

FED MONITOR: DON'T LET THE DOOR HIT YOU

Kevin Flanagan — Head of Fixed Income Strategy

05/04/2016

With one-third of calendar year 2016 in the books, the money and bond markets have now weathered the first three [Federal Open Market Committee \(FOMC\)](#) meetings. It came as no surprise that at last week's policy gathering, the [Federal Reserve \(Fed\)](#) once again decided to keep [interest rates](#) unchanged. Now, the fixed income arena has quickly pivoted to the next FOMC meeting scheduled for June 14 and 15. As we wrote in our March 21 blog post [Fed Monitor: Watch Your Language](#), the area investors should focus on for potential future Fed action lies in its policy statement. The latest version did not offer any groundbreaking insights, but some subtle adjustments were made. The voting members did acknowledge that "growth in economic activity appears to have slowed," a point underscored by the Q1 real [GDP](#) data, but they did not appear to alter their broader outlook that growth will ultimately still "expand at a moderate pace." More important to the Fed outlook are the Committee's views on global economic prospects and financial conditions. This is where the most notable shift occurred in the statement's language. At the March FOMC meeting, and a subsequent public appearance by Fed chair Yellen shortly thereafter, there was little doubt that concerns had arisen on this front and that these considerations played an integral role in turning the mindset more cautionary. However, the Fed's tone was less anxious this time around, as the policy statement replaced the phrase "global economic and financial developments continue to pose risks" with "[t]he Committee continues to closely monitor [inflation](#) indicators and global economic and financial developments." Should we be scrutinizing the Fed's words so closely? The answer is an unequivocal yes, because this is how the policy makers attempt to provide guidance to the markets. This shift does not necessarily mean the Fed is now actively considering raising rates at its June meeting, but it was meant to signal that perhaps too much complacency had set in on this front, and left the door open, not closed. There is a long way to go, and a lot of data—both here in the U.S. and abroad—to digest between now and mid-June, but financial conditions (the U.S. dollar, equity prices, oil and commodity prices) have turned less restrictive compared to earlier in the year. In order for the Fed to consider a [rate hike](#) at its next policy meeting, U.S. growth will need to improve in Q2, global economies such as China must show signs of stabilizing and/or improving, and the aforementioned financial conditions cannot take a step backward. Without a doubt, those are several hurdles to cross, but April's policy statement was the Fed's way of trying to interject itself back into the money and bond market discounting process. **Conclusion** Based on the initial reactions to the FOMC meeting, the [U.S. Treasury](#) market does not appear to have been swayed and is still not priced for a potential rate hike in June. If the Fed is going to consider such a policy move, monetary officials will more than likely telegraph their intentions beforehand and not surprise the markets. Within fixed income, we continue to see more relative value in investment-grade corporates (IG) rather than interest-sensitive vehicles such as Treasuries. WisdomTree believes fixed income investors should focus on a qualitative approach to IG credit while tilting for income.

Important Risks Related to this Article

Fixed income investments are subject to interest rate risk; their value will normally decline as interest rates rise. In addition, when interest rates fall, income may decline. Fixed income investments are also subject to credit risk, the risk that the issuer of a bond will fail to pay interest and principal in a timely manner or that negative perceptions of the issuer's ability to make such payments will cause the price of that bond to decline.

For more investing insights, check out our [Economic & Market Outlook](#)

View the online version of this article [here](#).

IMPORTANT INFORMATION

U.S. investors only: Click [here](#) to obtain a WisdomTree ETF prospectus which contains investment objectives, risks, charges, expenses, and other information; read and consider carefully before investing.

There are risks involved with investing, including possible loss of principal. Foreign investing involves currency, political and economic risk. Funds focusing on a single country, sector and/or funds that emphasize investments in smaller companies may experience greater price volatility. Investments in emerging markets, currency, fixed income and alternative investments include additional risks. Please see prospectus for discussion of risks.

Past performance is not indicative of future results. This material contains the opinions of the author, which are subject to change, and should not to be considered or interpreted as a recommendation to participate in any particular trading strategy, or deemed to be an offer or sale of any investment product and it should not be relied on as such. There is no guarantee that any strategies discussed will work under all market conditions. This material represents an assessment of the market environment at a specific time and is not intended to be a forecast of future events or a guarantee of future results. This material should not be relied upon as research or investment advice regarding any security in particular. The user of this information assumes the entire risk of any use made of the information provided herein. Neither WisdomTree nor its affiliates, nor Foreside Fund Services, LLC, or its affiliates provide tax or legal advice. Investors seeking tax or legal advice should consult their tax or legal advisor. Unless expressly stated otherwise the opinions, interpretations or findings expressed herein do not necessarily represent the views of WisdomTree or any of its affiliates.

The MSCI information may only be used for your internal use, may not be reproduced or re-disseminated in any form and may not be used as a basis for or component of any financial instruments or products or indexes. None of the MSCI information is intended to constitute investment advice or a recommendation to make (or refrain from making) any kind of investment decision and may not be relied on as such. Historical data and analysis should not be taken as an indication or guarantee of any future performance analysis, forecast or prediction. The MSCI information is provided on an "as is" basis and the user of this information assumes the entire risk of any use made of this information. MSCI, each of its affiliates and each entity involved in compiling, computing or creating any MSCI information (collectively, the "MSCI Parties") expressly disclaims all warranties. With respect to this information, in no event shall any MSCI Party have any liability for any direct, indirect, special, incidental, punitive, consequential (including loss profits) or any other damages (www.msci.com)

Jonathan Steinberg, Jeremy Schwartz, Rick Harper, Christopher Gannatti, Bradley Krom, Tripp Zimmerman, Michael Barrer, Anita Rausch, Kevin Flanagan, Brendan Loftus, Joseph Tenaglia, Jeff Weniger, Matt Wagner, Alejandro Saltiel, Ryan Krystopowicz, Kara Marciscano, Jianing Wu and Brian Manby are registered representatives of Foreside Fund Services, LLC.

WisdomTree Funds are distributed by Foreside Fund Services, LLC, in the U.S. only.

You cannot invest directly in an index.

DEFINITIONS

Federal Open Market Committee (FOMC) : The branch of the Federal Reserve Board that determines the direction of monetary policy.

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

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

Gross domestic product (GDP) : The sum total of all goods and services produced across an economy.

Inflation : Characterized by rising price levels.

Rate Hike : refers to an increase in the policy rate set by a central bank. In the U.S., this generally refers to the Federal Funds Target Rate.

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.