# Fixed Income Market Insights

April 27, 2023

## Key takeaways

Bond yields were little changed this week, with GT2s down 10 basis points and GT10s lower by 2 basis points and 2s/10s less inverted by 8 basis points (-55), as weaker consumer confidence and slower economic growth continue to weigh on yields. On the data front, consumer confidence came in weaker than expected during April to 101.3, the lowest level since July 2022, driven by more pessimistic consumer attitudes regarding the labor market and business conditions over the next six months. The S&P CoreLogic Case-Shiller 20-city home price index unexpectedly rose +.06% in February (+.36% YOY), the first increase in eight months, but the smallest annual advance since May 2012, as the combination of low affordability and higher mortgage rates have tempered prices from last year's all-time highs. Headline U.S. durable goods orders were stronger than expected in March, with new orders up 3.2%, driven by a rebound in the volatile commercial aircraft order component, which masked broad-based weakness across much of the core capital goods sub-sector. Real GDP was up for the third consecutive quarter and grew at a slower than expected 1.1% annualized rate during the first quarter, as large inventory drawdowns and another decline in residential fixed investment offset more robust consumer spending growth.

## We suggest

We continue to prefer playing rate defense given relatively low market rates, accelerating inflationary expectations and ongoing FOMC rate hikes. We favor barbell strategies in securitized products, anchored by short, higher current cash flow assets and longer, high quality bonds.

## Author


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# Housing Rebounding?

Recent housing data have revealed a surprising resilience in both activity and prices, bucking the conventional wisdom that a deeper correction is all but certain given the sharp rise in home values during the pandemic and the most aggressive monetary policy tightening in over four decades, which saw mortgage rates more than double by the turn of the new year. After all, housing prices, as measured by the S&P CoreLogic Case-Shiller 20 City index (CS20), were up a staggering 40% from June 2020 through June 2022's peak reading, while mortgage rates surged to 7% by the fourth quarter of last year, up from 3.25% at the end of January 2022. On its face, this set-up would appear to be an ideal breeding ground for a meaningful correction in prices, particularly given the durability of elevated, broad-based inflationary pressures still afflicting consumers today. While a deeper correction is surely possible, particularly given the very real prospect of tighter credit in the wake of last month's bank failures (SVB/SBNY), thus far, prices have held in remarkably well. Indeed, CS20 housing prices are down a mere 5% from last June's all-time high, erasing only a small portion of the 40% surge seen during the pandemic.

**Market Snapshot**

| | This week 4/27/23 | Last week 4/20/23 | Basis Points Change | Weekly % Change | YTD % Change |
|---|---|---|---|---|---|
| 3-month USD Libor | 5.27% | 5.26% | 1 | 0.19% | 10.48% |
| SOFR | 4.80% | 4.80% | 0 | 0.00% | 11.63% |
| 2-year US Treasury | 4.07% | 4.17% | -10 | -2.40% | -8.13% |
| 5-year US Treasury | 3.59% | 3.63% | -4 | -1.10% | -10.47% |
| 10-yr US Treasury | 3.52% | 3.54% | -2 | -0.56% | -9.28% |
| 2s-10s UST Spread | -55.00 | -63.00 | 8.00 | -12.70% | 0.00% |
| DJIA | 33,826 | 33,850 | -24.00 | -0.07% | 2.05% |
| S&P 500 | 4,135 | 4,138 | -3.00 | -0.07% | 7.68% |
| Spot Gold | 1,999 | 2,015 | -16.00 | -0.79% | 9.47% |
| WTI (Oil) Current Contract | 74.76 | 77.54 | -2.78 | -3.59% | -6.85% |
| 1-year Brokered CD | 5.10% | 4.95% | 15 | 3.03% | 10.87% |
| 5-year Brokered CD | 4.45% | 4.25% | 20 | 4.71% | 11.25% |
| 5-year Bullet US Agency | 3.76% | 3.79% | -3 | -0.79% | -7.84% |
| 5-year/NC1yr Callable US Agcy. | 5.15% | 5.15% | 0 | 0.00% | -4.63% |
| CDX IG Spread Index | 76.41 | 76.94 | -0.53 | -0.69% | -6.84% |
| CDX High Yield Index Spread | 101.26 | 101.09 | 0.17 | 0.17% | 0.64% |
| 15-yr UMBS | 4.68% | 4.70% | -2 | -0.43% | 0.43% |
| 30-yr UMBS | 5.19% | 5.18% | 1 | 0.19% | -2.63% |

