Don’t Leave Money on the Table!

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The American Deposit Management Co

Make the most of your cash…in any market

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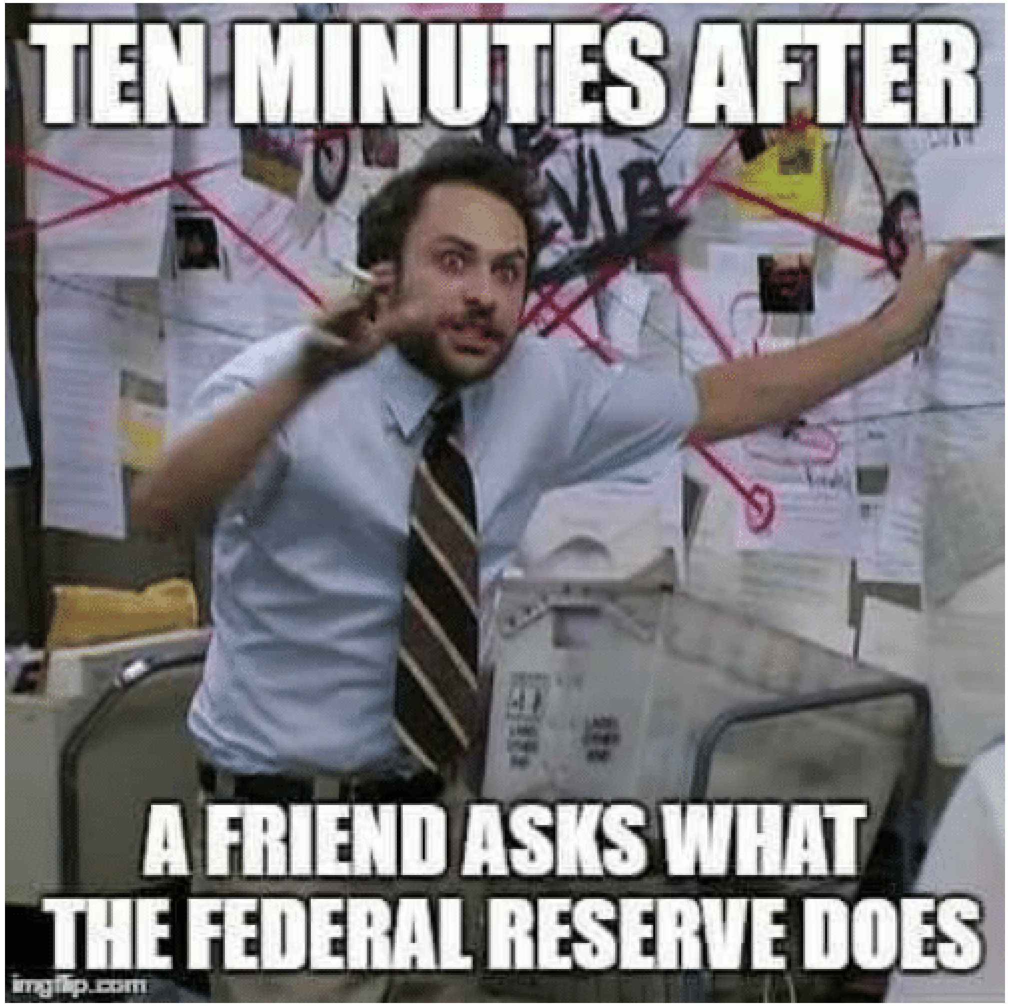
- How and why rates move
- Investment options
- Short-term investment theory and strategies
- Typical pitfalls
- Rate/market trends and effect on strategy
- Market update

How and why rates move

Hint: it’s The FED

Defining The FED

- Federal Reserve System (Board of Governors, Reserve Banks, FOMC)
  - FOMC – Federal Open Market Committee
  - Bank Reserve Requirements
  - Discount Window
- Dual mandate – Price stability and full employment
- How do they establish/implement monetary policy?
  - FOMC meeting (12 voting members) deliberate policy action and commentary
  - Purchase or sell securities to affect value of treasuries in the open market
  - Inverse rate/price relationship on bonds
- How do their actions/comments affect the markets?
  - Purchases/sales change yields
  - Comments filtered by market participants looking to “bet” on their next move, or make investments according to their perspective on the economy at large
  - Not just for investment purposes but also for refinancing debt


TEN MINUTES AFTER
A FRIEND ASKS WHAT THE FEDERAL RESERVE DOES
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THE FEDERAL RESERVE IS NECESSARY?
FALSE. THE FED CAUSES RECESSIONS.

