POWELL RIDING HERD CALMS (AT LEAST SOME OF) THE MARKETS

By Ellen Gaske, PhD, CFA, Lead Economist G10 Economies, Global Macroeconomic Research Team
and Robert Tipp, CFA, Chief Investment Strategist and Head of Global Bonds

The Federal Reserve kept its policies unchanged at its meeting on March 17, 2021, as expected, with little change to its statement released after the meeting. But alongside this steadiness, the Fed also released updated economic projections, which showed a significant boost in the outlook compared to their last release back in December. Chairman Powell nonetheless reiterated the Fed won't try to be pre-emptive in tightening monetary policy in anticipation of better growth. Instead, it intends to be more patient this cycle than it has in the past; the Fed will want to see a recovery in the actual data - not just in its forecasts - before removing any of its current stimulus.

After a slowdown in growth late last year amidst rising virus counts, economic activity appears to be reaccelerating alongside a pickup in the pace of vaccinations and over $4 trillion of fiscal support to date piled on top. Fed officials' median projection for GDP growth this year was raised by over 2 percentage points to 6.5%, echoing upward revisions made by private sector economists this year. The unemployment rate projected for this year dropped to 4.5% and now glides to 3.5% by 2023. Core PCE inflation is expected to temporarily rise this year as last year's low inflation readings fall out of year-over-year comparisons and short-term supply bottlenecks remain. The projections indicate core PCE is expected to settle at 2% next year and 2.1% in 2023.

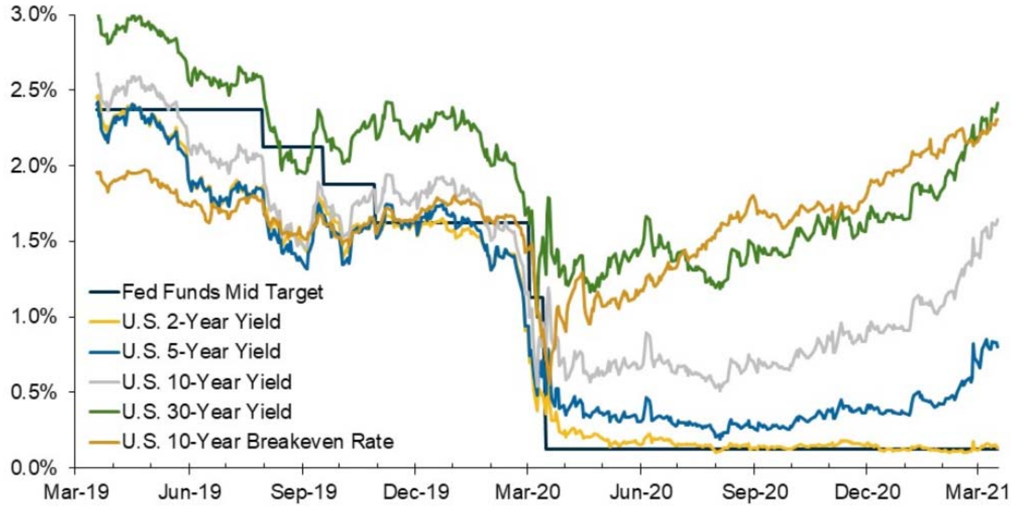
If the forecasted rebound in economic activity actually pans out this year, **our base case assumes that the Fed's tone will change later in 2021.** The Fed's current forward guidance on Treasury and MBS purchases indicates they will continue at least at a net pace of $80 billion and $40 billion, respectively, until substantial further progress has been made towards the Fed's 2% inflation and full employment goals. **We think this condition will likely be met towards the end of this year, with the Fed likely to announce tapering sometime later this fall or thereabouts with subsequent tapering over the next several quarters.**

On the rates front, though, the Fed's forward guidance tells us they plan to keep the Fed funds rate unchanged not just until the economy has made substantial further progress, but rather, until 2% inflation has actually been achieved (and is on track to exceed 2% for a time) and the labor market has reached full employment. Most Fed officials project this more stringent set of conditions for rate lift-off won't be achieved until sometime after 2023. But four Fed officials now project that time will likely come as soon as 2022, and seven now expect rate hikes by the end of 2023. **While we think rate lift-off in 2022 is unlikely, if the economy continues to recover rapidly as vaccinations accelerate this spring, we anticipate even more Fed officials might join those currently anticipating modest rate hikes beginning at some point in 2023.**

Expectations for Strong Growth Here for Now Before Potentially Fading

With the economy rapidly recovering, the Treasury curve had been aggressively bear steepening ahead of the Fed's latest meeting. Despite a few more dots in the FOMC's projections pencilling in rate hikes, the front-end of the Treasury yield curve was calmed by Chair Powell's emphasis on keeping rates low until the Fed solidly achieves its dual mandate. The Fed's growth-positive message was also well received by risk markets, boosting stock prices and driving credit spreads tighter. **On the other hand, longer-dated Treasury yields continued to inch higher, which we believe reflects concerns that the Fed may indeed create strong growth and potentially incite excessive inflation (Figure 1).**

FIGURE 1: CHAIR POWELL'S COMMENTS HELPED TO STABILIZE SHORT AND INTERMEDIATE TREASURY YIELDS, ALTHOUGH LONGER-DATED TREASURY YIELDS AND INFLATION EXPECTATIONS CONTINUED TO INCH HIGHER.