Source: Bloomberg data as of 5:00pm ET 4/27/2023 and 11:00am ET 4/20/2023

While prices and mortgage rates remain elevated, signs of positive momentum have emerged that appear to support the notion that the slowdown in housing may be short lived. To start, CS20 prices actual rose during February for the first time in eight months, surprising most market participants and fueling speculation that any further correction from here may be muted. Additionally, data this week revealed that new home sales rose in March to the highest level in a year and the number of homes sold in March pending construction jumped to 168,000, the highest level since February 2022 and indicative of a meaningful increase in backlogs. Taken together with historically low inventories of existing homes, recent moderation of mortgage rates and still-steamy rents, even small improvements in buying affordability may be enough to buffer a more meaningful contraction in home prices this year. Of course, this soft-landing scenario for housing is predicated on a soft-landing scenario for the economy as a whole, as any meaningful upswing in unemployment would presage a deeper correction in housing prices. For historical context of what a deep contraction could look like, enter the Great Financial Crisis (GFC) era, where the CS20 registered the largest annual drop on record at -19% during January 2009, with monthly declines of -1.5% or more for all but one month from November 2007 through March of 2009. While this appears unlikely to us as the GFC housing meltdown was due to poor underwriting and weaker borrowers, we would expect prices to moderate further from here should inflation remain elevated and regional/community banks significantly reduce credit extension, which would hasten a more meaningful economic downturn in the months to come. Stay tuned!

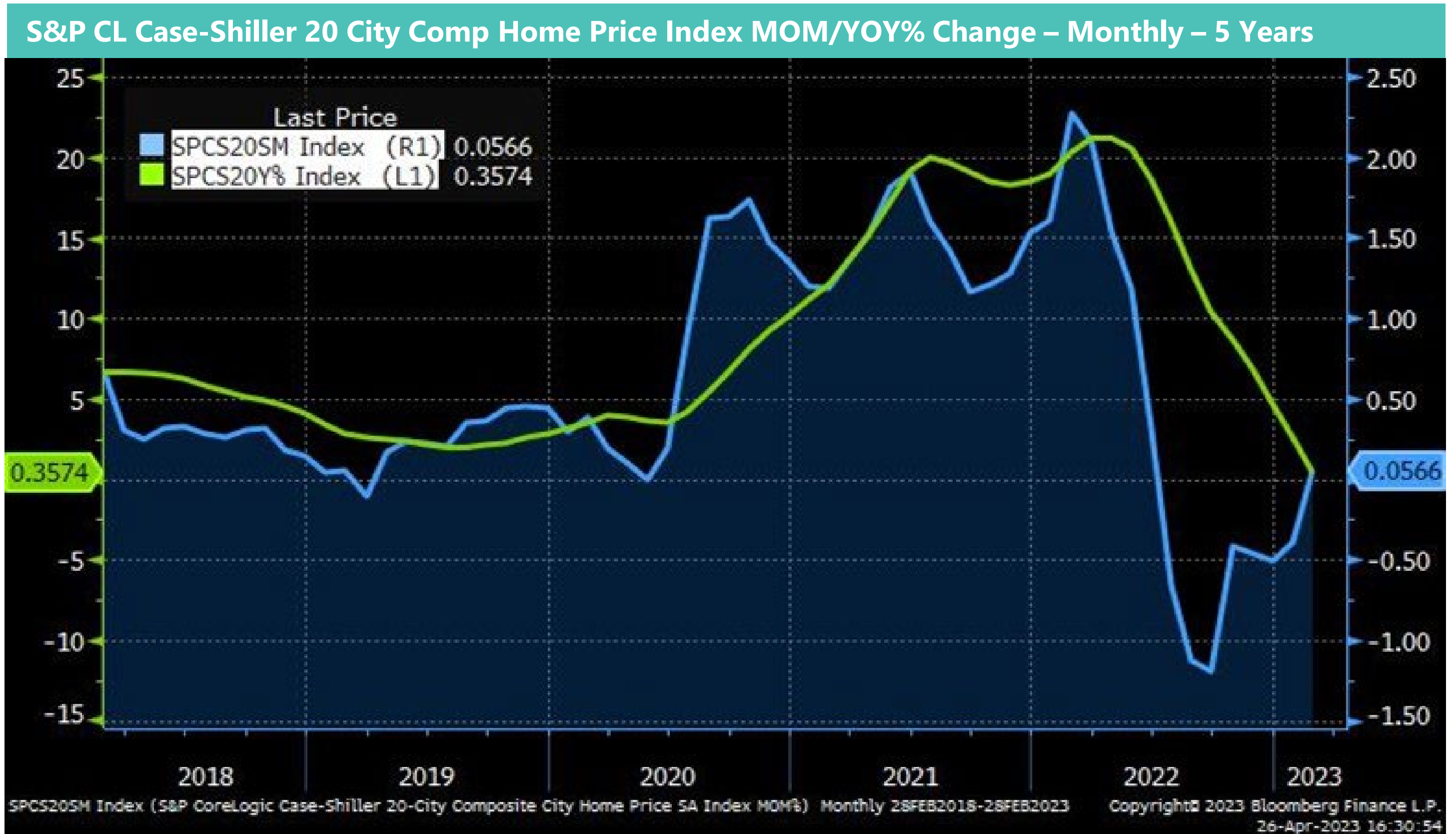
Still largely quiet on the fiscal front as House hearings continue to dominate the congressional calendar. That said, the House of Representatives narrowly passed (217-215) a bill on Wednesday that increased the debt ceiling by $1.5 trillion in exchange for a package of spending restrictions. While the bill has no chance of passing the Senate, passage by the House sets the table for what will likely be weeks of contentious and politically charged debate. Also look for more debate regarding tighter bank regulation in the wake of the SVB/SBNY failures last month, with public hearings likely.

