Economic and Market Update

San Mateo County Transportation Authority

June 2, 2022

Macroeconomic Themes

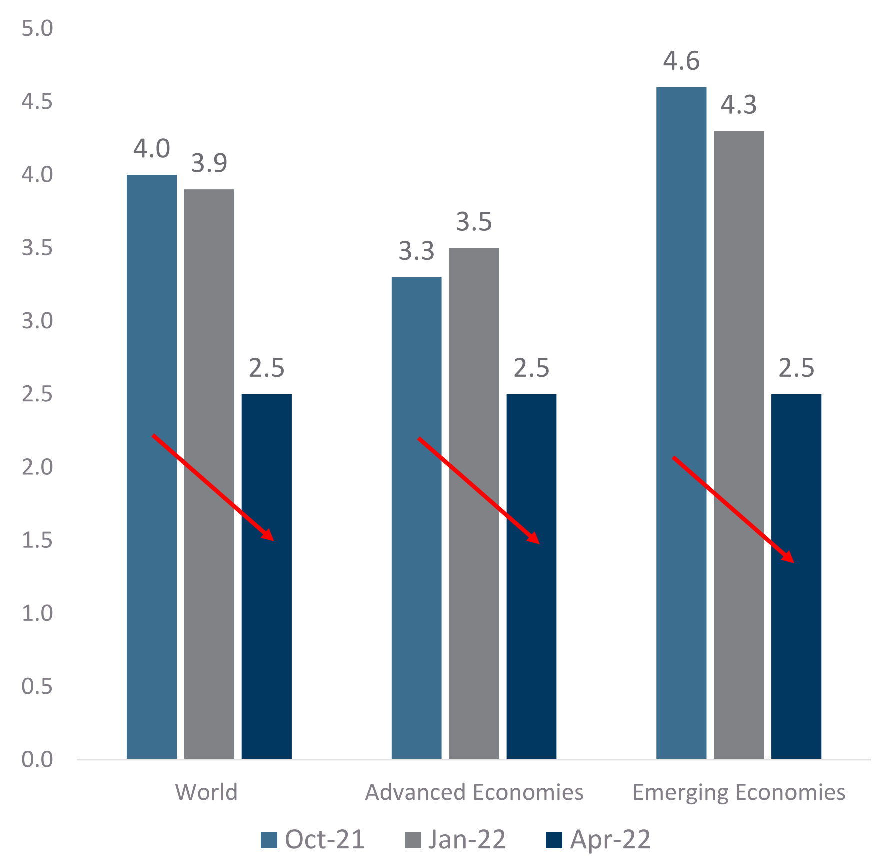
Ukraine Conflict

Persistent Inflation

Recession or Soft Landing

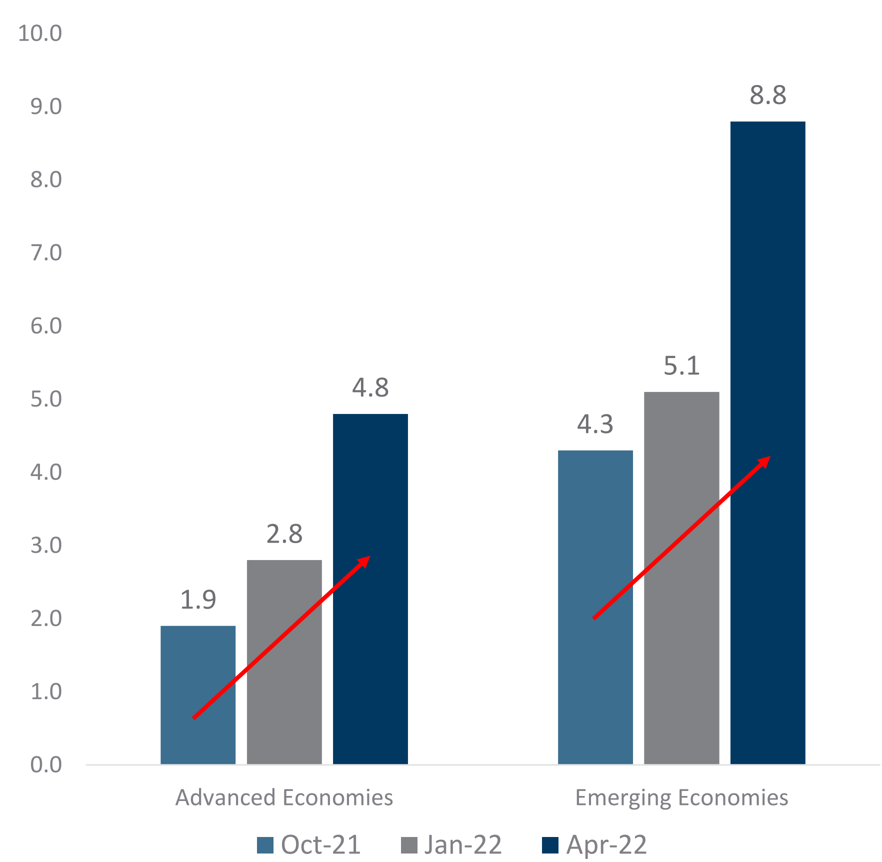
Global Growth: IMF's Updated Forecasts Highlight Stagflationary Impact of Russia-Ukraine Conflict

IMF Slashes Growth Forecasts for 2022



The International Monetary Fund forecasts that the economic damage caused by Russia's invasion of Ukraine will lead to a significant slowdown in global growth in 2022.

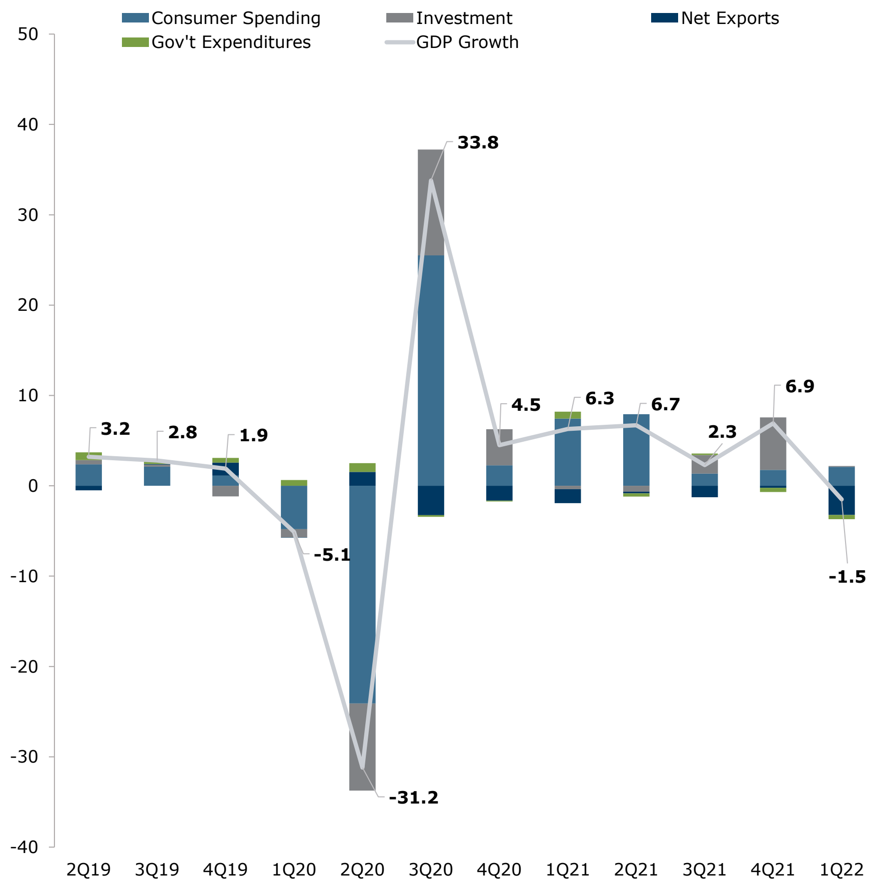
IMF Intensifies Inflation Forecasts for 2022



Meanwhile, global inflation is expected to accelerate notably as the western nations wean themselves from Russian oil and gas resulting in an energy supply shock on top of still-strained global supply chains.

