

## Summer Boom Meets COVID Concerns

### WATCH LIST

| Date                |  | Period | Consensus  |   | Previous   |
|---------------------|--|--------|------------|---|------------|
| <b>U.S.</b>         |  |        |            |   |            |
| Mon 7/26            | New Home Sales                                       | Jun    | 800 K      | ▲ | 769 K      |
| Tue 7/27            | FHFA House Price Index                               | May    |            |   | 1.8% M/M   |
| Tue 7/27            | Conference Board Consumer Confidence                 | Jul    | 124.0      | ▼ | 127.3      |
| Wed 7/28            | FOMC Monetary Policy Meeting                         | Jul    | 0.0%-0.25% | ▬ | 0.0%-0.25% |
| Thu 7/29            | GDP, annualized (Advance Estimate)                   | 2Q21   | 8.2% Q/Q   | ▲ | 6.4% Q/Q   |
| Thu 7/29            | Pending Home Sales                                   | Jun    | 0.5% M/M   | ▼ | 8.0% M/M   |
| Fri 7/30            | Employment Cost Index                                | 2Q21   | 0.9% Q/Q   | ▬ | 0.9% Q/Q   |
| Fri 7/30            | Personal Income                                      | Jun    | -0.6% M/M  | ▲ | -2.0% M/M  |
| Fri 7/30            | Personal Spending                                    | Jun    | 0.6% M/M   | ▲ | 0.0% M/M   |
| Fri 7/30            | PCE Deflator   | Jun    | 4.1% Y/Y   | ▲ | 3.9% Y/Y   |
| <b>Europe</b>       |  |        |            |   |            |
| Wed 7/28            | Consumer Confidence (France, Germany, Italy)         | Jul    |            |   |            |
| Fri 7/30            | EZ Unemployment Rate                                 | Jun    | 7.9%       | ▬ | 7.9%       |
| Fri 7/30            | EZ Core CPI (Preliminary Estimate)                   | Jul    | 0.7% Y/Y   | ▼ | 0.9% Y/Y   |
| Fri 7/30            | EZ GDP (Advance Estimate)                            | 2Q21   | 13.3% Y/Y  | ▲ | -1.3% Y/Y  |
| <b>Asia Pacific</b> |  |        |            |   |            |
| Mon 7/26            | Jibun Bank Japan Mfg PMI (Preliminary Estimate)      | Jul    |            |   | 52.4       |
| Mon 7/26            | Jibun Bank Japan Services PMI (Preliminary Estimate) | Jul    |            |   | 48.0       |
| Tue 7/27            | China Industrial Profits                             | Jun    |            |   | 36.4% Y/Y  |
| Fri 7/30            | Japan Jobless Rate                                   | Jun    | 3.0%       | ▬ | 3.0%       |
| Fri 7/30            | Japan Industrial Production (Preliminary Estimate)   | Jun    | 5.0% M/M   | ▲ | -6.5% M/M  |
| Fri 7/30            | Japan Retail Sales                                   | Jun    | 2.7% M/M   | ▲ | -0.4% M/M  |
| Sat 7/31            | China Non-manufacturing PMI                          | Jul    |            |   | 53.5       |
| Sat 7/31            | China Manufacturing PMI                              | Jul    | 51.0       | ▲ | 50.9       |

Arrows indicate consensus forecast compared to the previous period. Local dates of release.

#### U.S.

- The **FOMC meeting next week** will get attention given the upward surprise in inflation, but we don't expect any change in signaling future plans for tapering asset purchases.
- The advance estimate of **Q2 GDP comes out July 29**, while the **Employment Cost Index** will show if wage pressures are increasing.

#### Europe

- We will watch **consumer and business confidence**, particularly given the proliferating Delta variant. Retail sales data in major economies will show consumers' strength this summer.
- The release of **Q2 GDP on July 30** should highlight the strength of Europe's rebound.

