions have reached levels consistent with the Committee's assessments of maximum employment and inflation has risen to 2 percent and is on track to moderately exceed 2 percent for some time. Last December, the Committee indicated that it would continue to increase its holdings of Treasury securities by at least $80 billion per month and of agency mortgage-backed securities by at least $40 billion per month until substantial further progress has been made toward its maximum employment and price stability goals. Since then, the economy has made progress toward these goals, and the Committee will continue to assess progress in coming meetings. These asset purchases help foster smooth market functioning and accommodative financial conditions, thereby supporting the flow of credit to households and businesses.

In assessing the appropriate stance of monetary policy, the Committee will continue to monitor the implications of incoming information for the economic outlook. The Committee would be prepared to adjust the stance of monetary policy as appropriate if risks emerge that could impede the attainment of the Committee's goals. The Committee's assessments will take into account a wide range of information, including readings on public health, labor market conditions, inflation pressures and inflation expectations, and financial and international developments.

Voting for the monetary policy action were Jerome H. Powell, Chair; John C. Williams, Vice Chair; Thomas I. Barkin; Raphael W. Bostic; Michelle W. Bowman; Lael Brainard; Richard H. Clarida; Mary C. Daly; Charles L. Evans; Randal K. Quarles; and Christopher J. Waller.

## June 16, 2021

The Federal Reserve is committed to using its full range of tools to support the U.S. economy in this challenging time, thereby promoting its maximum employment and price stability goals.

Progress on vaccinations has reduced the spread of COVID-19 in the United States. Amid this progress and strong policy support, indicators of economic activity and employment have strengthened. The sectors most adversely affected by the pandemic remain weak but have shown improvement. Inflation has risen, largely reflecting transitory factors. Overall financial conditions remain accommodative, in part reflecting policy measures to support the economy and the flow of credit to U.S. households and businesses.

The path of the economy will depend significantly on the course of the virus. Progress on vaccinations will likely continue to reduce the effects of the public health crisis on the economy, but risks to the economic outlook remain.

The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. With inflation having run persistently below this longer-run goal, the Committee will aim to achieve inflation moderately above 2 percent for some time so that inflation averages 2 percent over time and longer-term inflation expectations remain well anchored at 2 percent. The Committee expects to maintain an accommodative stance of monetary policy until these outcomes are achieved. The Committee decided to keep the target range for the federal funds rate at 0 to 1/4 percent and expects it will be appropriate to maintain this target range until labor market conditions have reached levels consistent with the Committee's assessments of maximum employment and inflation has risen to 2 percent and is on track to moderately exceed 2 percent for some time. In addition, the Federal Reserve will continue to increase its holdings of Treasury securities by at least $80 billion per month and of agency mortgage-backed securities by at least $40 billion per month until substantial further progress has been made toward the Committee's maximum employment and price stability goals. These asset purchases help foster smooth market functioning and accommodative financial conditions, thereby supporting the flow of credit to households and businesses.

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# balanCD Rates

## Indicative CD Pricing as of 08/23/2021

### Fixed Rate Pricing

| TERM | UGGESTED TOTAL COS | | | TREASURY | LIBOR-SWAP |
|---|---|---|---|---|---|
| 3 MO | 0.10% | - | 0.15% | 0.05% | 0.13% |
| 4 MO | 0.10% | - | 0.15% | 0.05% | 0.14% |
| 6 MO | 0.15% | - | 0.20% | 0.04% | 0.15% |
| 9 MO | 0.15% | - | 0.20% | 0.05% | 0.16% |
| 1 YR | 0.15% | - | 0.25% | 0.06% | 0.17% |
| 15 MO | 0.20% | - | 0.30% | 0.09% | 0.20% |
| 18 MO | 0.25% | - | 0.35% | 0.15% | 0.24% |
| 2 YR | 0.30% | - | 0.45% | 0.23% | 0.32% |
| 30 MO | 0.40% | - | 0.55% | 0.34% | 0.43% |
| 3 YR | 0.45% | - | 0.60% | 0.45% | 0.55% |
| 42MO | 0.50% | - | 0.65% | 0.56% | 0.64% |
| 4 YR | 0.55% | - | 0.80% | 0.66% | 0.73% |
| 54 MO | 0.65% | - | 0.85% | 0.74% | 0.80% |
| 5 YR | 0.70% | - | 0.95% | 0.79% | 0.87% |
| 5.5 YR | 0.85% | - | 1.15% | 0.86% | 0.93% |
| 6YR | 1.00% | - | 1.25% | 0.94% | 0.99% |
| 7 YR | 1.10% | - | 1.30% | 1.06% | 1.08% |
| 8 YR | 1.35% | - | 1.50% | 1.12% | 1.16% |
| 9 YR | 1.45% | - | 1.55% | 1.21% | 1.22% |
| 10 YR | 1.55% | - | 1.65% | 1.27% | 1.28% |