What to Watch

Market Indicators

- Dual mandate
- Price stability
  - Inflation theory
    - No excess capacity, higher demand, prices rise
    - Full employment, wages rise, cost of production rises, cost of goods rises
  - Inflation target 2%
- Full employment
  - 4%
  - Underemployed?
- Leading economic indicators (see market analysis)

What are your options?

Not a lot of excitement here ☺

K.I.S.S. (Keep It Simple St***d)

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- **“Failing to plan is planning to fail”**
  - Determine risk tolerance
  - Define management style
    - Trader, Investor, or Buy-and-hold?
  - Create investment plan
  - Not just policy but based on specific needs
- **Options**
  - Treasuries - US gov’t debt, low risk low return
  - Agencies - implied US gov't backing, slightly higher risk, slightly higher return
  - Banks - CDs, repos, collateralized liquid, US gov't backed to a point, implied higher risk, higher return
  - Commercial Paper - short term unsecured debt from major corps, higher risk highest return
  - All fluctuate in value EXCEPT bank products (mark to market)
  - Opportunity to sell for profit, but lose guaranteed rate

Strategies

- **Fully liquid (Bank, MMKT, LGIP, etc.)**
  - Participate immediately with rate increases (with vigilance)
  - Most flexibility
  - Participate fully in rate declines…oops!
- **Ladder (CDs, Gov't, CP)**
  - Ladder maturities down the yield curve
    - Continual maturities participate in all markets
    - Ability to lock in (generally) higher rates for longer maturities
    - Less flexibility (must have cash and investment plan)
- **Barbell (CDs, Gov't, CP)**
  - "Ladder" without the medium-term maturities
  - Falling rates may provide short- and long-term opportunity where medium-term lags
  - Lock in for long term hedge on falling rates, can maintain short-term participation
- **Combination**
  - Each situation is different and will have unique considerations
  - One strategy in place as another is being implemented based on current market

Strategies

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	Open Date	Term	Rate	Fed Funds	
CDBKWEST17	3/13/2018	24 mo	2.50%	1.50%	
CDCIBC02	3/13/2018	24 mo	2.35%		
CDPROFIN1	2/20/2019	12 mo	2.82%	2.50%	11 mo later, 12 mo shorter
CDKEYBNK29	2/21/2019	12 mo	3.09%		
CDFIB43	3/13/2019	18 mo	2.84%		
CDFBOI16	8/28/2019	18 mo	2.35%	2.25%	
CDMSTB36	8/30/2019	36 mo	2.52%		18 mo later, 12 mo longer

Pitfalls

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- **Too much liquidity**
  - "Fully liquid" is NOT really a strategy, even in a rising rate environment
  - Lower: Ladder or barbell (short-term, longest reasonable term)
    - Longer term can decrease in price more
    - Income can be higher, but marketable securities will show mark-to-market losses in value
    - Maintain enough cash to avoid selling at a discount
  - Higher: Highly liquid + ladder - search for opportunities down the curve
  - Flat: Ladder or barbell, maturing every month or quarter or both depending on cash needs
- **Lack of diversification**
  - Institutions: brokers, banks, etc.
    - Why? Time
  - Instrument: treasuries, agencies, banks
    - Why? Understanding
  - Time: both liquid and term
    - Why? Strategy
- **Cash flow management**
  - Understand your yearly cycle
  - Evaluate past cycles both good and bad
  - Plan worst case scenario
  - Establish baseline and backup plan

Where are rates headed?

Pssst! No one knows, but probably down


YOU GOT ANY MORE OF THAT
3% CD RATE?
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Tricklin’ Down

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What happens when the FED *actually* changes rates

- Federal reserve moves
  - Higher rates make borrowing more expensive
  - Lower rates pull demand forward, that eventually needs to be reset
  - Mortgage for $100k for 30 yrs @ 4%=$477 5%=537
- Banks reaction
  - Lower rate expectations - extend loan terms (avoid lower reset) and follow deposit rates down
  - Higher rate expectations - shorten loan terms to keep up with deposit rate rises
- Investors reaction: opposite
  - Rising rates: lock in rates on loans, stay liquid in cash
  - Falling rates: float rates on loans, lock in rates on cash