#### Asia Pacific

- **Japan activity data** should show a sequential bounce, with the industrial sector remaining robust given resilient exports. All eyes will also be on the **Tokyo Olympics**, which officially open July 23 amid rising cases.
- We'll see whether the spread of the Delta variant is affecting **China Non-Manufacturing PMI**.

#### What This Week Means For Markets

Technical factors, perceived Fed hawkishness, the Delta variant, and U.S. infrastructure talks led to a capricious week in markets. The U.S. 10-year treasury yield ends the week close to where it was last week, after an initial move lower. While markets continue pricing in a Fed policy mistake and slower longer-term growth, solid economic data this week, such as retail sales, supports our baseline outlook of strong growth. Near-term market volatility will likely remain amid COVID concerns, and until monetary policy is more clear this fall. If our outlook holds, expect a move to general risk-on with a cyclical tilt and higher yields. Please see our [Monthly Macro Dashboard](#).

## IN REVIEW

### COVID Concerns Rising

Fueled by the spreading Delta variant, daily cases are surging in Asia and the U.K., while the U.S. and euro area are experiencing increases as well. Hospitalizations remain subdued in economies with advanced vaccination rates, as the shots appear to be breaking the link between cases and deaths. However, there's concern this could change in the coming weeks.

There is little political appetite to reinstate restrictive measures in the U.S., where vaccinations have plateaued. In Europe, authorities are allowing the summer holiday season to continue, choosing to discriminate depending on vaccination status.

Considerable risks remain for countries with low-vaccine coverage, particularly in Southeast Asia, where herd immunity is not expected until mid- to late-next year. Watch for travel restrictions or reinstated lockdowns to help slow the spread.

### BOJ Unlikely to Hit its Inflation Target

The Bank of Japan concluded its July 16 policy meeting with no policy changes, though it did unveil its new green lending program to promote climate change investments. There was also a small upward surprise in its CPI forecast for fiscal year 2021, following continued improvement in economic activity and a gradual rise in medium- to long-term inflation expectations.

While it's unlikely the BOJ's 2% inflation target is reached anytime soon, June headline CPI increased 0.2% Y/Y and Core CPI declined 0.2% Y/Y after a government ruling to reduce mobile phone charges also lowered inflation, though that should dissipate soon; excluding this, core inflation grew 0.4% Y/Y. Energy and food costs drove price increases while durable goods and services have been sluggish.

A revival in activity as vaccinations progress should lift prices into next year. Firms' price-cutting behavior to spur demand is also unlikely to be observed widely as the decrease in demand is due to virus concerns. Still-elevated energy prices could provide a modest lift to prices.

### A Summer of Services Spending in the U.S.

Retail sales surprised to the upside in June, showing consumers are shifting spending patterns as the economy reopens. Retail sales rose 0.6% M/M, contrary to consensus expectations for a 0.3% M/M decline. Despite May data being revised lower, from -1.3% M/M to -1.7%, consumers are continuing an impressive spending pace. Even as fiscal support to consumers is fading, the reopening is encouraging further spending.

U.S. RETAIL SALES, M/M%



Source: Haver. As of July 22, 2021.

The mix shift is apparent in the data, which showed an increase in areas such as clothing and dining out. Spending on furniture and home furnishings, garden equipment, and sporting goods—which all increased during the pandemic—fell over the month. As retail sales largely covers spending on goods, next week's broader personal spending data will provide more insight into the pace of spending on services outside of dining at restaurants.

We expect the mix shift in consumption patterns to continue through summer. Despite easing of government transfer payments, spending is set to remain strong in the near-term amid the reopening, ample excess savings, easing lending standards to consumers, and labor market improvement.

### ECB Sees Strong Growth but Still Dovish on Rates

At its policy meeting this week, the ECB estimated risks to the outlook to be balanced, despite a resurgence of the virus. This is good news, with projected GDP growth of 4.6% this year, 4.7% in 2022, and 2.1% in 2023. Yet, the ECB sees inflation remaining below target beyond its forecast horizon, a three-year rolling period currently ending in 2023, when inflation is forecast at 1.4%—not a bad place to be at a macro level. The admitted inability of monetary policy to spur inflation to its target opens the door for more fiscal action.

