

## Housing Trembles But The Foundation's Still Strong

### WATCH LIST

Date		Period	Consensus	Previous
<b>U.S.</b>				
Mon 5/30	Markets Closed for Memorial Day		--	--
Tue 5/31	FHFA House Price Index	Mar	2.1% M/M	2.1% M/M
Tue 5/31	Conference Board Consumer Confidence	May	103.9	107.3
Wed 6/1	ISM Manufacturing Index	May	55.0	55.4
Wed 6/1	JOLTS Job Openings	Apr		11549 K
Wed 6/1	Federal Reserve Beige Book		--	--
Wed 6/1	Wards Total Vehicle Sales	May	14.5 M	14.29 M
Thu 6/2	ADP Employment Change	May	302 K	247 K
Fri 6/3	Change in Nonfarm Payrolls	May	332 K	428 K
Fri 6/3	Unemployment Rate	May	3.5%	3.6%
Fri 6/3	ISM Services Index	May	57.0	57.1
<b>Europe</b>				
Tue 5/31	EA Consumer Price Index (Prelim. Est.)	May		7.5% Y/Y
Wed 6/1	EA Unemployment Rate	Apr		6.8%
Thu 6/2	EA Producer Price Index	Apr		36.8% Y/Y
Thu 6/2	Markets Closed for Spring Bank Holiday		--	--
Fri 6/3	Markets Closed for Platinum Jubilee Bank Holiday		--	--
Fri 6/3	EA Retail Sales	Apr		-0.4% M/M
<b>Asia Pacific</b>				
Tue 5/31	Japan Jobless Rate	Apr	2.6%	2.6%
Tue 5/31	Japan Retail Sales	Apr	0.3% M/M	2.0% M/M
Tue 5/31	Japan Industrial Production (Prelim. Est.)	Apr	-0.4% M/M	0.3% M/M
Tue 5/31	China Manufacturing PMI	May	48.9	47.4
Tue 5/31	China Non-manufacturing PMI	May	46.2	41.9
Wed 6/1	Caixin China Manufacturing PMI	May	49.6	46.0

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

#### U.S.

- We will watch the **May employment report**, which is expected to show a strong labor market, though the pace of job gains could ease as growth slows.
- The **ISM surveys** should show how higher input and output costs are impacting activity and firms.

#### Europe

- Military and economic responses to **Russia's war in Ukraine** remain at the top of the watch list as energy disruptions put added pressure on prices.
- EA inflation** is expected to stay at its record high, while we are also watching **EA employment data** to see if the labor market remains tight.

#### Asia Pacific

- Japan activity data** for April will reflect the extent of the rebound after restrictions were lifted in late-March.
- China PMIs** for May should show a slight improvement but remain in contractionary territory, amid mounting costs of the lockdowns.

#### What This Week Means For Markets

Market volatility is elevated given high uncertainty on the outlook. While hard economic data continues to show strong but normalizing growth, the Fed is looking for further tightening in financial conditions to help quell inflation. After disappointing last week, improved outlooks from a few major U.S. retailers combined with a less-hawkish tone from the FOMC led to some reprieve in equities. However, recession risks remain prominent for investors as PMIs, housing data, and China's economy all slow. Separately, rising expectations for ECB rate hikes helped reverse several weeks of continued dollar strength. We remain with our Stagflation Shock scenario, in which elevated inflation and tightening policy slow growth in the U.S. and lead to recession in the EA. Please see our latest [Macro Dashboard](#).

## IN REVIEW

### U.S. Housing Data Cooling, Not Collapsing

U.S. housing demand is cooling as the 30-year mortgage rate reached the highest level since 2009 and led the affordability index to decline. However, the housing market is not crashing, with housing starts and permits still well above pre-COVID levels. Homebuilders still face supply constraints and elongated production times, limiting supply. Expect demand to cool as the Fed raises rates, but prices are not expected to collapse given low supply and a possible increase in lending standards. We will watch the sector to see how tightening policy impacts demand.

### Global Flash PMIs Show Signs of Slowing

S&P Global flash PMIs show supply constraints and rising input prices still challenge businesses. Meanwhile, higher prices are starting to weigh on demand to varying degrees across the globe.

S&P GLOBAL PMIS

Region	Aug-21	Sep-21	Oct-21	Nov-21	Dec-21	Jan-22	Feb-22	Mar-22	Apr-22	May-22
U.S. Manufacturing	61.1	60.7	58.4	58.3	57.7	55.5	57.3	58.8	59.2	57.5
U.S. Services	55.1	54.9	58.7	58.0	57.6	51.2	56.5	58	55.6	53.5
EZ Manufacturing	61.4	58.6	58.3	58.4	58.0	58.7	58.2	56.5	55.5	54.4
EZ Services	59.0	56.4	54.6	55.9	53.1	51.1	55.5	55.6	57.7	56.3
UK Manufacturing	60.3	57.1	57.8	58.1	57.9	57.3	58	55.2	55.8	54.6
UK Services	55.0	55.4	59.1	58.5	53.6	54.1	60.5	62.6	58.9	51.8
Japan Manufacturing	52.7	51.5	53.2	54.5	54.3	55.4	52.7	54.1	53.5	53.2
Japan Services	42.9	47.8	50.7	53.0	52.1	47.6	44.2	49.4	50.7	51.7

Source: Bloomberg. As of May 26, 2022.