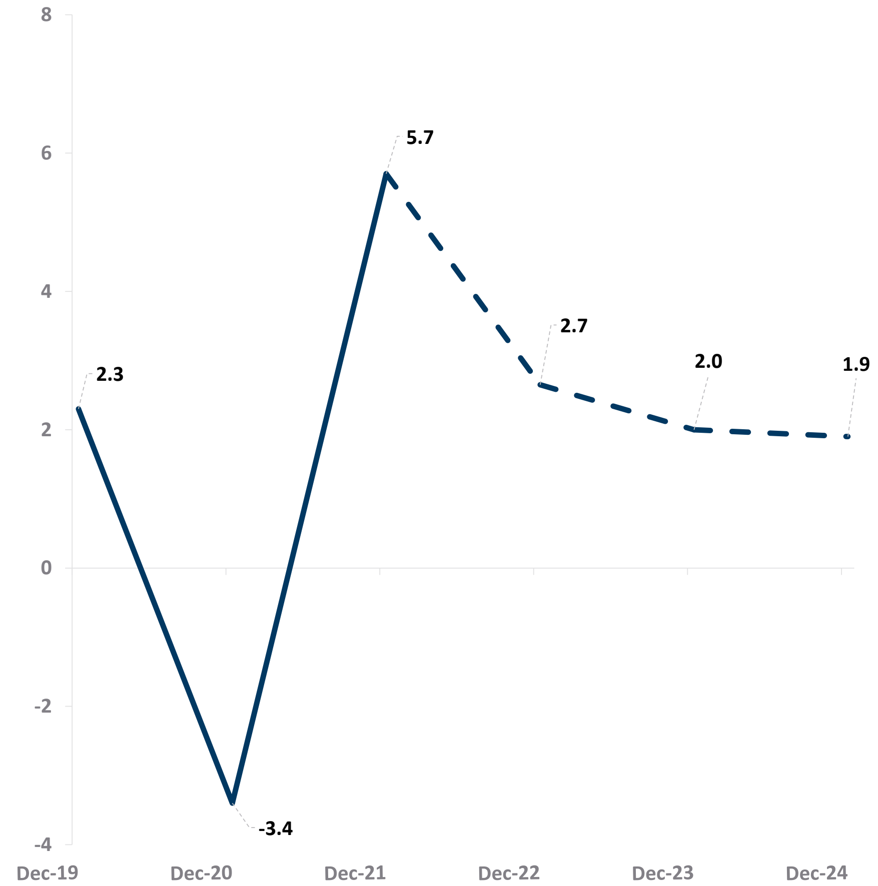
Domestic Growth: U.S. Economy Posts Surprise Contraction in First Quarter

U.S. GDP Unexpectedly Fell in Q1 but Underlying Expansion Continues



The decline in Q1 GDP overstates current economic fragility as a jump in net imports and slower inventory accumulation subtracted nearly 4% from headline growth while measures of domestic consumption remain resilient.

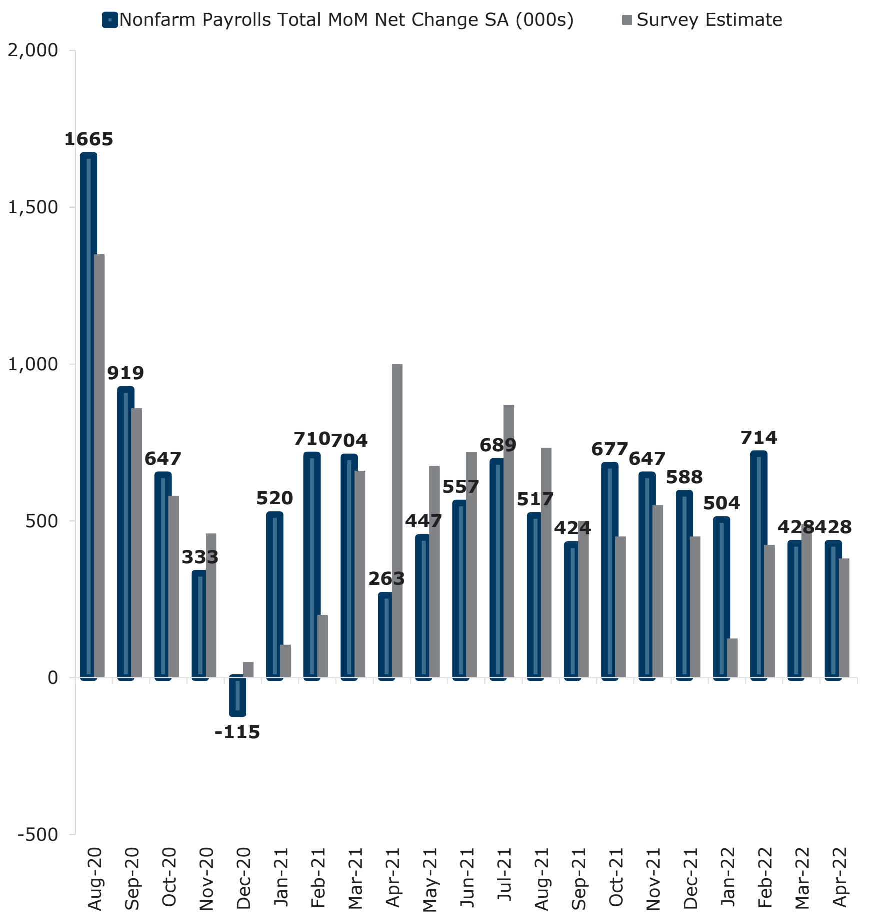
Bloomberg Real GDP Growth Estimates Moderate in Years Ahead



Despite the strong showing in 2021, U.S. GDP growth is expected to moderate in the years ahead as monetary and fiscal stimulus fades and elevated inflation weighs on consumer spending.

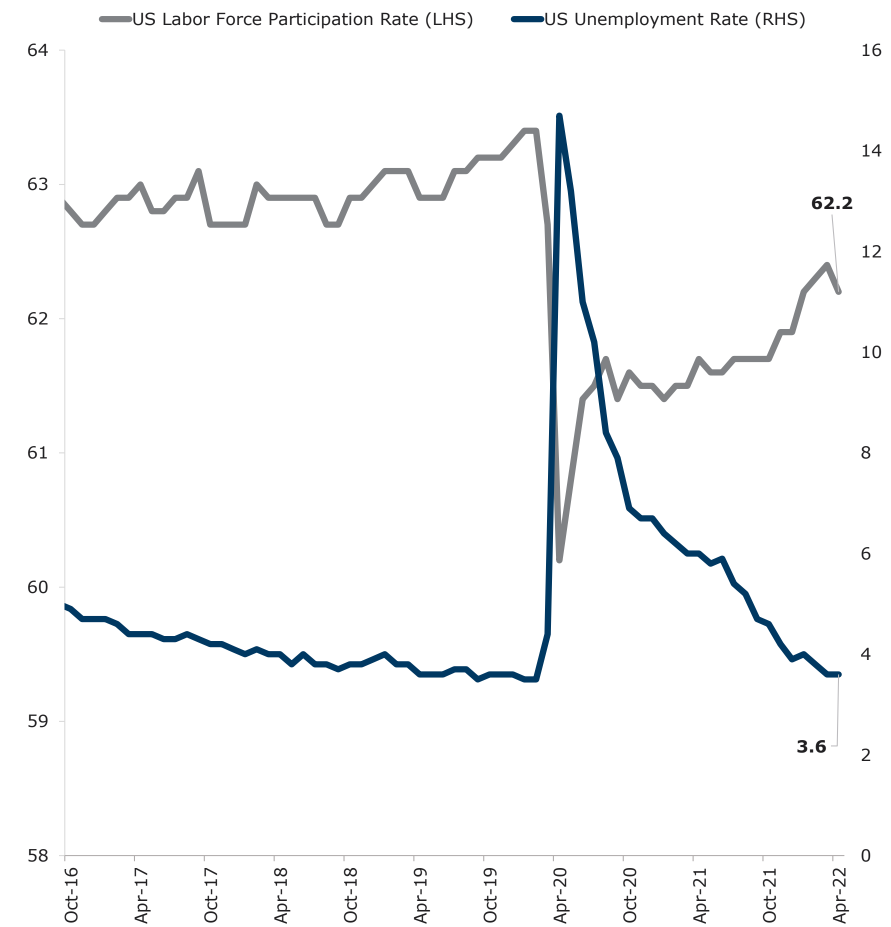
Labor Markets: Continued Job Gains Pave Way for Further Fed Rate Hikes

Tight Labor Market Conditions as Inflation Surges Support Rate Hikes



The pace of recovery in labor markets remains robust as tight labor market conditions, rising wage pressures, and surging inflation support expectations for higher rates in 2022.

