

The Fed's Market "Put" Option

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Fundamental valuations for asset prices are broadly attractive. The risks we need to be wary of stem from non-fundamental risk factors such as politics and trade. However, fixed income assets largely reflect this in their current pricing. As a result, a bull case for fixed income assets could be form of a residual, in that a specific catalyst may not be necessary. Instead, stability and the worst case scenarios not being realized may be enough to push asset prices higher.

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The U.S. Federal Reserve (Fed)

- Is there a "Powell put"? Yes.
 - Powell laid out a conditional case for raising rates gradually if inflation falls below target and growth slows
 - Balancing the risks: Tightening too little with tight labor market vs. too much if inflation doesn't break target
 - **Our takeaway:** Jackson Hole tells us Fed policy will support riskier assets

The Yield Curve

- What is the yield curve telling us?
 - This is a source of debate within the Fed, including which segment of the curve offers the strongest market signals
 - This tells us the Fed is concerned about the curve and what it may signal to investors
 - Note: the yield curve does not factor into the Fed's econometric models, so it's a bit of a mystery to them
 - **Our takeaway:** The fed is NOT tightening, they are removing accommodation and moving to neutral. The curve sends a stronger signal when the Fed is actively trying to slow the economy by hiking above neutral (i.e. tightening).

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U.S. Rates

- U.S. Treasury 10-year is likely range bound: 2.75% - 3.10%.
 - Little information until either end of the range is broken
 - Slower pace of rate hikes reduces the upside in 10-year yields during this cycle

Emerging Markets (EM) & the U.S. Dollar (USD)

- EM and the USD are going through a rough patch, but we believe opportunities have been created
 - We see the risk in EM as idiosyncratic (Argentina, Brazil, Turkey) not systemic
 - However, a general risk-off tone in the asset class has taken some of the strong countries down with the weak
 - This is where we see opportunities
 - **Our takeaway:** Global growth, firm commodity prices and now a weakening USD are three key factors that could support this asset class into year end, providing political risks do not dominate risk sentiment.

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