*Above levels represent best efforts and are subject to change*

### Fixed Rate Callable

| TERM | UGGESTED TOTAL COST | | |
|---|---|---|---|
| 2 YR | 0.35% | - | 0.55% |
| 30 MO | 0.45% | - | 0.65% |
| 3 YR | 0.50% | - | 0.80% |
| 42 MO | 0.55% | - | 0.85% |
| 4 YR | 0.65% | - | 0.90% |
| 54 MO | 0.75% | - | 1.00% |
| 5 YR | 0.80% | - | 1.10% |
| 5.5 YR | 0.95% | - | 1.15% |
| 6 YR | 1.05% | - | 1.25% |
| 7 YR | 1.20% | - | 1.50% |
| 8 YR | 1.40% | - | 1.60% |
| 9 YR | 1.50% | - | 1.70% |
| 10 YR | 1.60% | - | 1.80% |
| 12 YR | 1.75% | - | 1.90% |
| 15 YR | 1.85% | - | 2.00% |
| 20 YR | 2.10% | - | 2.30% |
| 25 YR | 2.15% | - | 2.35% |
| 30 YR | 2.20% | - | 2.35% |

**Issuing bank holds the call option*
**Lock out periods vary and can be structured according to banks' needs*

### Step-Up Callable

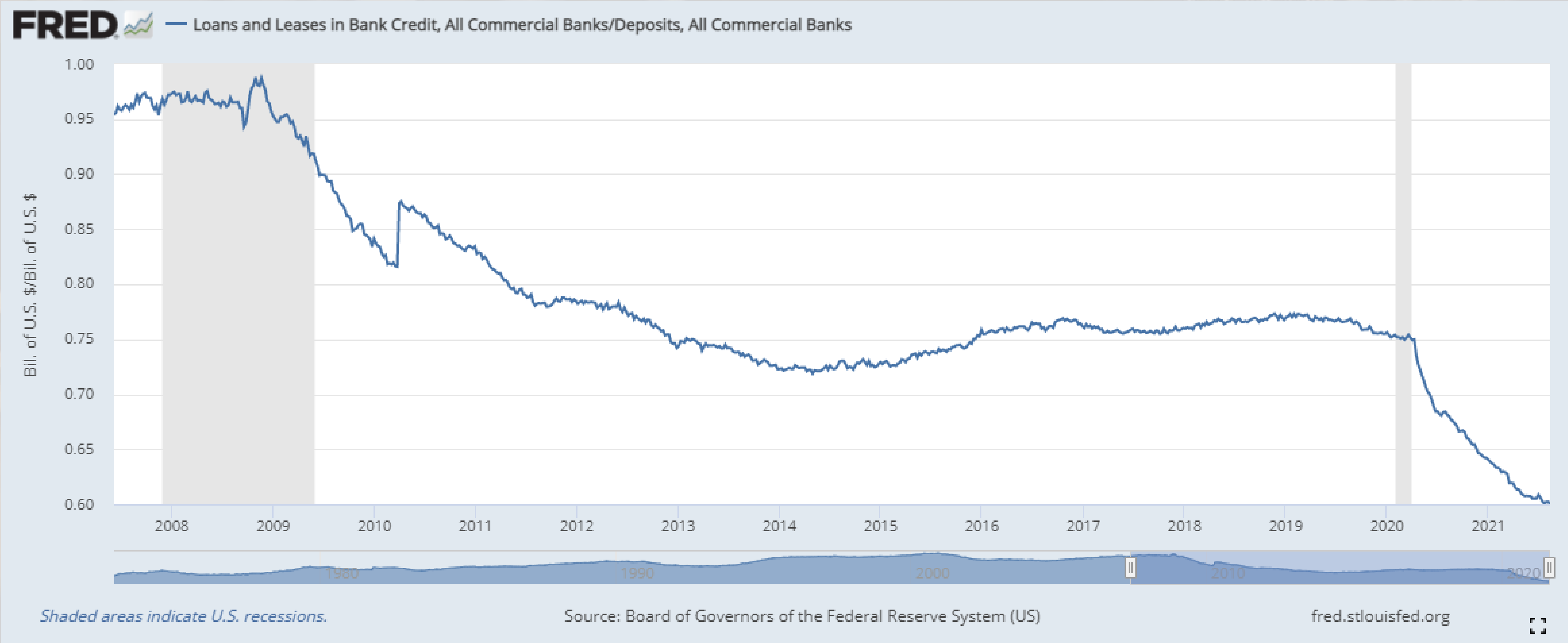
| 3 Year | |
|---|---|
| YR 1: | N/A |
| YR 2: | N/A |
| YR 3: | N/A |

