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Fixed Income Market Review – March 2024

US Yield Levels

Date	2-year	10-year	30-year
3/28/24	4.59%	4.20%	4.34%
2/29/24	4.64%	4.25%	4.38%
1/31/24	4.27%	3.99%	4.22%
12/29/23	4.23%	3.88%	4.03%
11/30/23	4.73%	4.61%	4.73%
10/31/23	5.07%	4.88%	5.04%
9/29/23	5.03%	4.59%	4.73%
8/31/23	4.85%	4.09%	4.20%
7/31/23	4.88%	3.97%	4.02%
6/30/23	4.87%	3.81%	3.85%
5/31/23	4.40%	3.64%	3.85%
4/28/23	4.04%	3.44%	3.67%
3/31/23	4.06%	3.48%	3.67%
2/28/23	4.81%	3.92%	3.93%
1/31/23	4.21%	3.52%	3.65%
12/30/22	4.41%	3.88%	3.97%
11/30/22	4.38%	3.68%	3.80%
10/31/22	4.51%	4.10%	4.22%
9/30/22	4.22%	3.83%	3.79%
8/31/22	3.45%	3.15%	3.27%
7/29/22	2.89%	2.67%	3.00%
6/30/22	2.92%	2.98%	3.14%
5/31/22	2.53%	2.85%	3.07%
4/29/22	2.70%	2.89%	2.96%
3/31/22	2.28%	2.32%	2.44%
2/28/22	1.44%	1.83%	2.17%
1/31/22	1.18%	1.79%	2.11%
12/31/21	0.73%	1.52%	1.77%
12/31/20	0.13%	0.93%	1.65%
12/31/19	1.58%	1.92%	2.39%

***Source US Treasury Department**

Interest rate levels declined but just to a very slight degree during March. The yield curve, 2-year to 10-year, remained inverted as it has been since July of 2022. This inversion continues to not be a predicter of a recession as it has been so many times in the past.

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Bloomberg Barclay's Fixed Income Index Returns

Index	March 2024	Last 3 Months	Last 12 Months
Aggregate	0.92%	-0.78%	1.70%
Int Agg	0.78%	-0.42%	2.30%
Gov't/Credit	0.88%	-0.72%	1.74%
Int Gov't/Credit	0.64%	-0.15%	2.69%
Gov't	0.64%	-0.93%	0.13%
MBS	1.06%	-1.04%	1.39%
ABS	0.49%	0.68%	4.32%
CMBS	0.91%	0.85%	4.42%
US Credit	1.23%	-0.41%	4.15%
US Corp High Yield	1.47%	11.15%	2.19%

Employment Report News

As reported by the Labor Department on March 8th, US employers added 275,000 jobs during February. The December number was revised sharply down from 353,000 to a level of 229,000. The unemployment rate rose from 3.7% to 3.9%, its highest level since January 2022. Ian Shepherdson, Chief Economist for Pantheon Macroeconomics stated, "The current trend in payrolls is steady, but a clear downtrend is coming." I disagree and continue to stick with Federal Reserve Chairman Powel who previously stated, "The economy is performing well, the labor market remains strong."

From the same Labor Department report, average hourly pay rose 5 cents to $34.57, but the year-long increase declined from 4.4% to 4.3%. This is above the level the Fed would like of 3.5% to align with its 2% inflation goal level, but is above the current inflation rate, which remains good news.

The report also indicated that in February the US labor force increased by 150,000. The share of adults in that group held steady at 62.5%, down somewhat from a recent high of 62.8% and the level of 63.3% before the pandemic. Looking forward, in January employers posted 8.9 million job ads. This is below the peak of 12 million posted ads in March 2022. In the reverse, just 3.4 million quit jobs, the fewest since January 2021.

The naysayers such as Shepherdson, identified above, are indicating the economy and job market will weaken. But I believe in the Fed, rather than economists at independent firms that don't influence the future.

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Housing Market

On March 15th Freddie Mac reported a current decline in mortgage rates with 30-year fixed-rate mortgages down from 6.88% to 6.74% and 15-year rates down to 6.16% from 6.22%. However, as continuing the progression of naysayers, with who I disagree, the Chief Economist of Freddie Mac stated after two straight weeks of rate declines, "there is a good possibility that rates will stay higher for a longer period of time."

