INVESTMENT COMMENTARY

The economic data continues to be negative in the third quarter with U.S. Gross Domestic Product having shrunk by 31.4% and the most recent Unemployment Rate at 8.4%, but the markets continue to focus on unprecedented Fiscal and Monetary relief. According to the Committee for a Responsible Federal Budget, the combined Administrative, Legislative and Federal Reserve Actions have created approximately $5 Trillion in Disbursed/Committed stimulus year to date. The Federal Reserve is now looking to expand beyond their unprecedented stimulus and market measures to the more difficult task of lowering unemployment and increasing inflation at a rate of 2 percent over the longer run. However, economic and market turbulence is likely to continue if the Covid-19 Coronavirus follows the path of the cold and flu season, where less daylight combined with a shift from outdoor to indoor activities leads to spikes in the number of infected cases.

Despite continued economic and stock market turbulence, Treasury yields continued to stay within a tight trading range during the third quarter. The yield on the 2-year Treasury declined by 2 basis points to 0.13%, while 10-year Treasury yields increased by 2 basis points to 0.68%. The muted interest rate moves led to a relatively flat (+0.17%) Treasury sector quarterly return. However, most spread sectors outperformed, as investment grade corporate bonds returned (+1.54%) for the quarter, while high yield bonds returned (+4.60%). In the investment grade market, U.S. Agency Securities (+0.55%), Commercial MBS (+1.71%) and Asset-backed Securities (+0.79%) all outperformed Treasuries. The laggard for the quarter was Mortgage-backed Securities (+0.11%), which trailed all other sector returns for the quarter.

Finally, we've rounded the third quarter and we're in the 2020 home stretch. With two solid quarters of historic fiscal and monetary relief at our backs, seemingly all that stands between U.S. and the 2020 finish line is the flu season, a potential second COVID wave and a hotly contested presidential election that may extend well beyond election day in early November. While the U.S. economy continues to recover, the pace and timeline of a full recovery appears increasingly unclear. Labor markets continue to improve but on a declining basis as the month over month trend is incrementally fewer jobs. While the unemployment rate continued to drop during the quarter, a growing number of people are leaving the work force and permanent job losses have risen to 2.5 million since February. Retail sales have also recovered rapidly, as consumers quickly adapted to shopping online, while non-store sales have grown more than 22% year over year. However, the U.S. economy is service-centric, which drives 66% of consumer spending and continues to be hampered by the pandemic. While market prognosticators are divided regarding the potential economic impact of a "blue wave" and which presidential candidate will prove better for our markets and the overall economy, there is universal consensus that a COVID-19 vaccine is essential to a healthy economy and a return to normalcy. Both consumer and market sentiment has pinned their hopes on the timely delivery of an effective vaccine and additional monetary/fiscal relief. The level of economic uncertainty remains unprecedented, which we believe is why the National Bureau of Economic Research (NBER) has held off from marking an end to the pandemic recession.

PIA remains cautious as we navigate this election cycle and year-end. The Fed's Secondary Market Corporate Credit Facility (SMCCF) provides a $250 billion backstop; however, to date the Fed has only utilized roughly $13 billion. Conventional wisdom would suggest both political parties would be more than willing to provide additional COVID relief this close to an election, yet another pre-election relief package seems remote, while the timing and delivery of COVID therapeutics and/or vaccines is anything but predictable. Lastly, we're growing increasingly cautious regarding the long-term effects of near-term decision-making.

In the third quarter, PIA portfolio duration remained short relative to our respective benchmarks, while the yield on the 10-year Treasury remained range-bound between 0.50%-0.75%. Following the Fed's outlook for near-zero short-term rates through 2022 and their seemingly unlimited commitment to purchase corporate bonds in the secondary market, we capitalized on the Fed's backstop for risk assets and the improved relative value in the credit market by adding to our BBB credit weighting. We currently maintain an overweight in corporate credit and continue to focus on high quality credits with strong balance sheets. Our Industrial credits provide incremental risk-adjusted yield and our Financials are senior domestic debt that we believe offer attractive compensation for their sector volatility. We modestly increased our high yield exposure in our Core Plus portfolios, as spreads continue to offer attractive risk-adjusted valuation. The Fixed Rate MBS sector posted a negative excess return during the 3rd quarter, as mortgage origination remained extremely high given the low rate environment, outpacing demand despite the Feds continued monthly MBS purchase program. We maintain a modest overweight to Agency Mortgage-backed Securities, as we believe the MBS sector offers long-term value on a risk-adjusted basis.

