# FFTW Weekly Commentary

FOR PROFESSIONAL INVESTORS


# Reform of The Affordable Care Act Fails


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## Key takeaways

- US interest rates continued to fall last week as the Republican Congress failed to move forward on replacing and reforming the Affordable Care Act
- Markets seem to have a growing uncertainty over the Trump reflation trade idea
- Quick and steady progress on tax reform is needed in order to further sustain the post-election rally in stock prices and the tightening of credit spreads

## Full commentary

US interest rates continued to fall last week as the Republican Congress failed to move forward on replacing and reforming the Affordable Care Act (ACA). US 10-year yields fell to 2.39% and US equities were off 1%. The US Dollar also declined versus the Euro (now 1.09) and the Yen (now 110.15). The tight range we have had in US yields so far in 2017 has held. After reaching 2.60% on March 15th when the Federal Open Market Committee (FOMC) hiked the funds rate and 10-year yields have now fallen more than 20 bps. Spreads for fixed income risk assets have been further pressured with negative excess returns: March month-to-date for US high yield is 106 bps, US corporate investment grade 20 bps, and US MBS -5 bps.

Rather than risk losing the health care reform and repeal vote on Friday, the House Republican leadership in coordination with the White House canceled the vote. Despite the Trump administration's efforts to strong arm his party. The 35 or so members of the conservative House Freedom Caucus were not convinced and with no support from the Democrats the measure simply did not have the votes. The failure to pass an ACA reform deals a serious blow to the credibility of the Republican Congress and to the Trump presidency. The infighting in the Republican Party calls into question their ability to govern effectively. The key question for markets is whether or not other market friendly priorities including tax reform, fiscal stimulus, military, and infrastructure spending are now also at risk?

As the week went on and the reform and repeal vote seemed less and less likely to pass, risk assets underperformed. Markets seem to have a growing uncertainty over the Trump reflation trade idea. Is the defeat of ACA reform a harbinger of future failures on Trump's pro-growth agenda? Should markets assign lower probabilities to tax reform and fiscal stimulus? Should we lower our expectations for the anticipated size of tax cuts and infrastructure spending? The Trump administration desperately needs a near term victory. And it would seem that the Republicans need to make quick and steady progress on tax reform in order to further sustain the post-election rally in stock prices and the tightening of credit spreads.

In other economic news, this week we had several reports on the US housing market. For only the second time since the global financial crisis the Federal Housing Finance Agency (FHFA) reported a flat month-on-month change in the Home Price Index. However, the year-on-year change in the Home Price Index was a healthy 5.7%. Mortgage origination rates moved sharply higher after the November election, and market participants are trying to gage the impact these higher rates are having on housing activity.

February existing home sales, reported last week, fell 3.7% versus the strong January report which had been the highest level in the series in 10 years. Conversely, sales on new homes rose 6.1% over January and have started the year on an upward trend. The warmer winter weather may have helped January and February sales, but it does not appear that the rise in mortgage rates is having a meaningful impact on housing activity.

One other important factor impacting existing homes sales and supporting home prices is scarce housing inventories. In many areas of the country a limited supply of homes for sale is driving home prices higher. At the same time, demand for homes is increasing due to improved job markets and growing consumer confidence. Our chart of the week shows the US Existing Home Sales Months of Supply near historic lows. The impact of the rate rise bears watching, but so far it is not having a material effect on housing activity.

## This week's market developments

**Monday, March 20**
- German PPI growth decreased to 0.2% m.o.m. for February

**Tuesday, March 21**
- UK CPI growth increased to 0.7% m.o.m. (s.a.) for February
- UK PPI Output growth decreased to 0.2% m.o.m. for February

**Wednesday, March 22**
- Japan All Industry Activity Index growth increased to 0.1% m.o.m. for January
- US Existing Home Sales decreased to 5,480,000 for February

**Thursday, March 23**
- UK Retail Sales ex Auto & Fuel growth increased to 1.3% m.o.m. (s.a.) for February
- US New Home Sales increased to 592,000 for February

**Friday, March 24**
- Markit Eurozone Manufacturing PMI (prelim estimate) increase to 56.2 for March
- Markit Eurozone Services PMI (prelim estimate) increased to 56.5 for March
- US Durable Goods Orders growth (prelim estimate) decreased to 1.7% m.o.m. (s.a.) for February
- Markit US Manufacturing PMI (prelim estimate) decreased to 53.4 for March

Source: Bloomberg, as of March 27, 2017

## Chart of the Week
### US Existing Home Sales Months of Supply


Sources: Bloomberg, as of February 28, 2017

## Central Bank Watch

| | Last move | Date of move | Current policy rate | Implied 3-Month Rate on June 2017 Interest Rate Futures Contract | Next meeting |
|---|---|---|---|---|---|
| Fed | +25 basis points | March 15, 2017 | 0.75% - 1.00% | 0.96% | May 3, 2017 |
| ECB | -5 basis points | March 10, 2016 | 0.00% | -0.18% | April 27, 2017 |
| BoJ | -20 basis points | February 16, 2016 | -0.10% - 0.00% | 0.06% | April 27, 2017 |
| BoE | -25 basis points | August 4, 2016 | 0.25% | 0.39% | May 11, 2017 |

Sources: Bloomberg, as of March 27, 2017

## Next week's market developments

**Monday, March 27**

- German IFO Business Climate Index is expected to increase to 111.1 for March

**Tuesday, March 28**

- US Wholesale Inventories growth (prelim estimate) is expected to increase to 0.2% m.o.m. (s.a.) for February

**Wednesday, March 29**

- UK Mortgage Approvals are expected to decrease to 69,100 for February

**Thursday, March 30**

- German CPI growth (prelim estimate) is expected to decrease to 0.4% m.o.m. (s.a.) for March
- US 4th Quarter Annualized GDP growth (third estimate) is expected to increase to 2.0% q.o.q.
- Japan National CPI growth is expected to decrease to 0.2% y.o.y. for February
- Japan Industrial Production growth (prelim estimate) is expected to increase to 1.2% m.o.m. (s.a.) for February

**Friday, March 31**

- UK 4th Quarter GDP growth (final estimate) is expected to remain at 0.7% q.o.q.
- US Personal Income growth is expected to remain at 0.4% m.o.m. (s.a.) for February
- US Personal Spending growth is expected to remain at 0.2% m.o.m. (s.a.) for February

Source: Bloomberg, as of March 27, 2017



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