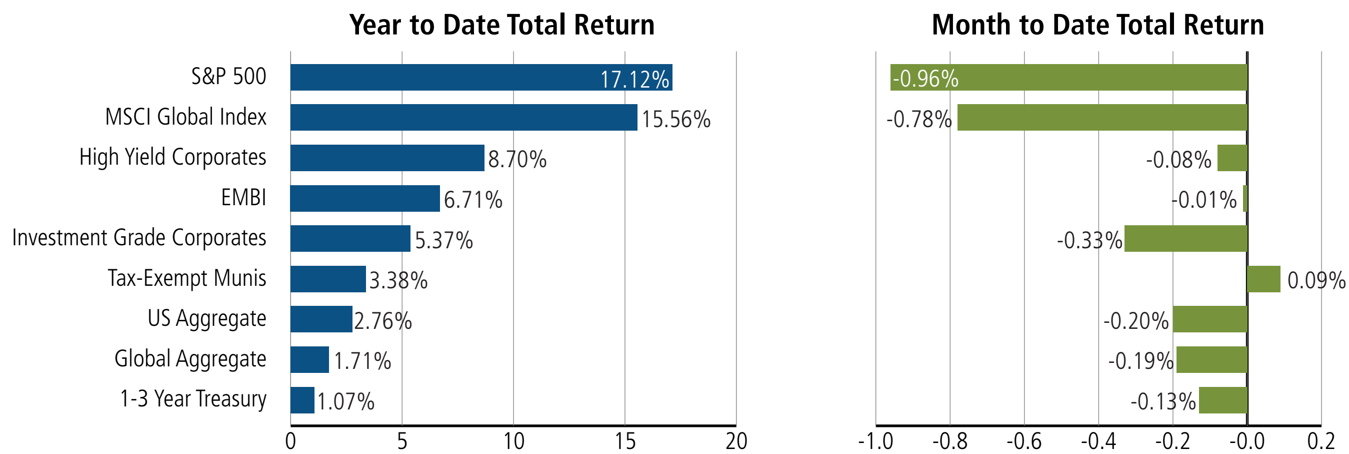
Week Ending **May 3, 2019**

Trim Your Rate Cut Forecasts

Economic Overview:

Fed Chair Jay Powell took to the podium after the May FOMC meeting and shrugged off concerns about "low inflation." Powell attributed the recent drift down in the Fed's preferred inflation gauge, core PCE, to "transitory" factors. Powell advised the assembled reporters to follow the Dallas Fed's Trimmed Mean PCE inflation, which excludes volatile components each month, giving policymakers (and investors!) a better underlying inflation gauge. Core PCE, on the other hand, crudely excludes food and energy each month, volatile or not. The problem: one-off, idiosyncratic factors often drive prices, muddying the inflation waters. Twice in the last five years, core PCE has drifted lower due to noise in the data. In 2015, the commodity prices plunged. In 2017 all-you-can-eat cellphone data plans sent core PCE lower. Each time, core PCE bounced back. Per Powell, apparel and financial services prices (which move with financial market valuations) have depressed core PCE of late. Trimmed Mean PCE, meanwhile, continues to register at ~2% year-over-year. Our hunch: it's time to trim your rate cut forecasts.

Total Returns by Asset Class



Highlights of the Week:

- **Currencies:** The British pound was the best performing G10 currency this week, rising by more than 0.9% against the U.S. dollar and 0.8% against the euro. A combination of improved growth forecast by the Bank of England and receding concerns about a no-deal Brexit helped lift the pound off its recent lows. While reasons to be cautious remain, the prospect of an interest rate hike by the more hawkish Bank of England resulted in a brighter outlook for sterling this week.

- **Corporates:** Spreads over Treasurys on the Bloomberg Barclays 1-30 year U.S. Corporate index tightened another 8 basis points in April, making spreads 42 basis points tighter on the year. Investor demand for corporate credit has been strong with the market easily absorbing the $92 billion of new bond issuance in April. U.S. corporate bond issuance is down 6% year-over-year, partially due to decreased M&A supply.

- **Securitized Products:** Like a delayed echo, the CLO market has finally followed the broader market tighter in spreads with lower investment grade classes tighter by 10 basis points over the week, and closer to 20 basis points month-over-month. Investor preferences have shifted from floating rate to fixed rate with the Fed on hold, but with 3-month LIBOR at 2.56% and 2-year U.S. Treasuries at 2.34%, the inversion doesn't look too bad for floaters.

- **Equities:** The U.S. equity market ended the week unchanged after the strong U.S. jobs report offset less dovish comments from the Fed. Broad equity prices (S&P 500) are now near record highs, which have been driven by better than expected corporate earnings results. The best performing sectors for the week were financials and health care, while the worst performers were energy and communications.