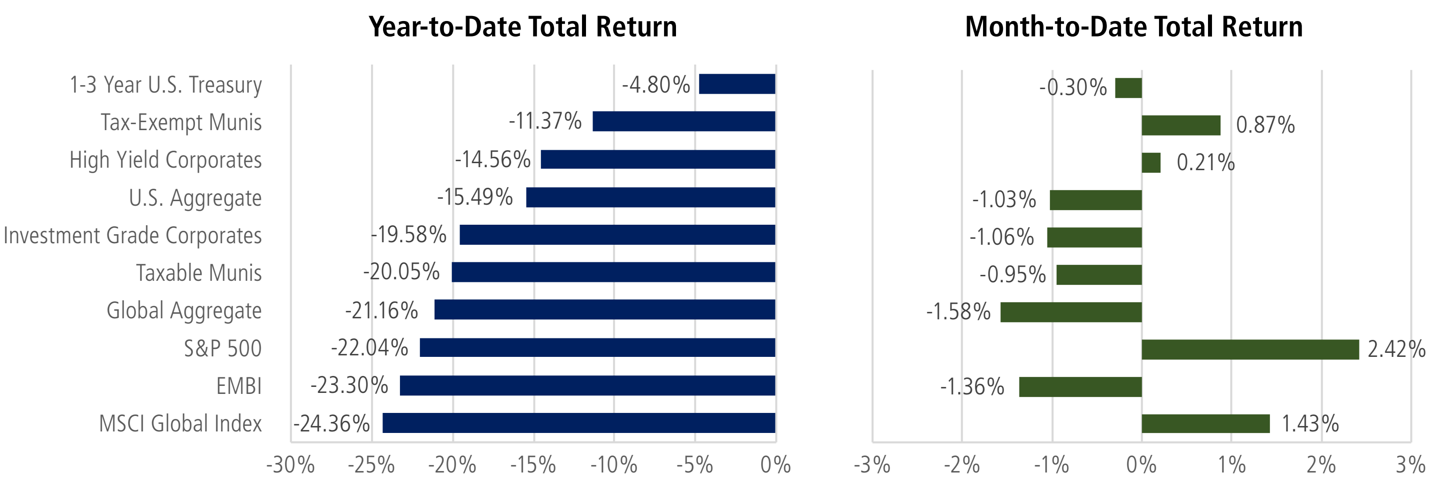
Week Ending: **October 14, 2022**

Shelter From The Storm

Economic Overview:

Hope springs eternal for an inflation slowdown that gives the Fed an "off-ramp" from rate hikes. Instead, inflation accelerated in September's CPI, with core CPI up 0.6% on the month and 6.6% versus a year ago. "But," cry the CPI contrarians, "inflation is all driven by the shelter component, which lags market rate rents!" Yes, the shelter* component rose 0.7%, accounting for 40% of the rise in core CPI. But the Fed expects inflation to slow regardless of the driver. More to the point, Fed Governor Christopher Waller says that neither data errors nor conspiracies explain the shelter lag. Instead, "only a fraction of households sign a new lease in a given month or renew their lease each month," meaning shelter prices move more slowly than market rents. Waller believes shelter prices will fade next year, but core inflation must moderate sooner. How? Non-shelter services and core goods (60% of core CPI) must slow "to a monthly average of less than 0.2%." How did Waller's basket fare in September? Not good, rising 0.5%, and cementing another 75-bps rate hike in November.

Total Returns by Asset Class



Source: Bloomberg

Highlights of the Week:

Corporates: Before Morgan Stanley announced Friday morning that they were issuing new debt, this week would have been the third week this year with no investment-grade corporate new issue supply. Potential issuers have been standing down amidst market volatility and the September CPI release. Further pressure pushed investment grade corporate spreads to reach new year-to-date highs this week, with the Bloomberg U.S. Corporate Index OAS widening to as high as 165 basis points.

Securitized Products: With the Fed no longer actively buying mortgages and financial institutions focused on making loans, money managers are tasked as the marginal buyer of new mortgage originations. According to Freddie Mac, the market's turbulence has lifted the 30-year mortgage rate to a two decade high at 6.92%. This rate should adversely impact housing demand and potentially lower 'shelter' inflation.

Municipals: Lipper reported another $5.8 billion in outflows from municipal mutual funds this week. That number takes the cumulative outflows this year to over $100 billion, creating sustained selling pressure in the market and far surpassing the previous calendar year record of 2013 when the "taper tantrum" helped spur $60 billion of outflows.

Equities: The equity market ended the week unchanged, despite inflation data remaining elevated. The third-quarter earnings season kicked off in earnest, with banks posting better-than-expected results. Value-oriented sectors such as consumer staples, health care, and financials were the best performers. Growth-oriented sectors such as technology, consumer discretionary, and utilities were the worst performers.

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