Before the Bell
Morning Market Brief

June 13, 2019

FOR IMPORTANT DISCLOSURES, PLEASE SEE THE DISCLOSURE PAGES AT THE END OF THIS DOCUMENT

MORNING MARKET COMMENTARY: Anthony M. Saglimbene, Global Market Strategist

• Quick Take: U.S. futures are pointing to a higher open; European markets are trading in the green; Asia ended lower overnight; West Texas Intermediate (WTI) oil trading at $53.40; 10-year U.S. Treasury yield at 2.11%.

• How Do Markets Respond To Fed Easing Cycles? – It Depends: Although the Federal Reserve is widely expected to remain on hold at next week's FOMC meeting, fed fund futures are currently pricing in an 86% chance the fed funds rate will be lower following the FOMC’s end of July meeting. Historically, when markets have priced in a rate cut thirty days in advance of the targeted meeting, the Federal Reserve has rarely disappointed the market — meaning they have cut interest rates, as expected.

• Recent data on employment and inflation show the Fed may have some room to become more accommodative if they choose to, and outside the potential economic impacts due to rising trade frictions. After nine 25 basis point increases in the fed funds target rate since December 2015, investors are seriously questioning whether the tightening cycle has finally reached its end. With that said, we believe it is too early to say definitively if the Fed is ready to start a new easing cycle, but markets are certainly starting to bake in this assumption based on recent equity performance. Along with the ebb and flow in trade headlines over the coming weeks, investors should expect increased market volatility as the “will they or won’t they?” debate builds more momentum.
• Since market expectations are now high that the Federal Reserve is on the cusp of cutting interest rates next month, we thought it would be appropriate to look at how stocks perform heading into and shortly following an initial fed funds rate cut. Below are some points to consider if/when the Federal Reserve decides to shift its focus from hiking rates to cutting rates:
  
  1. The last five times the Federal Reserve has lowered interest rates, on average, stock prices have moved higher six months before and six months after an initial reduction in the fed funds target rate, according to Bespoke Investment Group. However, the sample size is small, and the variability in S&P 500 Index performance over each individual period (6/5/89, 7/6/95, 9/29/98, 1/3/01, and 9/18/07) varies materially. As an example, six months leading up to the first fed funds rate cut in 1989, the S&P 500 gained roughly 17% and nearly 9% six months following the cut. But in 2001, the Index fell 7.5% six months before the first fed funds rate cut and declined over 8.0% six months after the initial cut.
  
  2. As the embedded FactSet chart helps identify, in periods where the Federal Reserve cut interest rates and the economy did not slow into a recession (highlighted with red ovals), the S&P 500 performed well shortly before and after the rate cuts. However, after the Fed initially cut its fed funds target rate in 2001 and 2007, stock prices struggled. This is because the rate cuts did not hold off a recession in those two periods and economic growth and corporate fundamentals deteriorated.
  
  3. According to an analysis done by Goldman Sachs, in the thirteen occasions since 1988 that the futures market priced in a cut in the fed funds rate the day before a scheduled meeting, the FOMC cut rates in all thirteen instances. Further, during the last thirty years where the futures market discounted an interest rate cut thirty days prior to a scheduled FOMC meeting, the Fed almost always cut rates. February 1990 and February 1992 stand as the two occasions futures markets unwound lower rate expectations before the scheduled meetings. Bottom line: If market expectations continue to discount lower interest rates by the July FOMC meeting, there is a strong historical precedent to support the Fed would cut rates. Although futures markets still have time to adjust their rate views before the July meeting, a self-fulling prophecy could develop the longer markets expect a rate cut.

• In our view, the most important takeaway for investors to keep in mind when it comes to shifting rate expectations are as follows:
  
  1. The longer the market expects the Fed to shift to an easing policy, the more likely the policy shift becomes.
  
  2. While stock prices on average perform well shortly before and after an initial cut in the fed funds target rate, that performance is highly contingent on the economy not contracting materially or falling into a recession.
  