**Consumer Confidence & Expectations – Monthly – 3 Years**

Source: Bloomberg as of 4/27/2023

Consumer confidence came in weaker than expected during April to 101.3 (vs. 104 est./104.0 Mar.), the lowest level since July 2022, driven by more pessimistic consumer attitudes regarding the labor market and business conditions over the next six months. Leading this month's decline was the expectations component, a measure of consumers' six-month outlook, which fell to 68.1 (74.0 Mar./70.4 Feb.), the lowest level since last July and below the recessionary reading (80) for the eleventh time over the past year as fewer respondents expect business conditions to improve (13.5% vs. 16.4% Mar.), a lower share see more jobs being added (12.5% vs. 15.5% Mar.), and fewer expect income to increase (15.7% vs. 16.2% Mar.). Conversely, the current conditions component edged higher to 151.1 (148.9 Mar.), led by more respondents stating that jobs are plentiful (48.4% vs. 47.9% Mar.) and fewer seeing weaker current business conditions (18.1% vs. 19.3% Mar.). Looking at the text of the report, the senior director of the survey stated that "While consumers' relatively favorable assessment of the current business environment improved somewhat in April, their expectations fell and remain below the level which often signals a recession looming in the short-term," and that "Consumers became more pessimistic about the outlook for both business conditions and labor markets. April's decline in consumer confidence reflects particular deterioration in expectations for consumers under 55 years of age and for households earning $50,000 and over." Notwithstanding persistently elevated inflationary expectations, overall confidence has been bolstered by durable strength in the labor market this year, and March's data revealed another solid read in the Labor Index, which measures the labor differential of jobs plentiful less hard to get, which came in at 37.3% (36.5% Mar.), the second highest level since September 2022. All in all, a weak report led by worsening expectations, portending further softness in consumer spending as higher interest rates, low personal savings rates and surging consumer debt are likely to weaken confidence further in the months to come.