I find a problem with this position because warmer spring weather traditionally brings out more buyers, especially with the recent realtor's settlement decreasing the amounts of sale prices lost to commissions. At the same time, reported March 18th, homebuilders' sentiment rose 3 points to 51 during March in the National Association of Home Builders/ Wells Fargo Housing Index. This represents the fourth-straight monthly gain and the highest level for the Index since July. Fifty in the dividing line between positive and negative sentiment.

Also in March, 24% of builders reported cutting home prices. Though this is the lowest cut percentage since December 2023, the average cut has held steady at 6%.

As to home prices, the S&P CoreLogic Case-Shiller US National Home Price Index rose 6% in January over the trailing year period. The average 12-month increase through December was 5.6%, Demand was stifled last year for a variety of reasons, but my expectation is it will pick up this year. This expectation on my part is without regard to any rate cuts by the FED.

Inflation

Published on March 29th, the Fed's preferred measure of inflation, the PCE, was reported by the Commerce Department as rising just 2.5% for twelve months through February. The Core PCE for the trailing 12-month period slowed slightly to 2.8% in February, down from 2.5% through January. Other measures were not as favorable.

Published March 12th, the Labor Department indicated its CPI measure rose 0.4% in February, up from 0.3% in January and by 3.2% for the 12-month period ending in February, versus 3.1% for 12-months ending in January. The Core CPI measure increased 0.4% in January with the 12-month number declined slightly to 3.8% ending in February, down from 3.9% in January. This was the smallest twelve-month increase since May 2021. The cost of services, especially rent, are the primary factors keeping the increases up.

In the face of these inflation numbers, the Commerce Department reported consumer spending jumped by 0.8% in February, up from 0.2% in January. This was the largest monthly rise in twelve months.

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Early in February, Chairman Powell reported to Congress the Fed will likely reduce its primary interest rate level this year, but not until there is more evidence inflation is moving toward the Fed's goal of 2%. The US futures market is now moving the date for the first cut from March to June and has reduced the projected number of cuts from six to four in 2024. I believe the market may be correct in the starting date for cuts, but is projecting more than will likely take place.

As to the sources of inflation apart from rent increases, gasoline prices jumped in February by 3.8%, after four straight months of declines. I believe this ties in to increasing demand with spring soon starting.

As to food, grocery prices were unchanged for the month, reducing the twelve-month increase number to 1%. However, egg prices jumped 5.8% for the month with the avian flu outbreak.

Even with a spate of minimum wage level increases across the country combined with a shortage of workers, restaurant prices increased only 1% on average across the country.

Rents rose 0.5% on average during February, but with the twelve-month increase now 5.8% from 6.5%. Air fares jumped 3.6% for the month. Used car prices jumped by 0.5% for the month and apparel by 0.6%. With improved supply chains, furniture prices fell by 0.7% and appliance prices by 0.9%.

Rent in February is now 30% above pre-pandemic levels. Zillow reports it as up 3.5% over the last year. Redfin separately reports the median rent levels were up 2.2% from the year before.

The New York Times monthly survey of sentiment reported 26% of registered voters felt the economy was good to excellent.

Goldman Sachs Briefings

I would not normally include their report but this month they made several interesting projections. These include:

- Their research arm has raised their fourth quarter forecast for core PCE to 2.4% and cut their projection for rate cuts from four to three. As little as I know compared to this group, I believe they are on target.
- They project new immigration was about 1.5 million last year above the long-term trend. They believe this increase will help increase US GDP growth and is the reason for the recent rise in the unemployment rate.
- Their economist projected with the European Central Bank, the Bank of England, the Bank of Canada and the Federal Reserve will all begin cutting rates in June.

- Even before the Baltimore Bridge tragedy, they believe maritime shipping was at its most dangerous level in history. They also include in the risk, the 500 undersea cables on which the internet runs.
- Except for the Baltimore tragedy, US supply lines are near their best levels in years.

Global Economies

I am repeating this section from last month's Review since I borrowed from news issued during early March for much of this information. Japan, which once the second largest economy in the world, had a fall in its GDP of 0.4% on an annualized basis in the 4th Quarter, after a revised decline of 3.3% in the 3rd Quarter. Though these recent quarters were negative, for the full year of 2023 Japan's nominal GDP (nominal means a value in current dollars without adjusting for inflation) grew by 5.7% to $4.2 trillion. As a comparison, Germany's nominal GDP grew by 6.3% to reach $4.46 trillion, which would marginally drop Japan to the 4th largest world economy.

As to China, from CNN on March 1st, the Chinese Purchasing Managers Index of primarily state-owned manufacturers fell for the fifth month in a row to stand at 49.1 in February, down from 49.2 in January. S&P Global instead indicated the Caixin manufacturing PMI, which is focused to smaller, private Chinese companies, rose to 50.9 in February, up from 50.8 in January.

