Fixed Income Market Trends & Relevance for Mortgage Rates

Speaker:
• Jay Ladieu
There can be no assurance that developments will transpire as forecasted and that the estimates are accurate.
10y Treasury Yields Moving Higher with Growth


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2y Treasury Yields Moving Higher with Tighter Monetary Policy

“A long way from getting rates to neutral...The Fed’s ultra-accommodative policy to bring the economy out of the Great Recession is no longer needed”
Fed Chairman Jay Powell Oct 2018

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Market Questions Fed Policy Mistake?


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"I am concerned we are on the precipice of a policy mistake. We are good where we stand right now..."
James Bullard, St Louis Fed Res Bank President  Jan 2019

“Especially with inflation low and under control, we have the ability to be patient”
Jay Powell, Chair of the Federal Reserve  Jan 2019

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2019 U.S. Market Outlook

**Economy**
- Growing at a slower rate
- Limited upside to inflation
- Fiscal stimulus fading

**Event Risk**
- Trade Tensions & Tariffs
- Brexit
- Late cycle credit concerns

**Monetary Policy**
- Dovish Pivot
- Wait and see approach
- Sustain the expansion

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**Fundamentals are not indicative of a recession, but does the market agree?**

**Is the neutral rate lower implying current policy is restrictive?**

**Negative sentiment, does behavioural feedback loop increase downside risk?**

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Source: SSGA as of June 5, 2019.
Global Growth Concerns

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Fading Fiscal Impulse

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Lower Yields Justified by Fundamentals?

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Market Uncertainty

Market pricing 2-3 rate cuts by 2020

Inflation & Inflation Expectations Remain Depressed

Growth Concerns


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Uncertainty & Risk Premiums

Aug 2011 - European sovereign debt crisis sparks contagion fears negatively impacting risk assets.

Feb 2016 – Price of oil declines over 50% from May 2015 – Feb 2016, combined with other factors causes credit spreads to widen materially. GNMA MBS outperform.

Policy uncertainty, trade concerns and late cyclical credit dynamics

Source: SSGA, Barclays Live data as of June 3, 2019.

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Summary

- Cyclical peak in long term U.S. rates is behind us
- Neutral rates of interest are lower than expected
- Fed may be behind the curve
- Less restrictive monetary policy should offset late cycle deceleration
- If so, rates should remain low and environment supportive of risk assets
- MBS spreads should remain range bound
- BUT...recession risk has increased
- Behavioral feedback loop is powerful

Source: SSGA as of June 6, 2019.

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Disclosure

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