THE DOG DAYS ARE NOT OVER

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08/09/2017

August has arrived in New York City, and the heat and humidity have returned as well. Meteorologically speaking, the dog days of summer are still here. Looking at recent developments in the money and bond markets, one can't help but come to a similar conclusion.

Over the last couple of weeks, activity within both the interest rate and credit-sensitive areas of the fixed income arena have witnessed some rather lackluster activity. Indeed, both investment-grade and high-yield credit spreads have moved in narrow ranges, and U.S. Treasury (UST) yields have also been confined to somewhat narrow bands. Interestingly, it's not as if there hasn't been potential market-moving news; it just appears as if investors have found "comfortable" trading ranges, at least for the time being.

An ideal case in point was last Friday's Employment Situation report. As readers are well aware, this is the one set of monthly economic data that has the potential to move the Treasury market in a visible fashion, if the results deviate from market expectations. Interestingly, not only did the widely followed nonfarm payroll headline figure come in visibly above consensus forecasts, but the underlying tenor of the data as a whole was on the solid side as well. To provide some perspective, total nonfarm payrolls rose by 209,000 in July, nearly 30,000 above consensus forecasts, while the unemployment rate ticked back down to 4.3%, as a hefty increase of 349,000 workers re-entered the civilian labor force and apparently found jobs.

For the Federal Reserve (Fed), it's no longer about jobs; it's about inflation—and in the case of the employment report, wages. On this front, average hourly earnings rose at an annual rate of 2.5%, slightly above expectations. While wage gains are off the cycle high of last December's rise of 2.9%, they have been holding steady for the last four months and not dropping. At Janet Yellen's recent Semiannual Monetary Policy testimony before Congress, the Fed Chair did acknowledge there are now "two-sided" risks to inflation going forward. While the policymakers would no doubt prefer to see some future upside, they most likely will welcome this latest data nonetheless.

The UST market did sell off a bit in reaction to the jobs report, but sentiment regarding Fed policy was not altered. Fed Funds Futures implied probability for year-end 2017 sees the odds of another rate hike at only 38.7%, as of this writing; before the jobs report, it was 37.4%. The UST 10-Year yield remained a basis point (bps) or two above the 2.25% threshold, a level it has been straddling since the month began.

Conclusion

So, what could jolt the bond market out of its lethargy? In terms of upcoming economic reports, the Consumer Price Index (CPI) is due out on Friday, August 11. According to the latest Bloomberg consensus, this inflation gauge is expected to show a year-over-year gain of 1.8%, up 0.2 percentage points from the prior month. If this forecast comes true, it will more than likely not be viewed as a game-changer. One other notable event in the weeks ahead could be the Kansas City Fed's Economic Symposium in Jackson Hole, Wyoming, to be held August 24–26. In the past, this event has hosted Fed Chairs, and it has been anxiously awaited by the bond market. This time around, it has been reported that European Central Bank (ECB) President Mario Draghi will attend, and speculation could build surrounding whether he may signal what the ECB's intentions are regarding its monetary policy.

Unless otherwise noted, data source is Bloomberg, as of August 4, 2017.

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DEFINITIONS

Interest rates : The rate at which interest is paid by a borrower for the use of money.

High Yield : Sometimes referred to as "junk bonds," these securities have a higher risk of default than investment-grade securitie.

Credit spread : The portion of a bond's yield that compensates investors for taking credit risk.

Treasury : Debt obligation issued by the U.S. government with payments of principal and interest backed by the full faith and credit of the U.S. government.

Yield : The income return on an investment. Refers to the interest or dividends received from a security that is typically expressed annually as a percentage of the market or face value.

Federal Reserve : The Federal Reserve System is the central banking system of the United States.

Inflation : Characterized by rising price levels.

Basis point : 1/100th of 1 percent.

Consumer Price Index (CPI) : A measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. The CPI is calculated by taking price changes for each item in the predetermined basket of goods and averaging them; the goods are weighted according to their importance. Changes in CPI are used to assess price changes associated with the cost of living.