Market Strategy
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Strategas Head of Fixed Income Research Tom Tzitzouris breaks down the big economic data of the week, answers whether he'd buy bonds at current yields, and takes a look at what the Federal Reserve might do in the month to come.

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JOBS AND INFLATION | WATCHING BOND YIELDS | FORECASTING THE FED

ROSS MAYFIELD: What is more important to the macro story – the recent jobs data or this week's inflation report?

TOM TZITZOURIS: I think both items are absolutely critical for telling us the trajectory of the U.S. economy over the near term, but I think the recent jobs numbers are probably more important for the Federal Reserve and the bond market because they tell us the direction of the economy in the very short term. And right now, we're getting a mixed signal from the data. The September jobs report out last Friday showed blockbuster job growth, while jobless claims this week are showing a spike in job losses. So, which is telling the full story? The truth is probably somewhere in the middle. I think the overall picture is one of a slowing labor market – not slowing at a pace that would suggest a recession is coming, but still slowing – and inflation that is also slowing, but not as fast as we would like because the consumer is still spending. And so, you have a slowly weakening economy with inflation pressures remaining, and that's something that financial markets and policymakers alike are going to have to deal with for the next year or so.

ROSS: With those inflation and jobs numbers, yields have actually ticked up here. How are you thinking about the bond market?

TOM: Let me start by saying we would be buyers with yields where they are today. Ten year yields are right around 4.10%, and I think they could reasonably be anywhere between a 3.70% and a 4.20%, but we're getting close to the upper end of that range. And just as we thought bonds were overbought when yields were down below 3.70% (more buyers pushes prices up and yields down), we're getting a little bit oversold here around 4.10%. So, we would be buyers at this level.

Now, where would 10s have to go to upset the stock market? Well, earlier this year, that level seemed to be 4.5%. That barrier might be declining as inflation and growth cool, but it's definitely above where we are today. The market has to sense that the move in 10-year yields is an indication that liquidity is coming out of the system. And a move from 3.70% to 4.10% is not really an indication of that. So, my best estimation of where we would start to worry about equity valuations and credit markets would be a 10-year Treasury yield between 4.25% and 4.50%, but I think it would take additional upside economic catalysts to get us there.

10-year Treasury yields have popped

Source: St. Louis Fed

ROSS: How do you handicap rate cuts for 2024 and 2025?

TOM: If the environment we see today doesn't change too much – i.e., no spike in unemployment or job gains – then we'd anticipate 25 basis point rate cuts in November and December, followed by 50 to 75 basis points of rate cuts in 2025, which would result in a fed funds rate around 4% by mid-to-late next year. But, if the economy shows any major signs of weakening, then we'd expect a 50 basis point cut in November or possibly December, and that's why the jobs numbers over the next few months are so important. So, I don't want to pound the table on a forecast because it's still very data-dependent right now.

This conversation is lightly edited and consolidated from an interview located at www.youtube.com/@BairdTV.

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