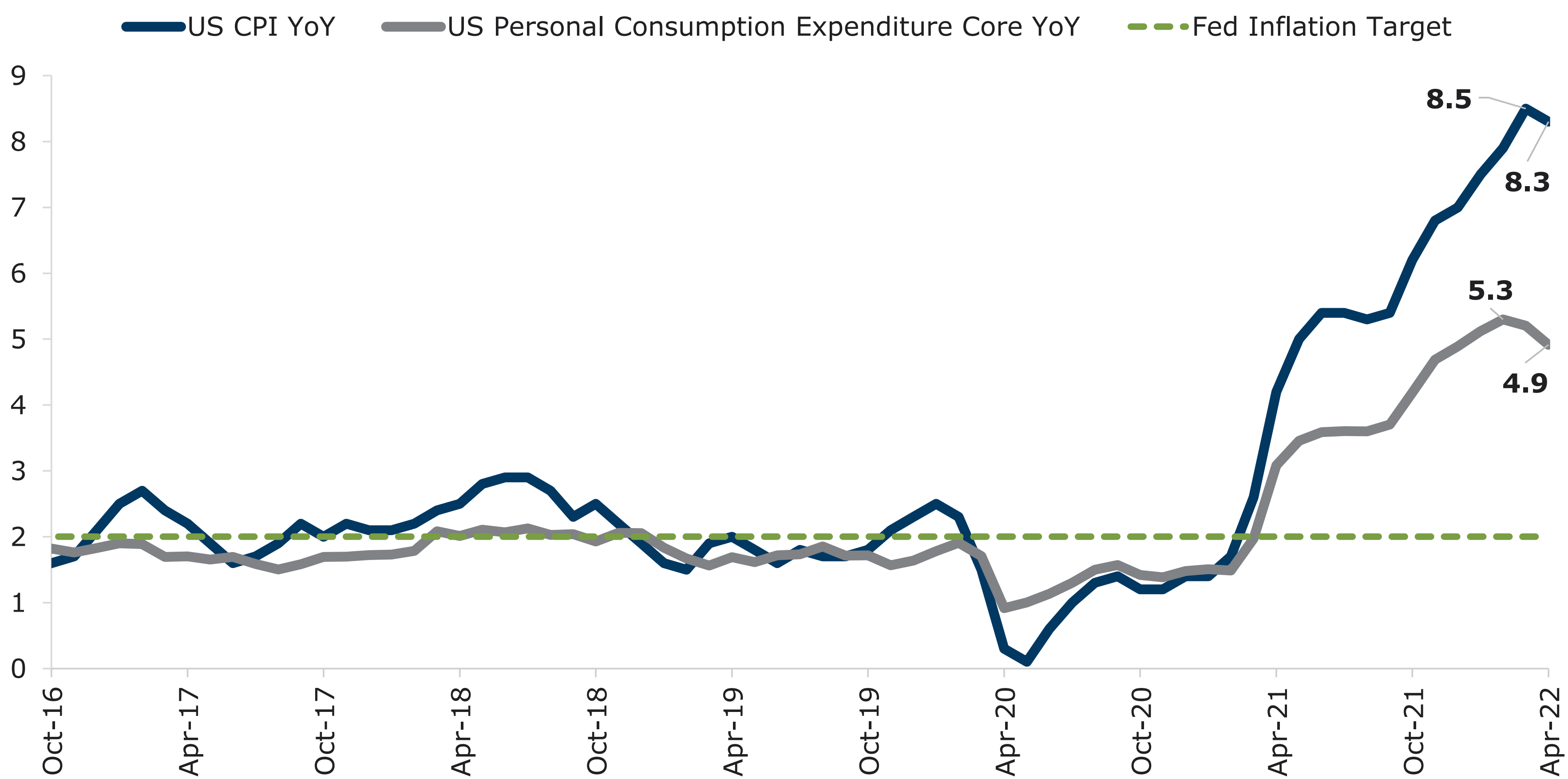
The Unemployment Rate Continues to Decline as Participation Rises



While the economy continues to recover jobs at a robust pace, the labor force participation rate continues to lag representing a headwind to a stronger recovery and underpinning wages and broader inflation pressures.

Inflation: Consumer Prices Surge at the Fastest Pace in 40 Years

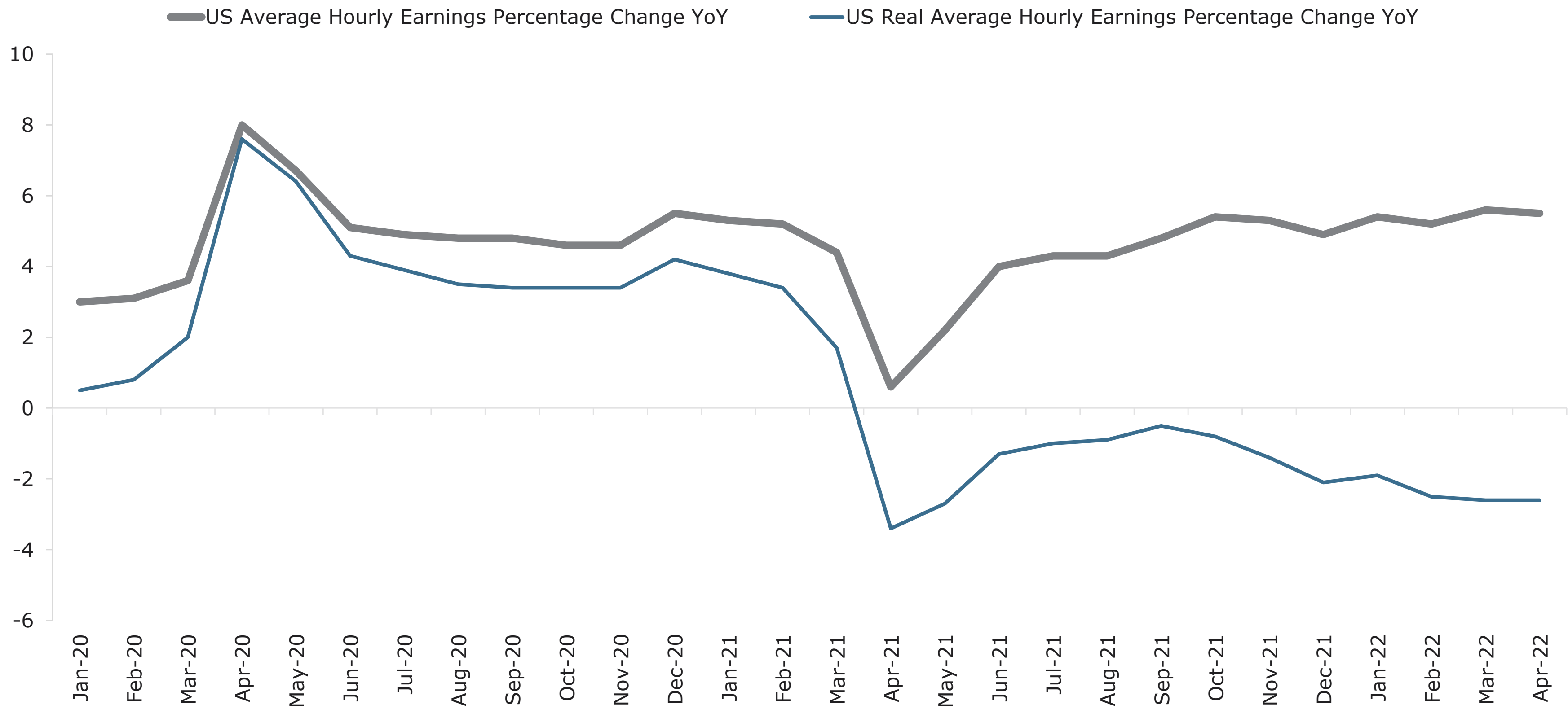
Inflation Has Proven More Persistent than the Federal Reserve Anticipated as Rents, Food, and Energy Prices Surge



Inflation continues to accelerate at a vigorous pace, threatening to undermine consumer spending and underscoring the growing pressure on the Federal Reserve to raise interest rates. The Consumer Price Index rose 8.3% through April as Russia's invasion of Ukraine in late February continues to pressure many energy and agricultural commodity prices. Excluding food & energy, measures of core inflation remain highly elevated with the Fed's preferred measure, the core Personal Consumption Expenditures Index, rising 4.9% through March.

