

June 20, 2023 – Investment Commentary

Macro Matters: The Big Four

Last week provided a wave of monetary policy announcements, with four major central banks releasing decisions. Their conclusions reflect the fact that their respective economies are in very different places.

US Federal Reserve Hawkish Pause: Higher for Longer

The week started with the US Federal Reserve (Fed) holding rates at current levels. But it was a decidedly hawkish pause, with the Fed suggesting more rate hikes could be coming soon. The Fed anticipates two more rate hikes this year. This outlook reflects concerns that core inflation is too sticky – the Fed revised up its projection for core inflation and revised down its projection for unemployment for the end of the year. As a reminder, “what the Fed says and what they do” are not always consistent. The Fed’s December 2021 forecast was for a median fed funds rate of 0.90% by the end of 2022. Actually, the fed funds rate ended 2022 in the 4.25%–4.50% range. We believe the Fed wants to keep inflation falling, prevent any reacceleration, and keep rates higher for longer. The reason is that the Fed is faced with a resilient US economy and tight labor market, which could keep inflation stubbornly high.

European Central Bank (ECB): Hut, Hut Hike

The ECB hiked rates last week. The eurozone economy is in a different place than the US economy. The ECB started hiking rates later and has not been as aggressive as the US ECB President Christine Lagarde believes there is more work to be done.

Bank of Japan (BOJ): Lower for Longer

The BOJ maintained its ultra-accommodative monetary policy at its meeting last week and said it would continue to “patiently” maintain this policy. Japan is an outlier among major developed economies. It’s experiencing its strongest economic growth in decades which is a welcome change for an economy that has been stagnant for multiple decades.

People’s Bank of China (PBOC): Show Me the Growth

The PBOC increased monetary policy accommodation by lowering policy rates while much of the world is tightening. Recent economic data has triggered a growing view that China may not have provided enough stimulus during the pandemic relative to other major economies and that its economy could benefit from more stimulus now.

Bull vs. Bear

There is an expectation the US is coming close to the end of its tightening cycle. US high yield credit spreads have narrowed in recent months, suggesting a greater likelihood of a softer landing for the US economy, which would be positive for the global economy. As a result, there is an increasing FOMO (fear of missing out) dynamic. We believe market expectations of US central bank rate cuts in 2023 are likely to decrease over the coming weeks. We anticipate the next wave of public company earnings announcements in mid-July to be the next market catalyst as investors focus on valuations for both stocks and bonds, profit margin pressures and earnings forecasts. As a result, we emphasize global exposures to high quality companies as measured by strong balance sheets, resilient business models and management teams with a demonstrated track record of prudent capital allocation.

Disclosures

Investment Commentary Sources: Bloomberg

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