U.S. preliminary PMIs showed the economy expanding, but at a slower pace in May. Input costs for companies climbed to a record high, while output costs rose at the second-fastest recorded pace, down slightly from April. Higher prices are impacting demand, with new orders rising at the slowest pace since August 2020. Employment rose at an impressive clip across services and manufacturing sectors. Higher prices are keeping business confidence lower than earlier in the year, but continued sales growth and hopes that local supply chains will ease bottlenecks kept firms optimistic on output for the coming year. This supports our Stagflation Shock scenario, with higher prices and tightening policy weighing on demand and growth.

The **euro area** composite PMI fell to 54.9 in May (cons. 55.3) after increasing to 55.8 in April. Data points to robust growth despite supply disruptions, macro uncertainty, low consumer sentiment, and rising living costs. The services PMI fell to 56.3, below expectations, but still the strongest expansion in eight months. Manufacturing growth eased, and forward-looking components (such as new and export orders) fell below 50. Growth appears strong and inflation is high, which we think will lead the ECB to tighten policy. However, we expect growth will

slow following the reopening boom and summer tourist season, and, with tightening monetary policy, lead to a EA recession.

The **U.K.** composite PMI surprised sharply to the downside, registering 51.8 in May (cons. 56.5), down from 58.2 in April. This signals the slowest rise in business activity since the first COVID wave. New orders fell for the third-consecutive month, while input costs hit a record high. The U.K. services PMI fell to 51.8 from 58.9, with survey respondents noting client demand weakened due to economic and geopolitical uncertainty. Average costs rose to the highest level since the survey began in 1996. Expansion in manufacturing was the slowest since November. Even with a sizable VAT cut, the U.K. should see a sharp slowdown in growth with another hike in energy bills in August.

**Japan's** manufacturing PMI fell slightly to 51.4 in May, given the continued impact from the Russia-Ukraine war and lockdowns in China exacerbating supply chain disruptions, which saw supplier delivery times and backlogs lengthening. Services rebounded, rising to 51.7 amid economic reopenings.

### U.K. Retail Sales Decelerating, But Not Dropping Off

U.K. retail sales decreased 4.9% Y/Y in April, the biggest annual decrease since early 2021 (cons. -7.2%). Retail sales rose 1.4% M/M, above market expectations of -0.2%, rebounding from the previous month's decline. The increase came from food, alcohol and tobacco in supermarkets, clothing from non-store retailers and automotive fuel, while sales at non-food stores fell 0.6%.

### China Easing Welcome, But Downside Risks Remain

Authorities in China ramped up policy support measures to help shore up economic activity, which surprised to the downside in April. The PBOC on May 20 lowered the five-year loan prime rate (LPR) by 15 bps to 4.45%, the first cut since January and its largest ever. With the reduction of first-home mortgage rates, this should help support the property sector (mortgage rates are referenced against the five-year LPR) that saw new home price growth contract across 70-cities for the first time in six years. The State Council also announced new fiscal support measures to stabilize the labor market; the package included tax rebates and deferrals to the business sector, credit support for struggling small- and medium-size enterprises, auto purchase tax cuts to boost consumption, and additional infrastructure investment. While welcome, the magnitude of monetary and fiscal easing has been managed and much smaller compared to 2020. Authorities are unlikely to diverge from zero-COVID until after elections in fall and risks are firmly to the downside, leaving the 5.5% growth target in doubt. Authorities appear to be more concerned with social stability and employment than their growth target.

