Strategy

JefMacro Weekly—Story of Sticky ULCs; More On Stimulative CB Losses

March 5, 2023

Key Takeaway

Zervos shares more thoughts on weakening of monetary policy tightenings due to QE. One point, $3T mortgage portfolio on Fed's balance sheet has extended duration, could explain deep curve inversion. Aneta thinks 2 endings to sticky ULC. Neither solution creates a good ending. According to Mohit, if the rates market is correct in terms of aggressive hikes from Fed and ECB, equities and credit look rich. Sherif sees duration as more attractive than spread risk.

David Zervos—Macro prudential regulation has come a long way and likely leads to fewer negative feedback effects. And there's been a healthy amount of tightening "pain" already delivered into the global economy, just not as much as might have been expected. For every existing debtor that struggles with higher rates, there is a creditor that benefits from higher rates, mitigating some aggregate pain. The $3T mortgage portfolio on Fed's balance sheet has extended duration and could explain the deep curve inversion.

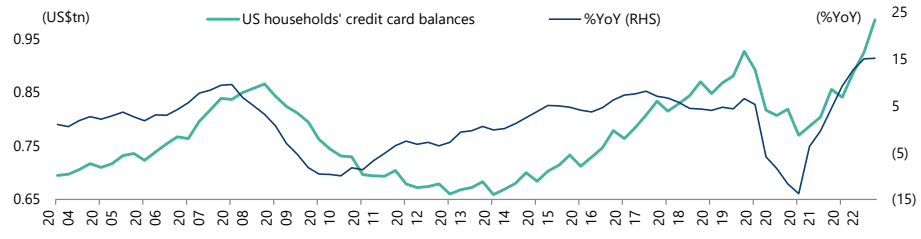
GREED & fear—Our main reason for taking a bearish view on the US economy is the collapse in money supply growth and the inverted yield curve. We remain tactically bullish on Treasury bonds on the view that the US economy will slow due to tightening. However, GREED & fear remains a structural bear on Treasuries because the Fed will look to fudge the 2% inflation target when presented with evidence of a weakening labor market.

Aneta Markowska—There are two possible endings to the story of sticky ULCs. Firms continue to pass through labor cost increases; preserves margins, keeps labor market intact. But, inflation remains elevated and Fed hikes rates further than our 5.1% terminal rate. Or, consumers push back against higher prices; firms fail to pass through cost increases. Margins contract, triggering cost cuts and layoffs, bringing the cycle to an end.

Mohit Kumar—If the rates market is correct in terms of aggressive hikes from Fed and ECB, equities and credit look rich. Short term, the market is pricing in too much from CBs and see a consolidation in rates, which gives support to risky assets. Medium-term, we see a resolution via lower rates and lower credit/equities.

Sherif Hamid—We see the strong performance of stocks and spreads a tad disturbing against the backdrop of the move higher in rates. We see rate duration as materially more attractive than spread risk; we would be trading long duration and smaller long in spread risk, with a view to buy dips should they come.

US household credit card balances are up over 15% YoY



Source: Federal Reserve Bank of New York; Jefferies

JefMacro

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^Prior trading day closing price unless otherwise noted.

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