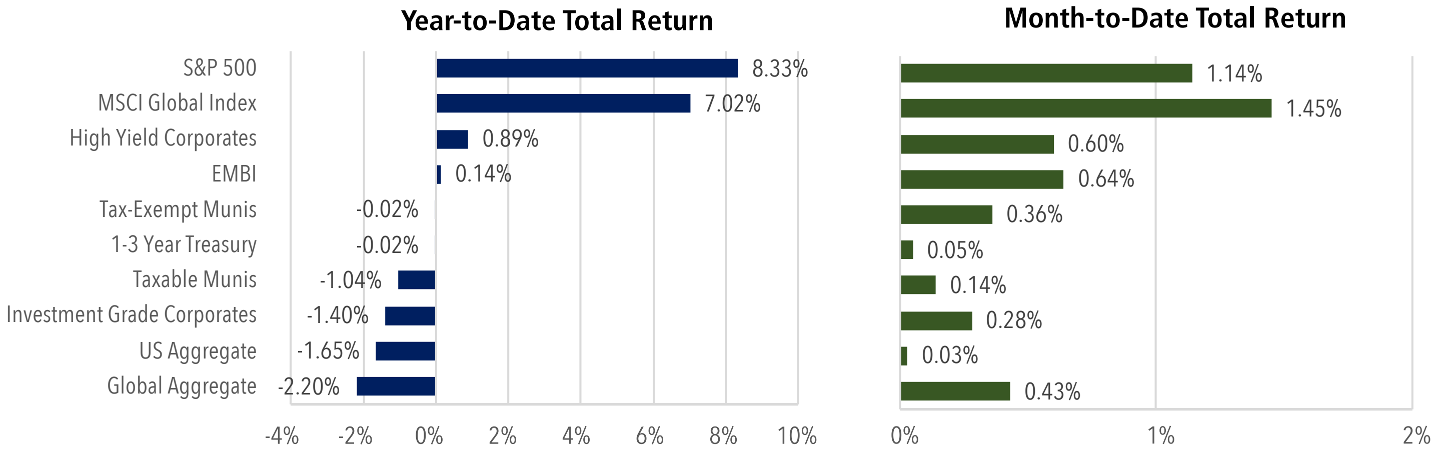
Week Ending: **March 15, 2024**

Percolating Prices

Economic Overview:

Last week, Fed Chair Jerome Powell's five-hour testimony on Capitol Hill prompted politicians and market participants to conclude that we are "not far" from a rate cut. "Not so fast," as we often say. This week's Consumer Price Index (CPI) report portrayed some percolating price pressures. February's core CPI jumped 0.4%, repeating its hot January print, which many called "a fluke." Perhaps more worrisome, while some may still want to chalk up January and February to noise, the six-month annualized rate of change has been accelerating since last fall. In our view, policymakers, expecting price pressures to continue to wane, can no longer be so confident. In the words of Chair Powell, FOMC economic projections are not "plans," as the "economy will do something different" than expected, and policy will need to adjust. Next week, when the FOMC meets in D.C., projections may shift again to reflect ongoing uncertainty around inflation.

Total Returns by Asset Class



Source: Bloomberg

Highlights of the Week:

High Yield: High yield spreads continue to grind tighter, driven by a strong economy, robust earnings, and a correspondingly benign default outlook. Over the long term, the default outlook is the most important driver of high-yield spreads. However, security selection remains critical as investor confidence risks transitioning into complacency.

Corporates: A heavy front-loaded week of issuance resulted in $38 billion coming to market across a broad range of sectors and tenors. Next week, expectations of issuance range from $20-$35 billion. With continued strength in inflows into the asset class and seemingly less supply to digest relative to prior weeks, corporate spreads resumed their path lower, tightening four basis points this week to +91 and two basis points off their year-to-date tights.

Municipals: With 89% of ballots counted, the votes favor passing California's Proposition 1, which would authorize issuing $6.4 billion of debt to fund initiatives reducing homelessness. While the approval vote is leading by less than half a percentage point, the main group opposing the measure conceded that the remaining ballots would likely secure its approval. However, the narrow margin underlines weakening support for the Governor's agenda.

Equities: The U.S. equity market ended the week modestly lower as hotter-than-expected inflationary data drove interest rates higher and pushed back potential Fed rate cuts. Sector leadership was mixed, with energy, materials, and financials posting positive returns, while real estate, consumer discretionary, and health care posted losses.

Securitized Products: As liquidity returns to the European Leveraged Loan space, spreads continue to tighten, and risk-free rates decline, the European Collateralized Loan Obligations (CLO) market is starting to resemble 2021 more closely. Spreads on mezzanine paper are getting close to 2021 levels, albeit loan prices are currently about two basis points lower while AAA-rated levels are still wider. This flattening of the credit curve continues to be driven by the demand for yield as markets normalize following the rate hiking cycle.