Average Hourly Earnings: Wage Pressures Fail to Keep Pace with Inflation

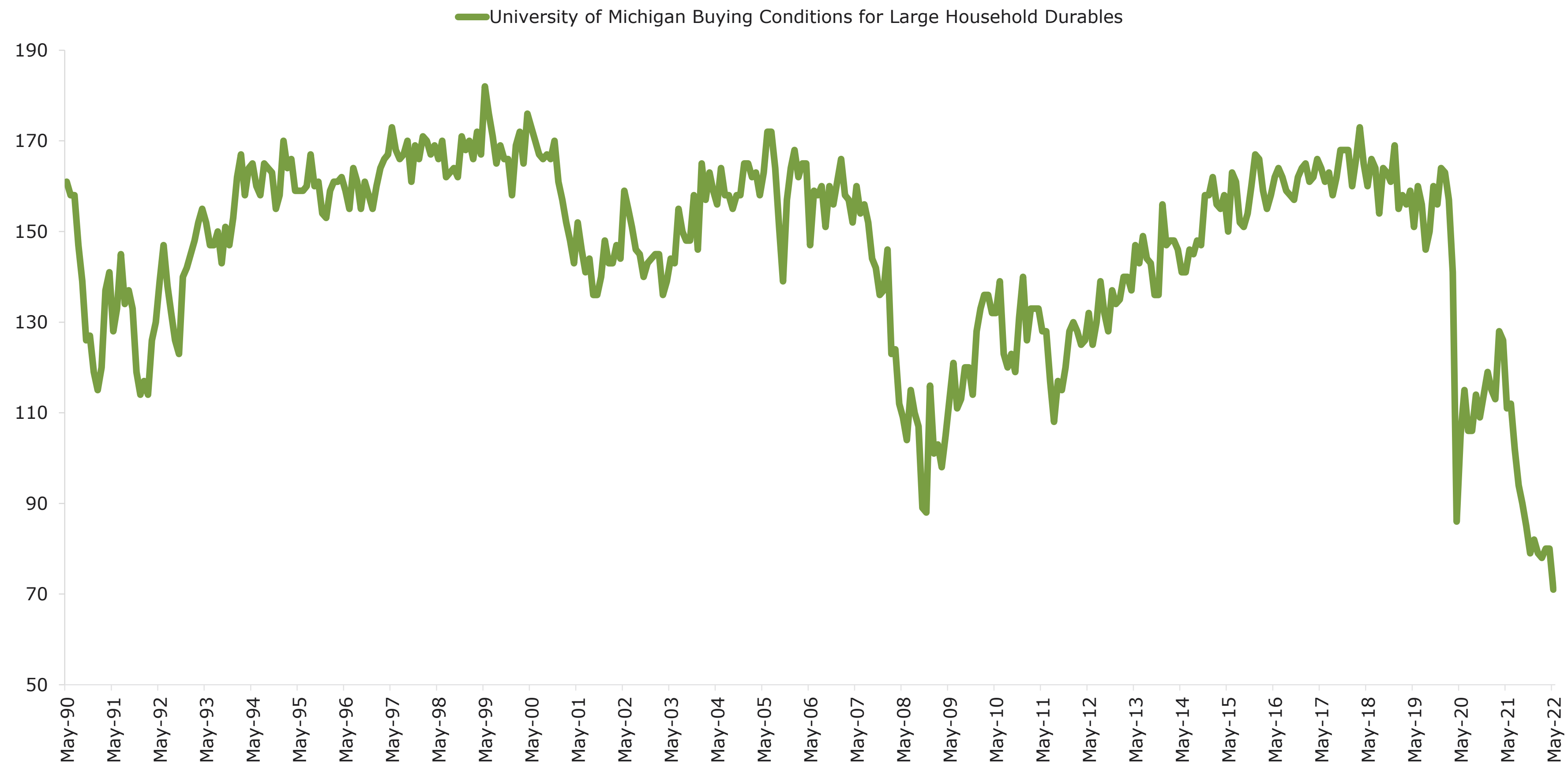
Inflation Continues to Accelerate at a Faster Pace than Wages



As employers increase wages to attract employees in the face of persistent labor shortages, wage increases have failed to keep pace with rising and persistent inflation. While average hourly earnings rose 5.5% in nominal terms through April., real earnings growth (i.e., after adjusting for inflation) was -2.6% through the same period and has been negative on a YoY bases since April 2021. The inability of wages to keep pace with inflation represents a headwind to consumer confidence and spending – the primary driver of growth in the U.S. economy.

Consumer Sentiment: Consumer's Increasingly Pessimistic as Inflation Erodes Purchasing Power

Measures of Consumer Sentiment Remain Under Pressure as Rising Prices Weigh on Optimism



The University of Michigan's buying conditions index for large household durable items reached its lowest reading on record in May as rising inflation continues to weigh on household budgets. Consumer spending accounts for nearly 70% of US. Gross Domestic Product (GDP) and persistent inflation coupled with higher interest rates and tighter financial conditions have recently raised concerns that growth may slow more quickly than the Federal Reserve's forecasts.

Personal Savings and Credit: Fading Stimulus and Rising Prices Weigh on the Consumer

US Personal Savings Rate Plummets as Fiscal Stimulus Wanes

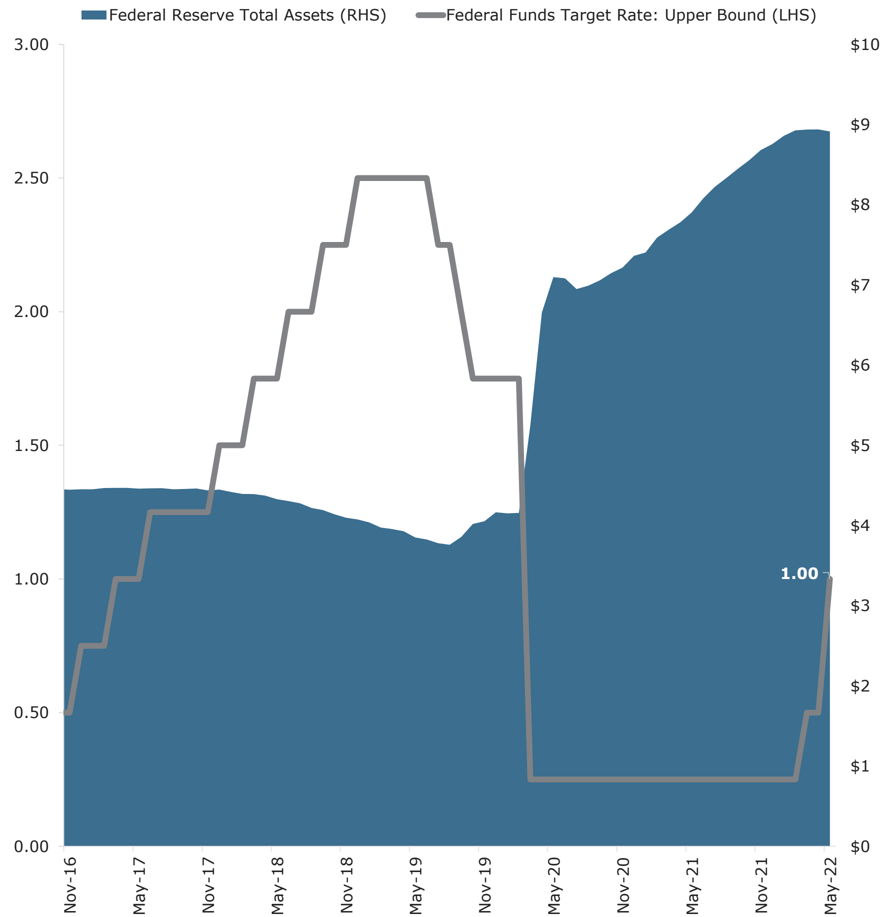
As fiscal stimulus wanes, consumers have depleted savings in an effort to sustain spending in the face of rising prices. The personal savings rate plummeted to its lowest level since 2008 through April.