27 May 2022 | The Week Ahead

## KEY FINANCIAL INDICATORS

Rates	Yield	1 W Change	1M Change	3M Change	6M Change	12M Change	YTD Change
Fed Funds	1.00%	0 bps	50 bps	75 bps	75 bps	75 bps	75 bps
U.S. SOFR	0.78%	-1 bps	51 bps	73 bps	73 bps	77 bps	73 bps
3 Month USD Libor	1.55%	7 bps	33 bps	103 bps	137 bps	141 bps	134 bps
3 Month Euribor	-0.35%	2 bps	6 bps	18 bps	23 bps	19 bps	22 bps
3 Month U.S. T-Bill	1.06%	4 bps	24 bps	74 bps	100 bps	104 bps	101 bps
2-Year U.S. Treasury	2.50%	-19 bps	-14 bps	91 bps	186 bps	235 bps	177 bps
10-Year U.S. Treasury	2.75%	-14 bps	-8 bps	77 bps	111 bps	119 bps	124 bps
10-Year German Bund	0.96%	-8 bps	9 bps	74 bps	119 bps	112 bps	114 bps
10-Year U.K. Gilt	1.92%	6 bps	5 bps	47 bps	93 bps	113 bps	95 bps
10-Year JGB	0.21%	-4 bps	-4 bps	1 bps	13 bps	14 bps	14 bps
Fixed Income	Yield	OAS	1W Return	1M Return	3M Return	12M Return	YTD Return
Barclays Capital U.S. Government-Treasury	2.70%	N/A	1.0%	0.4%	-4.5%	-6.9%	-7.7%
Barclays Capital U.S. TIPS	2.96%	N/A	-0.1%	-1.3%	-3.2%	-1.6%	-6.0%
Barclays Capital U.S. Aggregate	3.31%	49	1.2%	0.5%	-4.8%	-7.9%	-8.6%
Barclays Capital Global Aggregate	2.51%	50	1.3%	-0.4%	-7.3%	-12.8%	-10.7%
Barclays Capital U.S. ABS	3.27%	79	0.3%	0.3%	-1.7%	-3.7%	-3.1%
Barclays Capital U.S. MBS	3.39%	35	1.2%	1.2%	-4.0%	-7.3%	-6.9%
Barclays Capital U.S. Corporate Investment Grade	4.21%	140	1.7%	-0.1%	-6.2%	-10.4%	-12.0%
BAML Euro Corporate Investment Grade	2.25%	168	0.0%	-1.3%	-5.1%	-8.8%	-8.7%
Barclays Capital U.S. Corporate High Yield	7.51%	460	1.4%	-2.5%	-6.1%	-7.0%	-9.8%
BAML European Currency High Yield Non-Financial	6.01%	527	-0.9%	-3.7%	-5.8%	-8.3%	-9.4%
CS U.S. Leveraged Loans	8.71%	590	-1.1%	-3.6%	-3.1%	-0.9%	-3.2%
JPM CEMBI Broad Diversified	6.46%	371	0.5%	-1.5%	-8.4%	-11.1%	-11.6%
JPM EMBI Global Diversified	7.58%	472	1.5%	-2.1%	-10.3%	-15.9%	-15.7%
JPM GBI-EM Global Diversified	6.76%	N/A	2.5%	-1.1%	-12.2%	-16.7%	-11.2%
Equities	Price	Div Yield	1W Return	1M Return	3M Return	12M Return	YTD Return
S&P 500	3,978.73	1.51%	1.4%	-7.2%	-8.9%	-3.6%	-16.0%
Euro STOXX 600 (Local)	434.31	2.40%	0.1%	-2.4%	-4.2%	-2.4%	-11.0%
U.K. FTSE 100 (Local)	7,522.75	3.45%	1.1%	1.9%	0.4%	7.0%	1.9%
Japan Nikkei 225 (Local)	26,677.80	2.07%	-0.9%	0.3%	0.8%	-6.6%	-7.3%
China Shanghai Composite (Local)	3,107.46	2.31%	0.7%	6.1%	-10.0%	-13.2%	-14.6%
MSCI AC World (Local)	629.97	2.21%	0.7%	-5.6%	-5.6%	-5.5%	-14.0%
MSCI Emerging Markets (Local)	1,019.59	2.93%	-1.6%	-4.0%	-11.7%	-17.9%	-13.8%
Commodities/Currencies	Price	1W Change	1M Change	3M Change	6M Change	12M Change	YTD Change
S&P GS Commodity Index	771.90	2.3%	6.2%	18.3%	32.9%	50.6%	37.5%
WTI Crude (\$/bbl)	110.33	0.6%	10.8%	20.3%	40.9%	66.5%	46.5%
Copper (\$/lb)	4.28	2.3%	-3.9%	-4.4%	-4.1%	-5.4%	-4.0%
Gold (\$/oz)	1,847.20	2.0%	-2.5%	-2.0%	3.7%	-2.1%	2.3%
U.S. Dollar Index	102.06	-1.7%	0.3%	5.6%	5.3%	13.9%	6.3%
Euro (USD/EUR)	1.07	1.6%	-0.3%	-5.0%	-4.7%	-12.8%	-6.1%
British Pound (USD/GBP)	1.25	1.1%	-1.3%	-6.5%	-5.8%	-11.2%	-7.4%
Japanese Yen (Yen/USD)	127.36	-0.9%	-0.4%	10.2%	10.4%	16.9%	10.6%
Chinese Yuan (CNY/USD)	6.67	-1.1%	1.8%	5.7%	4.5%	4.1%	4.7%

Source: FactSet and Bloomberg. As of May 26, 2022.

27 May 2022 | *The Week Ahead*

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