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Weekly Market Commentary
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What's Up With Bonds Being Down?

Volatility in the stock market has been front and center, with the S&P 500 experiencing the first 10% correction in two years in March. While swings like this are rather normal for equities, it's the recent pullback in bonds that's capturing more of the attention, as the surge in interest rates has driven abnormal (though not unprecedented) bond-market returns so far this year. So, what are these move-in bonds telling us about the road ahead? Here are some answers to today's key questions:

What is the bond market signaling?

- Inflation is stickier - Short- and longer-term interest rates have moved sharply higher in 2022, with 10-year Treasury yields rising 1.4% and two-year yields rising 1.9% year-to-date. The broad increase in rates reflects the progressing inflation environment, as the year-over-year increase in consumer prices has reached 40-year highs. While this is not completely surprising given the ongoing impacts of the pandemic, inflation pressures have received an unanticipated boost from the commodity-price effects stemming from the war in Ukraine. In other words, for a variety of factors, inflation has not proved to be as transitory as markets and policymakers expected (or hoped).

- A more aggressive response from the Fed – The market, as well as Federal Reserve officials, seem to be acknowledging that the Fed has fallen behind the curve. The sizable jump in two-year rates reflects an expectation for meaningfully more aggressive policy tightening compared with expectations coming into 2022. Recent commentary from FOMC members tells us that they are committed to establishing the central bank's credibility in fighting inflation. The abrupt rise in yields suggests that they have been fairly effective in this effort. Ten-year Treasury yields have increased 60 basis points (0.60%) in the last three weeks, which reflects the next phase of Fed tightening – balance-sheet reduction. As the Fed reduces its bond holdings, we think this provides some scope for longer-dated yields to move higher from here, though not at the same pace or magnitude as we've seen recently.

- More pessimism than equities – Rising rates have been the primary catalyst for equity-market weakness this year, with the S&P 500 falling 12% between January 4 and March 14, as 10-year Treasury yields rose above the 2% mark for the first time since mid-2019. Since mid-March, however, equities have signaled a more positive tone, rallying as much as 10%, including signs of strength last week even as interest rates rose to fresh three-and-a-half-year highs. The bond market seems to be pricing in a higher probability of an approaching recession than is currently being corroborated by economic fundamentals, financial conditions, or equity-market behavior.

How does this move in rates compare with past spikes?

Significant, but not completely unique - There is no question that this jump in interest rates has been abrupt, and that this jump has had a negative impact on bond-market returns. This is not uncharted territory, however. Ten-year yields are up more than 150 basis points (1.5%) over the last six months. As the table below shows, there have been 10 periods in the last 20 years in which 10-year yields have risen more than 1% in a short period of time. Each was followed by a period of moderation as markets adjusted to new economic conditions and market valuations.

Timeframe	Increase in 10-yr Treasury yield	Change in 10-yr yield over following 6 months
Dec. '21-Apr. '22	1.6%	?
Aug. '20-Mar. '21	1.2%	-0.4%
Sep. '17-Apr. '18	1.0%	+0.1%
July '16-Dec. '16	1.2%	-0.4%
May '13-Sep '13	1.4%	-0.3%
Oct. '10-Feb. '11	1.4%	-1.4%
Dec. '08-Jun. '09	1.9%	-0.4%
Sep. '05-May '06	1.2%	-0.6%
Mar. '04-May '04	1.2%	-0.7%
Jun. '03-Sep. '03	1.5%	-0.6%

Source: Past performance does not guarantee future results. Market indexes are unmanaged and cannot be invested into directly. FactSet.

This table shows that 10-year interest rates typically fall after a period of increasing rates.

(Source: oXYGen & Jones)

Markets For The Week

INDEX	CLOSE	WEEK
Dow Jones Industrial Average	33,813	-1.85%
S&P 500 Index	4,272	-2.75%
NASDAQ	12,839	-3.83%
MSCI EAFE	2,127	.61%
10-yr Treasury Yield	2.90%	2.47%
Gold	$1,932	-2.18%
Bonds	$102.95	-.98%

Source: Reuters/Wall Street Journal

Earnings Highlights This Week

Verizon: Verizon lost fewer-than-expected monthly phone subscribers in the first quarter, a sign the wireless carrier is benefiting from its hefty investments in expanding 5G services and new broadband networks. The company on Friday reported a loss of 36,000 monthly phone subscribers in the quarter, compared with FactSet estimates of a loss of 49,300. Net income, however, fell 12.4% to $4.7 billion in the quarter. Verizon said that included a pre-tax loss from special items of approximately $1.5 billion, including a pre-tax loss of approximately $1.2 billion from early debt redemption costs.

SAP: The company said it plans to exit Russia completely in response to Moscow's invasion of Ukraine. Despite the impact on its Russian business, SAP affirmed its 2022 forecast for cloud revenue of between 11.55 billion euros and 11.85 billion euros at constant currency rates.

Snap: Snap missed Wall Street expectations for profit and sales when it reported first-quarter results on Thursday after the bell.

Tesla: Tesla beat analysts' expectations on the top and bottom lines for Q1 2022. For the period ending March 31, 2022, Tesla reported $3.22 earnings per share and revenue of $18.76 billion. It also recorded record automotive margins of 32.9%

Proctor & Gamble: Procter & Gamble's fiscal third-quarter earnings and revenue topped Wall Street's estimates. The company raised its forecast for fiscal 2022 revenue growth but said it also expects inflation to rise in its next quarter. Price hikes and productivity savings have helped offset some of the impact on P&G's margins.

News and Notes

What Is Going To Happen With Mortgage Rates?

What do you predict will happen here with mortgage rates?

- 5% sounds like a big number, but it is still a relatively cheap rate to borrow money for the long term at 5%.
- On a $300,000 mortgage over 30 years, the difference from a 3% and 5% mortgage is about $350 a month.
- As inflation goes up, the fed must raise interest rates to slow down inflation- so mortgage rates will probably go up if inflation goes up. If inflation tapers off, so will mortgage rates.

It is a good time to buy because housing prices are only going to get worse?

- Housing prices probably won't get worse in the next six to 12 months simply due to inventory- this is the basic law of supply and demand.
- Rents are also growing at a record high, and people need to remember in 1981, mortgages were 18% not 5%.
- Just be ready for the one-time expenses of home improvements (and) the ongoing cost of maintenance.

Any sign of rates going back down in the near future?

- We enjoyed historically low interest rates in 2020 and 2021, some people did a 15-year mortgage for under 2%!
- It's unlikely rates will come back down anytime soon. People who wanted to refinance probably missed out at this point.
- Remember, a home is a long-term investment and it's not a great idea to try to time the market.

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