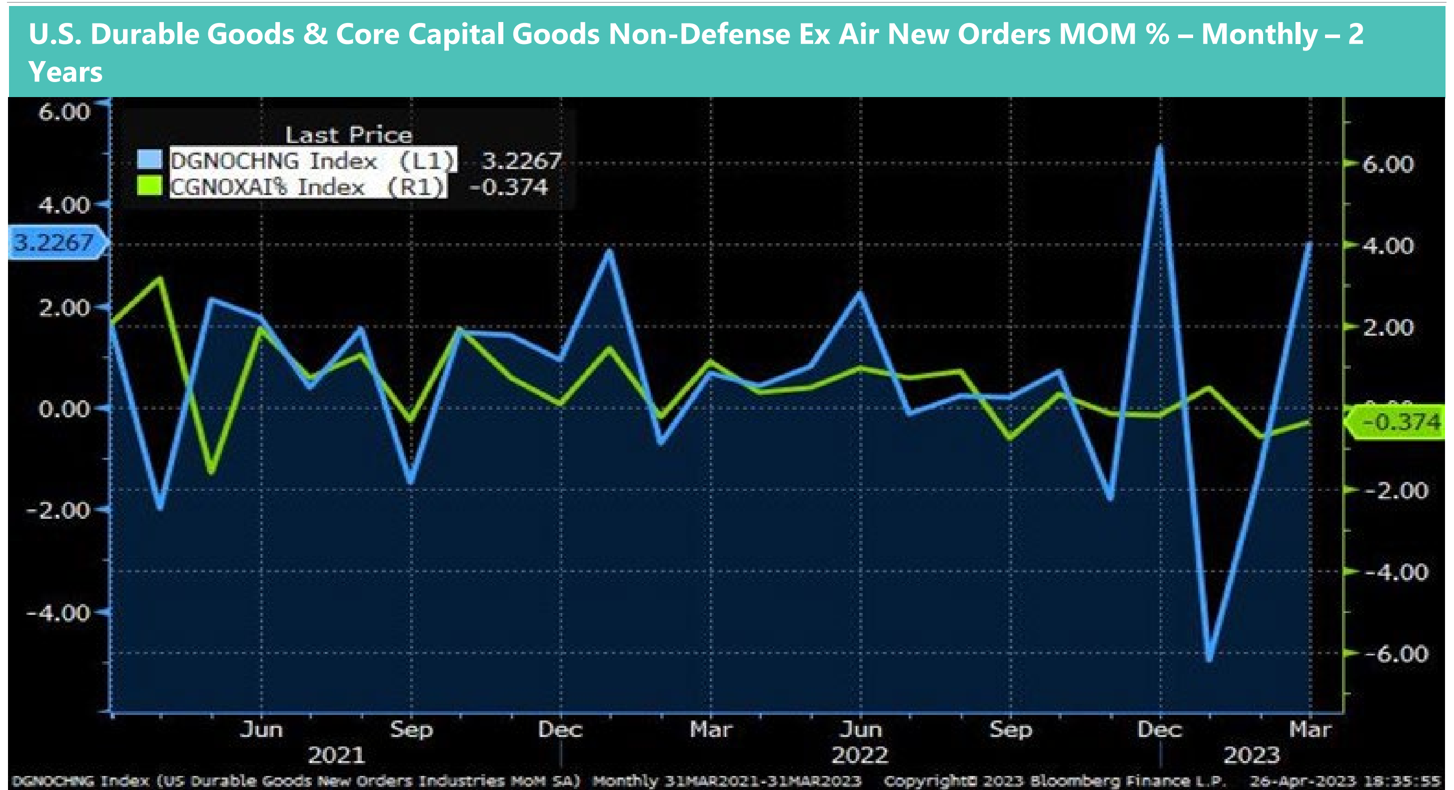
**S&P CL Case-Shiller 20 City Comp Home Price Index MOM/YOY% Change – Monthly – 5 Years**




Source: Bloomberg as of 4/27/2023

The S&P CoreLogic Case-Shiller 20-city home price index unexpectedly rose +.06% in February (-.35% est./+.36% YOY), the first increase in eight months, but the smallest annual advance since May 2012, as the combination of low affordability and higher mortgage rates have tempered prices from last year's all-time highs. While this moderation was inevitable given the dramatic run up in prices from mid-2020, housing market technicals continue to be supportive as supply is still challenged in many areas (2.6 months in Mar./record low 1.8), listings continue to sell quickly (29 days on market in Mar./record low 14) and the rental market remains robust. Regarding inventories, March's existing home sales data revealed that there were 980,000 previously owned homes for sale, down over 20% since last June and marginally higher than January 2022's cycle low of 850,000, which should provide a meaningful buffer to more extreme depreciation in the months to come. In total, 12 of the 20 cities continued to show annual price gains, albeit well-off of their cycle highs last year, with Miami (+10.8%), Tampa (+7.7%) and Atlanta (+6.6%) posting the largest annual gains, with San Diego (-4.2%), Seattle (-9.3%) and San Francisco (-10.0%) rounding out the bottom three. While price appreciation has surely slowed as affordability continues to slide and mortgage rates remain high, demand is still robust in many areas and migration away from larger cities should support elevated home prices for much of the country in the months to come. On a national basis, the housing price index rose 2.05% for the year ended February, well off of March's 20.8% all-time record high (1988 index inception) and the smallest annual gain since July 2012. All in all, market participants expected lower home prices given the steep rise in mortgage rates over the past year and the magnitude of price appreciation during the pandemic, with the former and potential credit contraction from last month's bank failures now likely to dictate how far prices will fall into 2023.

