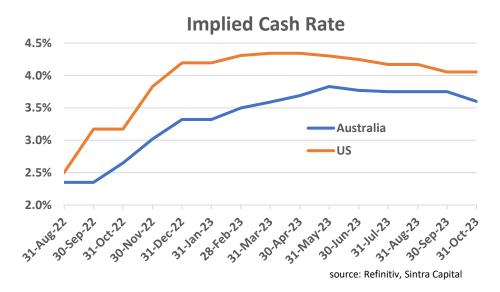


Walking the Tightrope

Like Nik Wallenda, the world's most famous tightrope walker who is best known for crossing Niagara Falls, we believe central bankers face a delicate balancing act as they raise interest rates to combat inflation.

Government bond yields tell us where the market thinks rates are heading. In Australia the current expectation is for the cash rate to peak at **3.85%** in May 2023, implying a further 1.50% increase. This compares to a peak of **4.35%** in March 2023 in the US, an increase of 1.85% from the current level (see chart below).



With inflation in the US running above that in Australia, it is no surprise that US interest rates are expected to peak at higher levels. Mortgage rates in both countries will climb to over 6%, severely impacting consumer spending.

While Australia releases inflation data quarterly, the US report monthly, making for a more turbulent journey. Though it is easy to be distracted by day-to-day noise we prefer to focus on the longer-term destination. Ultimately, we expect inflation to moderate and that excessive interest rates rises will do more harm than good.

Despite their current rhetoric, central bank governors are acutely aware of the dangers lurking in the waters below and will continue to proceed with caution.

Is the bond market overshooting? We think so.