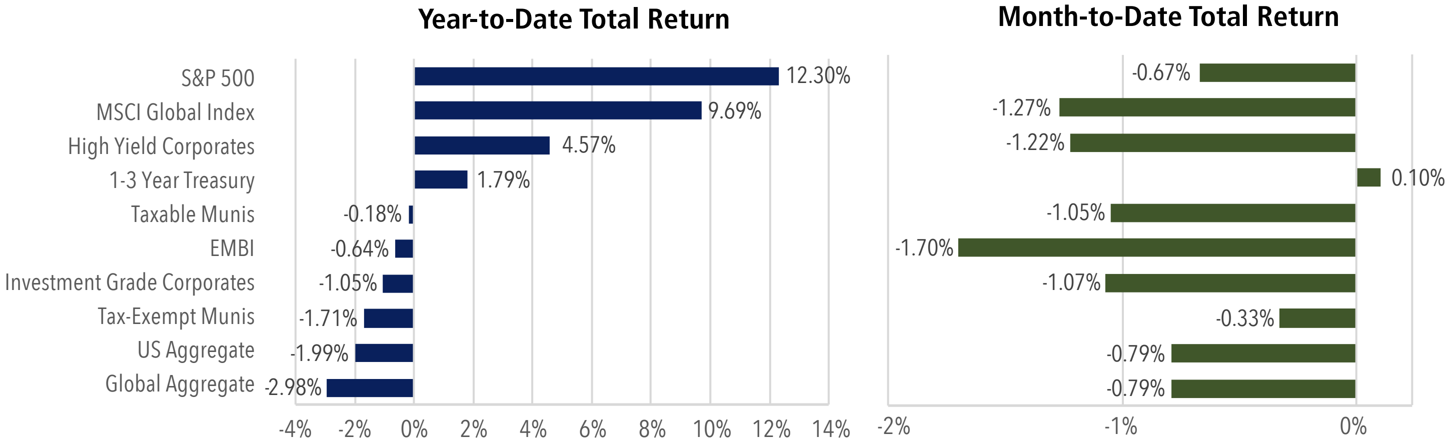
Week Ending: **October 6, 2023**

Thrown For A Curve

Economic Overview:

Ah, the yield curve. Like a deck of tarot cards, investors see the future in the yield curve. If inverted, investors expect a recession. If steepening, an expansion. Oddly enough, since June, the yield curve has "bear steepened," with longer-term yields up more than short-term yields. It's odd because it's both rare and unexpected. Rare because a bear steepening while the yield curve is inverted has occurred only four times since 1977. Unexpected because if the economy were on the cusp of a recession, with the Fed expected to cut rates, one might expect a bull steepening with short-term rates leading the way lower. So, what is the yield curve telling us now? A few possibilities are in play. First, the “higher-for-longer” mantra moved markets (note the yield curve move from August to September after the FOMC meeting). Second, the economy was stronger than expected through Q3. Third, sprinkle a hefty supply of Treasury issuance for investors to digest, and you have the recipe for a late-cycle steepening.

Total Returns by Asset Class



Source: Bloomberg

Highlights of the Week:

High Yield: Loans have been a beneficiary of the higher rate environment, returning +3.1% since the end of June. Within this period, 10-year Treasury yields have risen almost 100 basis points. Loans should be well positioned if rates remain elevated and economic growth remains strong.

Corporates: Issuance for the first week of October was just shy of $9 billion versus average expectations of $15 billion. Volatile market conditions, which resulted in Treasury and corporate yields reaching their highest levels in over a decade, kept several issuers on the sidelines. While 11 issuers did tap the market, no tranche had larger than $1 billion. The largest total deal came from Honda, with $1.75 billion across three tranches. Expectations for October remain low, ranging from $65-$100 billion.

Municipals: After municipal benchmark yields surged to their highest levels in over a decade, more than 70,000 trades were executed on Tuesday, making it the busiest trading day of 2023 thus far. Trade volume was about 40% higher than the daily average over the past 12 months.

Equities: The U.S. equity market snapped a streak of four consecutive weekly losses after ending the week modestly higher. Market sentiment improved as investors focused on the resilient economy following Friday’s strong employment report, which outweighed concerns about higher rates. Communications, technology, and healthcare led markets higher, while the worst-performing sectors were energy, utilities, and consumer staples.

Securitized Products: Spreads were wider across securitized products this week, with higher rates and weakness in risk assets. Lower-rated products underperformed higher-quality products across all four major securitized sectors. Agency mortgages also saw lower prices and wider spreads, with the current coupon now touching 6.5% for the first time since 2007. Secondary trading has been orderly with consistent volume, albeit at wider levels. New issuance volumes declined towards the end of the week as volatility increased.