PIA Investment Strategy Group

KEY RATES

	9/30/20	6/30/20	12/31/19
Fed Funds Target Rate	0.0-0.25%	0.0-0.25%	1.5-1.75%
3 Month LIBOR	0.23	0.30	1.91
On-the-run Treasuries:			
3 Months	0.09	0.13	1.54
6 Months	0.10	0.13	1.58
2 Years	0.13	0.15	1.57
5 Years	0.28	0.29	1.69
10 Years	0.68	0.66	1.92
30 Years	1.46	1.41	2.39

Source: Bloomberg

KEY ECONOMIC INDICATORS

as of	9/30/20	9/30/19
U.S. $ (DXY)	93.89	99.38
Oil	40.22	54.07
Gold	1,885.82	1,472.39
CRB	148.51	173.94
GDP	-31.4	2.0
CPI	1.3	1.7
Core (Ex - Food & Energy)	1.6	1.8
Unemployment Rate	8.4	3.7
Consumer Confidence	101.80	125.10
S&P/Case-Shiller – Comp-20	3.95	2.00

Source: Bloomberg

INDEX RETURNS

	3Q'20	YTD	1-Year
Bloomberg Barclays –			
Universal	0.99%	6.20%	6.68%
Aggregate	0.62	6.79	6.98
Aggregate ex-credit	0.21	6.75	6.55
Gov-Credit	0.78	8.04	8.03
Int. Gov-Credit	0.61	5.92	6.32
Corporate	1.54	6.64	7.90
Treasury only	0.17	8.90	8.04
1-3 year Gov	0.10	3.09	3.62
BofA Merrill – 1-yr T-Note	0.08	1.77	2.37
High Yield	4.60	0.62	3.25
International Debt	4.14	4.77	5.48
Emerging Markets Debt	2.37	1.93	4.06
S&P 500	8.93	5.57	15.14
DJIA	8.22	-0.91	5.70
NASDAQ 100	12.62	31.65	48.75
MSCI EAFE	4.87	-6.69	0.99

Source: Bloomberg Barclays

SECTOR RETURNS

3Q'20	Total Return	Excess Return
U.S. Treasuries	0.17%	0.00%
Government-related U.S. Agency	1.06	0.90
Government-related Credit	1.27	1.11
Corporate	1.54	1.40
Corporate Financials	1.41	1.24
Corporate Industrials	1.63	1.50
Corporate Utilities	1.38	1.28
Corporate AAA-rated	1.09	1.03
Corporate AA-rated	0.82	0.73
Corporate A-rated	1.13	1.00
Corporate BBB-rated	2.00	1.86
Corporate High-Yield	4.60	4.38
Securitized	0.24	0.05
Mortgage-backed Securities-FR	0.11	-0.07
CMBS	1.71	1.48
ABS	0.79	0.65

Source: Bloomberg Barclays

Pacific Income Advisers, Inc. (PIA) is an autonomous investment management firm registered under the Investment Advisers Act of 1940. PIA manages a variety of fixed income and equity assets for primarily United States clients.

BENCHMARK DESCRIPTION

Bloomberg Barclays U.S. Universal Index represents the union of the U.S. Aggregate Index, U.S. Corporate High-Yield Index, Investment-Grade 144A Index, Eurodollar Index, U.S. Emerging Markets Index, and the non-ERISA eligible portion of the CMBS Index. The index covers USD-denominated, taxable bonds that are rated either investment-grade or below investment-grade. Some U.S. Universal Index constituents may be eligible for one or more of its contributing subcomponents that are not mutually exclusive. These securities are not double-counted in the index. You can not invest directly in an index.

Bloomberg Barclays U.S. Aggregate Bond Index is an unmanaged index that covers the investment grade fixed rate bond market with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities. The issues must be rated investment grade, be publicly traded, and meet certain maturity and issue size requirements. You can not invest directly in an index.

Bloomberg Barclays U.S. Aggregate Ex-Credit Index (LB Agg (Ex-Credit)) The index covers the U.S. investment grade fixed rate bond market, with index components for government, mortgage pass-through securities, and asset-backed securities. These major sectors are subdivided into more specific indices that are calculated and reported on a regular basis. You can not invest directly in an index.

Bloomberg Barclays U.S. Government/Credit Bond Index includes securities in the Government and Credit Indices. The Government Index includes treasuries (i.e., public obligations of the U.S. Treasury that have remaining maturities of more than one year) and agencies (i.e., publicly issued debt of U.S. Government agencies, quasi-federal corporations, and corporate or foreign debt guaranteed by the U.S. Government). The Credit Index includes publicly issued U.S. corporate and foreign debentures and secured notes that meet specified maturity, liquidity, and quality requirements. You can not invest directly in an index.

Bloomberg Barclays U.S. Intermediate Government/Credit Bond Index is the Intermediate component of the U.S. Government/Credit index. The Government/Credit Index includes securities in the Government and Credit Indices. The Government Index includes treasuries (i.e., public obligations of the U.S. Treasury that have remaining maturities of more than one year) and agencies (i.e., publicly issued debt of U.S. Government agencies, quasi-federal corporations, and corporate or foreign debt guaranteed by the U.S. Government). The Credit Index includes publicly issued U.S. corporate and foreign debentures and secured notes that meet specified maturity, liquidity, and quality requirements. You can not invest directly in an index.

Bloomberg Barclays U.S. 1-3 Year Government Bond Index consist of securities in the U.S. Government Index with a maturity from 1 up to (but not including) 3 years. Securities issued by the U.S. Government (i.e., securities in the Treasury and Agency Indices). Inclusions: Public obligations of the U.S. Treasury with a remaining maturity of one year or more. Publicly issued debt of U.S. Government agencies, quasi-federal corporations, and corporate or foreign debt guaranteed by the U.S. Government. You can not invest directly in an index.