Market Analysis

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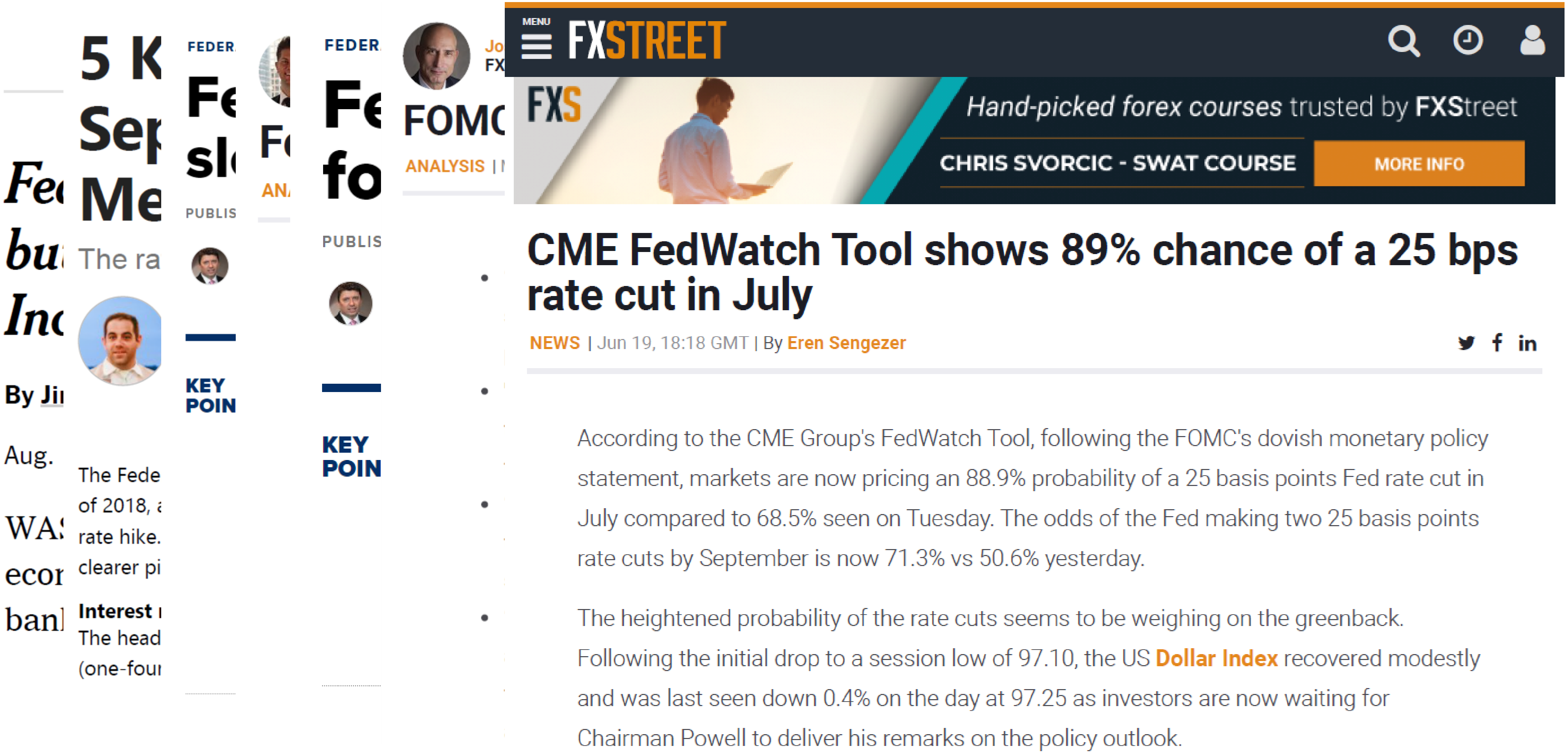

