INVESTMENT STRATEGY
WEEKLY VIEW

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THIS SELL-OFF IS STARTING TO MAKE BONDS LOOK INTERESTING

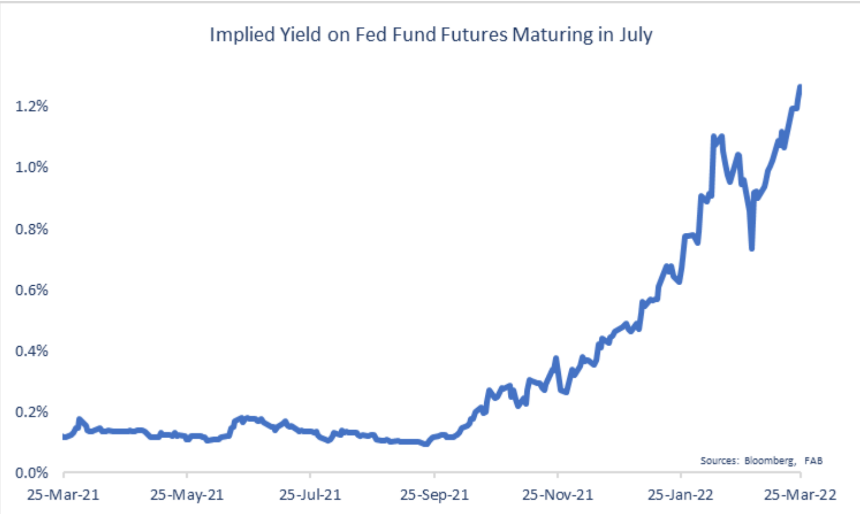
March 28th 2022

- The yield on two-year US Treasuries hit 2.4% today and the five-year hit 2.67%
- Fed fund futures are signalling aggressive rate hikes this year and cuts in 2024
- EM dollar bond yield premiums have fallen but yields are approaching recent highs
- The rally in commodities prices has slowed down but its underlying strength remains

The market has all but priced in at least a couple of 50 basis points hikes by the Federal Reserve in the coming months. And several Fed speakers are somewhat confirming those expectations with three of them suggesting last week that they would favour a bigger move in April while Chairman Jerome Powell indicated he was not against it either.

Fed fund futures, however, are signaling that after hiking to 2.9% by the end of 2023, the central bank may have to cut rates in 2024. The Treasury yield curve is also inverting indicating markets see a potential recession ahead. The two facts together suggest that, after yields rise a bit further, long-term, high duration bonds could start to be an attractive proposition.

THE MARKET HAS ALREADY PRICED IN TWO 50 BASIS POINTS FED HIKES BY JULY



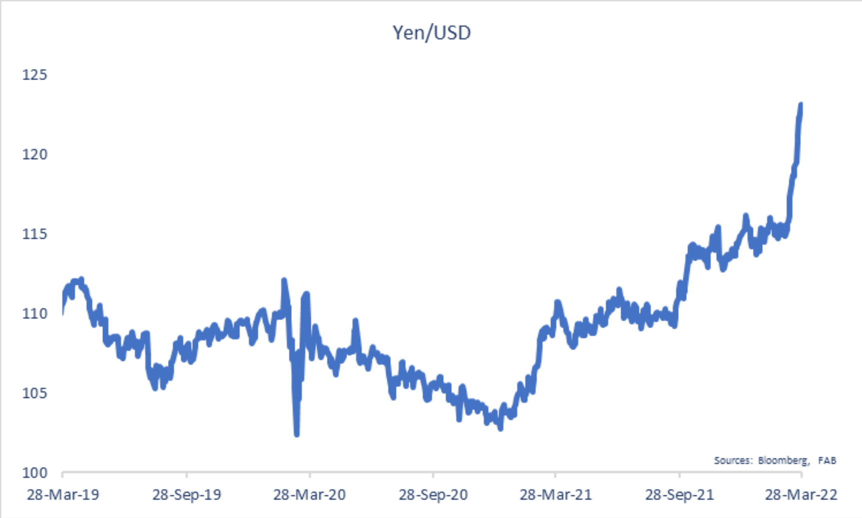
- The implied yield on Fed fund futures maturing in July is already at 1.27%, which implies two 50 basis points hikes in the next two meetings.
- Futures are indicating expectations that the US benchmark rate will be at 2.4% by January.
- However, Fed fund futures suggest that the central bank will have to start cutting rates in 2024 after hiking rates to nearly 2.9% by the end of 2023.
- This inverted curve indicates markets are now expecting the Fed to cause a recession before it reverses course.

