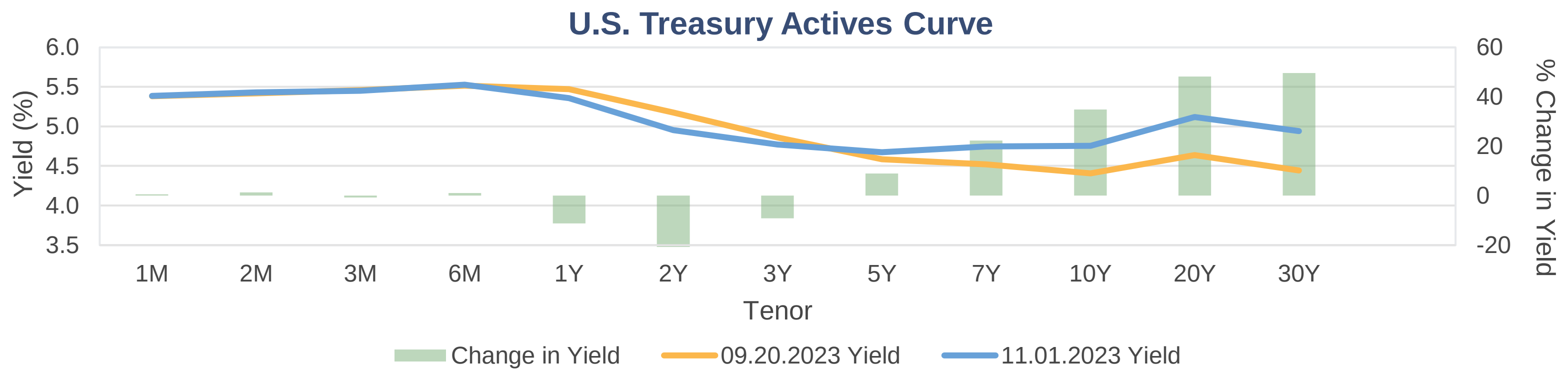
No Surprises from the Fed

November 2, 2023

Markets breathed a sigh of relief as the Federal Reserve (Fed) maintained the current fed funds rate at an upper bound of 5.50%. The statement that was released was nearly identical to the September 20 statement with a notable exception, referencing the recent sharp increase in rates and noting that “tighter **financial** and credit conditions for households and businesses are likely to weigh on economic activity, hiring and inflation.” The insertion of **financial** is the key addition. During the press conference Fed Chair Jerome Powell also referenced this increase in rates and its potential headwind for the economy. However, he also acknowledged that while progress has been made on the inflation front, more work is needed to bring inflation down to their goal. The option to hike again is still on the table, but the Fed is also weighing the cumulative effect of the recent hikes which may not be fully realized yet.

U.S. Treasuries, which were already rallying on the news that the treasuries refunding requirements were below expectations, continued to gain during the press conference. Both U.S. Treasuries and risk assets appreciated on the perception that this statement and subsequent press conference were more dovish than anticipated. Both 2-year and 10-year yields dropped by more than ten basis points, falling to 4.77% and 4.96%, respectively.



Our View:

This marks two consecutive pauses for the Fed, but we remain unconvinced that this hiking cycle is over. Importantly, we think a change in Fed policy to cuts is an even higher hurdle. Inflation is still well above goal, and employment, growth and wages remain strong. However, we do expect a slowdown in growth next year and remain positioned with an up in quality bias. Tactically, we may add incremental exposure to risk assets as opportunities emerge. On the duration front, we are generally neutral but will also opportunistically add or reduce exposure as rate volatility remains elevated.

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Chart and textual data is as of 11.01.2023 and is sourced from Bloomberg L.P.