GALLIARD
Capital Management, Inc.

ARCHITECTS OF INVESTMENT SOLUTIONS

3rd Quarter 2020

Even with all of the inherent volatility in the markets and the world in general, it was a busy and productive 3rd quarter at Galliard:

- We marked an all-time high for Assets Under Management at the Firm
- Many of our fixed income portfolios (and corresponding composites) are posting performance track records, relative to their benchmarks, on pace as one of the best years in the history of the firm
- Many of our staff participated in our COVID friendly community service Month of Action, which included an emphasis this year on performing acts of kindness to support one another and our planet

We are optimistic that the economy will continue to recover and make progress into the end of the year. We also must continue to keep an eye on the future, and in the fixed income markets, that means keeping tabs on what the Federal Reserve is thinking (and doing) about rates. Below, you will find a few thoughts from our team on what may be in store. As we enter the fall season, we hope you and your colleagues are doing as well as can be hoped as we continue to work through this pandemic together. If there is anything we can help with, please don't hesitate to call.

Ajay Mirza, Mike Norman, and Andrew Owen

Senior Managing Principals

Some thoughts on the Federal Reserve, interest rates, and what's to come

The Federal Reserve continues to provide an unprecedented level of monetary support. Since cutting the policy rate to zero and enacting unlimited QE in March, the Federal Reserve has purchased ~$2.0 trillion in Treasury securities and ~$1.1 trillion in Agency MBS (gross of paydowns). In contrast, the additional Fed credit facilities targeting money markets, corporate bonds, asset securitizations, and municipal bonds have largely gone unutilized.

As expected, the Fed kept rates unchanged at its June and September meetings, while published forecasts indicate that Fed members universally agree that policy rates will remain near zero for at least the next several years. Indeed, in his Congressional testimony in September, Chairman Jerome Powell reiterated that the central bank will continue to provide support "for as long as it takes, to ensure the recovery will be as strong as possible, and to limit lasting damage to the economy." In August, the Fed also announced a change to the Flexible Average Inflation Targeting (FAIT) policy framework. The new regime gives the Fed flexibility to allow inflation to overshoot its 2.00% target for a time so that "average" inflation will be ~2.00%. Notably, this change was NOT in response to the pandemic but rather the result of an ongoing policy review. Nevertheless, the new framework provides the Fed with extra breathing room to keep policy rates lower for longer.

Interest rates were practically unchanged between June and September, with 10-year and 30-year Treasury rates ending the quarter at 0.68% and 1.45% respectively. With the aforementioned Fed policies in place, the short-end of the curve is anchored at ~0.15% out to 3-years. After reading negative for most of 2Q, headline and core CPI have rebounded nicely with both measures coming in a 0.6% m/m in July followed by 0.4% m/m in August. Measured year-over-year at 1.3% and 1.7%, headline and core CPI are not yet back to pre-pandemic levels. Despite the aforementioned Fed commitment, the market continues to price in subdued inflation expectations for the foreseeable future with 5-year and 10-year breakeven inflation rates ending the quarter at 1.49% and 1.63%.