THE YIELD ON 10-YEAR US TREASURIES IS BACK AT LEVELS NOT SEEN SINCE EARLY 2019

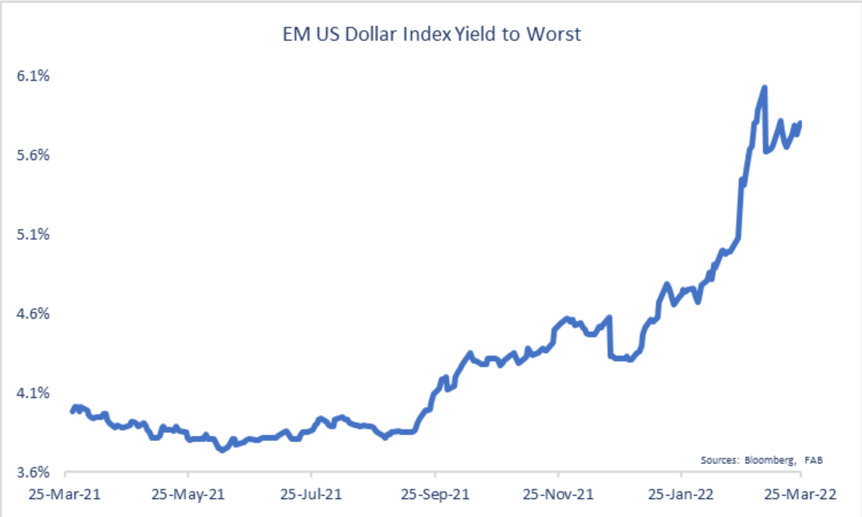
- The yield on 10-year US Treasuries has increased 52 basis points in the past two weeks to 2.51% on Monday, as markets priced in potential 50 basis points hikes ahead for the Fed.
- The yield on the three– and five-year US Treasuries moved even more, by more than 70 basis points each, in the past two weeks, to 2.59% and 2.62%.
- Yields on emerging market and corporate bonds did not move as fast but are likely to catch up in the coming weeks, potentially providing a good entry point for investors.

THE JAPANESE YEN IS ON TRACK FOR ITS BIGGEST MONTHLY LOSS SINCE MARCH 2001

- The Japanese yen has fallen 7.27% against the US dollar since the end of February and the pair was trading at 124.01 at the time of writing.
- The Bank of Japan intervened in the bond market today as the yield on 10 -year Japanese government bonds approached 0.25%, the highest level since 2016.
- Unlike other central banks, the BoJ has stuck to a loose monetary policy.
- A falling yen tends to support Japanese stocks, and the Nikkei is up 5.34% so far this month.