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MORE INFO

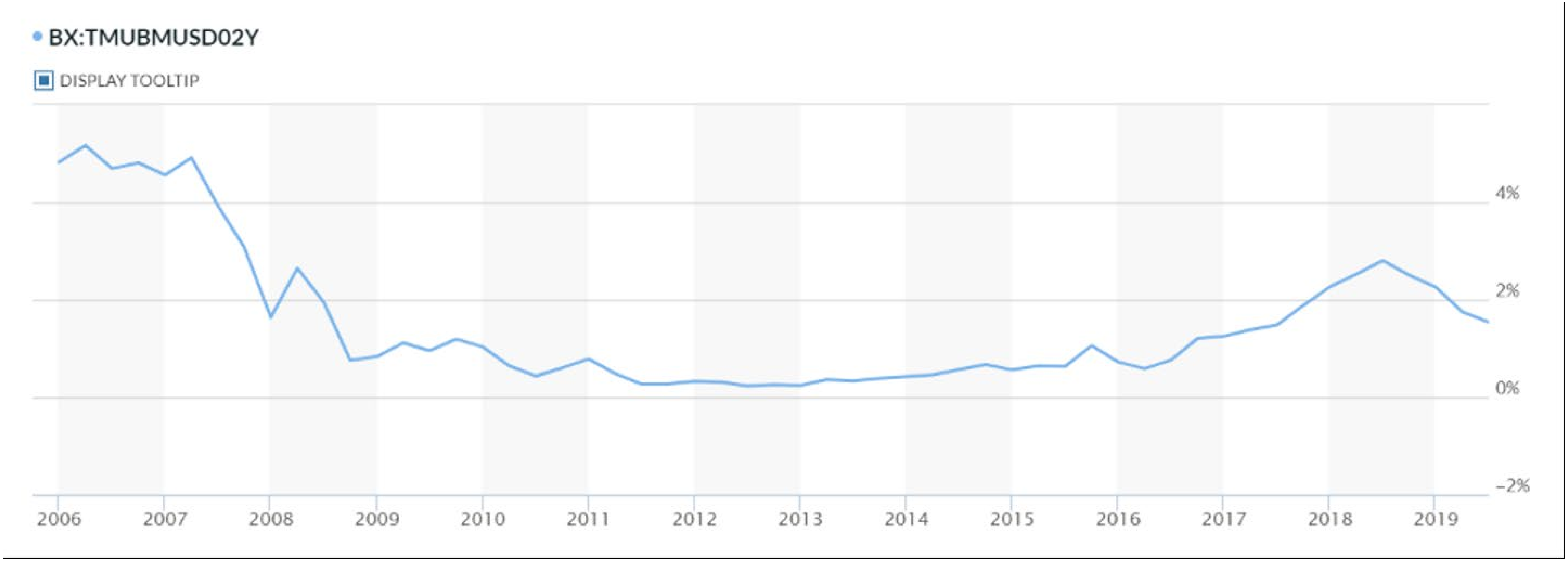
CME FedWatch Tool shows 89% chance of a 25 bps rate cut in July

NEWS | Jun 19, 18:18 GMT | By Eren Sengezer

According to the CME Group's FedWatch Tool, following the FOMC's dovish monetary policy statement, markets are now pricing an 88.9% probability of a 25 basis points Fed rate cut in July compared to 68.5% seen on Tuesday. The odds of the Fed making two 25 basis points rate cuts by September is now 71.3% vs 50.6% yesterday.

The heightened probability of the rate cuts seems to be weighing on the greenback. Following the initial drop to a session low of 97.10, the US **Dollar Index** recovered modestly and was last seen down 0.4% on the day at 97.25 as investors are now waiting for Chairman Powell to deliver his remarks on the policy outlook.