| 4 Year | |
|---|---|
| YR 1: | N/A |
| YR 2: | N/A |
| YR 3: | N/A |
| YR 4: | N/A |

| 5 Year | |
|---|---|
| YR 1: | N/A |
| YR 2: | N/A |
| YR 3: | N/A |
| YR 4: | N/A |
| YR 5: | N/A |

*Indications only / Subject to change*

# Loan / Deposit Ratios Have Not Retreated

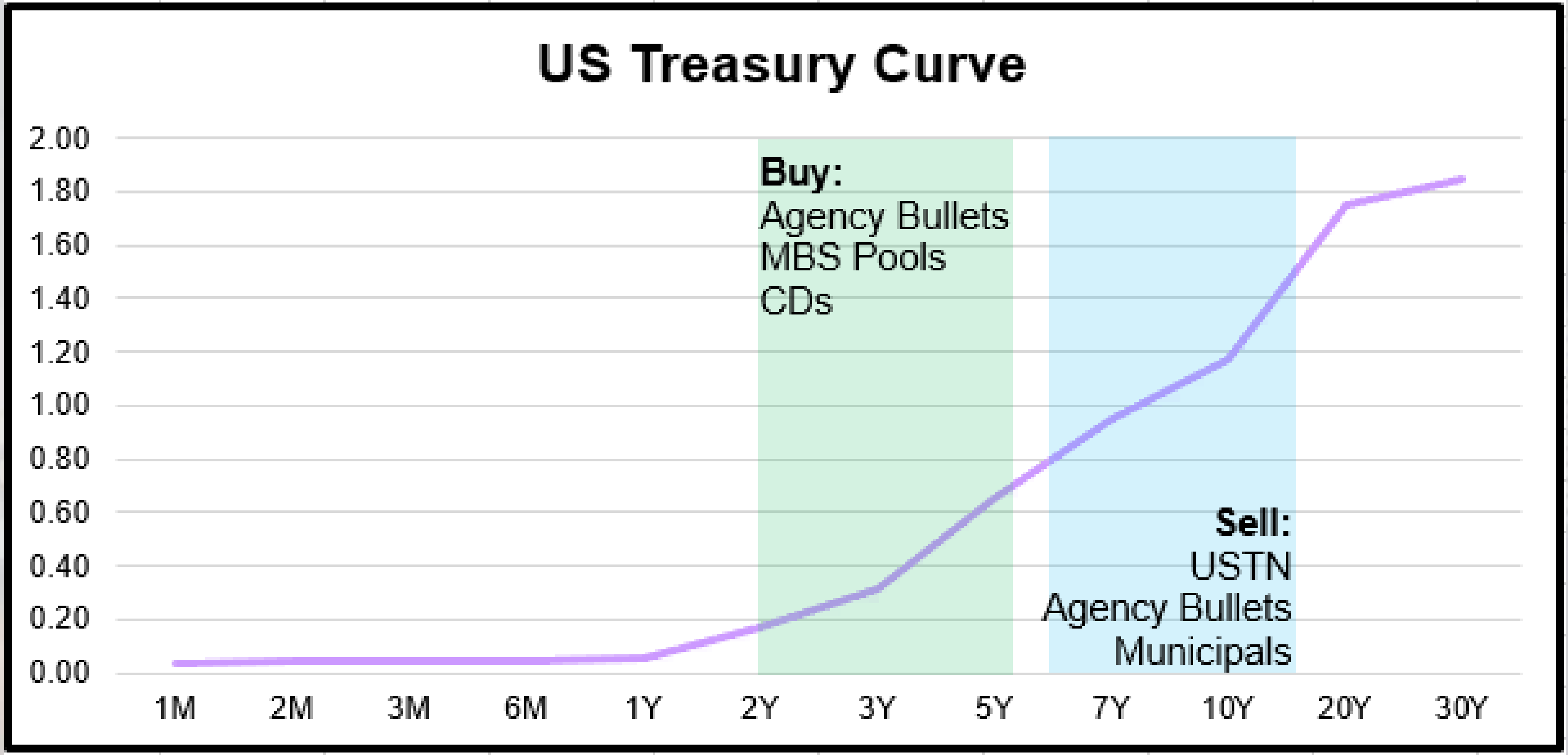


# Implementing / Revising Strategies

- Barbell
- Ladder
- Yield Targeting
- Duration Targeting

Important in any strategy: Credit Quality

