

Pathfinder Investment Outlook

For the week ending May 19th, 2023

Thoughts on Central Banks

Three weeks ago, we identified three areas of focus that we will be discussing this spring (the economy, employment and inflation). This week, we discuss the US Federal Open Market Committee (FOMC) and how it might approach its positioning in the coming months. One of the most difficult parts of finance is to predict what the FOMC will do and how “the market” will react. This is essentially one equation with two unknowns and tends to cause a lot of confusion for investors. It is also probably not predictable with any level of consistency. We note two quotes below that we thought were interesting from this perspective. One from Jamie Dimon, CEO of JPMorgan and one from Jerome Powell, US Fed Chair.

“And while this is **nothing like 2008**, it is not clear when this current crisis will end.... it will clearly cause some **tightening of financial conditions** as banks and other lenders become more conservative...We are seeing people reduce lending... It won’t necessarily force a recession, but it is recessionary.” - JPMorgan Chase (\$JPM) CEO Jamie Dimon

“You will have noticed that in the statement for March, we had a **sentence** that said the committee anticipates that some additional **policy firming may be appropriate**. That **sentence is not in the statement anymore**...you will know that the summary of economic projections... this was the ultimate high level of rates.” - US Federal Reserve Chair Jerome Powell

Figure 1 presents the probability of a potential hike or cut for US rates at the coming meetings, calculated from Fed Funds futures. It indicates that at the next meeting, there is a 30% chance that the FOMC will **hike rates**. However, it also says that 7 months out, there is an 84% chance the FOMC will **rate cuts** 2.5 times. If you look at the same data for Europe, the market believes that there is a 95% chance of an ECB **rate hike** at the next meeting.

This means that the current outlook from central banks around the world is diverse. While corporations are seeing some signs of implied tightening from bank failures, central banks, depending on what part of the world they manage, have very different views from each other. It is difficult to have a convicted opinion, and even if one did, “the market” reaction will be difficult to gauge. For example, is an 80% probability of 2.5% rate cut in January of 2024 positive for equities because we have avoided recession and will start a new economic cycle? Or is it negative because we have formally entered a recession and the FOMC was too aggressive for too long, and needs to cut quickly to try to fix its error? It’s probably truly impossible to tell.

Figure 1: World Interest Rate Probability

May 19, 2023

Region: United States »		Instrument: Fed Funds Futures »			
Target Rate	5.25	Pricing Date	05/19/2023		
Effective Rate	5.08	Cur. Imp. O/N Rate	5.078		
Meeting	#Hikes/Cuts	%Hike/Cut	Imp. Rate Δ	Implied Rate	A.R.M.
06/14/2023	+0.296	+29.6%	+0.074	5.152	0.250
07/26/2023	+0.308	+1.2%	+0.077	5.155	0.250
09/20/2023	-0.067	-37.5%	-0.017	5.061	0.250
11/01/2023	-0.787	-71.9%	-0.197	4.881	0.250
12/13/2023	-1.631	-84.4%	-0.408	4.670	0.250
01/31/2024	-2.402	-77.1%	-0.601	4.477	0.250

Source: Bloomberg Markets LP, Pathfinder Asset Management Limited

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Sources: Bloomberg, Pathfinder Asset Management Limited

Disclosure

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Changes in Leverage. We are increasing the asset ceiling to 2.0 times the market value of equity for [Pathfinder International Fund](#) and [Pathfinder Real Fund](#) to be consistent with [Pathfinder Partners' Fund](#) and [Pathfinder Resource Fund](#)

For more information, please follow the links above to review the fund term sheets.

*All returns are time weighted and net of investment management fees. Returns from the Pathfinder Partners' Fund and Pathfinder Real Fund are presented based on the masters series of each fund. The Pathfinder North American Equity Portfolio and The Pathfinder North American Income Portfolio are live accounts. These are actual accounts owned by the Pathfinder Chairman (Equity) and client (High Income) which contain no legacy positions, cash flows or other Pathfinder investment mandates or products. Monthly inception dates for each fund and portfolio are as follows: Pathfinder North American Equity Portfolio (January 2011), Pathfinder North American High-Income Portfolio (October 2012) Pathfinder Partners' Fund (April 2011), Pathfinder Real Fund (April, 2013), and Pathfinder International Fund (November 2014).

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