Credit Card Usage Surges as Consumers Struggle with Higher Prices

Falling savings and waning fiscal stimulus pushed consumers to the credit card to sustain spending. Revolving credit jumped 35.3% on a YoY basis through March, its largest increase since 1998.

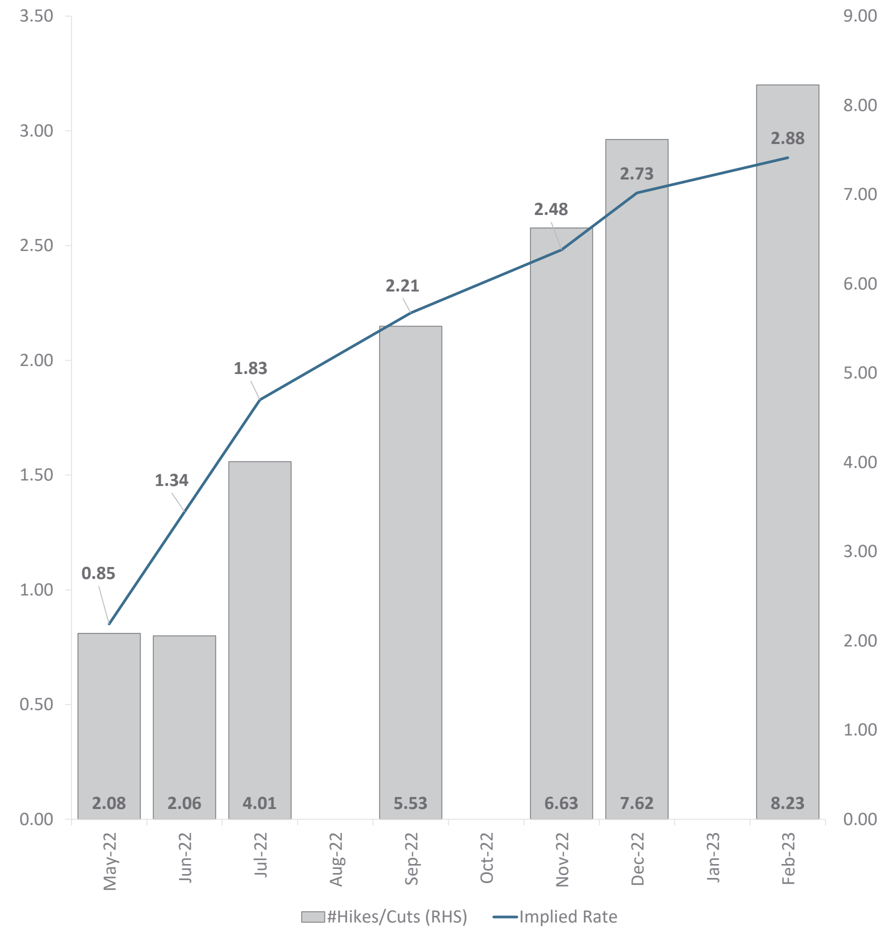
Monetary Policy: Fed's Aggressive Policy Stance Likely to be Tested by Financial Market Volatility

Federal Reserve Raised the Federal Funds Rate by 0.50% in May



The Russia-Ukraine conflict has complicated the Fed's goal of normalizing policy as efforts to contain inflation will likely be costly to growth and employment and increase the risk of a policy error.

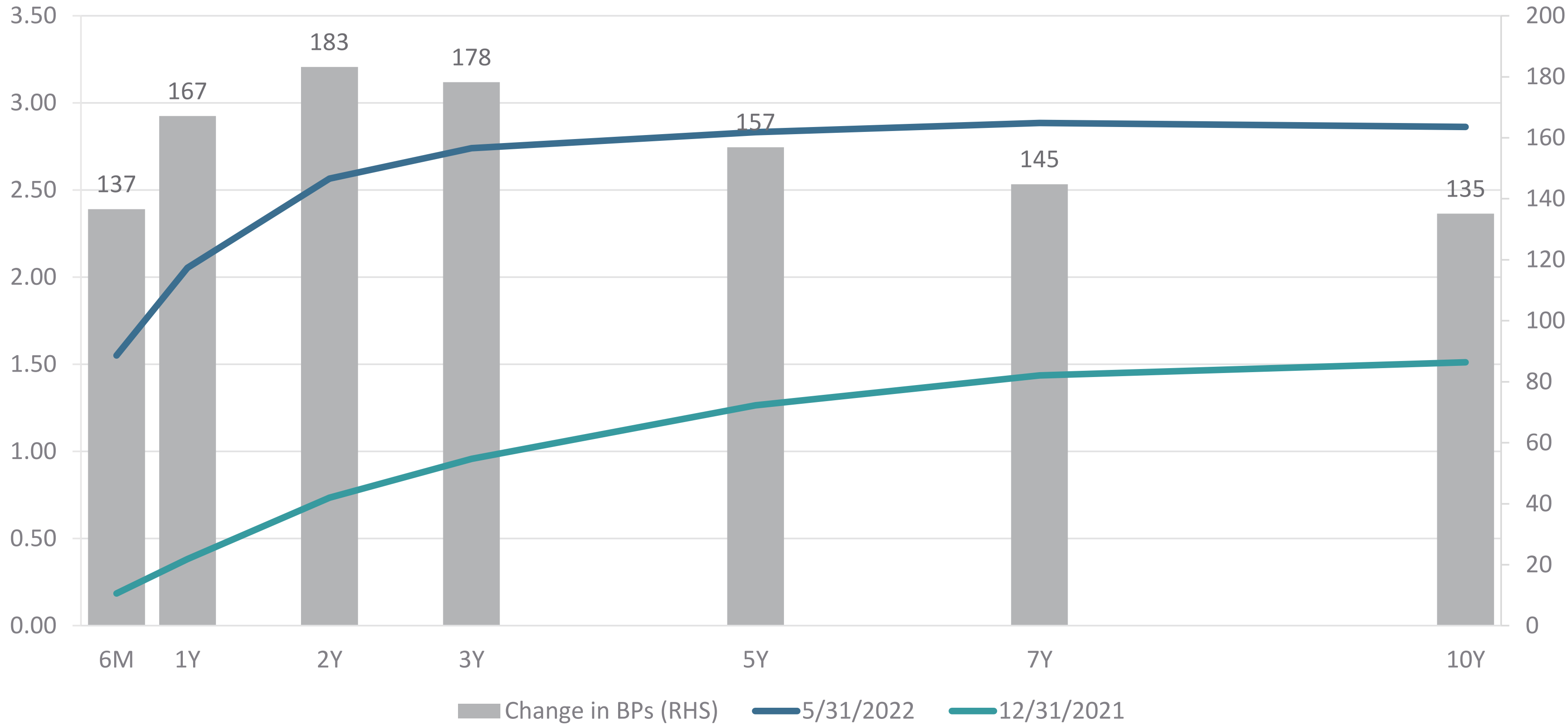
Fed Funds Futures Now Reflect a Much More Aggressive Fed in 2022



Fed fund futures market now reflect expectations that the Fed will raise the federal funds rate to nearly 2.75 % in 2022 while simultaneously reducing the balance sheet to rein in inflation.

Treasury Market: Yields Surged Higher over the Quarter as the Fed Turned Decidedly Hawkish

Treasury Yields Surged as the Fed Adopted a Notably Hawkish Policy Stance Which Includes Planned Rate Hikes and Balance Sheet Reduction



The continuing labor market recovery and broadening wage and inflation pressures have compelled the U.S. Federal Reserve (Fed) to pivot monetary policy to a more neutral stance earlier that was previously anticipated. The persistency of inflation coupled with the Fed's more aggressive policy stance helped to push Treasury yields notably higher over the quarter. The rise in yields was led by maturities in the range of between 1-5 years.

