Weekly Market Insights

May 1, 2023

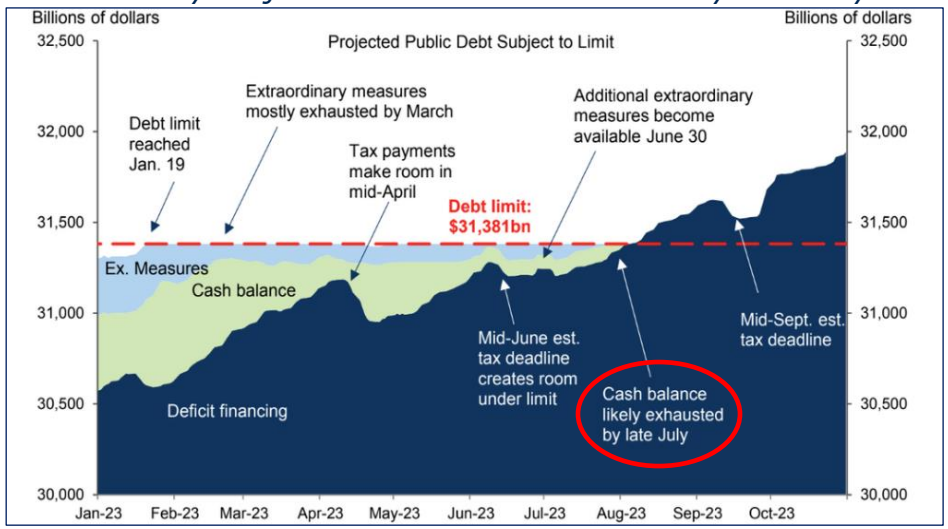
ARVEST Wealth Management

"We all know what to do, but we don't know how to get re-elected once we have done it" – Jean-Claude Juncker, Politician

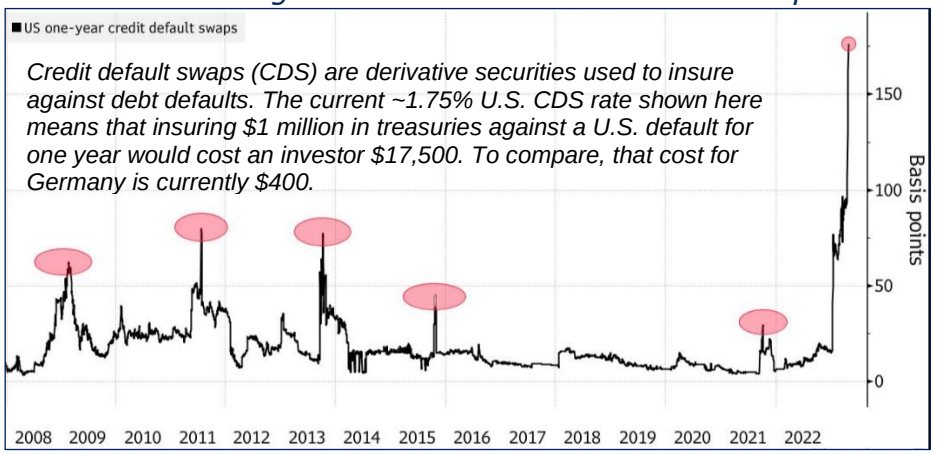
The 1970s sitcom Welcome Back, Kotter was always pushing this narrative of us versus them. Mainly, the lovable group of troubled students and their goofy teacher versus the school's curmudgeonly vice principal who hates Gabe Kotter's less structured teaching style. In the pilot episode, Kotter convinces his class to enter a debate with the school's debate team that ultimately ends up not feeling much like a real debate at all. Us versus them, with little emphasis on the real issue. That brings us to the current U.S. debt ceiling "debate," which is even less of a debate than Kotter's class versus the debate team. It is more like a tool in a hostage negotiation where the balance of power changes every electoral season. The details of the debt ceiling issue are relevant, and real policy is always important, but it is also important to understand how much of a political game this mechanism has become.

