Strategy

JefMacro Weekly—How High Is High Enough? Thoughts On The Terminal Rate

February 26, 2023

Key Takeaway

GREED & fear thinks Fed willing to fudge 2% inflation target in interest of supporting economy/preserving negative real interest rates. Mohit favors expressing long rates in Europe, favors Europe & Asia equities vs. US. Aneta does not change base case; terminal rate 5.1%, chance of June hike. Sherif would close net risk short, use weakness to inch longer, if spreads crack further, get aggressive. Interesting chart from Vanda Research on retail trading volume.

GREED & fear—Our base case remains that it will become clear to investors that the Fed is willing to fudge its 2% inflation target in the interest of supporting the economy and preserving negative real interest rates. The question will become how the government bond market reacts, and it is unlikely to be a bullish reaction. However in the short term, GREED & fear's expectation would be for the bond market rally to resume in the US.

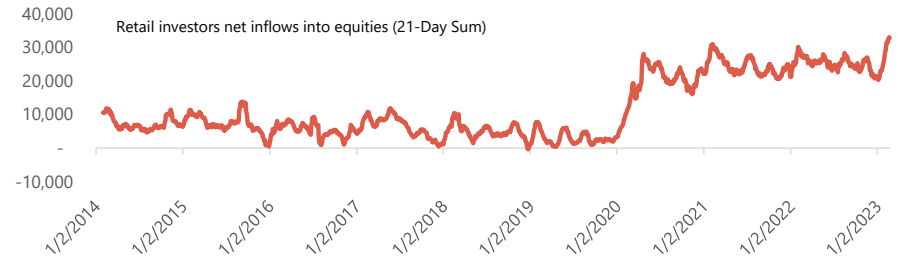
Aneta Markowska—Our base case has not changed: we continue to see a 5.1% terminal rate. We acknowledge upside risk to view, and see a June hike as a realistic possibility. But, a July hike is very unlikely. We think the Fed will view policy as "sufficiently restrictive" by mid-year, which will raise threshold for further hikes. We expect the data to be notably softer, which means that we won't clear the threshold.

Mohit Kumar—Market is pricing in more than 3 hikes from the Fed, 3.85% as terminal rate for the ECB. We maintain the view that the rates market is pricing a lot from CBs, and should not sell-off significantly from current levels. We favor expressing the long rates view in Europe rather than US. We remain neutral on equities and credit. We see continued resilience of European equities and credit and favor Europe & Asia over the US.

Sherif Hamid—With rates continuing to march higher, we have finally seen risk assets start to "crack" to catch up. Valuations have moved a long way, with IG yields in the mid 5% and HY back to 8.75%. We would be closing net risk short, start to use weakness to inch longer; however would love to see spreads crack further to get more aggressive.

Global Strategy—The Euro-zone is beginning to show how responsive the economies are to both a change in the cost of living and an inexpensive euro. Europe might produce the best relative earnings revisions globally.

US retail investors have bought a record amount of stocks lately



Source: Vanda Research; Jefferies

JefMacro

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^Prior trading day closing price unless otherwise noted.

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