Treasury Markets: Rise in Yields Results in Worst Quarter in 45 Years for 1-5 Year Treasury Index

ICE BofA 1-5 Year US Treasury Index

Monthly/Quarterly/Annual Returns

Monthly	2022	2021	2020	2019	2018	2017	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003	2002	2001	2000	1999	1998	1997	1996	1995	1994	1993	1992	1991	1990	1989	1988	1987	1986	1985	1984	1983	1982	1981	1980	1979	1978
Jan	-0.90%	-0.05%	0.87%	0.32%	-0.57%	0.17%	1.08%	1.01%	0.43%	-0.13%	0.32%	0.32%	1.06%	-0.67%	2.15%	0.14%	0.08%	-0.05%	0.31%	-0.15%	0.28%	1.25%	-0.20%	0.46%	1.17%	0.44%	0.90%	1.55%	0.83%	1.56%	-0.52%	0.96%	-0.19%	0.83%	1.94%	0.75%	0.71%	1.28%	1.56%	0.59%	0.46%	0.36%	0.01%	1.68%	0.00%
Feb	-0.43%	-0.38%	1.17%	0.04%	-0.13%	0.15%	0.25%	-0.51%	0.14%	0.24%	-0.30%	-0.23%	0.31%	-0.22%	1.22%	1.00%	0.01%	-0.44%	0.70%	0.71%	0.65%	0.77%	0.71%	-0.96%	-0.03%	0.16%	-0.72%	1.69%	-1.03%	1.20%	0.33%	0.55%	0.37%	-0.17%	0.91%	0.53%	1.45%	-0.60%	-0.09%	1.47%	1.39%	-0.23%	-4.36%	0.27%	0.47%
Mar	-1.86%	-0.10%	1.71%	0.85%	0.32%	0.05%	0.23%	0.42%	-0.32%	0.04%	-0.21%	-0.07%	-0.46%	0.89%	0.29%	0.36%	0.00%	-0.11%	0.51%	0.12%	-1.07%	0.85%	0.84%	0.74%	0.37%	-0.25%	-0.31%	0.55%	-0.96%	0.34%	-0.24%	0.61%	0.26%	0.42%	-0.04%	-0.11%	2.16%	1.48%	0.06%	-0.02%	0.60%	2.21%	1.27%	0.94%	0.39%
Apr		0.16%	0.08%	0.16%	-0.35%	0.31%	-0.01%	0.03%	0.25%	0.23%	0.49%	0.73%	0.46%	-0.48%	-1.20%	0.39%	0.25%	0.82%	-1.58%	0.21%	1.40%	0.00%	0.14%	0.30%	0.46%	0.95%	-0.11%	1.03%	-0.58%	0.76%	0.98%	1.02%	0.00%	1.71%	0.04%	-1.05%	0.69%	1.83%	0.40%	1.73%	2.22%	-1.33%	7.85%	0.45%	0.25%
May		0.17%	0.14%	1.00%	0.48%	0.22%	-0.15%	0.09%	0.40%	-0.52%	0.19%	0.72%	0.76%	-0.07%	-0.65%	-0.31%	0.10%	0.52%	-0.18%	0.86%	0.59%	0.50%	0.41%	-0.35%	0.58%	0.72%	0.06%	2.33%	0.13%	-0.34%	1.18%	0.61%	1.76%	1.72%	-0.31%	0.12%	-0.69%	3.04%	-1.09%	-0.29%	1.78%	2.32%	3.37%	1.47%	0.06%
Jun		-0.22%	0.07%	0.65%	-0.01%	-0.15%	0.97%	-0.10%	-0.10%	-0.40%	-0.09%	0.04%	0.80%	-0.33%	0.38%	0.34%	0.17%	0.23%	0.08%	0.03%	1.00%	0.33%	1.23%	0.32%	0.58%	0.77%	0.84%	0.59%	0.19%	1.04%	1.29%	0.25%	1.17%	2.17%	1.24%	1.11%	1.84%	1.22%	0.76%	0.34%	-0.79%	0.24%	0.96%	1.62%	-0.19%
Jul		0.35%	0.16%	-0.18%	-0.09%	0.28%	-0.04%	0.19%	-0.23%	0.23%	0.41%	0.76%	0.58%	0.25%	0.51%	1.14%	0.85%	-0.58%	0.49%	-1.19%	1.62%	1.43%	0.64%	0.21%	0.43%	1.45%	0.35%	0.25%	1.05%	0.19%	1.48%	1.00%	1.38%	1.76%	-0.04%	0.42%	1.25%	0.07%	2.51%	-0.83%	3.86%	-1.01%	-0.56%	0.14%	0.82%
Aug		-0.06%	-0.06%	1.18%	0.43%	0.34%	-0.31%	-0.02%	0.35%	-0.28%	0.05%	0.77%	0.47%	0.58%	0.69%	1.23%	0.85%	0.87%	1.06%	0.05%	0.65%	0.69%	0.87%	0.27%	1.61%	-0.14%	0.24%	0.69%	0.33%	1.23%	1.10%	1.63%	0.04%	-1.00%	0.11%	-0.03%	1.91%	1.15%	1.14%	0.79%	2.87%	0.07%	-2.33%	-0.30%	0.86%
Sep		-0.29%	0.02%	-0.24%	-0.28%	-0.34%	0.17%	0.53%	-0.18%	0.51%	0.01%	-0.14%	0.27%	0.37%	0.85%	0.70%	0.59%	-0.50%	-0.05%	1.42%	1.32%	1.93%	0.78%	0.73%	1.84%	0.92%	1.08%	0.56%	-0.53%	0.34%	1.21%	1.37%	0.87%	0.54%	1.37%	-0.76%	-0.46%	0.88%	1.83%	2.21%	2.38%	0.98%	-0.08%	0.15%	0.36%
Oct		-0.46%	-0.12%	0.32%	0.13%	-0.09%	-0.20%	-0.23%	0.50%	0.25%	-0.13%	0.11%	0.37%	0.24%	1.27%	0.45%	0.40%	-0.19%	0.41%	-0.64%	0.10%	1.16%	0.57%	0.20%	0.41%	0.92%	1.36%	0.98%	0.12%	0.19%	-1.00%	1.16%	1.23%	1.76%	1.15%	2.58%	1.06%	1.32%	2.70%	0.71%	3.26%	4.55%	-0.70%	-2.70%	-0.98%
Nov		0.06%	0.07%	-0.11%	0.48%	-0.28%	-0.92%	-0.30%	0.32%	0.12%	0.22%	0.14%	-0.39%	0.99%	2.06%	2.19%	0.61%	0.37%	-0.75%	-0.07%	-0.61%	-0.62%	1.13%	0.13%	-0.27%	0.21%	0.96%	1.07%	-0.54%	-0.20%	-0.37%	1.14%	1.16%	0.93%	-0.55%	0.62%	0.78%	1.33%	1.98%	0.90%	1.03%	5.62%	-0.14%	2.88%	0.85%
Dec		-0.28%	0.07%	0.14%	1.11%	-0.01%	0.02%	-0.15%	-0.33%	-0.48%	-0.05%	0.17%	-0.64%	-1.29%	0.89%	0.28%	-0.15%	0.45%	0.33%	0.70%	1.33%	-0.20%	1.41%	-0.02%	0.33%	0.76%	-0.26%	0.88%	0.28%	0.37%	1.14%	1.90%	1.31%	0.35%	0.15%	0.74%	0.20%	1.72%	1.45%	0.43%	1.63%	-1.36%	2.65%	0.70%	-0.32%