The debt ceiling is technically the maximum amount of debt that the U.S. government can legally accrue. Since the US runs a budget deficit each year, the Treasury must borrow to make up the difference. Congress authorizes spending but they also separately (?!?!) authorize how much the Treasury is allowed to borrow to fund the spending that was already approved. If the amount of borrowing allowed is less than what is needed to cover the already agreed upon budget from Congress, then we all get the pleasure of hearing politicians grandstand for months about how the other party is being the obstructionist. Since 1960, this "debate" has happened 78 times without defaulting. The current debt ceiling sits at $31.4 trillion, which was breached on January 19 (see chart, top right). The Treasury is currently using accounting gimmicks, called "extraordinary measures," to continue to satisfy spending requirements. It is estimated that true exhaustion of the Treasury's cash balance would happen between early June and September, depending on how much in tax receipts the Treasury continues to receive this year. Goldman Sachs did an analysis of those tax receipts so far and they estimate that the exhaustion date is likely in late July. That's more than enough time to find a compromise, but the political climate is so polarized right now that it has investors more worried about the potential for a U.S. default than prior episodes. The cost to insure against a U.S. default (via credit default swaps) is currently higher than any prior debt ceiling squabble (see chart, bottom right), including 2011 when the credit rating agencies downgraded the U.S. debt rating from AAA to AA+. We can learn something from that ***(cont.)***

Treasury Projected to Exhaust Resources by Late July



Cost to Insure Against US Default Above Previous Episodes



(Top Source: Treasury, Goldman Sachs; Bottom Source: Bloomberg LP, ICE Data Services)

About Arvest Wealth Management

Arvest Wealth Management currently manages over $14 billion in client assets by providing a diverse mix of services including brokerage, trust, investment management, retirement plans, IRAs, custodial accounts, estate settlement and insurance. We are people helping people find financial solutions for life.

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2011 episode. After the S&P downgraded the U.S. credit rating, both political parties suddenly found common ground. Democrats and Republicans both lambasted the move as dangerous, which ended with S&P's then-president "stepping down" merely 18 days after the downgrade was announced. Per S&P at the time, the downgrade reflected the belief that the gridlocked political system was incapable of fixing the growing debt problem in the long term. So, instead of compromising to alleviate the very valid concerns from the S&P, politicians attacked the company for saying the quiet part out loud. Point being, all of this is irrational political theater. That irrationality has real consequences in the immediate term, but those consequences are highly unpredictable. There is as much risk to investors in overreacting to the potential US debt issues as there is with ignoring it altogether.

Politics will always be tempting to consider when thinking about your investment strategy, but it is a fool's game. The current scenario is no different. It will create additional market volatility with every ominous headline about what happens if the U.S. defaults on its debts. There is no historical template for what investors should do in that scenario because it has never happened. As default approached in 2011, there was a sell-off in U.S. treasury debt maturing near the default date, but longer dated treasuries rallied. Risk assets sold off across the board, but quickly rebounded once the issue was "resolved." Investors should prepare themselves for that volatility, but also to resist the temptation to treat the political kabuki performances as a signal to ***do something***. Market volatility is a normal part of investing, and politics is a familiar culprit. Investors should maintain focus on their goals and the time horizon left to accomplish them. If your goals or time horizon have changed, your portfolio may need updating as well. If not, turn off the news, take a deep breath, and resist letting politics drive your investment decisions.

We will not be publishing next week. We will return on May 15.

Join our monthly market call.

Arvest Wealth Management hosts a monthly Market Viewpoint webinar.
To join us for our next meeting, please contact Charles Kurtz at ckurtz@arvest.com

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Alex supports the portfolio management team through market research that aids asset allocation decisions and due diligence on third party investment managers. He has a BSBA in finance, as well as a certificate in integrated investment management, and holds the CFA designation as a member of the Chartered Financial Analyst Institute and the Kansas City Society of Chartered Financial Analysts.

CURRENT ASSET CLASS OUTLOOK

Equities	Current
US Equity – Large Cap	Slightly Unfavorable
US Equity – Mid Cap	Neutral
US Equity – Small Cap	Slightly Favorable
Int'l Equity	Slightly Favorable
Emer. Mkts	Slightly Favorable

Real Assets	Current
Real Estate	Neutral
Infrastructure	Neutral
Commodities	Slightly Favorable

Fixed Income	Current
Invest Grade Credit	Neutral
Treasury/Agency	Slightly Favorable
Mortgage (MBS)	Slightly Favorable
Commercial MBS	Slightly Favorable
Asset Backed (ABS)	Favorable
High Yield	Unfavorable
Emer. Mkts Debt	Slightly Unfavorable
Taxable Muni	Slightly Favorable
Tax-Exempt	Unfavorable
Tips	Neutral

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Market Returns & Rates (as of 4/28/2023)