# Opportunities Along the Curve




*Source: Bloomberg, L.P.*

# Yield Comparison

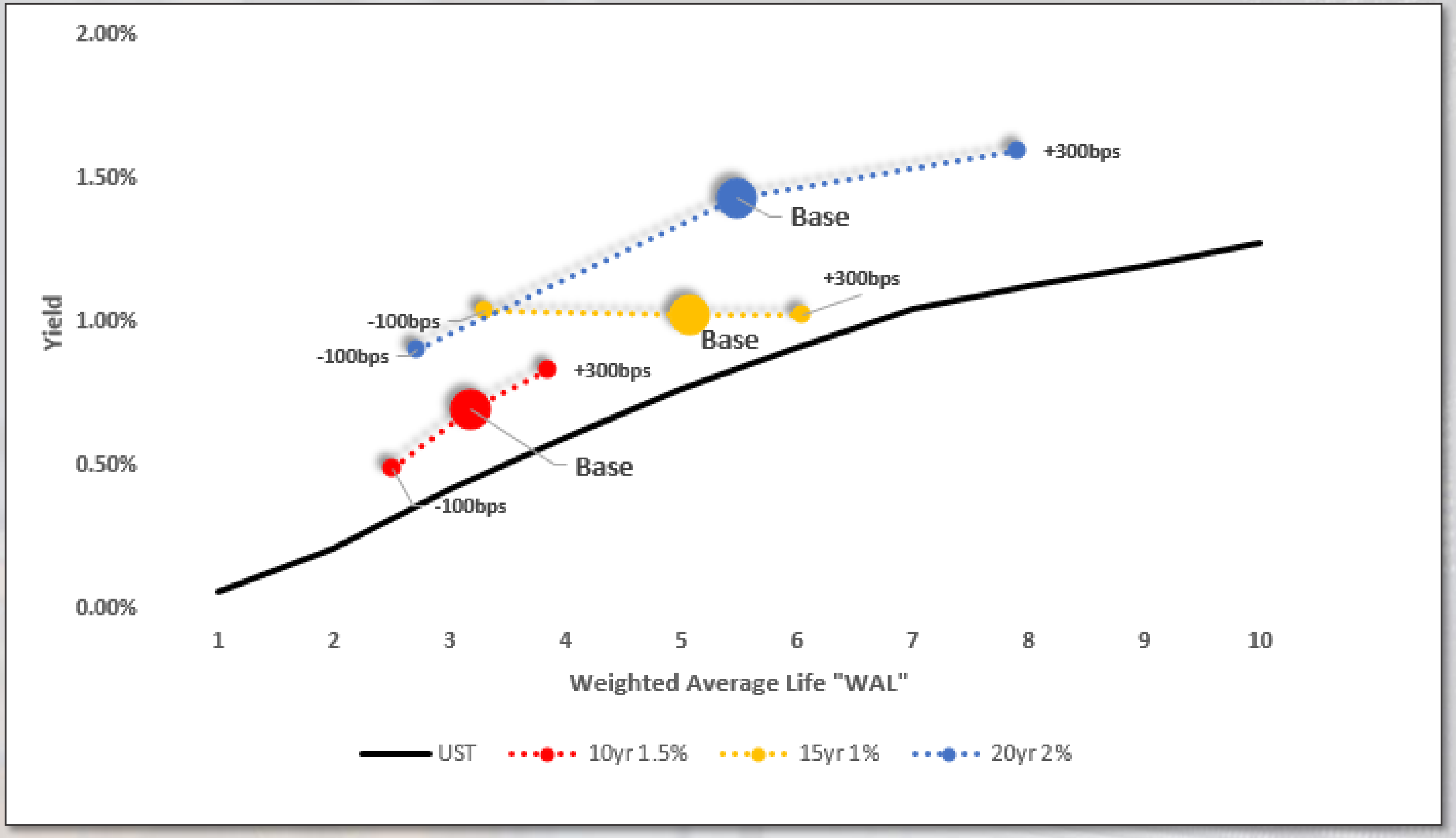
| Maturity | Treasuries | Agency Bullets | Discounted Callables | Current Coupon Callables (berm or am) | Current Coupon Callables (1X) |
|---|---|---|---|---|---|
| 2 Year | 0.17 | 0.19 | | 0.27 | |
| 3 Year | 0.41 | 0.41 | | 0.50 | |
| 4 Year | 0.60 | 0.61 | | 0.75 | |
| 5 Year | 0.75 | 0.77 | | 1.00 | |
| 7 Year | 1.03 | 1.09 | | 1.25 | |