Source: Bloomberg as of March 17, 2021

Looking ahead, longer-dated yields may remain on edge as the next round of stimulus checks flow through the economy, keeping investor concerns about economic overheating and rising inflation at a low boil. **However, looking towards the second half of 2021 and 2022, as growth begins to moderate, market concerns about overheating, inflation, and significant Fed rates hikes are likely to wane. In turn, expectations for a slow-going Fed should prove supportive of asset markets, particularly fixed income, and encourage investors to move further out the yield curve and down-in quality in search of yield and return.**

This material reflects the views of the author as of March 18, 2021 and is provided for informational or educational purposes only. Source(s) of data (unless otherwise noted): PGIM Fixed Income.

Important Information

PGIM Fixed Income operates primarily through PGIM, Inc., a registered investment adviser under the U.S. Investment Advisers Act of 1940, as amended, and a Prudential Financial, Inc. ("PFI") company. Registration as a registered investment adviser does not imply a certain level or skill or training. PGIM Fixed Income is headquartered in Newark, New Jersey and also includes the following businesses globally: (i) the public fixed income unit within PGIM Limited, located in London; (ii) PGIM Netherlands B.V. located in Amsterdam; (iii) PGIM Japan Co., Ltd. ("PGIM Japan"), located in Tokyo; (iv) the public fixed income unit within PGIM (Hong Kong) Ltd. located in Hong Kong; and (v) the public fixed income unit within PGIM (Singapore) Pte. Ltd., located in Singapore ("PGIM Singapore"). PFI of the United States is not affiliated in any manner with Prudential plc, incorporated in the United Kingdom or with Prudential Assurance Company, a subsidiary of M&G plc, incorporated in the United Kingdom. Prudential, PGIM, their respective logos, and the Rock symbol are service marks of PFI and its related entities, registered in many jurisdictions worldwide.

These materials are for informational or educational purposes only. The information is not intended as investment advice and is not a recommendation about managing or investing assets. In providing these materials, PGIM is not acting as your fiduciary. These materials represent the views, opinions and recommendations of the author(s) regarding the economic conditions, asset classes, securities, issuers or financial instruments referenced herein. Distribution of this information to any person other than the person to whom it was originally delivered and to such person's advisers is unauthorized, and any reproduction of these materials, in whole or in part, or the divulgence of any of the contents hereof, without prior consent of PGIM Fixed Income is prohibited. Certain information contained herein has been obtained from sources that PGIM Fixed Income believes to be reliable as of the date presented; however, PGIM Fixed Income cannot guarantee the accuracy of such information, assure its completeness, or warrant such information will not be changed. The information contained herein is current as of the date of issuance (or such earlier date as referenced herein) and is subject to change without notice. PGIM Fixed Income has no obligation to update any or all of such information; nor do we make any express or implied warranties or representations as to the completeness or accuracy or accept responsibility for errors. All investments involve risk, including the possible loss of capital. These materials are not intended as an offer or solicitation with respect to the purchase or sale of any security or other financial instrument or an y investment management services and should not be used as the basis for any investment decision. No risk management technique can guarantee the mitigation or elimination of risk in any market environment. Past performance is not a guarantee or a reliable indicator of future results and an investment could lose value. No liability whatsoever is accepted for any loss (whether direct, indirect, or consequential) that may arise from any use of the information contained in or derived from this report. PGIM Fixed Income and its affiliates may make investment decisions that are inconsistent with the recommendations or views expressed herein, including for proprietary accounts of PGIM Fixed Income or its affiliates.

The opinions and recommendations herein do not take into account individual client circumstances, objectives, or needs and are not intended as recommendations of particular securities, financial instruments or strategies to particular clients or prospects. No determination has been made regarding the suitability of any securities, financial instruments or strategies for particular clients or prospects. For any securities or financial instruments mentioned herein, the recipient(s) of this report must make its own independent decisions.

Conflicts of Interest: PGIM Fixed Income and its affiliates may have investment advisory or other business relationships with the issuers of securities referenced herein. PGIM Fixed Income and its affiliates, officers, directors and employees may from time to time have long or short positions in and buy or sell securities or financial instruments referenced herein. PGIM Fixed Income and its affiliates may develop and publish research that is independent of, and different than, the recommendations contained herein. PGIM Fixed Income's personnel other than the author(s), such as sales, marketing and trading personnel, may provide oral or written market commentary or ideas to PGIM Fixed Income's clients or prospects or proprietary investment ideas that differ from the views expressed herein. Additional information regarding actual and potential conflicts of interest is available in Part 2A of PGIM Fixed Income's Form ADV.