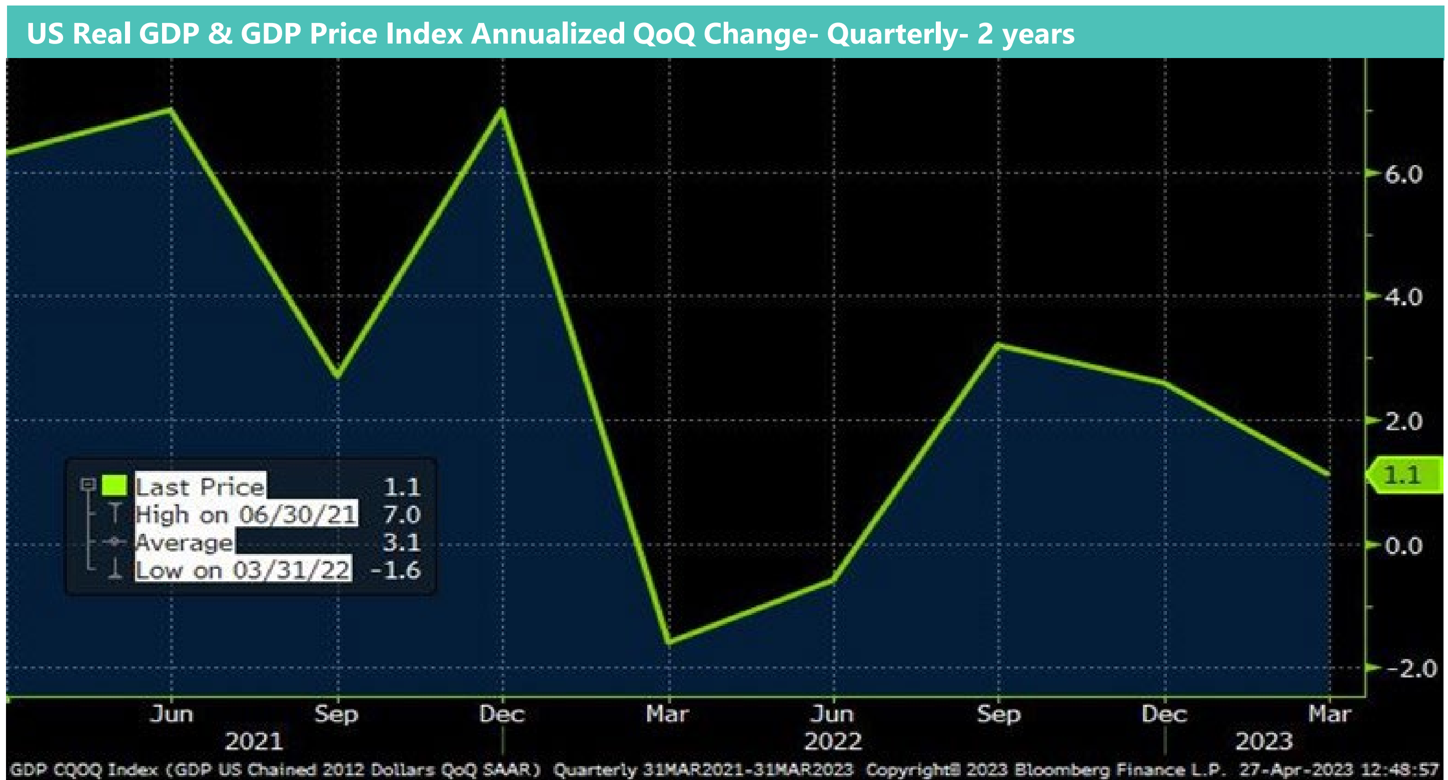
**U.S. Durable Goods & Core Capital Goods Non-Defense Ex Air New Orders MOM % – Monthly – 2 Years**




