

1st Quarter 2023

Not surprising, the battle between market expectations and actual Federal Reserve actions was evident over the course of the quarter. Until expectations and the Fed fall into (relative) sync, we will continue to see volatility manifest itself in the market in different ways.

The banking sector challenges this past quarter are a prime example. As we touched on a few weeks ago in our note to clients, the aggressive interest rate hikes by the Fed during 2022 led to some stress on the banking sector. What was eye opening to many was the suddenness of the impact to a handful of names at the end of last month. We do not see recent events causing a broader contagion as we believe most banks - including U.S. money center, large regional and global banks - remain well capitalized and very diversified. However, the situation continues to evolve and, we expect volatility and poor liquidity to persist as the market digests daily headlines, all while market expectations and Fed actions work to find a level of coexistence.

Volatility was apparent in the US Treasury yield curve as well. As the quarter came to a close, we were greeted with a steeper inverted curve, with short maturities up while the longer end shifted down. There is likely more shape and shifts to come as the market and the Fed work to get in sync.

Volatility can bring opportunity, but we also need to remain vigilant. Our consistency in approach in buying good bonds with realizable yield will be hard at work over the coming months. The good news is overall rates are significantly up from where they were a year ago. For our stable value clients, you are more insulated in the gyrations of the rates, but in general, the crediting rates of your portfolios continue to work their way up. To our fixed income clients, you are seeing some of the volatility in your total returns, but you also continue to see strong yield-to-maturity in your portfolios. We are likely not done talking about volatility. We'll report back next quarter.

Ajay Mirza and Mike Norman
Senior Managing Principals