Market Analysis



Market Analysis

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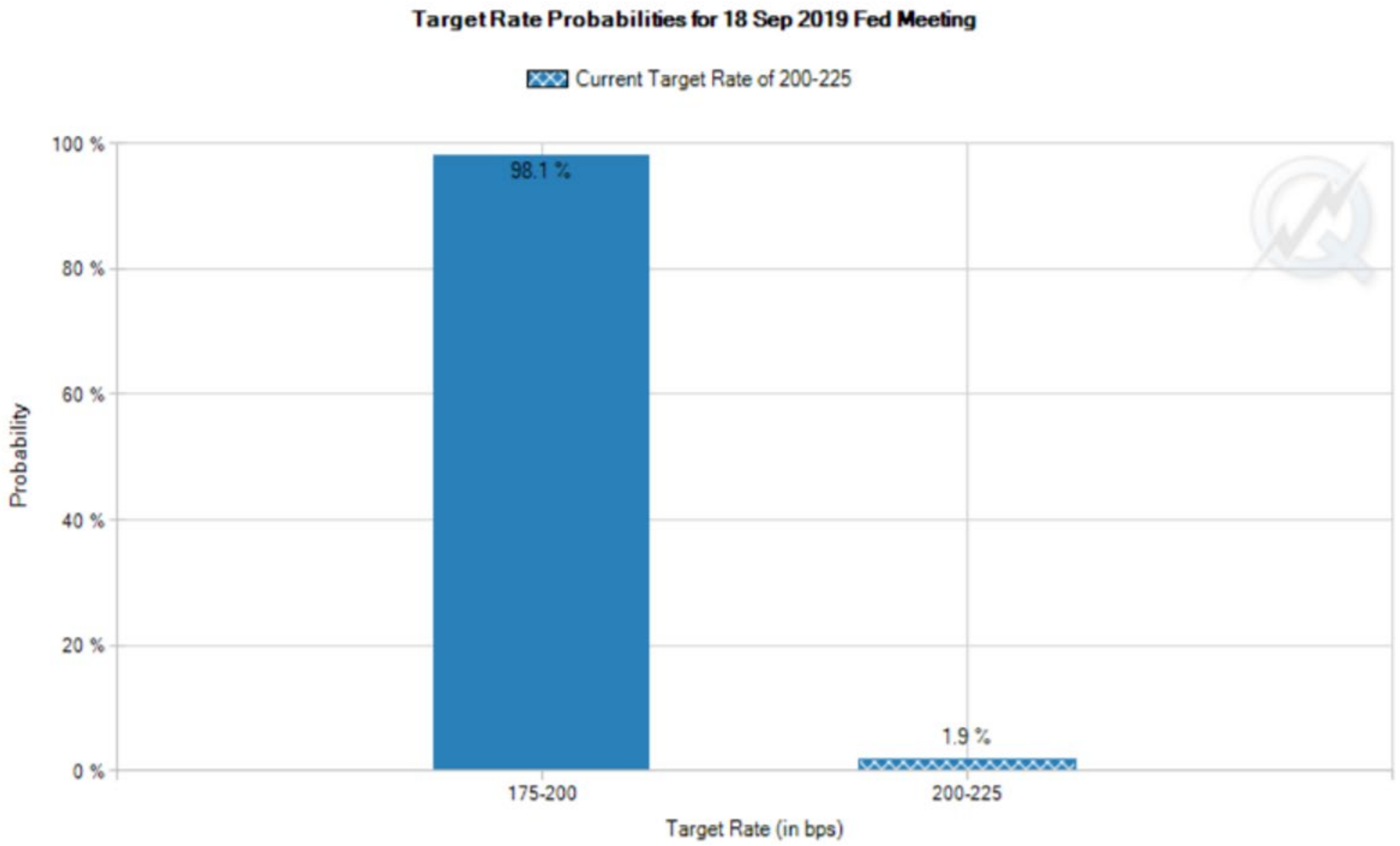