China is about to conduct its annual session of the National People's Congress at which its global growth target will be announced. With this year's growth rate expected to be slowing to 4.5%, the Congress is expected to hear the announcement of several economic incentives from Beijing. HSBC's analysts call for China's fiscal deficit to be set at 8% of GDP.

As to OPEC, it is forecasting a much tighter oil market during the rest of 2024. It is calling for demand at 2.2 million bpd, with oil production growth only at 1.2 million bpd outside of the OPEC cartel.

Though not globally based, but a major international company, on March 27th Kimberly-Clark announced it would reorganize into three separate business units. In doing so, it would incur $1.5 billion in related costs over the next three-year period. Two of the three segments are international in nature and even the third is North America versus strictly the US. I know they are a very big company and may well be able to absorb this size hit to their financials, and I expect has a very good business reason for this approach. But it's a drastic step to take and may be an indication of some significant risks in the global economy.

As to what is much more of an international company, the rating of SBB, the Swedish property group, has this month had its credit rating cut by Standard & Poors to selective default, down from CCC+. SBB is one of Sweden's largest commercial landlords. SBB has announced it would buy back existing debt at a 60% discount to its original value. According to Standard & Poors,

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SBB has 10 billion in Swedish Crowns in upcoming debt maturities during the remainder of 2024 and 2025.

I am concerned. Is this situation an example of overleveraged debt just as has taken place in the recent months with Chinese real estate developers, that may be an indication of a global debt problem?

Bitcoin

If you have read my prior monthly Reviews, you will be aware of my distaste about bitcoin. Let me give you a little personal background on that distaste. During the period I was a principal at Allegiance Capital, a fixed income management firm, I/we had a Taft Hartley client in the Saratoga Springs area of New York State. We managed the fixed income component of their retirement plan assets. The equity component was managed by Bernie Madoff.

I regularly conducted reviews for the members of the group on how we were doing with the fixed income money. Mr. Madoff sat in on my reviews. I was not permitted to sit in on Mr. Madoff's reviews. Though we were doing well with their fixed income assets, the union members regularly questioned why, with Mr. Madoff doing so well, all funds should not be placed in Mr. Madoff's hands. Fortunately for us, he did not manage fixed income assets and the consultant emphasized the program should employ a balanced fixed income/equity approach.

It was not my place to criticize what Mr. Madoff was doing so I never did, though I had regular conversation with the consultant for the overall fund. He agreed that Mr. Madoff's returns were beyond belief, but assured me he had seen all the trade records in Madoff's office for the funds.

The end result of Madoff being sent to jail did not surprise me. It always sounded fishy to me. However, I was astounded Madoff's wife's and daughter's personal assets were all managed in the same way as all other client assets.

I have had the same reaction to crypto currency. Just as with Madoff, I have been concerned about the way the concept exists. I believe crypto may have value, just not as it exists today. There is too much room for illegal activity. Reflecting that on March 28th Sam Bankman-Fried, the self-proclaimed god of the crypto industry was convicted and sentenced to 25 years in Federal prison. He used deposits to his crypto exchange, FTX, as the assets for investment in his hedge fund. I hope he devotes his time in prison to construct an approach in which the crypto world can operate without the risk of illegal activity taking place. He might be the most informed person for working toward that goal.

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My Economic Outlook

The Federal Reserve is indicating cuts to rates are possible, but not imminent. That expectation caused Fixed Income Markets to have a decently positive month in March. However, the bigger issues for the Fixed Income markets, as well as to a degree the stock markets, are what I have been talking about for almost a year. If we have had discord across the US with national elections now less than six months away, it's only going to get worse the closer we get. Both the Republican and Democratic parties are hell bent on pulling out all stops to win.

The investment markets will as a result suffer, and volatility will be off the charts. Further, with Putin's saber rattling, coupled with Israel's unwillingness to compromise for the protection of Palestinian citizens (with the deaths of Jose Andres's aid workers deaths being a prime example) we have a huge risk of a broader war in the Middle East. This risk has increased in the last week with Iran having a general killed by Israel.

I believe people need to hunker down for the next year and protect asset holdings above all else. In this environment, fixed income might be the most conservative bet especially if the Fed begins indicating the potential for cuts sooner than what might otherwise be expected.

Bob Southard, on Behalf of Greenrock Research
April 4, 2024