  3. As the chart above shows, while near-term performance in stock prices may be beholden to changes in monetary policy, over long periods of time, stocks move up and to the right — regardless where interest rates sit. Economic growth and corporate profits drive stock prices longer-term, and that’s something we should all keep in mind as market volatility has edged higher and uncertainty about where rates are headed has increased.

• Asia-Pacific: Asian equities finished lower on Thursday. According to Reuters, China Vice Premier Liu He said regulators in China should step up their support of the economy and maintain ample liquidity in the financial system. Some see Liu’s recent comments as a preamble for more stimulus support in the economy and a means to support economic growth amid rising trade tensions with the U.S. Liu added that Beijing has several tools capable of dealing with various challenges and local economists believe the People’s Bank of China (PBoC) could soon ease monetary policy and credit supply.

• Europe: Markets across the region are trading in the green at mid-day. Conservative members of parliament (MPs) will vote in the first round of the leadership contest today, which will decide who replaces Prime Minister Theresa May. Candidates must receive at least 17 votes or face elimination. The candidate with the lowest votes will exit the contest. Further ballots will be cast next week (slated to begin on Tuesday) to reduce the number of candidates down to two MPs, which will face a runoff vote from Conservative party members. Frontrunner Boris Johnson reaffirmed his pledge to remove the UK from the European Union (EU) on October 31st with or without a deal.

• U.S.: Equity futures are pointing to a higher open this morning. Month-to-date, Materials, Information Technology, and Consumer Staples are leading U.S. markets higher. Communication Services, Real Estate, and Utilities are all underperforming the S&P 500 in June. Since May, sector performance has been volatile, but overall market volatility has dipped near its one-year average. With the S&P 500 just 2.5% off its all-time high, sector performance more
erratic, and the potential for very binary reactions to a few uncertain macro events, investors should refrain from being over/underexposed to any one sector area today.

- Oil prices are up over 4.0% today on reports that two oil tankers were damaged near the Strait of Hormuz. The U.S. Navy’s Fifth Fleet said one of the ship’s operators described the incident as a suspected attack. This most recent incident in the Gulf of Oman near the Iranian coastline follows the sabotage of four vessels last month, which included two Saudi oil tankers. On May 29th U.S. national security advisor John Bolton said naval mines were most likely used in the previous tanker attacks off the United Arab Emirates last month. Bolton also warned Iran against conducting future attacks using naval mines. Although it’s still unclear what caused the recent tanker incidents, U.S. Naval ships are in the area and assisting the damaged ships. The ramp in oil tanker issues comes following mounting tensions between the U.S. and Iran.

- In addition to our headline comments on the Federal Reserve and market implications for easing monetary conditions, more economists now expect the Fed to cut rates this year. According to a recent Reuters poll of economists, 40 out of 100 respondents currently believe the Fed will cut rates by 25 basis points at least once this year – up from 8 last month. Although most respondents still believe the Fed will remain on hold this year, the dramatic shift in the number of economists that believe the central bank will cut rates is notable. However, The Wall Street Journal highlighted there are very few warning signs of a recession outside of an inverted yield curve on the short end. Pressure from the White House, soft inflation trends, and trade headwinds that are difficult to predict all complicate the Fed’s forward guidance strategy. But as the article noted, and we support, if a full-blown trade war looks like it’s going to develop with China, the Fed should cut rates and brush off any criticism it receives on placating President Trump.