Quarterly	2022	2021	2020	2019	2018	2017	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003	2002	2001	2000	1999	1998	1997	1996	1995	1994	1993	1992	1991	1990	1989	1988	1987	1986	1985	1984	1983	1982	1981	1980	1979	1978
Q1	-3.16%	-0.52%	3.80%	1.22%	-0.38%	0.37%	1.57%	0.92%	0.26%	0.15%	-0.19%	0.02%	0.90%	-0.01%	3.69%	1.50%	0.09%	-0.60%	1.53%	0.69%	-0.15%	2.89%	1.36%	0.24%	1.52%	0.36%	-0.13%	3.84%	-1.17%	3.13%	-0.44%	2.13%	0.43%	1.07%	2.83%	1.18%	4.38%	2.17%	1.53%	2.05%	2.46%	2.35%	-3.14%	2.91%	0.00%
Q2		0.11%	0.29%	1.83%	0.13%	0.38%	0.81%	0.02%	0.55%	-0.69%	0.59%	1.49%	2.04%	-0.87%	-1.47%	0.42%	0.52%	1.58%	-1.67%	1.10%	3.01%	0.84%	1.79%	0.27%	1.64%	2.45%	0.80%	3.99%	-0.25%	1.47%	3.49%	1.88%	2.96%	5.70%	0.97%	0.18%	1.83%	6.20%	0.07%	1.78%	3.22%	1.20%	12.55%	3.58%	0.13%
Q3		0.00%	0.13%	0.75%	0.05%	0.29%	-0.19%	0.70%	-0.06%	0.46%	0.47%	1.39%	1.32%	1.20%	2.06%	3.10%	2.31%	-0.22%	1.50%	0.27%	3.64%	4.10%	2.31%	1.21%	3.93%	2.24%	1.68%	1.50%	0.85%	1.77%	3.83%	4.05%	2.31%	1.28%	1.45%	-0.37%	2.71%	2.11%	5.57%	2.17%	9.39%	0.04%	-2.95%	-0.01%	2.05%
Q4		-0.68%	0.02%	0.35%	1.72%	-0.38%	-1.09%	-0.67%	0.49%	-0.11%	0.04%	0.42%	-0.67%	-0.08%	4.27%	2.93%	0.85%	0.63%	-0.01%	-0.01%	0.82%	0.33%	3.15%	0.31%	0.48%	1.90%	2.07%	2.95%	-0.15%	0.36%	-0.25%	4.25%	3.74%	3.06%	0.74%	3.98%	2.06%	4.43%	6.25%	2.05%	6.02%	8.92%	1.80%	0.81%	-0.46%

Yearly	2022	2021	2020	2019	2018	2017	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003	2002	2001	2000	1999	1998	1997	1996	1995	1994	1993	1992	1991	1990	1989	1988	1987	1986	1985	1984	1983	1982	1981	1980	1979	1978
Year	-3.16%	-1.10%	4.25%	4.20%	1.52%	0.65%	1.09%	0.98%	1.24%	-0.19%	0.91%	3.36%	3.61%	0.23%	8.73%	8.16%	3.81%	1.39%	1.32%	2.06%	7.47%	8.37%	8.87%	2.04%	7.75%	7.11%	4.47%	12.83%	-0.74%	6.87%	6.72%	12.88%	9.74%	11.52%	6.12%	4.99%	11.43%	15.70%	13.96%	8.29%	22.65%	12.85%	7.70%	7.44%	0.00%

The persistency of inflation coupled with an aggressively hawkish pivot in Fed policy expectations propelled yields notably higher in the first quarter of 2022. The historically low level of starting yields provided little income protection against market value declines as interest rates increased and resulted in the worst quarter in 45 years for the ICE BofA 1-5 Year Treasury Index which declined 3.16% on a total return basis. The markedly higher level of current yields will provide a greater cushion against future market value declines should yields rise further.

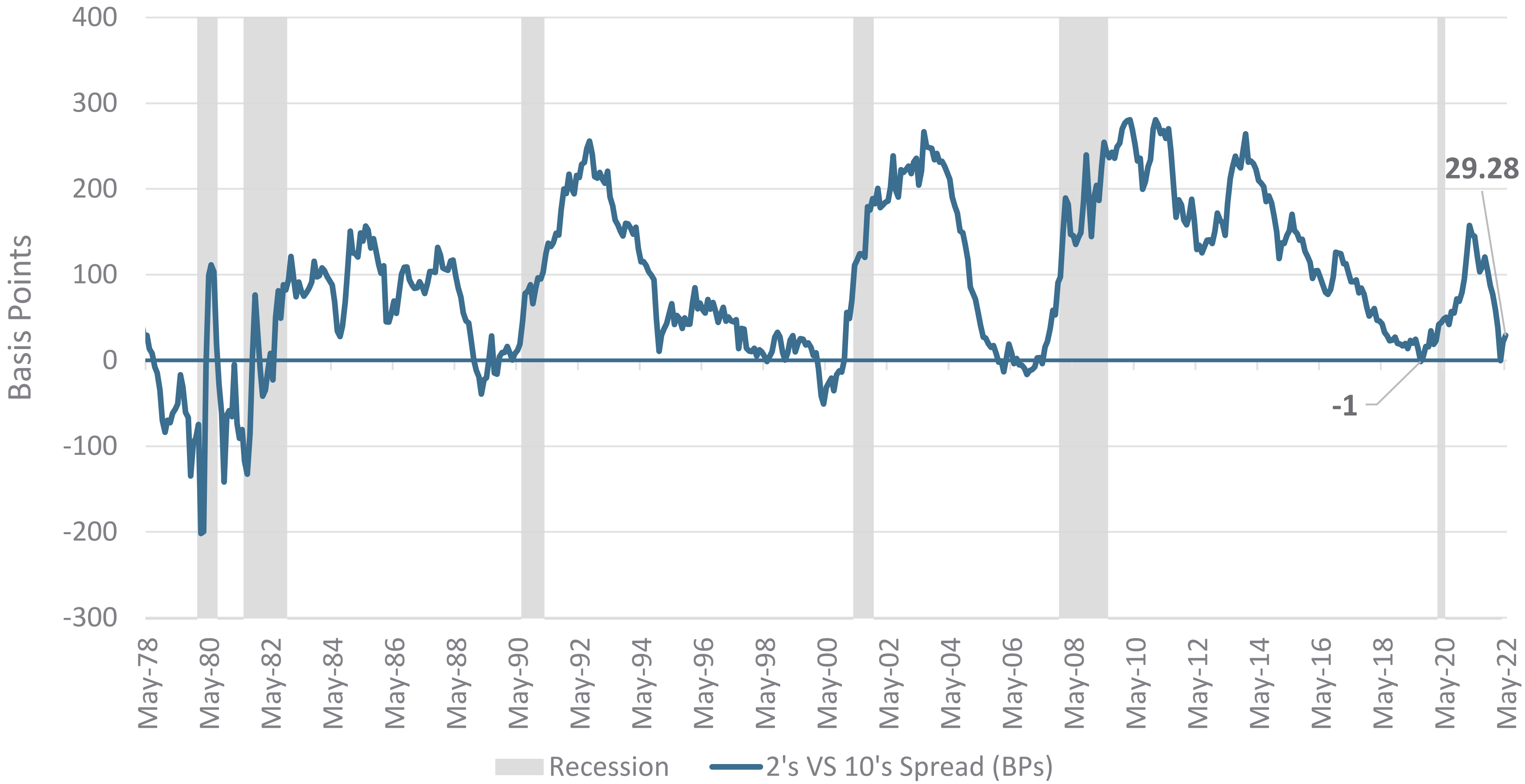
Treasury Market: Yield Curve Beginning to Reflect Growing Expectation of Fed Overtightening

As the Federal Reserve Moves Aggressively to Catch Policy Up with Surging Inflation, the Yield Curve Prices In Growing Chance of Policy Error

Historically, the Federal Reserve has overtightened policy after periods of low interest rates often prompting a reversal of monetary policy. The Fed has acknowledged the need to potentially raise rates beyond the so-called "neutral rate" to tame the highest rates of U.S. inflation in over 40 years. Amidst a backdrop of elevated geopolitical risks and uncertainty, the yield curve has begun to reflect expectations of a potential Fed policy error.