Asset Class	Sub-Asset Class	Index	YTD	1-Year	3-Year	5-Year	10-Year	2022
Equity	U.S. Large Cap Equities	S&P 500	9.16%	-1.08%	15.15%	11.44%	12.21%	-18.13%
Equity	U.S. Mid Cap Equities	S&P 400	2.98%	-1.46%	16.88%	7.54%	9.71%	-13.10%
Equity	U.S. Small Cap Equities	Russell 2000	0.88%	-6.38%	12.23%	4.12%	7.92%	-20.46%
Equity	Developed ex. U.S. Equities	MSCI ACWI ex U.S.	8.96%	4.87%	10.83%	3.04%	4.62%	-15.53%
Equity	Emerging Markets Equities	MSCI Emerging Mkts	2.85%	-4.14%	5.53%	-0.71%	2.29%	-19.81%
Fixed Income	Broad Aggregate	BB Aggregate	3.59%	-0.93%	-3.14%	1.18%	1.32%	-13.01%
Fixed Income	U.S. Treasury	BB U.S. Treasury	3.56%	-1.38%	-4.29%	1.01%	0.86%	-12.46%
Fixed Income	U.S. Treasury Inflation Prot.	BB U.S. Inflation Linked	3.52%	-5.06%	0.40%	2.96%	1.39%	-12.60%
Fixed Income	U.S. Investment Grade	BB U.S. Invest. Grade	4.29%	0.02%	-1.96%	1.99%	2.20%	-15.76%
Fixed Income	U.S. High Yield	BB U.S. High Yield	4.60%	0.73%	4.98%	3.28%	4.03%	-11.19%
Fixed Income	U.S. Leveraged Loans	CS Leveraged Loan	4.09%	2.81%	7.30%	3.64%	3.88%	-1.06%
Fixed Income	U.S. Municipals	BB Municipal Bond	2.54%	2.77%	0.59%	2.06%	2.26%	-8.53%
Fixed Income	Non-U.S. Gov't Bond	FTSE Non-U.S. WGBI	4.03%	-4.98%	-6.21%	-3.81%	-1.55%	-22.07%
Fixed Income	Emerging Markets Debt	JPMorgan EMBI	2.76%	-0.53%	0.37%	0.17%	1.62%	-16.45%
Real Assets	Real Estate	FTSE NAREIT	3.54%	-19.06%	9.78%	5.90%	5.50%	-24.37%
Real Assets	Energy Infrastructure	Alerian MLP	5.74%	13.81%	31.78%	5.94%	0.57%	30.54%
Real Assets	Broad Commodities	Bloomberg Commodity	-6.07%	-16.40%	21.99%	4.67%	-1.57%	16.09%
Real Assets	Oil	WTI Crude	-4.34%	-27.13%	83.93%	2.43%	-1.90%	6.71%
Real Assets	Gold	Gold COMEX	9.47%	5.70%	5.33%	8.60%	3.24%	-0.13%

Key Market Interest Rates	Current Rate	1 Month Ago	2 Months Ago	3 Months Ago	4 Months Ago	6 Months Ago	1 Year Ago
Federal Funds Rate	4.83%	4.83%	4.57%	4.33%	4.33%	3.08%	0.33%
Secured Overnight Fin. Rate (SOFR)	4.81%	4.83%	4.55%	4.30%	4.30%	3.04%	0.28%
90-Day Treasury Rate	4.95%	4.43%	4.67%	4.56%	4.21%	3.88%	0.78%
2-Year Treasury Rate	4.01%	4.10%	4.78%	4.20%	4.36%	4.27%	2.62%
5-Year Treasury Rate	3.48%	3.68%	4.17%	3.61%	3.94%	4.06%	2.84%
10-Year Treasury Rate	3.42%	3.56%	3.91%	3.50%	3.81%	3.92%	2.82%
30-Year Treasury Rate	3.67%	3.76%	3.93%	3.62%	3.90%	4.08%	2.89%
3-Mon/10-Yr Treasury Spread	-1.53%	-0.86%	-0.76%	-1.05%	-0.40%	0.03%	2.04%
2-Yr /10-Yr Treasury Spread	-0.58%	-0.54%	-0.86%	-0.70%	-0.55%	-0.36%	0.21%
6-Month CD Rate	1.91%	1.90%	1.84%	1.86%	1.83%	1.34%	0.29%
1-Year CD Rate	2.44%	2.43%	2.37%	2.38%	2.35%	1.86%	0.51%
2-Year CD Rate	2.52%	2.54%	2.48%	2.49%	2.48%	2.10%	0.58%

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