Bloomberg Barclays U.S. Treasury Index includes public obligations of the U.S. Treasury. Treasury bills are excluded by the maturity constraint but are part of a separate Short Treasury Index. In addition, certain special issues, such as state and local government series bonds (SLGs), as well as U.S. Treasury TIPS, are excluded. STRIPS are excluded from the index because their inclusion would result in double-counting. Securities in the Index roll up to the U.S. Aggregate, U.S. Universal, and Global Aggregate Indices. You can not invest directly in an index.

Bloomberg Barclays U.S. Corporate Bond Index covers USD-denominated, investment-grade, fixed-rate, taxable securities sold by industrial, utility, and financial issuers. It includes publicly issued U.S. corporate debentures and secured notes that meet specific maturity, liquidity, and quality requirements. Securities in the index roll up to the U.S. Credit and U.S. Aggregate indices. The U.S. Corporate Index was launched on January 1, 1973. You can not invest directly in an index.

BofA Merrill Lynch 1-Year US Treasury Note Index is comprised of a single issue purchased at the beginning of the month and held for a full month. At the end of the month that issue is sold and rolled into a newly selected issue. The issue selected at each month-end rebalancing is the outstanding Treasury note that matures closest to, but not beyond, one year from the rebalancing date. To qualify for selection, an issue must have settled on or before the month-end rebalancing date. You can not invest directly in an index.

Bloomberg Barclays Corporate U.S. High Yield Index - covers the universe of fixed rate, non-investment grade debt. Eurobonds and debt issues from countries designated as emerging markets (e.g., Argentina, Brazil, Venezuela, etc.) are excluded, but Canadian and global bonds (SEC registered) of issuers in non-EMG countries are included. Original issue zeroes, step-up coupon structures, 144-As and pay-in-kind bonds (PIKs, as of October 1, 2009) are also included. The index includes both corporate and non-corporate sectors. The corporate sectors are Industrial, Utility, and Finance, which include both U.S. and non-U.S. corporations. The Yankee sector has been discontinued as of 7/1/00. The bonds in the former Yankee sector have not been removed from the index, but have been reclassified into other sectors. You cannot invest directly in an index.

Bloomberg Barclays Global Aggregate Index provides a broad-based measure of the global investment-grade fixed-rate debt markets. The Global Aggregate Index contains three major components: the U.S. Aggregate Index (USD 300 million), the Pan-European Aggregate Index (EUR 300 million), and the Asian-Pacific Aggregate Index (JPY 35 billion). In addition to securities from these three benchmarks (94.4% of the overall Global Aggregate market value), the Global Aggregate Index includes Global Treasury, Eurodollar (USD 300 million), Euro-Yen (JPY 35 billion), Canadian (CAD 300 million), and Investment-Grade 144A (USD 300 million) index-eligible securities not already in the three regional aggregate indices. The Global Aggregate Index family includes a wide range of standard and customized subindices by liquidity constraint, sector, quality, and maturity. The Global Aggregate Index is a component of the Multiverse Index. You can not invest directly in an index.

Bloomberg Barclays Global Emerging Markets Index consists of the fixed and floating-rate USD-denominated U.S. Emerging Markets Index and the primarily EUR and GBP-denominated fixed-rate Pan-European Emerging Markets Index and includes emerging markets debt from the following regions: Americas, Europe, Asia, Middle East, and Africa. For the index, an emerging market is defined as any country that has a long term foreign currency debt sovereign rating of Baa1/BBB+/BBB+ or below using the middle rating of Moody's, S&P, and Fitch. The index does not overlap with the U.S. Corporate High-Yield Index or the Pan Euro Corporate High-Yield Index, but may overlap with other investment-grade Aggregate Indices if the securities meet their index eligibility rules. You can not invest directly in an index.

S&P 500 Index – The S&P 500 index includes 500 leading companies in leading industries of the U.S. economy. The S&P 500 is designed to be a leading indicator of U.S. equities and is meant to reflect the risk/return characteristics of the large cap universe. You can not invest directly in an index.

The NASDAQ-100 Index is a modified capitalization-weighted index of the 100 largest and most active non-financial domestic and international issues listed on the NASDAQ. No security can have more than a 24% weighting. The index was developed with a base value of 125 as of February1, 1985. Prior to December 21, 1998 the Nasdaq 100 was a cap-weighted index. You can not invest directly in an index.

The Dow Jones Industrial Average (DJIA) is an index used to measure the performance of the U.S. financial markets. Introduced on May 26, 1896 by Charles H. Dow, it is the oldest stock price measure in continuous use. Over the past century "the Dow" has become the most widely recognized stock market indication in the U.S. and probably in the entire world. Most of the stocks included in the index are listed on the New York Stock Exchange, and are all large blue-chip companies that reflect the health of the U.S. economy. All but a handful of these have major business operations throughout the world, thus providing some insight into the economic well-being of the global economy. You can not invest directly in an index.

MSCI EAFE Index is a capitalization weighted index that monitors the performance of stocks from Europe, Australiasia, and the Far East. You can not invest directly in an index.

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