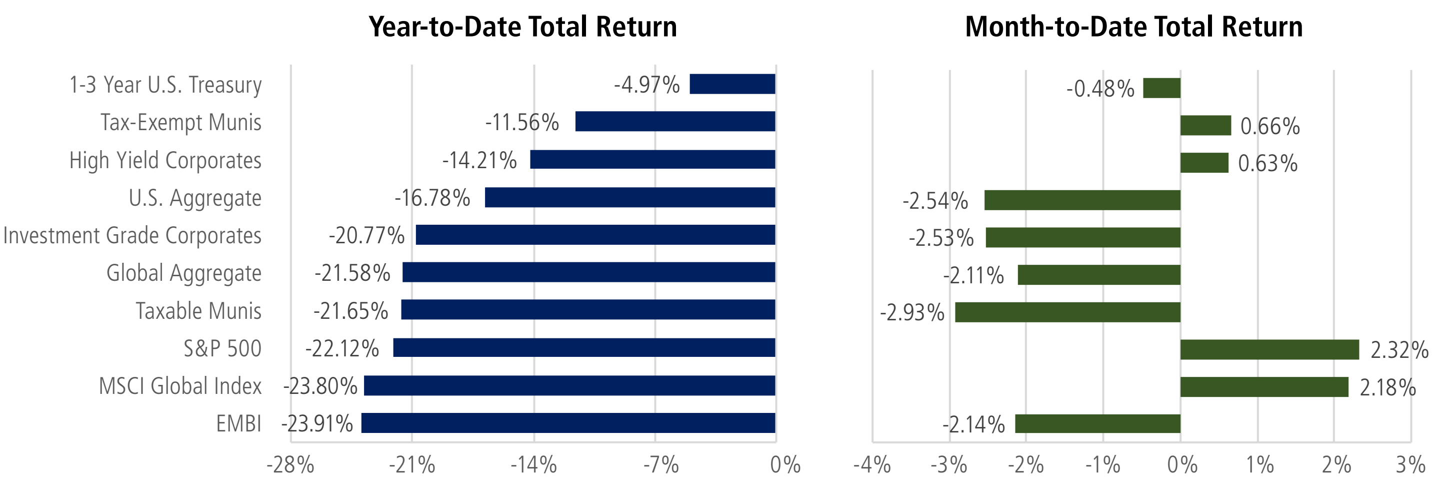
Week Ending: **October 21, 2022**

Regime Shift?

Economic Overview:

After last week's surprising September U.S. inflation data, friends and colleagues complained that shelter prices were driving inflation. We countered that while shelter prices have contributed, price pressures are worrisomely broad. This week brought more bad news on the global breadth of inflation. The U.K., euro area, and Canadian statistical agencies all reported September inflation readings that topped expectations, again confounding hopes of a downshift in price pressures. Inflation is global and not getting better. Interest rates resumed their march higher as a result, with risk assets a casualty. Worse, after a decent 20-year run, inflation is running away from central bank targets. Again, some colleagues blame drivers beyond central bank control. Perhaps. But central banks who accepted plaudits for a period of price placidity must demonstrate their worth in times of unwanted instability. We share our colleagues' skepticism that inflation can be easily tamed, but we do not doubt that charts like the above will force central banks to make every effort to prove their worth.

Total Returns by Asset Class



Source: Bloomberg

Highlights of the Week:

High Yield: BBB corporate bonds represent a $3.4 trillion universe, but despite slowing economic conditions, a wave of downgrades to high yield does not appear imminent. While $603 billion of investment-grade debt is one or two agency downgrades away from a high yield rating, only $8 billion is on negative watch by at least one agency.

Corporates: The new issue market for investment-grade corporates has been relatively active, with five consecutive days of new issues starting from last week Friday. Despite this, volume stands at $39.7 billion on the month, which is on track to miss estimates of $75 billion with only six trading days left. This miss could be due to a lack of self-led big-six bank deals. So far, Morgan Stanley is the sole issuer.

Securitized Products: The end of September saw one of the most relentless 5-day periods of European CLO sales. While the unwinding of 2008 was larger, it took longer to play out. Liability-driven investment (LDI) investors needed to raise funds with any means possible to meet margin calls amidst rising gilt yields following the U.K.'s 'mini budget.' Relatively short-duration CLO's appeared to be some of the most liquid and highest cash price assets they owned.

Municipals: Today, the tax-exempt municipal index's yield reached 4.20%, the highest since 2011. For a California investor in the top tax bracket, that's the equivalent of a 9.15% yield in fully taxable security.

Equities: The U.S. equity market continued its recent grind higher, with all sectors up on the week on better-than-expected earnings announcements. Energy, technology, and materials led the market higher, while health care, staples, and real estate lagged.