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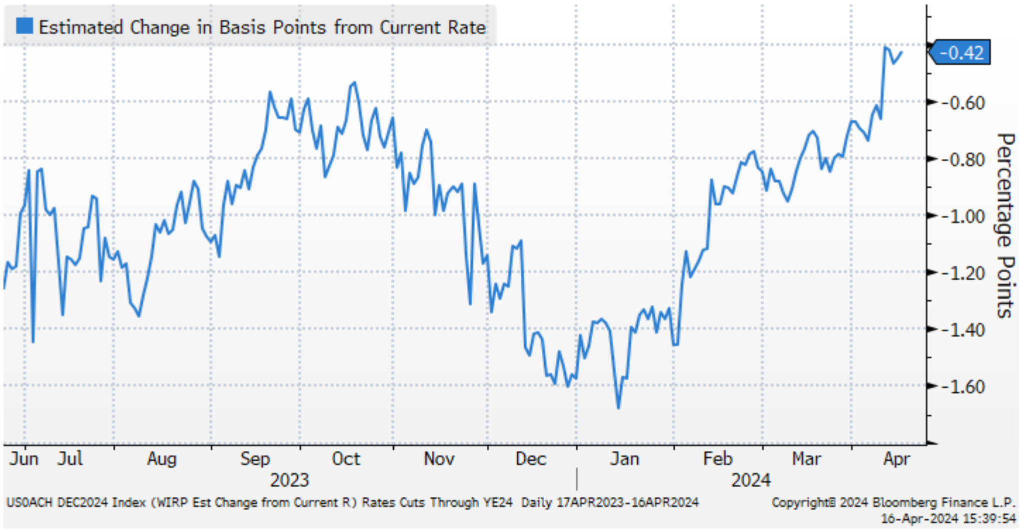
The First Cut is. . .



- In mid-January, markets were pricing 170 basis points (bps) of rate cuts (equivalent to nearly seven 25 bps rate cuts) to occur during 2024.
- However, the persistence – and in some cases the re-acceleration – of inflation this year (and to a lesser degree the strength of the U.S. economy) has led investors to push out the timing of the first rate cut and decrease the quantum of cuts forecasted for 2024.
- Currently, only 42 bps of rate cuts (equivalent to one 25 bps cut and a 68% chance of another 25 bps rate cut) are priced into markets.
- At a conference today, Federal Reserve Chair J Powell stated that “policymakers need more confidence that inflation is moving back to the 2% target sustainably before adjusting policy”.
- He added that if higher inflation does persist, the Fed can maintain its current rate to allow restrictive policy to work for a time.
- His comments suggested that rate cuts in either May or June are unlikely.
- During his comments, the yield on the 2-year U.S. Treasury topped 5%, its highest mark since November.
- Our view entering the year was that the Fed was unlikely to cut interest rates as much as the market was pricing. To express this view, we added more floating rate exposure to portfolios.
- Following the re-pricing of yields (higher) as investors reduced their outlook for rate cuts, we now believe that the market is more balanced and intermediate-maturity bonds are attractive as both a source of income and as a hedge against risk-off environments.

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