*Source: Bloomberg, L.P.*

*Indications only / Subject to change*

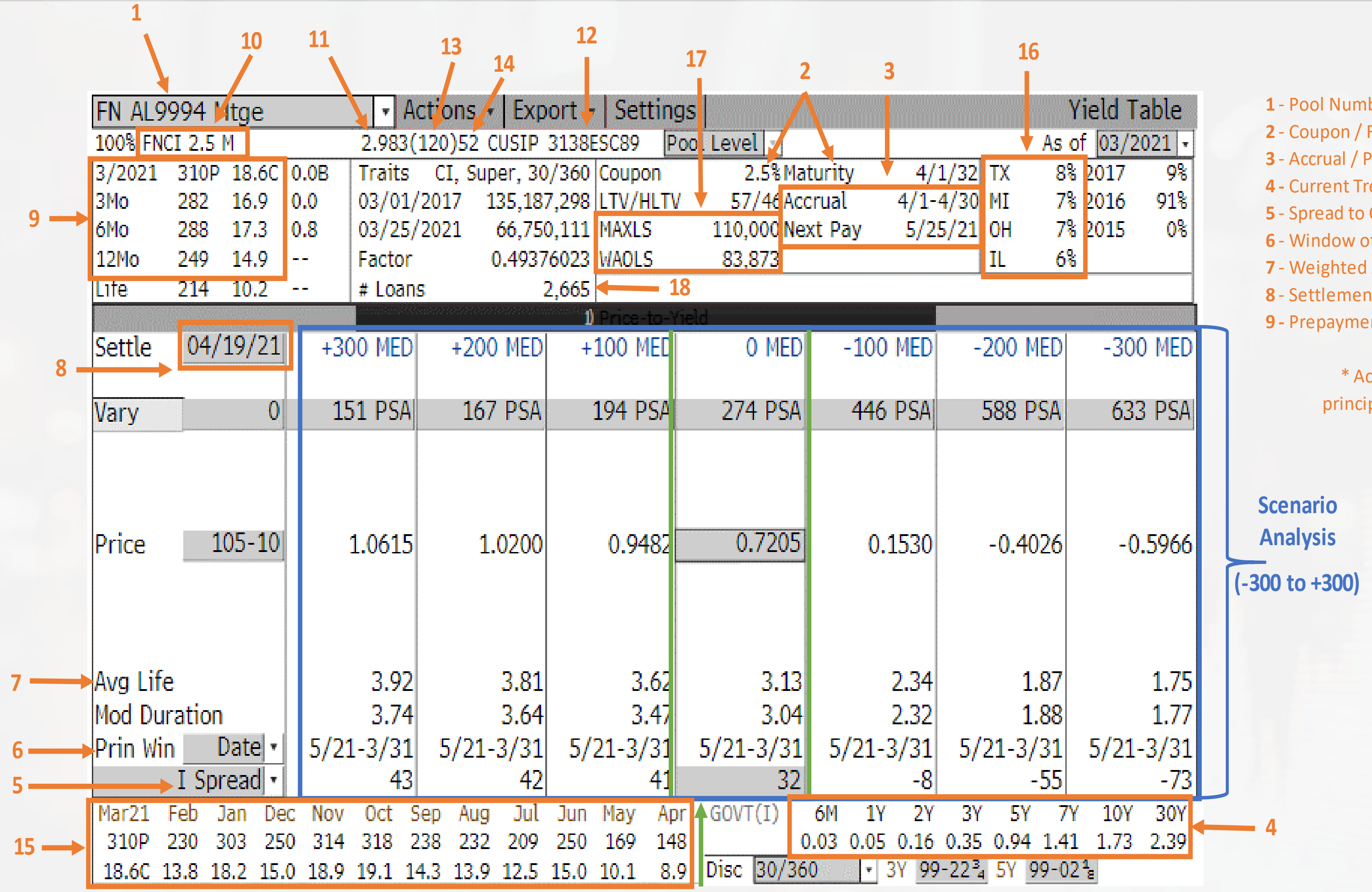
*Priced as of 8/24/21*

# MBS Sector Analysis




*Source: Bloomberg, L.P.*

# Components of a Yield Table



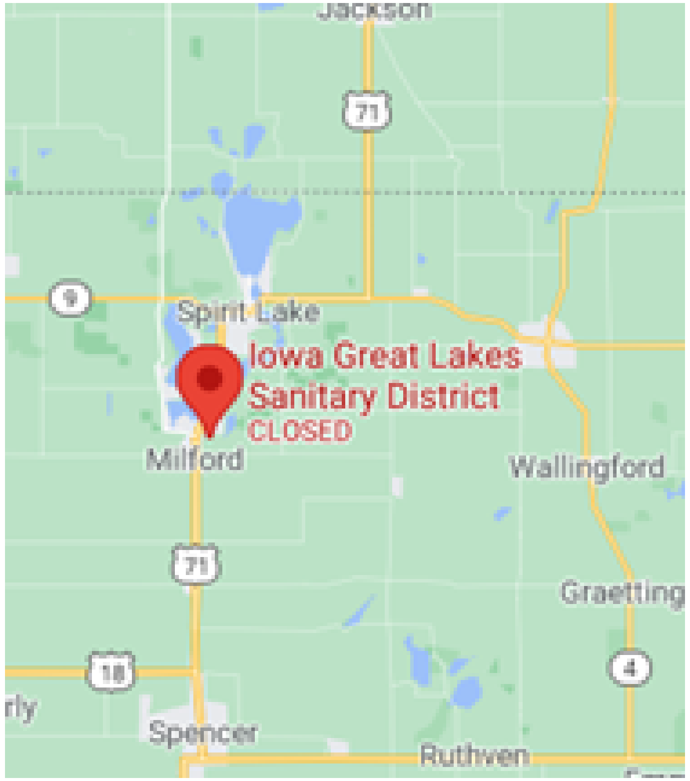

*Source for Screen: Bloomberg, L.P.*

Base Case Street Expecations

1 - Pool Number
2 - Coupon / Final Maturity
3 - Accrual / Payment Date*
4 - Current Treasury Curve
5 - Spread to Curve Type (MBS to "I": Interpolated Yield Curve)
6 - Window of Principal Payments (First & Last)
7 - Weighted Average Life (WAL)
8 - Settlement Date
9 - Prepayment History (Both PSA/CPR): 1, 3, 6, 12mo and Life
10 - Pool type / Collateral Type / Seasoning**
11 - Weighted Average Coupon (WAC)
12 - CUSIP
13 - Weighted Average Maturity (WAM)
14 - Weighted Average Loan Age (WALA)
15 - 12mo Historical Speeds (Both PSA/CPR)
16 - Collateral Distribution by State - Top 4
17 - Max Loan Size / Weighted Average Original Loan Size
18 - Number of Loans in Pool

* Accrual Date = current interest accrual period, Record Date - If owned on this date, owner receives next principal & interest payment, Next Pay - principal & interest payment date for current interest accruals period
** N (New <30 months), M (Moderate 30-60 months), S (Seasoned >60 months)

# Municipal Credit Checklist




**Iowa Great Lakes Sanitary District**

- ✓ Bank Qualified Unlimited General Obligation
- ✓ Aa2 Underlying Rating
- ✓ Actual Value: $4,469,085,809
- ✓ Assessed Value: $2,640,993,992
