Goldman Sachs The Markets

Markets make sense of the Fed

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Mike Washington: The Fed chair Powell holds rates steady but says we're meaningfully above the neutral rate. What does it mean for investors? This is The Markets.

I'm Mike Washington, equity sales trader with Goldman Sachs Global Banking and Markets, sitting in for Chris Hussey this week. My guest is Lindsay Rosner, head of multi sector investing in Goldman Sachs asset management. Lindsay, great to have you.

Lindsay Rosner: Thanks for having me.

Mike Washington: So the Fed held rates steady today and also removed a reference to progress toward inflation goal.

What did you take away from this statement, and from Fed Chair Powell's comments?

Lindsay Rosner: Yeah, so I think the important thing is that there was a statement, and then like every FOMC, we have a presser. And from the statement, I think the market took one thing, including myself. And the presser kind of cleared up a lot of what was going on.

So in the statement, as you mentioned, the Fed very clearly stated that they were going to pause and not lower rates at this meeting. But they did two things. They said that the labor market now remains solid. Where prior there was some language around the labor market maybe faltering.

And the other thing was they used to have language in the statement talking about it trending in the right direction. They were making progress towards their two percent goal. That got removed completely. And instead it said inflation remains somewhat elevated. So the statement short. And people like to compare, you know, statement over statement, and they cross things out, and they show where the changes are, and those two things, the change around the labor market and the change around inflation, was immediately interpreted as hawkish.

The market said, wait a second, this actually sounds like a Fed that's not just pausing for a meeting and then looking for a data print and going to cut. This actually may be a Fed that wants to pause a lot longer, and that made the market a little bit jittery.

Yields backed up five basis points. Treasury yields higher, five basis points. And stocks that were already down 40 basis points on the S&P moved down to 80. That was the statement. Then we got into the presser, and we learned why those actions around the language happened.

And in fact, Powell told us that they did some cleanup. They did apparently not spring cleaning, a winter cleanup on the language, and that it wasn't meant to send a signal, and that signal is what the market had knee jerk reaction initially interpreted. And then things got better.

Mike Washington: Yeah, so hawkish statement, leaning dovish presser, I'd say.

Lindsay Rosner: Yeah, and Powell, I think, gave one really comforting answer in the Q&A, which was he felt the policy was still restrictive. And that means there's still some distance to go between where we are now on Fed funds and where they think they need to be.

Mike Washington: Just in general, there's been a lot of attention on five percent, in the 10-year yield. We approach it in early January, we've backed away from it pretty materially, actually. What do you see as the most likely path for rates over the course of this next year?

Lindsay Rosner: So we think in general rates will stay around this zip code or go a little bit lower, but what's important also there is to break out the front end of the curve from the back end of the curve. And a big thing that we've heard, the buzz phrase that's out there, is term premium.

And that basically means that when you're lending, whether it's to the U.S. government or you're lending to an individual or a corporation, when you're lending them money over a longer period of time, the expectation is you should be compensated because with more time, there's more uncertainty and more unknown.

There wasn't much term premium in the U. S. Treasury curve. And after we had the December FOMC, we got that. Said in a different way, the back end of the curve, we saw some movement. Now given where this curve currently stands, we think actually the two year part of the curve could go a little bit lower.

You could say maybe we're in a range where it's going to be 10 basis points lower from here, to maybe 20 basis points higher. In the back end of the curve. That's more of a question mark. What the back end of the Treasury curve prices in is questions around fiscal policy, and that is front and center.

And it even came up today in the presser that what fiscal policy will be. What, trade policy will be in this new administration, I mean, we're not even two weeks in. There are a lot of question marks. And that's what gets priced into the back end. And so I'd say probably yields around here, but less certainty in the back end than we do have in the front end of the curve.

Mike Washington: So with all that in mind, I guess where across the curve do you find that people that you're speaking to, investors you're speaking to, are most focused? Where are the best opportunities in the bond market?

Lindsay Rosner: Sure. So the questions are focused on, do I get out of cash? There's a ton of money in money markets, and it's still there.

I think we've all been on this money market watch. When is it going to actually move? And it hasn't moved. And in fact, even over 2024, we've seen money markets actually increase in asset size. Not dramatically, but it actually went higher. It didn't go lower as you had a Fed that began cutting. So the question is, when do we move out the curve?

And where we think the opportunities really are, are kind of in that middle intermediate duration. And back to that idea of term premium or the steepness of the curve, once you start getting out of the very front end of the curve, there's not only more opportunities to take part in many different asset classes, so there's structured products, there's credit, there's all sorts of things as you get out the curve, that don't finance themselves at the very, very front end, so you have more opportunities there.

And you have more yield, and as we've gone through this whole, Fed cutting and what happened in December and those moves, there's actually also something now that's important called real yield. I. e., you can actually earn yield when you remove the inflation piece from nominal yield. So there's real stuff to earn in fixed income.

Mike Washington: Yeah, great. I mean, I don't know about you, Lindsay, but for me, the month of January has felt like an entire quarter. we're finally flipping the calendar next week. We've had a really busy end to January this week. What is it that you're most looking towards next week as we do flip the calendar into February?

Lindsay Rosner: Well, the word February is important because we've heard from Trump and team that February 1st is kind of the first guidepost potentially for tariff.

So that is absolutely something we're waiting to see. There's been a lot of discussion that there are two time frames right now of tariffs. One is February 1st against specific countries, and then April 1st will be the review of the memorandum on American trade policy, and there could be more tariffs coming April 1st.

But that first date is right around the corner. So we're waiting to see what happens there in terms of tariffs. we're also, there's a lot of data that's going to be important. We're going to get GDP, which should be important. We're going to get an insight on, wages and Fed's preferred measure.

And then we're going to continue to get some insight into inflation indicators. And, what we did learn once again today, I think, fine point pen there, the Fed is data dependent. And so every one of these data prints really matters in terms of the course of monetary policy.

Mike Washington: Such a fun time to be in the markets right now. There's so much to talk about. Lindsay, this has been awesome. Thanks again for coming along.

Lindsay Rosner: Yeah. Thanks for having me.

Mike Washington: That does it for this week's episode of The Markets. I'm Mike Washington. Thanks for listening.

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