TheINVESTOR

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TheECONOMY

We Have Liftoff but What About Landing?

The Federal Reserve raised interest rates last month by 25 basis points for the first time since cutting rates to zero in March 2020. The move was widely expected and coincides with the Fed suspending asset purchases and allowing securities to roll off its balance sheet. 25 bps was less than market participants had been pricing in earlier in the year and was influenced by the crisis in Ukraine clouding the outlook for global growth. But with persistently high U.S. inflation, the market believes the Fed will hike at a much faster pace through the rest of the year.

With inflation exceeding 8% and unlikely to abate in the second quarter, the Fed is poised to move much more quickly than it has in prior cycles, and it is not just inflation that underpins the Fed's urgency. U.S. unemployment is down to 3.6%, just .1% off pre-pandemic lows though labor force participation remains 1% below its pre-pandemic highs. Both the service and manufacturing sectors remain strong yet burdened by employment, prices, and inventories, further clouding the outlook.

All of this signals to the Fed that they need to move faster to wrestle the inflationary pressures in the economy. Because of the Fed's recent hawkish tone, market participants are pricing in a 100% chance of one hike (25 bps) and an 89% chance of two (50 bps) at the May meeting which would bring overnight rates up to between .75% - 1.00%. Looking at the rest of the year, the market now expects nine hikes or an implied overnight rate of 2.50%.

The Fed's primary risk is hiking too quickly and choking off economic growth, resulting in a recession or what we would call a "hard landing." We have already seen mortgage rates climb ~1.5 percentage points since the beginning of the year while rates across the curve have risen materially over the last month alone. Money market investors will certainly appreciate the higher yields available, but the Fed will need to be careful to not choke off growth and leave the consumer holding the bag.

Treasury Yields

MATURITY	4/8/22	3/4/22	CHANGE
3 Month	0.679%	0.500%	0.179%
6 Month	1.139%	0.628%	0.511%
1 -Year	1.735%	0.991%	0.744%
2 -Year	2.512%	1.476%	1.036%
3 -Year	2.725%	1.606%	1.119%
5 -Year	2.754%	1.637%	1.117%
10 -Year	2.700%	1.731%	0.969%
30 -Year	2.718%	2.155%	0.563%

Source: Bloomberg

Agency Yields

MATURITY	4/8/22	3/4/22	CHANGE
3 Month	1.049%	0.513%	0.536%
6 Month	1.291%	0.674%	0.617%
1 -Year	1.821%	1.019%	0.802%
2 -Year	2.585%	1.576%	1.009%
3 -Year	2.726%	1.677%	1.049%
5 -Year	2.839%	1.767%	1.072%

Source: Bloomberg

Commercial Paper Yields (A-1/P-1)

MATURITY	4/8/22	3/4/22	CHANGE
1 Month	0.450%	0.290%	0.160%
3 Month	0.940%	0.640%	0.300%
6 Month	1.490%	0.970%	0.520%
9 Month	1.870%	1.120%	0.750%

Source: Bloomberg

Current Economic Releases

DATA	PERIOD	VALUE
GDP QoQ	Q4 '21	6.90%
US Unemployment	Mar '22	3.60%
ISM Manufacturing	Mar '22	57.10
PPI YoY	Mar '22	11.20%
CPI YoY	Mar '22	8.50%
Fed Funds Target	Apr 11, 2022	0.25% - 0.50%

Source: Bloomberg