The ECB's new forward guidance that translates its symmetric 2% inflation target into policy rule is as bold as it is clear, with three criteria determining when to raise rates; all three imply no rate hike until at least 2024. It will raise its policy rate when: (1) projected inflation reaches 2% well ahead of the end of the inflation horizon; (2) 2% inflation looks durable for the rest of the projection horizon, even if this takes transitory overshoots; and (3) the inflation dynamics are consistent with inflation stabilizing at 2% afterwards.

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## KEY FINANCIAL INDICATORS

| Rates  | Yield     | 1 W Change | 1M Change | 3M Change | 6M Change | 12M Change | YTD Change |
|--|-----------|------------|-----------|-----------|-----------|------------|------------|
| Fed Funds  | 0.25%     | 0 bps      | 0 bps     | 0 bps     | 0 bps     | 0 bps      | 0 bps      |
| U.S. SOFR  | 0.05%     | 0 bps      | 0 bps     | 4 bps     | 1 bps     | -6 bps     | -2 bps     |
| 3 Month USD Libor                                | 0.14%     | 1 bps      | 0 bps     | -4 bps    | -8 bps    | -12 bps    | -10 bps    |
| 3 Month Euribor                                  | -0.55%    | 0 bps      | 0 bps     | -1 bps    | 0 bps     | -9 bps     | 0 bps      |
| 3 Month U.S. T-Bill                              | 0.05%     | -1 bps     | 1 bps     | 3 bps     | -3 bps    | -7 bps     | -3 bps     |
| 2-Year U.S. Treasury                             | 0.21%     | -2 bps     | -4 bps    | 6 bps     | 8 bps     | 6 bps      | 9 bps      |
| 10-Year U.S. Treasury                            | 1.28%     | -7 bps     | -20 bps   | -28 bps   | 18 bps    | 68 bps     | 36 bps     |
| 10-Year German Bund                              | -0.41%    | -9 bps     | -24 bps   | -14 bps   | 9 bps     | 6 bps      | 17 bps     |
| 10-Year U.K. Gilt                                | 0.59%     | -5 bps     | -19 bps   | -14 bps   | 26 bps    | 45 bps     | 40 bps     |
| 10-Year JGB                                      | 0.01%     | -1 bps     | -4 bps    | -6 bps    | -2 bps    | 0 bps      | -2 bps     |
| Fixed Income                                     | Yield     | OAS        | 1W Return | 1M Return | 3M Return | 12M Return | YTD Return |
| Barclays Capital U.S. Government-Treasury        | 0.85%     | N/A        | 0.3%      | 1.2%      | 1.7%      | -2.7%      | -1.6%      |
| Barclays Capital U.S. TIPS                       | 0.98%     | N/A        | 0.1%      | 2.1%      | 3.5%      | 6.2%       | 3.0%       |
| Barclays Capital U.S. Aggregate                  | 1.42%     | 36         | 0.2%      | 1.0%      | 1.6%      | -0.6%      | -0.9%      |
| Barclays Capital Global Aggregate                | 1.03%     | 35         | 0.0%      | 0.6%      | 0.3%      | 1.6%       | -2.6%      |
| Barclays Capital U.S. ABS                        | 0.47%     | 25         | 0.0%      | 0.2%      | 0.3%      | 1.2%       | 0.3%       |
| Barclays Capital U.S. MBS                        | 1.70%     | 34         | 0.1%      | 0.6%      | 0.0%      | -0.2%      | -0.4%      |
| Barclays Capital U.S. Corporate Investment Grade | 1.98%     | 87         | 0.2%      | 1.3%      | 3.1%      | 1.4%       | -0.5%      |
| BAML Euro Corporate Investment Grade             | 0.20%     | 85         | 0.3%      | 0.8%      | 0.9%      | 3.2%       | 0.4%       |
