Bonds are Making a Turn

Mark Grant | December 19, 2022

Who's kidding who? The equity markets have just been miserable, all year. Most of this has been caused by the Fed, and their unrelenting battle to bring down Inflation. They have not backed up. They have not stopped, and practically every word out of their mouths have been to suggest higher and higher interest rates to be forthcoming. There has been no paling around but there has certainly been plenty of Powelling around.

I don't expect this to stop until the Fed sends some more benign signals. Frankly, in my opinion, they should say that they will stop at 4%-5% inflation and just let things cool down. While our combined Inflation number is now down to approximately 7.00%, we are nowhere close to their 2.00% desired number and the collateral damage that they have caused in both the equity and the debt markets seems to have no space in their thinking. This, in my view, is just a huge mistake and one that is hitting people and institutions alike.

They are also causing a huge increase in the cost of money as our borrowing rates seem to climb with each passing week. This will hit corporate revenues and profits and also individual pocketbooks as everything from mortgages to credit card rates have all rise dramatically this year.

The one segment of the markets though, has begun to make the turn. It has not been noticed by many, but it is there, none the less, and this is the bond markets.

Bloomberg Index	**Year-to-Date**	**Last 30 days**	**Yield Now**
TREASURIES	**-10.71%**	**+2.66%**	**3.86%**
IG CORPORATES	**-13.73%**	**+3.54%**	**7.58%**
HY CORPORATES	**-9.96%**	**+1.84%**	**8.56%**
MBS	**-9.69%**	**+3.07%**	**4.33%**
MUNICIPALS	**-7.81%**	**+2.06%**	**3.40%**

***Data according to Bloomberg**

Pay particular attention to both Investment Grade and High Yield Corporate bonds. They are both now beating our average Inflation rate for the first time this year. This means that you can own a fixed income security and be on the "green side" of Inflation. On the cautionary side though are the High Yield bonds because they only yield 98 basis points more than our IG bonds which, to me, is not enough spread yet, to justify their purchase, in most cases.

The cost of borrowing money is bringing forward "credit risk" in a manner not seen in quite a long time. There is a tremendous amount of refinancing that has been to be done in the next several years and the costs, for lower quality companies, is going to be quite steep, in my estimation. I also expect a slew of ratings downgrades and bankruptcies.

Therefore I favor investments in IG bonds, for the moment. This all moves around and changes but, at this point in time, I think that Investment Grade bonds are a better and safer bet. I would also pay particular attention to bonds spread off of short term Treasuries, which are currently at the height of the Yield Curve. Our Yield Curve is flummoxed, no doubt, and signaling an upcoming Recession, in my opinion.

> "I would say it's our judgment today that we're not at a sufficiently restrictive policy stance yet, which is why we say that we would expect that ongoing hikes would be appropriate."
>
> -Fed Chairman, Jerome Powell

Yes, Mr. Chairman, please take an "ongoing hike" and leave our interest rates alone for the present time.

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