Source: Bloomberg as of 4/27/2023

Headline U.S. durable goods orders were stronger than expected in March, with new orders up 3.2% (+.7% est), driven by a rebound in the volatile commercial aircraft order component, reversing two months of weakness, which masked broad-based weakness across much of the core capital goods sub-sector. To be sure, demand for equipment and other fixed business investment (excluding aircraft and military hardware) has slowed from the brisk pace observed for much of 2022, as higher interest rates and less sanguine business sentiment has slowed a years' long push to increase production and invest in labor-saving technologies. This metric, known as core capital goods orders, slid -.4% in March (-.7% Feb.), which rendered three-month and year-over-year growth rates to -1.2% and 1.9%, a sharp slowdown from the .1% and 3.3% run rates during the fourth quarter of last year. Notwithstanding headline strength, trend data reveals a meaningful slowdown in larger-ticket spending (ex-aircraft) over the past six months, a moderation well-underway given FOMC rate hikes and heightened risks of recession, both of which may dampen new orders further, particularly given the likelihood of some form of credit contraction via last month's bank failures.

**US Real GDP & GDP Price Index Annualized QoQ Change- Quarterly- 2 years**




Source: Bloomberg as of 4/27/2023

Real GDP was up for the third consecutive quarter and grew at a slower than expected 1.1% annualized rate during the first quarter (+1.9% est.; +2.6% Q4), as large inventory drawdowns (-2.3% of top line) and another decline in residential fixed investment offset more robust consumer spending growth. On the consumption side, consumer spending reaccelerated to +3.7% during the quarter (+1% Q4/+2.3% Q3), with resilience seen in both goods and services, which came in at +6.5% and +2.3% respectively. Surely a bright spot was the rebound in real (inflation-adjusted) final sales to private domestic buyers, a key measure of underlying demand that subtracts out the trade, inventories, government spending and investment, which jumped +2.9% during the quarter (+0.0 Q4/+1.1% Q3), the fastest pace since the second quarter of 2021. Additionally, inflation-adjusted residential and business fixed investment (equipment) dropped -4.2% and -7.3% respectively, as rising interest rates and elevated prices continue to erode purchasing power, though the decline in residential investment was more tepid than expected (-25.1% Q4/-27.1% Q3). On the inflation front, today's report revealed another, stubbornly high 4.9% annualized increase in the Core PCE deflator (+4.4% Q4/+4.7% Q3), the largest gain since March 2022, a condition expected by most consumers and businesses to persist in the near term. All in all, another quarter of below trend growth, surely welcome news for a Federal Reserve attempting to cool the economy enough to dampen inflation, whilst avoiding a deeper contraction in growth. That said, residential and business investment are likely to be challenged in the months to come as the negative impact of higher interest rates and elevated inflation continue to weigh on consumers and businesses.

## The Week Ahead

The data calendar heats up over the next week, headlined the FOMC Rate Decision, PCE Deflator, JOLTS Job Openings and ISM Services and Manufacturing. Looking ahead, markets remain focused on inflation, employment data and more signs of softening economic activity. On the new issue front, ABS volumes slowed from last week's red-hot pace, with 5 deals totaling $1.8 billion priced through the 26th and $88.0 billion year to date ($98.2 billion over same period last year; $276.7 billion for 2022) and IG corporate issuance also slowed with $12.8 billion priced as of the 26th and $456.5 billion year to date ($579.4 billion over same period last year; $1.26 trillion for 2022). While new issue supply slowed last year given FOMC rate hikes and higher volatility, market conditions have generally improved for much of 2023 and the new deal landscape remains favorable for a wider spectrum of ABS and corporate issuers as investor demand remains strong.

**Friday 4/28**
PCE Deflator; MNI Chicago PMI

**Monday 5/1**
ISM Manufacturing

**Tuesday 5/2**
JOLTS Job Openings; Factory Orders

**Wednesday 5/3**
FOMC Rate Decision; ISM Services

**Thursday 5/4**
Weekly Jobless Claims

## About the author

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As a fixed income trader with more than 25 years of experience, David Petrosinelli brings deep knowledge and unique perspectives to InspereX's clients. His background includes sales and trading of mortgage-backed securities, commercial mortgage-backed securities, asset-backed securities, collateralized loan obligations, and collateralized mortgage obligations. Before joining InspereX (formerly known as Incapital) in 2020, he served as a Managing Director at Brean Capital and previously held various positions with Piper Sandler Companies and Shay Asset Management. David closely monitors underlying trends within the bond markets and how those markets are shaped by both American policymakers and the global macro economy. He earned a bachelor's degree in accounting and finance from Northeastern University and an MBA in economics and finance from Loyola University Chicago. He is a CFA Charterholder and holds FINRA Series 7 and 63 licenses. He is based in New York City.

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