SOURCE: CME FedWatch Tool

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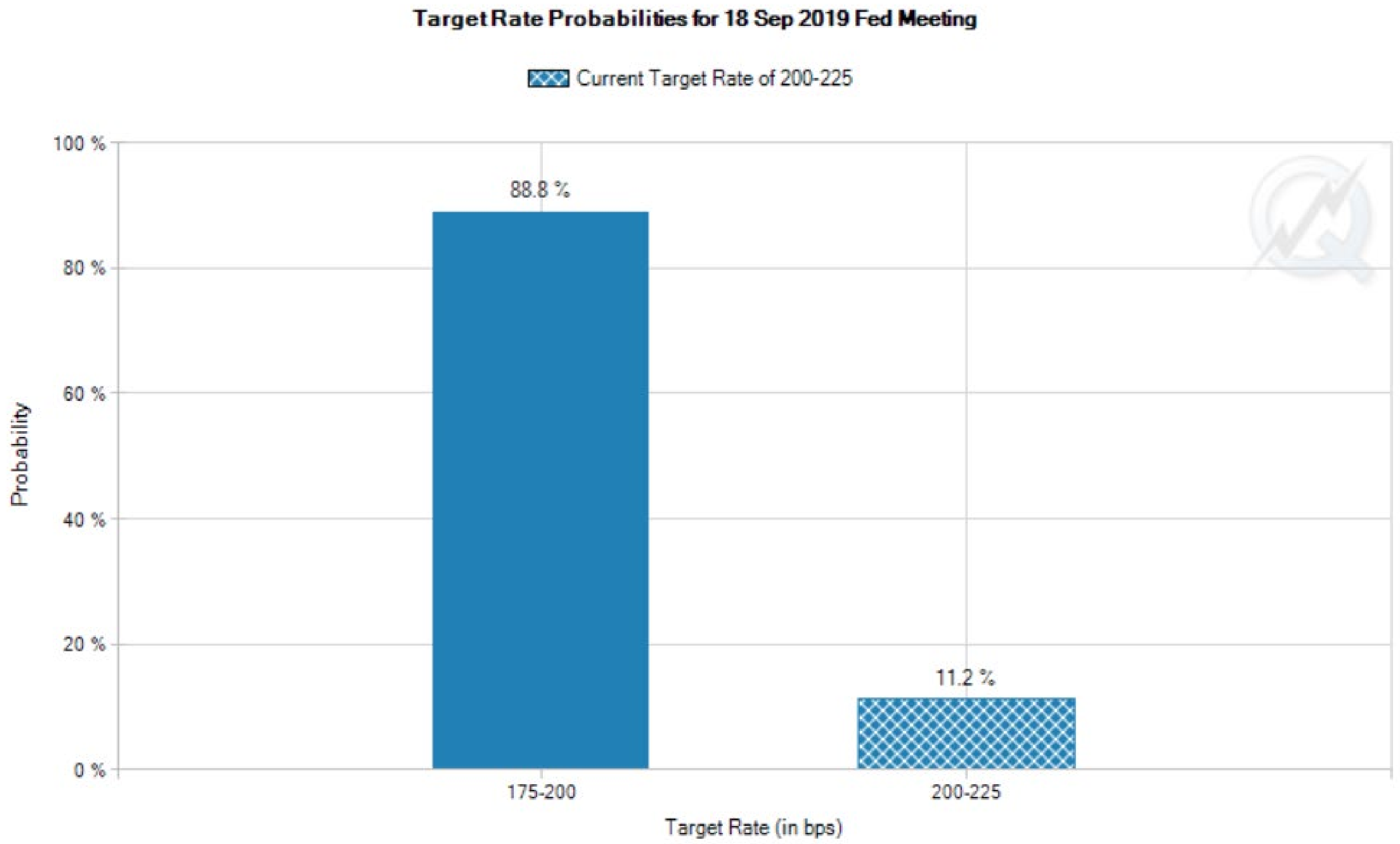

SOURCE: CME FedWatch Tool

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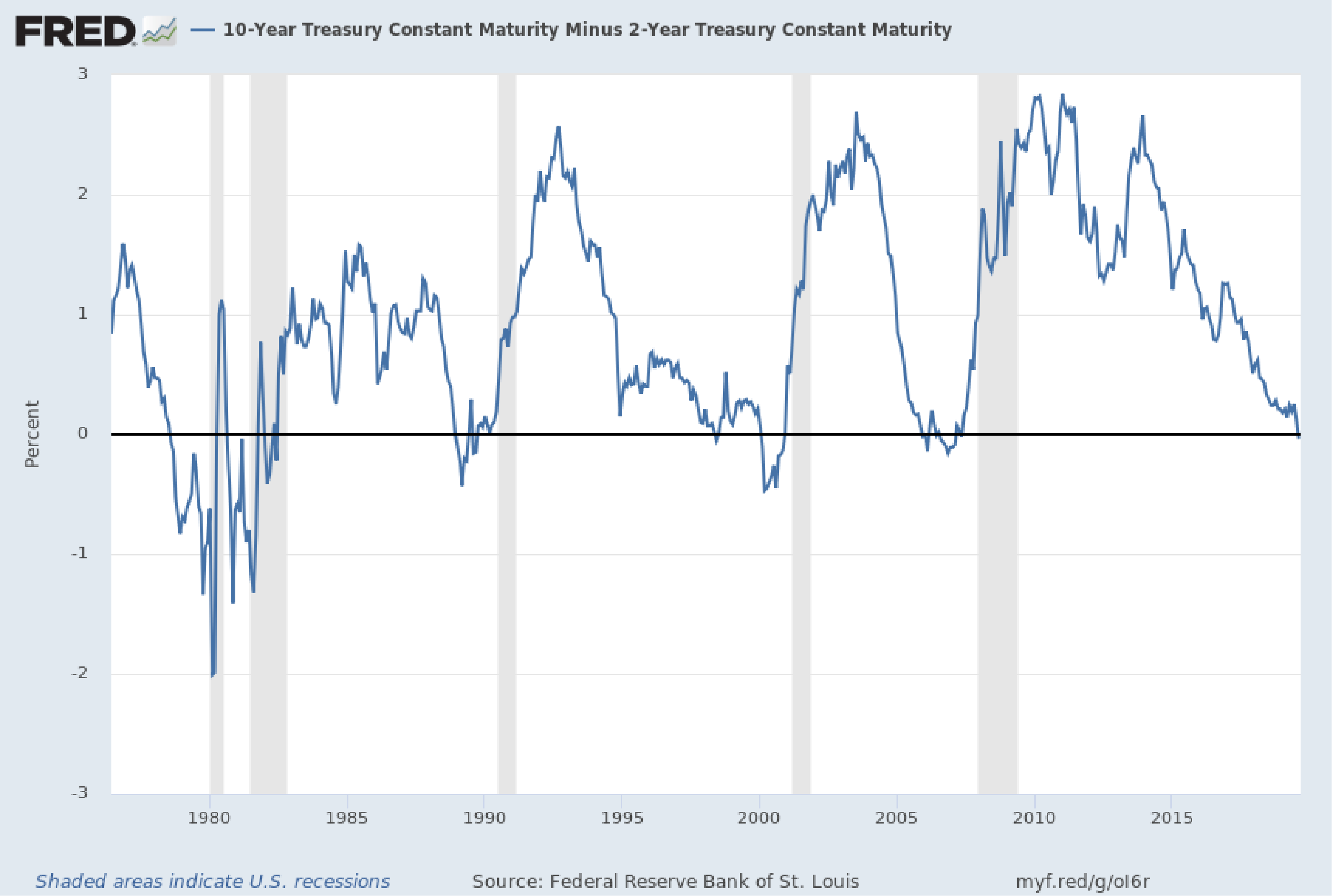