**WORLD CAPITAL MARKETS**

*(all data as of approximately 8:00 AM ET)*

<table>
<thead>
<tr>
<th>Americas</th>
<th>% chg.</th>
<th>% YTD</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>S&amp;P 500</td>
<td>-0.20%</td>
<td>15.98%</td>
<td>2,879.8</td>
</tr>
<tr>
<td>Dow Jones</td>
<td>-0.17%</td>
<td>12.77%</td>
<td>26,004.8</td>
</tr>
<tr>
<td>NASDAQ</td>
<td>-0.38%</td>
<td>18.07%</td>
<td>7,792.7</td>
</tr>
<tr>
<td>Russell 2000</td>
<td>0.05%</td>
<td>13.37%</td>
<td>1,519.8</td>
</tr>
<tr>
<td>Brazil Bovespa</td>
<td>-0.65%</td>
<td>11.87%</td>
<td>9,832.0</td>
</tr>
<tr>
<td>S&amp;P/TSX Comp. (Canada)</td>
<td>-0.13%</td>
<td>14.86%</td>
<td>16,227.2</td>
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<tr>
<td>Mexico IPC</td>
<td>0.20%</td>
<td>17.17%</td>
<td>43,800.2</td>
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<tr>
<td>MSCI EAFE</td>
<td>-0.36%</td>
<td>12.27%</td>
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<thead>
<tr>
<th>Global % chg.</th>
<th>% YTD</th>
<th>Value</th>
</tr>
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<tbody>
<tr>
<td>MSCI All-Country World Index</td>
<td>-0.28%</td>
<td>14.02%</td>
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<table>
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<tr>
<th>Equity Income Indices</th>
<th>% chg.</th>
<th>% YTD</th>
<th>Value</th>
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<tr>
<td>JPM Alerian MLP Index</td>
<td>0.00%</td>
<td>11.01%</td>
<td>24.7</td>
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<tr>
<td>FTSE NAREIT Comp.</td>
<td>0.38%</td>
<td>20.75%</td>
<td>20,404.0</td>
</tr>
<tr>
<td>DJ US Select Dividend</td>
<td>0.00%</td>
<td>10.75%</td>
<td>2,060.5</td>
</tr>
<tr>
<td>DJ Global Select Dividend</td>
<td>-0.49%</td>
<td>3.61%</td>
<td>214.2</td>
</tr>
<tr>
<td>S&amp;P Div. Aristocrats</td>
<td>0.18%</td>
<td>14.32%</td>
<td>2,742.7</td>
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<th>Bond Indices</th>
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<th>% YTD</th>
<th>Value</th>
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<tbody>
<tr>
<td>Barclays US Agg. Bond</td>
<td>0.06%</td>
<td>5.03%</td>
<td>2,149.6</td>
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<tr>
<td>Barclays HY Bond</td>
<td>-0.05%</td>
<td>8.84%</td>
<td>2,078.2</td>
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<table>
<thead>
<tr>
<th>Equity Indices</th>
<th>% chg.</th>
<th>% YTD</th>
<th>Value</th>
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<tbody>
<tr>
<td>CRB Raw Industrials</td>
<td>0.09%</td>
<td>4.61%</td>
<td>1,458.2</td>
</tr>
<tr>
<td>NYMEX WTI Crude (per bbl.)</td>
<td>4.11%</td>
<td>17.24%</td>
<td>52.3</td>
</tr>
<tr>
<td>ICE Brent Crude (per bbl.)</td>
<td>4.12%</td>
