Rates

Opportunities as the Fed Stays Put

A resilient economy has led to significant market repricing in rates.

With continued strength in employment data and with inflation data surprising to the upside for three consecutive months, the market is reassessing the Fed's expected 2024 easing campaign. Even with the lower than anticipated increase in April employment, Federal Open Market Committee participants have indicated a longer timeline to rate cuts. In turn, Treasury yields have moved higher. This has not changed our call for the next cyclical move in the Treasury yield curve to be a bull steepening, nor where we continue to find value in the market.

Sector Commentary

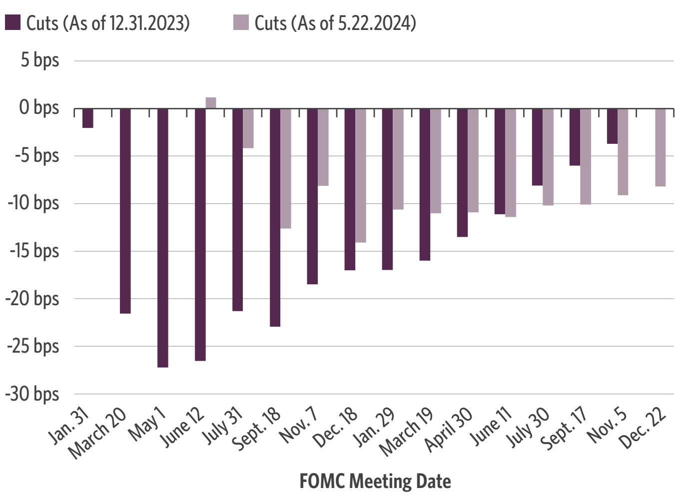
- Solid economic data and continued strength in realized inflation readings in the first quarter led the market to significantly reprice the number of Fed rate cuts expected this year, down from six 25 basis point cuts at the beginning of the year to just two cuts as of May.
- As the balance of economic data has proven more resilient than Fed officials expected, Fed messaging has shifted toward a higher-for-longer theme on rates.
- As the higher for longer rate messaging and market pricing has taken hold, real yields have increased on inflation-linked bonds.

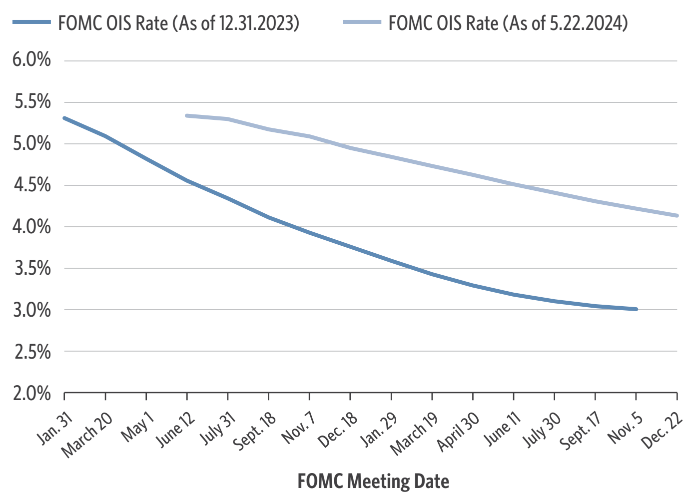
Investment Themes

- We expect yields to remain in a tighter range than 2023 and favor tactically adjusting duration based on where we are in the range.
- The front end of the Treasury curve looks attractive both on a real and nominal yield basis as Fed easing expectations have been scaled back.
- In an environment where inflation remains sticky and front-end nominal Treasury yields have risen close to 5 percent, we favor front-end Treasury Inflation-Protected Securities.
- With the increase in Treasury yields and nominal spreads remaining wide, longer-maturity callable Agency bonds look compelling for yield-oriented accounts.
- We continue to expect that the next large cyclical move in the Treasury market will be a bull steepening of the yield curve where front-end yields will decline more than longer-term yields.

By Kris Dorr and Tad Nygren

Dwindling Expectations of Rate Cuts Drove the Front End of the Yield Curve to Attractive Levels





Source: Guggenheim Investments, Bloomberg. Data as of 5.22.2024.

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