Market Analysis

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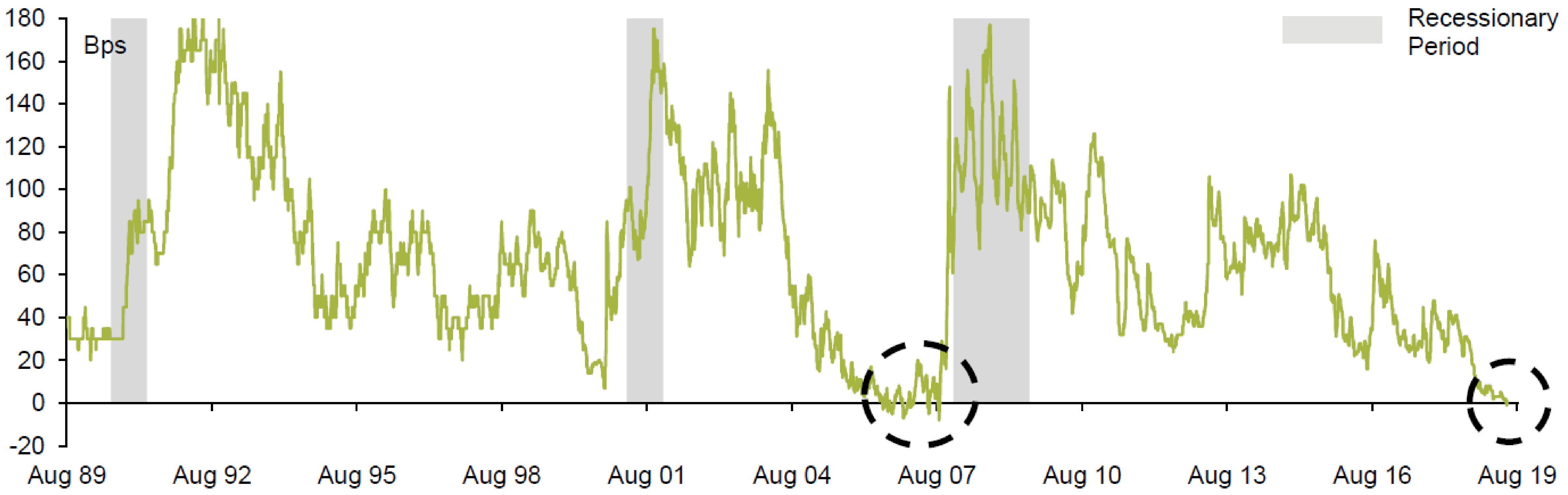
MMD yields in the 1s4s spot inverted by 1 bp on August 22, 2019, the first time since 2007