- ✓ Direct Debt to Actual: 0.43%
- ✓ Direct Debt to Assessed: 3.72%
- ✓ D&O Debt to Actual: 0.73%
- ✓ D&O Debt to Assessed: 2.20%
- ✓ Population: 12,000
- ✓ Direct Debt Per Capita: $1,614
- ✓ D&O Debt Per Capita: $8,192

# Comments from the trading desk

*"One thing I think people need to be out in front of is coupon drift. If rates do rise the average coupon on portfolio has drifted even lower and your MTM loss could be worse than 2018 cycle (pure mathematical standpoint with lower coupon, more price volume). Would try to keep options short on duration side or get something like kicker muni's if you are going to go out longer duration."*

*Look for positive risk reward convexity pools such as 15yr 1.5% 200k max loan size (minimal payup vs TBA but much better performance if rates were to fail vs generic collateral)*

***Tip: Make sure you are getting paid for premium risk.***
***Ex. 15yr 1.5% vs 15yr 2%.***
*The 2% coupon is actually projected at a lower yield than 15yr 1.5% and more premium on 15yr 2%.*

*"The last week has been a pretty quiet one in the market. The most talked about event is tapering and there are so many differing opinions. I will say one thing that I think was expected earlier but less so now was to have an announcement of something at Jackson Hole. I am in the camp that they will most likely push it off to next year but I think the consensus is now for sure not until the end of the year."*

***Municipal Market Facts:***

Cusips outstanding:
~1 million

Average daily trade volume:
~$12.4 billion

Average number of daily trades:
~33,000

Banks own 12% of municipal bonds.

**MUNI MARKET THEN & NOW**

In 1945, there was less than $20 billion of municipal debt outstanding.
In 1960, there was $66 billion of municipal debt outstanding.
In 1981, there was $361 billion of municipal debt outstanding.
Today, investors hold approximately $3.9 trillion of municipal debt.

I’m so sorry I’m late, the traffic was crazy…

The traffic:

"Sometimes I just want it to stop. Talk of COVID, looting, brutality. I lose my way. I become convinced that this "new normal" is real life. Then I meet an 87-year-old who talks of living through polio, diphtheria, Vietnam protests and yet is still enchanted with life.

He seemed surprised when I said that 2020 must be especially challenging for him. "No," he said slowly, looking me straight in the eyes. "I learned a long time ago to not see the world through the printed headlines, I see the world through the people that surround me. I see the world with the realization that we love big. Therefore, I just choose to write my own headlines:

"Husband loves wife today." "Family drops everything to come to Grandma's bedside." He patted my hand. "Old man makes new friend."

His words collide with my worries, freeing them from the tether I had been holding tight. They float away. I am left with a renewed spirit and a new way to write my own headlines."

Story by Andy Stanley.

# Thank You

## for Participating!

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