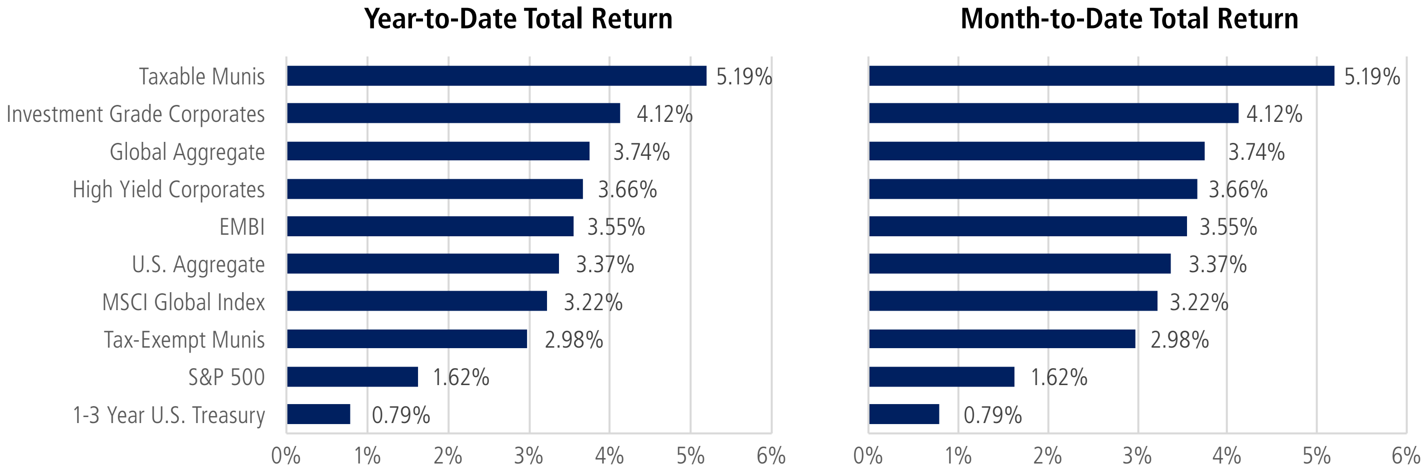
Week Ending: **January 20, 2023**

You Have Been Served

Economic Overview:

The December euro area Harmonized Index of Consumer Prices (HICP) released this week showed a worrisome picture. Sure, headline (all items) inflation cooled for the second month in a row, registering 9.2% year-over-year, down from the all-time high of 10.6% in October. And, yes, a warmer-than-expected winter sent energy prices lower, leaving energy prices up "only" 26% in December compared to 44% last March. But the euro area inflation story is about more than just energy. Core inflation, which excludes food and energy, accelerated in December. Non-energy industrial goods hit a new record high of 6.4%. And services rose 4.4% in December—a new record high for the series. We're sure you're beginning to see a pattern. But the market seems less concerned than we are about inflation. Most measures of longer-term inflation expectations hover around 3%. But we doubt the European Central Bank will take much comfort in the December data, which likely means more monetary policy tightening ahead.

Total Returns by Asset Class



Source: Bloomberg

Highlights of the Week:

High Yield: CCCs underperformed BB/B rated high yield by -505 basis points in 2022 as the market priced in a higher probability of recession. In 2023, CCCs are outperforming by +179 basis points as recent data points to a higher likelihood of a "soft landing," which could portend a lower default rate than expected.

Corporates: Google parent Alphabet Inc is next in line for firmwide layoffs, planning to eliminate 6% of its workforce or roughly 12,000 jobs, as the past several years of mass hiring to meet booming demand have left companies scrambling to downsize amidst a souring industry. In a similar fashion to other high-profile tech layoffs in recent months, the cuts will take place across units, with areas such as recruiting and non-core business will feel the brunt of the reductions.

Securitized Products: The consumer ABS new issue market is off to a busy start, with over $8 billion in new issue pricing this week across eight deals. The market tone is more favorable to issuers to start the year with lower yields, tighter spreads, and strong demand for bonds. However, new issue supply in the ABS market is expected to be lower than last year. Investors are still closely watching how fundamentals unfold amidst macroeconomic uncertainty.

Municipals: Earlier this month, Governor Newsom introduced a $223.6 billion budget for the next fiscal year beginning on July 1st. Unfortunately, a $22.5 billion deficit is included in the fiscal 2023-2024 budget plan as revenue is expected to fall from historically high levels during the pandemic fueled by a remarkable stock market rally generated by the massive federal stimulus that is coming to an end.

Equities: U.S. equities ended the week lower as concerns about slower economic growth weighed on market sentiment. The utility, industrial, and consumer staple sectors led markets lower, while communications, energy, and technology were the best performers.

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