Yield Curve Inversion

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Uh oh! With all of the news about the stock market and G20 meetings, little press has been made about the slight curve inversion we saw yesterday. Actually, there are a few more headlines today.

Good morning!

- **First, on the G20**
    - **The stock market took off flying yesterday after the weekend's G20 meetings**
        - Where, in reality, nothing was really accomplished but a cease-fire, so to speak
        - Even Trump's top economic advisor Larry Kudlow is dialing back expectations over elements of the deal
        - There is still confusion of the 90-day tariff truce begins on Dec. 1st or Jan. 1st (the White House says Dec. 1st…not sure what China thinks)
        - Need to keep an eye on this over the next few weeks as we get information on how China saw the deal
- **Now, the yield curve inversion**
    - **So yes, it is not that much of an inversion…The spread between three- and five-year Treasury yields dropped below zero yesterday, with the two-year yield also trading higher than the five-year this morning**…see below
    - The 3yr/5yr was the first benchmark spread to invert this cycle
        - The 2yr/5yr may be the next point to invert, hitting an intraday low of 0.1 bp yesterday and this morning, essentially flat…if you round
            - 2yr: 2.831%, 5yr: 2.829%
        - The spread between he 2yr and 10yr is now ~13 bs
    - Interesting that the first inversion on the curve happened yesterday when there was some decent economic news (G20, ISM and new orders) and a good day in the stock markets
        - **The credit markets are telling us the trade war is far from over and there are still a number of headwinds facing this economy (i.e. housing)**
    - What does it mean for the Fed?
        - **Chances are still good for a Fed hike in few weeks at the December 19th FOMC meeting, but fed funds futures have only about a 50% probability of a March hike and 1.3 hikes priced in for 2019**

        - Analysts will look closely at the dot plots that are announced at the next FOMC meeting
    - As one analyst said yesterday, *"Monday's move could be the first signal that the market is putting the Federal Reserve on notice that the end of its tightening cycle is approaching."*
- Yesterday
    - **The ISM manufacturing index rose to 59.3 in November amid stronger growth in new orders, backlogs and employment**
        - Prices rose at a significantly slower rate as oil prices tumbled, but the supply chain remains tight
        - Of the 18 manufacturing industries surveyed for this report, 13 reported growth in November
    - **Total construction outlays fell 0.1% to $1.309 billion in October**
        - With revisions to prior months' data, spending has declined for three consecutive months
- **This week, the market closes tomorrow for the National Day of Mourning, but we have a host of data being released**
    - Initial claims (watch this, it has been creeping up lately), factory orders and durable goods
    - **Friday we get the payroll report, more importantly wage data**
- We also had a host of Fed speakers yesterday
    - Powell's testimony before the Joint Economic Committee was cancelled due to the National Day of Mourning on Wednesday
        - No new date has been set although the Beige Book will be released as originally scheduled
        - Markets will eb closed Wednesday as well
    - Clarida said the US economy is in good shape but acknowledged that a low r* means there is less room for rates in a future downturn
        - On inflation he said the 2% target is symmetric but the Fed could operate somewhat above that level
    - Quarles said we're coming up to the bottom of the neutral rate range, but that the neutral rate is not a terribly precise concept
        - He reiterated the FOMC's data dependence and added the current tools are adequate to respond to a future crisis
    - Brainard said inflation is around 2% and the economy is now at or beyond full employment
        - She said the normalization of the Fed's balance sheet is well underway
    - The New York Fed's John Williams speaks at an economic press briefing today at 10am

- News
    - **Bloomberg story on the inverting yield curve**
    - **Oil prices are heading back up thanks to tightening supply**
    - **Cash is king as the markets struggle**
- Treasuries
    - 2-yr: 2.82%
    - 3-yr: 2.83%
    - 5-yr: 2.82%
    - 10-yr: 2.96%
    - 30-yr: 3.23%
- LIBOR
    - 1-month: 2.35%
    - 3-month: 2.74%

Have a wonderful Tuesday!

Fred

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