Citizens Market Update

July 9, 2024

- CPI was unchanged on a seasonally adjusted basis in May, after rising 0.3% in April. Over the last 12 months, the all items index increased by 3.3% before seasonal adjustment. More than offsetting a 2.0% decline in the energy index, housing prices continues to put upward pressure on inflation by rising 0.4% for the fourth consecutive month. Core CPI rose by 0.2% in May and 3.4% in over the past 12 months. Shelter, the largest spending category for the average household, is by far the largest component of Core CPI and rose by 5.4% over the past 12 months (accounting for over two thirds of the total 12-month increase of Core CPI).
- Total nonfarm payroll employment increased by 206,000 in June and the unemployment rate increased to 4.1% with 6.8 million unemployed persons – these numbers are higher than a year earlier when the unemployment rate was 3.6% and the number of unemployed persons were 6.0 million and is the highest rate since October 2021. The labor force participation rate remains little changed at 62.6% and has held fairly constant over the past 12 months.
- The Fed left its benchmark rate unchanged at its June 2024 meeting after raising it 11 times since March 2022 to the current range of 5.25%-5.50%. The market is currently expecting the first of the potential two cuts this year to occur in September or November, but economic data will drive the timing and number of cuts this year. The Fed is balancing its campaign against elevated inflation with ensuring the economy does not slip into a recession.
- The Fed has indicated it will slow the process of letting its balance sheet roll-off, which has seen approximately $1.5 trillion of bonds roll off to a current level of approximately $7.4 trillion. Since fall 2022, the Fed had been allowing up to $60 billion per month in Treasuries and $35 billion per month in mortgage bonds to expire and not be replaced. Now, the Fed will lower the monthly cap on Treasuries roll-off, to $25 billion from $60 billion, while keeping the cap for mortgage-backed securities unchanged at $35 billion. With principal payments of agency securities currently running at about $15 billion per month, the total portfolio runoff will be about $40 billion per month.
- The Fed is projecting inflation to steadily cool, while the labor market remains historically strong, personal consumption remains high, and energy prices have recently increased. We expect GDP to increase 2.1% this year and 1.6% in 2025.
- While we believe the U.S. economy will slow this year, we do not believe that the slowdown is going to be enough to bring economic growth to negative territory for two consecutive quarters, or a technical recession.
- Two of the reasons for a "soft landing" is resiliency in the housing market and continued non-residential investment. The lack of supply of homes, especially in the existing homes market has increased real residential construction and new homes construction as well as sales is going to continue to keep real residential investment in positive territory. The impacts from

Fed rate increases were neutralized by the effects of the CHIPS Act and Inflation Reduction Act, which increased the construction of manufacturing plants in the U.S.

- The yield curve remains inverted with the spread between the 3-month and 10-year Treasury at approximately 1.09% and the spread between the 2-year and 10-year Treasury at approximately 0.33%. Since the beginning of the year, the 1-year UST has increased from 4.80% to 5.00%, the 2-year UST has increased from 4.33% to 4.62%, the 5-year UST has increased from 3.93% to 4.23% and the 10-year UST has increased from 3.95% to 4.28%.

U.S. Treasury Rates						
	1-Year	2-Year	3-Year	5-Year	10-Year	2-10 Yr Spread
Current (7/5)	**5.01**	**4.61**	**4.40**	**4.23**	**4.28**	**(0.33)**
Beginning of 2024 (1/2)	4.80	4.33	4.09	3.93	3.95	(0.38)
1-Yr Prior	5.44	4.99	4.68	4.37	4.05	(0.94)
2-Yrs Prior	2.82	2.97	2.99	2.96	2.93	(0.04)
3-Yrs Prior	0.07	0.22	0.42	0.81	1.37	1.15
5-Yrs Prior	1.96	1.84	1.81	1.86	2.12	0.28
5-Yr Average	2.35	2.28	2.25	2.28	2.46	0.19
10-Yr Average	1.75	1.83	1.92	2.09	2.39	0.57
Current as % Above / Below 5-Yr Average	114%	103%	95%	85%	74%	-278%
Current as % Above / Below 10-Yr Average	186%	152%	130%	102%	79%	-158%

- The current unrealized losses in the portfolio has continued to decrease and is still negative, however, these values are non-economic and non-cash as these negative values pull to par as the securities mature. Our portfolio duration is much shorter today than it was a year ago, so the evaporation pace will increase.

- Lastly, our income return is stable and historically high interest rates are economically beneficial as they lead to higher interest income. Currently, the book yield for the portfolio is 3.22% and $4.25 billion (approximately 42% of the portfolio) will mature over the next 12 months.

- The reinsurance markets are stable but are capacity constrained with pricing flat to +/- 5%.