In the United Kingdom, information is issued by PGIM Limited with registered office: Grand Buildings, 1-3 Strand, Trafalgar Square, London, WC2N 5HR. PGIM Limited is authorised and regulated by the Financial Conduct Authority ("FCA") of the United Kingdom (Firm Reference Number 193418). In the European Economic Area ("EEA"), information is issued by PGIM Netherlands B.V., an entity authorised by the Autoriteit Financiële Markten ("AFM") in the Netherlands and operating on the basis of a European passport. In certain EEA countries, information is, where permitted, presented by PGIM Limited in reliance of provisions, exemptions or licenses available to PGIM Limited under temporary permission arrangements following the exit of the United Kingdom from the European Union. These materials are issued by PGIM Limited and/or PGIM Netherlands B.V. to persons who are professional clients as defined under the rules of the FCA and/or to persons who are professional clients as defined in the relevant local implementation of Directive 2014/65/EU (MiFID II). In certain countries in Asia-Pacific, information is presented by PGIM (Singapore) Pte. Ltd., a Singapore investment manager registered with and licensed by the Monetary Authority of Singapore. In Japan, information is presented by PGIM Japan Co. Ltd., registered investment adviser with the Japanese Financial Services Agency. In South Korea, information is presented by PGIM, Inc., which is licensed to provide discretionary investment management services directly to South Korean investors. In Hong Kong, information is provided by PGIM (Hong Kong) Limited, a regulated entity with the Securities & Futures Commission in Hong Kong to professional investors as defined in Section 1 of Part 1 of Schedule 1 (paragraph (a) to (i) of the Securities and Futures Ordinance (Cap.571). In Australia, this information is presented by PGIM (Australia) Pty Ltd ("PGIM Australia") for the general information of its "wholesale" customers (as defined in the Corporations Act 2001). PGIM Australia is a representative of PGIM Limited, which is exempt from the requirement to hold an Australian Financial Services License under the Australian Corporations Act 2001 in respect of financial services. PGIM Limited is exempt by virtue of its regulation by the FCA (Reg: 193418) under the laws of the United Kingdom and the application of ASIC Class Order 03/1099. The laws of the United Kingdom differ from Australian laws. In South Africa, PGIM, Inc. is an authorised financial services provider – FSP number 49012. In Canada, pursuant to the international adviser registration exemption in National Instrument 31-103, PGIM, Inc. is informing you of that: (1) PGIM, Inc. is not registered in Canada and is advising you in reliance upon an exemption from the adviser registration requirement under National Instrument 31-103; (2) PGIM, Inc.'s jurisdiction of residence is New Jersey, U.S.A.; (3) there may be difficulty enforcing legal rights against PGIM, Inc. because it is resident outside of Canada and all or substantially all of its assets may be situated outside of Canada; and (4) the name and address of the agent for service of process of PGIM, Inc. in the applicable Provinces of Canada are as follows: in Québec: Borden Ladner Gervais LLP, 1000 de La Gauchetière Street West, Suite 900 Montréal, QC H3B 5H4; in British Columbia: Borden Ladner Gervais LLP, 1200 Waterfront Centre, 200 Burrard Street, Vancouver, BC V7X 1T2; in Ontario: Borden Ladner Gervais LLP, 22 Adelaide Street West, Suite 3400, Toronto, ON M5H 4E3; in Nova Scotia: Cox & Palmer, Q.C., 1100 Purdy's Wharf Tower One, 1959 Upper Water Street, P.O. Box 2380 – Stn Central RPO, Halifax, NS B3J 3E5; in Alberta: Borden Ladner Gervais LLP, 530 Third Avenue S.W., Calgary, AB T2P R3.

留意事項 2

※本資料はPGIMフィクト・インカムが市場動向に関する情報提供としてプロの投資家向けに作成したものです。PGIMフィクスト・インカムは、米国SECの登録投資顧問会社であるPGIMインクの債券運用部門です。

※本資料は情報提供を目的としたものであり、特定の金融商品の勧誘又は販売を目的としたものではありません。また、本資料に記載された内容等については今後変更されることもあります。

※記載されている市場動向等は現時点での見解であり、これらは今後変更することもあります。また、その結果の確実性を表明するものではなく、将来の市場環境の変動等を保証するものでもありません。

※本資料に記載されている市場関連データ及び情報等は信頼できると判断した各種情報源から入手したものですが、その情報の正確性、確実性について当社が保証するものではありません。

※過去の運用実績は必ずしも将来の運用成果等を保証するものではありません。

※本資料は法務、会計、税務上のアドバイスあるいは投資推奨等を行うために作成されたものではありません。

※当社による事前承諾なしに、本資料の一部または全部を複製することは堅くお断り致します。

※PGIMジャパン株式会社は、世界最大級の金融サービス機関プルデンシャル・ファイナンシャルの一員であり、英国プルーデンシャル社とはなんら関係がありません。

PGIMジャパン株式会社
金融商品取引業者 関東財務局長（金商）第392号
加入協会 一般社団法人日本投資顧問業協会、一般社団法人投資信託協会
PGIMJ80013