| Barclays Capital U.S. Corporate High Yield       | 3.91%     | 293        | -0.2%     | 0.7%      | 2.1%      | 11.8%      | 3.8%       |
| BAML European Currency High Yield Non-Financial  | 2.68%     | 317        | 0.0%      | 0.1%      | 1.1%      | 9.8%       | 3.0%       |
| CS U.S. Leveraged Loans                          | 4.78%     | 446        | -0.1%     | 0.2%      | 1.1%      | 9.9%       | 3.5%       |
| CS Western European Leveraged Loans Non-USD      | 4.23%     | 413        | 0.1%      | 0.0%      | 0.9%      | 9.2%       | 3.0%       |
| JPM CEMBI Broad Diversified                      | 4.23%     | 311        | 0.1%      | 0.5%      | 1.9%      | 7.5%       | 1.6%       |
| JPM EMBI Global Diversified                      | 4.89%     | 353        | 0.2%      | 0.2%      | 2.2%      | 5.1%       | -0.3%      |
| JPM GBI-EM Global Diversified                    | 4.93%     | N/A        | -0.4%     | -0.9%     | -0.3%     | 2.8%       | -4.7%      |
| Equities   | Price     | Div Yield  | 1W Return | 1M Return | 3M Return | 12M Return | YTD Return |
| S&P 500  | 4,358.69  | 1.30%      | -0.3%     | 3.3%      | 4.8%      | 35.9%      | 17.0%      |
| Euro STOXX 600 (Local)                           | 453.97    | 2.75%      | -1.4%     | -0.3%     | 4.0%      | 20.5%      | 13.8%      |
| U.K. FTSE 100 (Local)                            | 6,998.28  | 3.04%      | -1.3%     | -0.9%     | 1.5%      | 11.6%      | 8.3%       |
| Japan Nikkei 225 (Local)                         | 27,548.00 | 1.58%      | -3.7%     | -1.7%     | -3.4%     | 20.4%      | 0.4%       |
| China Shanghai Composite (Local)                 | 3,562.66  | 2.00%      | 1.0%      | 0.9%      | 2.6%      | 7.3%       | 2.6%       |
| MSCI AC World (Local)                            | 719.78    | 1.71%      | -0.6%     | 2.4%      | 4.0%      | 30.9%      | 14.0%      |
| MSCI Emerging Markets (Local)                    | 1,312.15  | 2.05%      | -1.5%     | -2.2%     | -0.6%     | 21.3%      | 4.5%       |
| Commodities/Currencies                           | Price     | 1W Change  | 1M Change | 3M Change | 6M Change | 12M Change | YTD Change |
| S&P GS Commodity Index                           | 525.44    | -1.1%      | 0.0%      | 7.9%      | 21.2%     | 53.1%      | 28.3%      |
| WTI Crude (\$/bbl)                               | 70.30     | -3.8%      | -4.5%     | 14.6%     | 32.6%     | 68.3%      | 45.4%      |
| Copper (\$/lb)                                   | 4.28      | 0.1%       | 2.3%      | -0.1%     | 17.2%     | 45.6%      | 21.9%      |
| Gold (\$/oz)                                     | 1,802.15  | -1.2%      | 1.5%      | 0.2%      | -3.2%     | -2.2%      | -4.5%      |
| U.S. Dollar Index                                | 92.75     | 0.4%       | 0.9%      | 1.8%      | 2.9%      | -2.5%      | 3.1%       |
| Euro (USD/EUR)                                   | 1.18      | -0.3%      | -1.0%     | -2.0%     | -3.0%     | 2.6%       | -3.7%      |
| British Pound (USD/GBP)                          | 1.37      | -1.4%      | -1.7%     | -1.8%     | -0.4%     | 7.3%       | 0.0%       |
| Japanese Yen (Yen/USD)                           | 110.34    | 0.2%       | 0.1%      | 2.0%      | 6.5%      | 3.2%       | 6.9%       |
| Chinese Yuan (CNY/USD)                           | 6.47      | 0.0%       | 0.1%      | -0.3%     | 0.2%      | -7.4%      | -1.0%      |

Source: FactSet and Bloomberg. As of July 21, 2021.

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