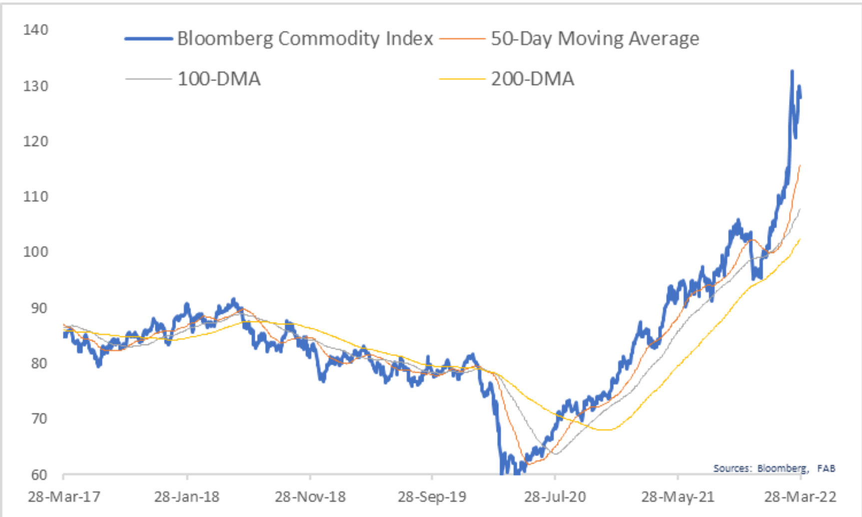
THE EM DOLLAR BOND INDEX YIELD IS NEAR 6%, AND IS LIKELY TO MOVE HIGHER



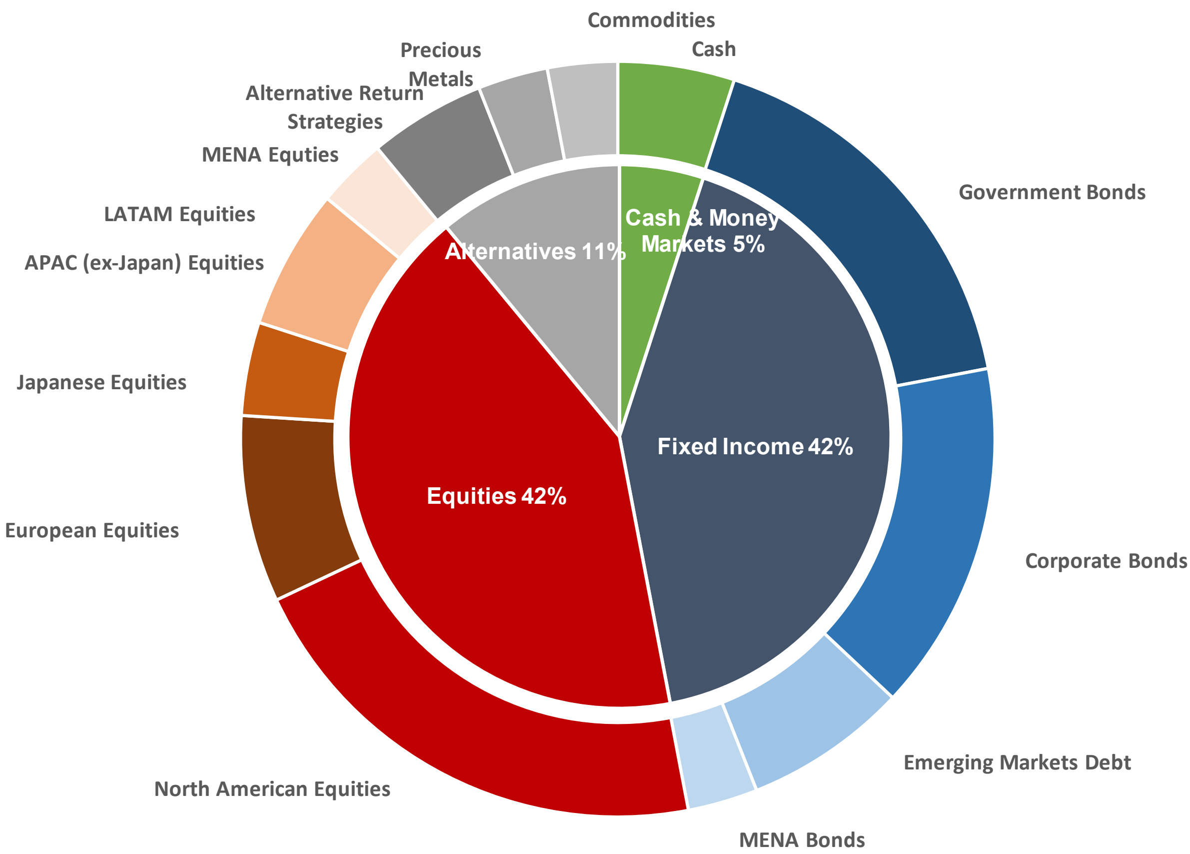
- After spiking on the back of the Eastern European crisis, the yield on the EM dollar index has retreated as Russia was removed from it.
- Average yields for the index are close to 6%, though, a level from which they have retreated most of the time since the 2008 crisis.
- The average spread for the EM dollar bond index, however, has tightened to 328 basis points after touching as high as 421 basis points on March 7th.
- Spreads are likely to rise as corporate bonds catch up with Treasuries.

THE COMMODITIES RALLY IS FALTERING, BUT THE BULL MARKET COULD CONTINUE

- Oil prices retreated today after Yemeni groups said they would halt attacks on Saudi Arabia.
- The US, however, said it is not optimistic about a deal with Iran happening so soon.
- The lack of investment in new energy and metals output over the past five years, however, suggests that prices for these materials will remain high.
- Some soft commodities which require heavy use of fertilizers, such as wheat, could continue to see high prices for a couple of years.



Asset Class	Positioning	Detail
Cash	Underweight	Putting cash to work in risk assets.
Fixed Income	Overweight	Keeping a slight overweight focused on EM dollar debt.
Equities	Overweight	Slightly overweight in Asia ex-Japan and US markets.
Alternatives	Underweight	However, reducing the underweight in hedge funds.



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