<td>16.06%</td>
<td>62.4</td>
</tr>
<tr>
<td>NYMEX Nat Gas (MMBtu)</td>
<td>-0.71%</td>
<td>19.42%</td>
<td>2.4</td>
</tr>
<tr>
<td>Spot Gold (troy oz.)</td>
<td>0.20%</td>
<td>4.19%</td>
<td>1,386.2</td>
</tr>
<tr>
<td>Spot Silver (troy oz.)</td>
<td>0.28%</td>
<td>4.51%</td>
<td>14.8</td>
</tr>
<tr>
<td>LME Copper (per ton)</td>
<td>-0.59%</td>
<td>2.12%</td>
<td>5,823.0</td>
</tr>
<tr>
<td>LME Aluminum (per ton)</td>
<td>0.64%</td>
<td>5.54%</td>
<td>1,759.5</td>
</tr>
<tr>
<td>CBOT Corn (cent/lb/bushel)</td>
<td>0.84%</td>
<td>17.77%</td>
<td>452.3</td>
</tr>
<tr>
<td>CBOT Wheat (cents/lb/bushel)</td>
<td>0.48%</td>
<td>1.98%</td>
<td>528.8</td>
</tr>
<tr>
<td>Japanese Yen (¥/$)</td>
<td>0.04%</td>
<td>1.13%</td>
<td>108.46</td>
</tr>
<tr>
<td>Australian Dollar (A$/$)</td>
<td>-0.19%</td>
<td>-1.90%</td>
<td>0.69</td>
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<table>
<thead>
<tr>
<th>Commodity Sectors</th>
<th>% chg.</th>
<th>% YTD</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Consumer Discretionary</td>
<td>-0.11%</td>
<td>19.21%</td>
<td>925.3</td>
</tr>
<tr>
<td>Consumer Staples</td>
<td>0.04%</td>
<td>16.75%</td>
<td>602.0</td>
</tr>
<tr>
<td>Energy</td>
<td>-1.44%</td>
<td>6.87%</td>
<td>445.3</td>
</tr>
<tr>
<td>Financials</td>
<td>-0.95%</td>
<td>14.45%</td>
<td>448.3</td>
</tr>
<tr>
<td>Real Estate</td>
<td>0.26%</td>
<td>21.74%</td>
<td>231.3</td>
</tr>
<tr>
<td>Health Care</td>
<td>0.51%</td>
<td>6.34%</td>
<td>1,056.6</td>
</tr>
<tr>
<td>Industrials</td>
<td>0.20%</td>
<td>17.65%</td>
<td>632.0</td>
</tr>
<tr>
<td>Materials</td>
<td>0.31%</td>
<td>15.03%</td>
<td>360.6</td>
</tr>
<tr>
<td>Technology</td>
<td>-0.58%</td>
<td>23.99%</td>
<td>1,339.3</td>
</tr>
<tr>
<td>Communication Services</td>
<td>-0.28%</td>
<td>15.11%</td>
<td>158.8</td>
</tr>
<tr>
<td>Utilities</td>
<td>1.33%</td>
<td>14.45%</td>
<td>302.5</td>
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<table>
<thead>
<tr>
<th>Foreign Exchange (Intra-day)</th>
<th>% chg.</th>
<th>% YTD</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Euro ($/€)</td>
<td>0.0%</td>
<td>-1.6%</td>
<td>1.33</td>
</tr>
<tr>
<td>British Pound (£/$)</td>
<td>0.0%</td>
<td>-0.5%</td>
<td>1.27</td>
</tr>
</tbody>
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<table>
<thead>
<tr>
<th>Exchange Rates</th>
<th>% chg.</th>
<th>% YTD</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Canadian Dollar ($/C$)</td>
<td>0.2%</td>
<td>2.4%</td>
<td>1.33</td>
</tr>
<tr>
<td>Swiss Franc (SFr/US$)</td>
<td>0.3%</td>
<td>-1.1%</td>
<td>0.99</td>
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**Note:** International market returns shown on a local currency basis. **Equity index data is total return, inclusive of dividends.**
BY THE NUMBERS: ECONOMIC ACTUALS AND FORECAST:

Current Projections:

<table>
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<tr>
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</thead>
<tbody>
<tr>
<td>Real GDP (YOY)</td>
<td>2.5%</td>
<td>2.9%</td>
<td>1.6%</td>
<td>2.2%</td>
<td>2.9%</td>
<td>2.2%</td>
<td>1.6%</td>
</tr>
<tr>
<td>Unemployment Rate</td>
<td>5.6%</td>
<td>5.0%</td>
<td>4.7%</td>
<td>4.1%</td>
<td>3.9%</td>
<td>3.6%</td>
<td>3.5%</td>
</tr>
<tr>
<td>CPI (YoY)</td>
<td>1.6%</td>
<td>0.1%</td>
<td>1.3%</td>
<td>2.1%</td>
<td>2.4%</td>
<td>2.0%</td>
<td>2.2%</td>
</tr>
<tr>
<td>Core PCE (YoY)</td>
<td>1.6%</td>
<td>1.3%</td>
<td>1.7%</td>
<td>1.6%</td>
<td>1.9%</td>
<td>1.8%</td>
<td>2.0%</td>
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Sources: Historical data via FactSet. Estimates (Est.) via American Enterprise Investment Services, Inc.

ECONOMIC NEWS OUT TODAY:


<table>
<thead>
<tr>
<th>Time</th>
<th>Period</th>
<th>Release</th>
<th>Consensus Est.</th>
<th>Actual</th>
<th>Prior</th>
<th>Revised to</th>
</tr>
</thead>
<tbody>
<tr>
<td>8:30 AM</td>
<td>Jun 8</td>
<td>Initial Jobless Claims</td>
<td>215k</td>
<td>222k</td>
<td>218k</td>
<td>219k</td>
</tr>
<tr>
<td>8:30 AM</td>
<td>Jun 8</td>
<td>Continuing Claims</td>
<td>1600k</td>
<td>1695k</td>
<td>1682k</td>
<td></td>
</tr>
<tr>
<td>8:30 AM</td>
<td>MAY</td>
<td>Import Price Index (MoM)</td>
<td>-0.2%</td>
<td>-0.3%</td>
<td>16.6</td>
<td></td>
</tr>
<tr>
<td>8:30 AM</td>
<td>MAY</td>
<td>Import Price Index (YoY)</td>
<td>-1.3%</td>
<td>-1.5%</td>
<td>+0.2%</td>
<td></td>
</tr>
</tbody>
</table>
Economic Perspective:  Russell T. Price, CFA – Chief Economist

• Import prices were down 1.5% year-over-year in the month of May. Most of the decline has come from lower commodity prices as trade disputes offer a concern about economic growth prospects, combined with the influence of a stronger U.S. dollar. We note that import prices are measured before any taxes, tariffs or duties (which are each basically the same thing) are imposed. The price of imports from China were 1.4% lower year-over-year which would have easily been accounted for by a decline in the value of the Chinese Yuan (offshore) versus the U.S. dollar over the period.

• Consumers hang tough. May was a tough month for financial markets and, of course, the trade outlook. Consumers seemed to take it all in stride, however, and tomorrow’s retail sales report is expected to show a solid month (with a stress on “expected”).

• But one key factor of the retail sales report we already know was pretty good, and a good indication of consumer confidence overall: new auto sales.

• The Bureau of Economic Analysis (part of the Commerce Department) previously estimated new auto sales to have bounced back in May to a seasonally adjusted, annualized rate 17.3 million units, versus the 16.4 million posted in April. Sales were also heavily skewed toward light trucks and SUV’s (accounting for an estimated 72% of total sales in the month), vehicles which carry higher average price tags than cars, thus the dollar value of retail sales is likely to get a nice boost from this aspect, as well.

• As seen in the chart at right, the expanding share of the market going to light trucks and SUVs is historic. A data point that simply speaks for itself. The chart is sourced from American Enterprise Investment Services, Inc, based on data from the National Automobile Dealers Association.

FIXED INCOME NEWS & VIEWS:  Brian M. Erickson, CFA, Fixed Income Research & Strategy

Trading today:

• Treasury yields are trading roughly a basis point lower across the curve this morning after two tankers suffered damage just outside the Strait of Hormuz. New York Merc WTI crude futures rose +1.90 to 53.05 in trading ahead of the open this morning.

Is the Fed the Key to What Ails Markets Today?

• Fed futures markets priced in 67 basis point of Fed rate cuts by year end as of this morning; the equivalent of two to three cuts. Even the upcoming policy meeting scheduled to wrap up on June 19 is associated with a 19% chance of a quarter point cut based on Bloomberg calculations. In some camps, prospects for rate cuts are a foregone conclusion. A swift about face by Chair Powell from a path of successive rate hikes at the November 2018 policy meeting to the about-face this past January emboldened markets to lead the way for Fed policy.

• Why are markets nervous? Slow growth in China and Europe kicked off the sour market tone late last year. Can the Fed help those dynamics? Fed policy directly targets financial conditions and economic activity here in the U.S. The latest wall of worry domestically comes from President Trump’s propensity for employing trade as a poker in foreign policy by adding a tariff against Mexico because of immigration and flogging China with trade tariffs. We do not see Fed policy as the right tool for off-setting trade uncertainty. The right tool would be a fiscal plan to counter economic impacts driven by uncertainties. On the margin, the Fed could serve as a surrogate coach guiding markets to be patient since there is not a more holistic plan in place to bolster the U.S. negotiating position as it attempts to rebalance trade inequalities with China. Is that their role? It’s not in our view. But, absent other U.S. leaders willing to act, the Fed may be drawn in.