Source: J.P. Morgan, Thomson Reuters Municipal Market Data, J.P. Morgan Research, *US Fixed Income Markets Weekly – Municipals*, 8/16/2019 and 8/23/2019, jpmm.com; Rates as of 8/23/2019

Market Analysis

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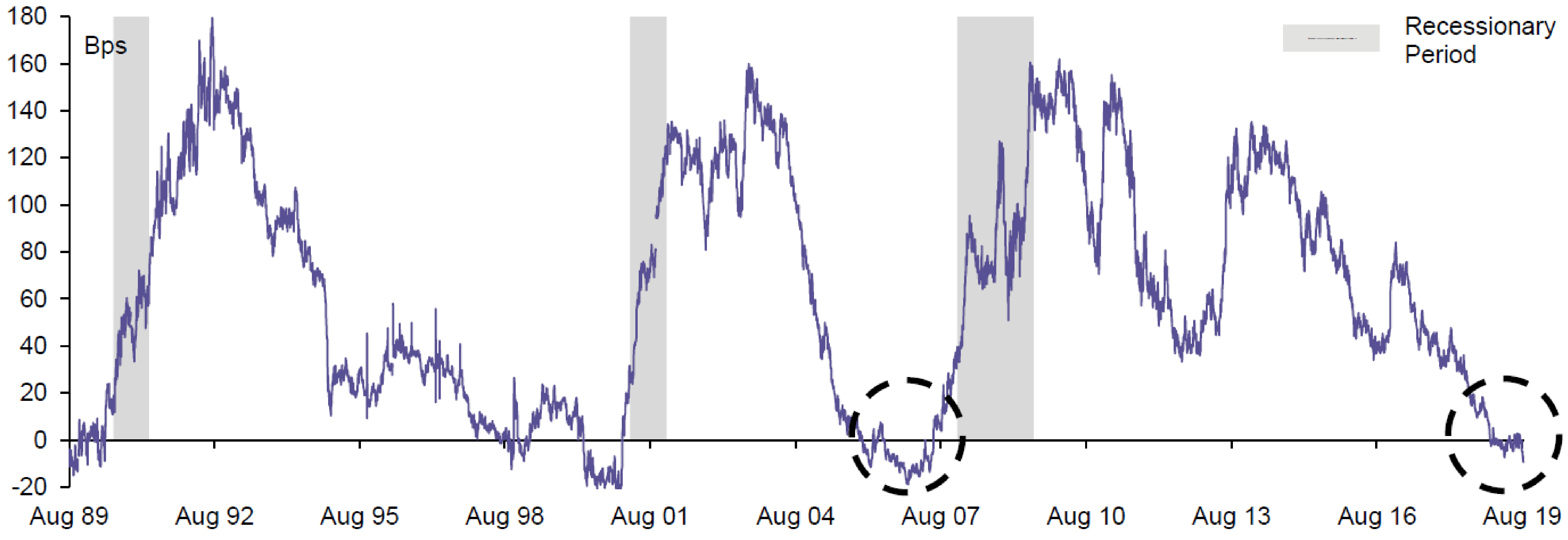
UST yields in the 2s5s spot are currently inverted by 6 bps and have historically inverted preceding recessions



Source: J.P. Morgan, Thomson Reuters Municipal Market Data, J.P. Morgan Research, *US Fixed Income Markets Weekly – Municipals*, 8/16/2019 and 8/23/2019, jpmm.com; Rates as of 8/23/2019

Market Analysis

Leading Economic Indicators

- Negative

- 2-10 year Treasury Yields – Inverted in August 2019
- Consumer Confidence – Down/flat in August 2019
- Pending Home Sales – Lower in August
- Construction Spending – Missed expectations in September
- Weekly Jobless Claims – Up in September

+ Positive

- PMI – Beat expectations in August
- Unemployment – Flat
- Factory Orders – Beat expectations (increased)

Market Analysis

Takeaway #1:

Is a recession on the horizon?

- Maybe
- Still mixed economic data
- Self-fulfilling prophecy

Global trade tensions could cool, but a slow down may be inevitable

Takeaway #2:

Are rates going to stabilize?

- Maybe
- At least one more .25% decrease
- Lots of economic headwinds
- Fed has telegraphed its moves more than ever

Opportunity to lock in rates before decline

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