Cash decay

August 2023

Stuck in cash? History suggests opportunity

KEY TAKEAWAYS

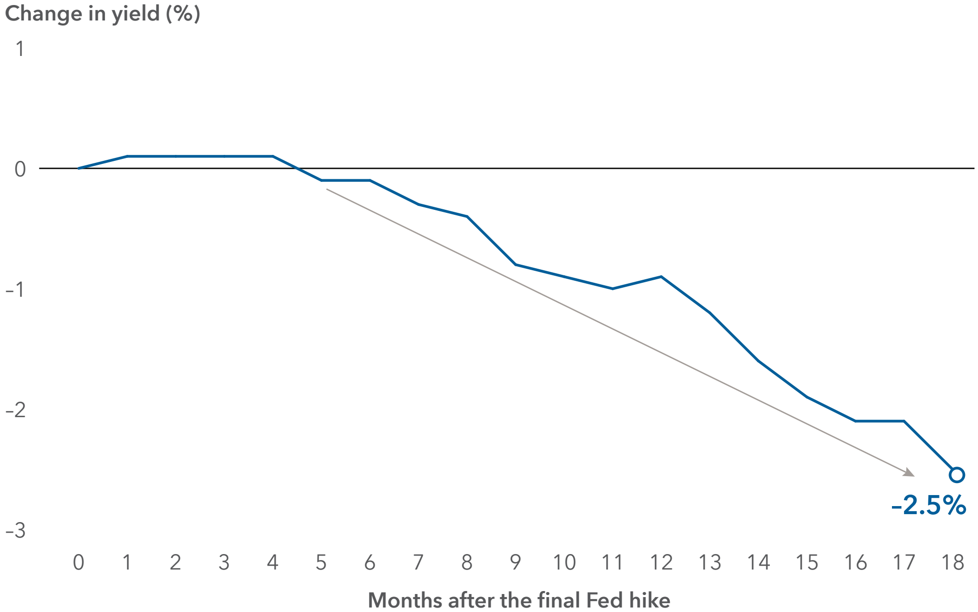
1. **Yields of cash-like instruments have decayed quickly** following the last Fed hike
2. **Equity and fixed income sharply outpaced cash** after the Fed finished hiking

1 **Yields of cash-like instruments have decayed quickly** following the last Fed hike

As the Federal Reserve approaches the end of its historic rate hiking cycle, cash yields, as represented by the U.S. 3-month Treasury bill (T-bill) yield, have risen to their highest level in 22 years. Elevated cash rates are meant to slow economic growth. As a result, those cash rates haven't remained elevated for long.

- Over the last four rate hike cycles, U.S. 3-month T-bill rates were an average of 2.5% lower 18 months after the last Fed hike.
- Similarly, markets are currently pricing in five 25 basis points (bps) interest rate cuts in 2024.

U.S. 3-month T-bill yields declined sharply following the Fed's final hike in the last four cycles



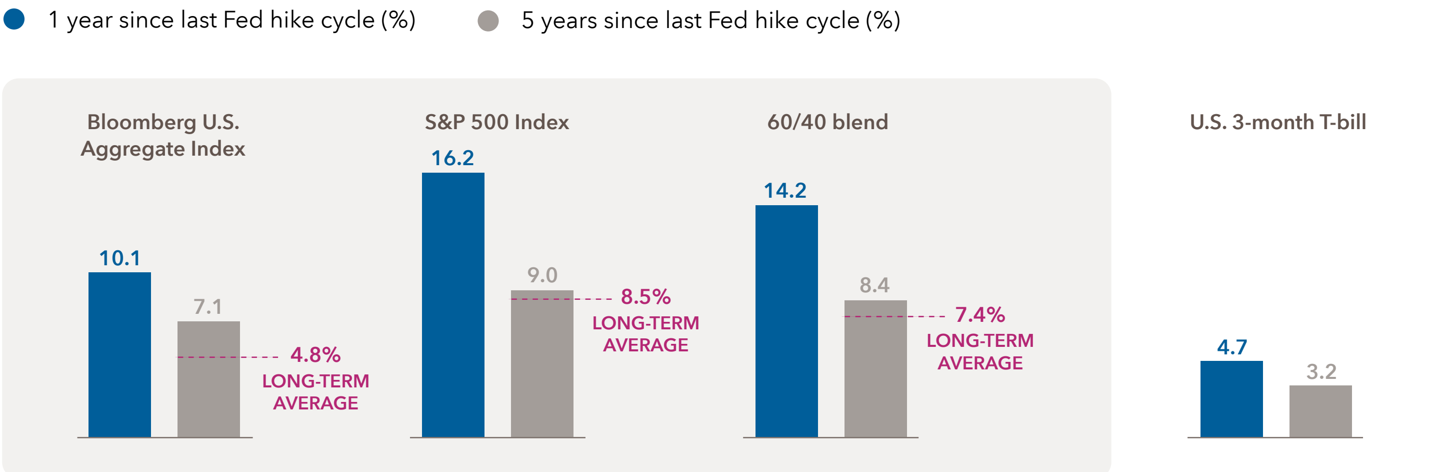
Sources: Bloomberg, Federal Reserve. As of 6/30/23. Chart represents the average decline in 3-month T-bills starting in the month of the last Fed hike in the last four transition cycles from 1995 to 2018.

❷ **Equity and fixed income sharply outpaced cash** after the Fed finished hiking

The end of an interest rate hiking cycle has presented a strong opportunity for investors to redeploy cash. Because change happens quickly, investors attempting to time the market could be left with weaker returns.

- Even in early months following the Fed's final hike, equities and fixed income outpaced cash-like instruments. Their advantage persisted over time.*
- Stocks, bonds and a blended hypothetical 60/40 portfolio (60% stocks, 40% bonds) sharply outpaced U.S. 3-month T-bill returns in the first year after the last Fed hike.
- In the 5-year periods that followed the final hike, annualized returns also exceeded long-term average returns for these asset classes.

After Fed hikes ended, long-term results outpaced cash, with the first year contributing most



Sources: Capital Group, Morningstar. Chart represents the average returns across respective sector proxies in a forward extending window starting in the month of the last Fed hike in the last four transition cycles from 1995 to 2018 with data through 6/30/23. The 60/40 blend represents 60% S&P 500 Index and 40% Bloomberg U.S. Aggregate Index. Long-term averages represented by the average 5-year annualized rolling returns from 1995.

Past results are not predictive of results in future periods.

* For three-month periods following the final hike, cumulative bond and stock returns outpaced 3-month T-bills by 3.1% and 2.1% and for six-month periods by 4.2% and 5.6% on average, respectively.

Unlike stocks and non-U.S. government bonds, investments in U.S. Treasuries are guaranteed by the U.S. government as to the payment of principal and interest.

The indexes are unmanaged and, therefore, have no expenses. Investors cannot invest directly in an index.

Bloomberg U.S. Aggregate Index represents the U.S. investment-grade fixed-rate bond market.

S&P 500 Index is a market capitalization-weighted index based on the results of approximately 500 widely held common stocks. This index is unmanaged, and its results include reinvested dividends and/or distributions but do not reflect the effect of sales charges, commissions, account fees, expenses or U.S. federal income taxes.

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