• We anticipate the Fed to remain on hold next week, and to adapt language in the policy statement around potential economic risks. Chair Powell has already muted the spotlight on inflation by suggesting that forces depressing...
inflation were transient in his view in the press conference following the May policy meeting. The decline in crude prices over the past four weeks may also prove a transient influence weighing on inflation over the next few months. This likely focuses the Fed on labor markets, with unemployment near record lows and credit conditions where corporate yields are steady to lower relative to last summer. Activity indicators, on the other hand softened in recent months, suggesting the potential for knock-on impacts on business and consumer sentiment may lie ahead. We see the press conference following the meeting as the critical time for Chair Powell to parse through the data; separating the meaningful data points from the static. In addition, we anticipate the Fed reiterates its mantra of data dependence; meaning they are unlikely to act in advance of data, rather in response to data. Based on what is currently priced into markets, we see greater risk of a surprise around a less responsive Fed than a more responsive Fed than is currently priced into fed futures.

• There are many factors that divide equity and fixed income investors. One has been the tendency for firms to borrow to pay one-time dividends in recent years. The positive for stocks, has left higher leverage for creditors to manage with no improvement in cashflow or business prospects. Thus, the move is a net negative for bonds. From a credit perspective, bond markets count on the Fed to stick to its mandate, and pragmatically tighten rates at the appropriate time and to cut rates at the appropriate time. Using monetary policy tools when other levers should be used, may leave the Fed and the economy in a more precarious position down the road.

• Maybe a preemptive Fed would be a good idea. Certainly, equity markets would welcome the support. From a bond perspective, we would regard using up limited monetary policy tools preemptively as increasing the risk that the Fed was less prepared when the market fundamentally required Fed stimulus. Recall, the Fed cut rates by more than 500 basis points in the most recent rate cut cycle and today the Fed only has 2.25% to but before the bottom of the target range stands at zero. The Fed has other policy tools as well, but none as tested and proven to be as effective as the Fed policy rate in our view.

• We anticipate the Fed may begin shaping how markets should anticipate Fed rate cuts if they were to take shape in coming months. So far market speculation is for a string of quarter point cuts or potentially a 50 basis point cut to start off the process. If the measured pace of hikes are any indication, a preemptive Fed would likely cut 25 basis points and guide toward potential cuts in the future. Bond markets may read a 50 basis point cut as the Fed responding to imminent recession risk that could shake investor confidence; providing a negative impulse rather than a positive one.

• Conclusion: We believe there are better tools to achieve what market are looking for than Fed policy. A tool, yes, but for a different problem. Without a defined approach for trade beyond the short-term, business investment may soften and the Fed may need to act in response to weaker data.

• Given implied market levels based on fed futures and a sagging belly of the Treasury curve, we believe Treasury markets are fully priced for aggressive Fed cuts. We remain persistent in our thinking that markets are ahead of themselves, suggesting Chairman Powell’s comments are likely to guide to a more rationale outcome echoing the Fed’s mantra of “patience” and ‘data dependency’. This may cause investors to parse the Treasury rally between what it means for rates and the portion of the rally simply driven by the influence from the global yield context.

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Before The Bell

Ameriprise Investment Research Group

Ameriprise Financial
1441 West Long Lake Road, Suite 250, Troy, MI 48098
investment.research.group@ampf.com
For additional information or to locate your nearest branch office, visit ameriprise.com

RESEARCH & DUE DILIGENCE LEADER
Lyle B. Schonberger - Vice President

Business Unit Compliance Liaison (BUCL)
Open – Sr Manager
Jeff Carlson, CLU, ChFC – Manager

Investment Research Coordinator
Kimberly K. Shores

Sr Administrative Assistant
Jillian Willis

EQUITY RESEARCH

Equity Research Director
Justin H. Burgin – Vice President

Consumer Goods and Services
Patrick S. Diedrickson, CFA – Director

Energy/Utilities
William Foley, ASIP – Director

Financial Services/REITs
Lori Wilking-Przekop – Sr Director

Health Care
Daniel Garofalo – Director

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Parveen Vedi – Sr Research Associate
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