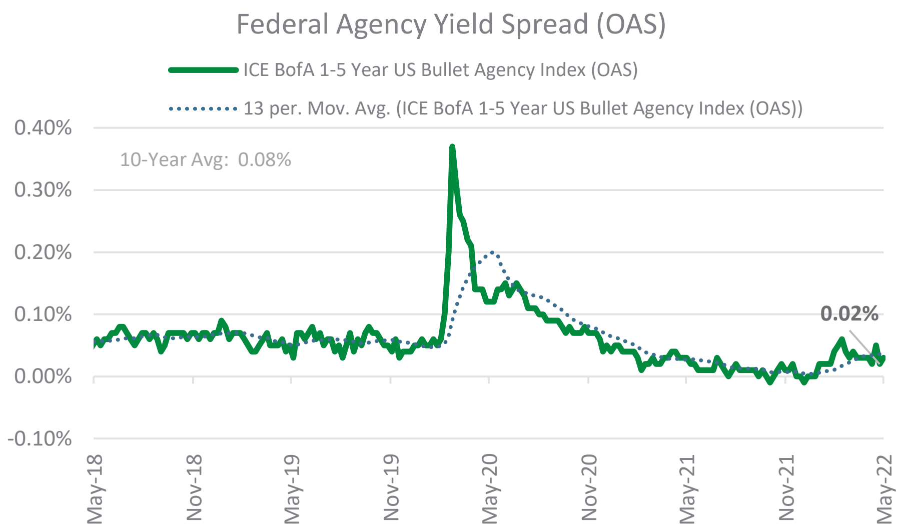
Treasury Market: Yield Curve Flattening Stirs Recession Debate

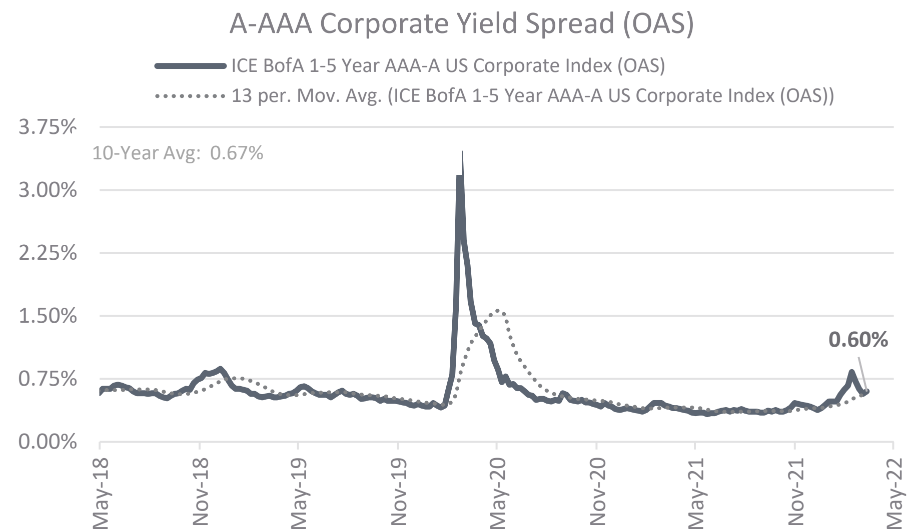
The Spread Between 2 and 10-Year Treasury Yields Approaches Inversion and Sounds Recession Alarm

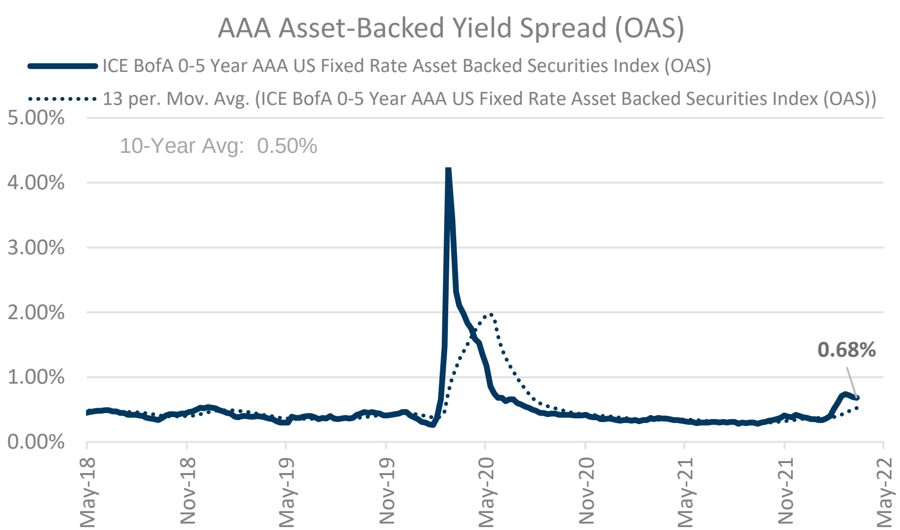


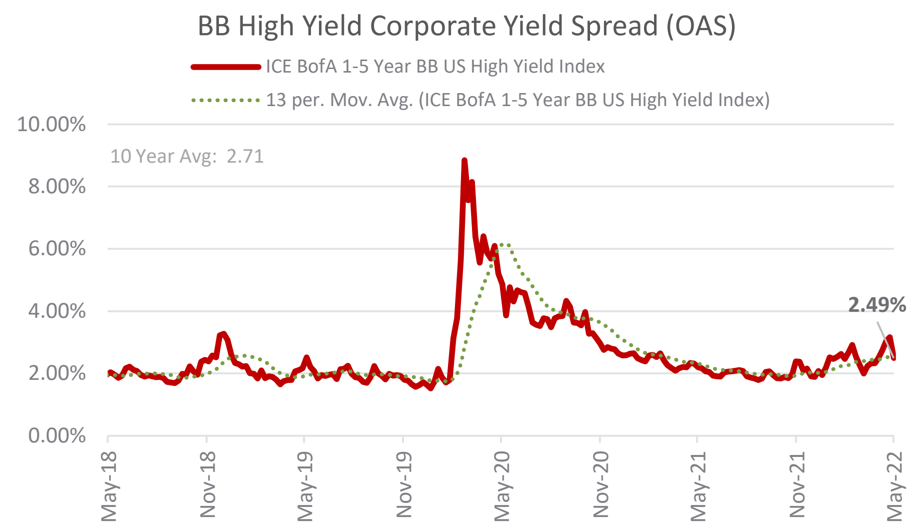
Market perceptions that the Federal Reserve had fallen behind the data in dealing with inflation and a subsequent aggressive hawkish policy pivot propelled shorter-term yields higher over the first quarter. The rise in longer-term yields was comparatively more contained with Russia's invasion of Ukraine adding additional uncertainty to the global growth outlook. The yield curve has flattened notably with the spread between 2- and 10-year Treasury yields modestly re-steepening following a brief inversion at the end of the first quarter.

Credit Markets: Credit Spreads Perked Up From the Lows of Last Summer









Disclosures

- The U.S. economy unexpectedly contracted in the first quarter of 2022 with Gross Domestic Product (GDP) falling at a 1.4% annualized pace and marking a notable contraction from the prior quarter's robust 6.9% gain. At first glance, the weak headline figure raises concern but details of the report suggest underlying demand remained intact, at least for now. Taken together, net exports and inventories, two of the more volatile components of GDP, sliced 4% from real GDP growth as still shuttered global supply chains continue to weigh on activity. More optimistically, consumer spending, which accounts for approximately two-thirds GDP, remained heathy with personal consumption expenditures expanding at a 2.7% annualized rate, up slightly from last quarter's 2.5% pace. Looking ahead, however, economic uncertainty remains on the rise as the Russia-Ukraine conflict, runaway inflation, and expectations for an aggressive tightening of monetary policy by the Federal Reserve (Fed) weigh on consumer activity and financial conditions. The Fed raised their benchmark interest rate by 50 basis points (0.50%) to a range of 0.75% to 1.0% at their May 4th FOMC meeting and is expected continue raising rates throughout the year to combat the highest rate of inflation in 40 years.

  - **Portfolio Duration:** Public trust anticipates maintain portfolio duration generally neutral to the portfolio benchmark as market participants seek to determine whether the Fed will be successful in tightening financial conditions sufficiently to thwart inflation without tipping the U.S. economy into recession. Incoming economic data has softened recently, and growing recession fears have cast a shadow on the growth expectations. As incoming data shapes expectations, PTA may implement certain tactical duration adjustments as bouts of volatility present opportunities to improve risk-adjusted returns.

  - **Yield Curve Positioning:** While short-term rates are expected to continue rising with Fed policy, intermediate and longer-term rates have already priced in expectations for aggressive Fed tightening and may be subject to swings lower should incoming economic data soften and cause the Fed to capitulate in its policy outlook. As incoming data shapes growth, inflation and policy expectations, PTA will review opportunities to tactically underweight or overweight certain maturity tenors to capitalize on anticipated changes in the slope of the yield curve.

  - **Asset Allocation:** While credit spreads on GSE and investment-grade U.S. corporate bonds remain subdued, recent financial market volatility has prompted a slight widening of corporate credit spreads with new primary market issues selling wider than secondary market offerings. As the fed continues to raise interest rates and begins shrinking its balance sheet, PTA anticipates that credit spreads will be pressured moderately wider and provide opportunities to tactically add selectively add high-quality issuers and structujres at more attractive valuations. Current corporate bond allocations are below the City's investment policy limits and PTA will evaluate opportunities to prudently add to such allocations as relative value opportunities arise.

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