6 May 2022

THE WEEK AHEAD

50 is the New 25

WATCH LIST

Date		Period	Consensus		Previous
U.S.					
Tue 5/10	NFIB Small Business Optimism	Apr			93.2
Wed 5/11	Consumer Price Index	Apr	8.1% Y/Y	▼	8.5% Y/Y
Thu 5/12	Producer Price Index	Apr	10.6% Y/Y	▼	11.2% Y/Y
Fri 5/13	U. of Michigan Sentiment (Prelim. Est.)	May	63.5	▼	65.2
Europe					
Thu 5/12	U.K. GDP (Prelim. Est.)	1Q22	1.0% Q/Q	▼	1.3% Q/Q
Thu 5/12	U.K. Industrial Production	Mar			-0.6% M/M
Fri 5/13	EA Industrial Production	Mar	-0.5% M/M	▼	0.7% M/M
Asia Pacific					
5/8-5/15	China Aggregate Financing	Apr	2300 B	▼	4650 B
5/8-5/9	China Exports	Apr	2.7% Y/Y	▼	14.7% Y/Y
Mon 5/9	Japan Labor Cash Earnings	Mar	1.0% Y/Y	▼	1.2% Y/Y
Wed 5/11	China Producer Price Index	Apr	7.8% Y/Y	▼	8.3% Y/Y
Wed 5/11	China Consumer Price Index	Apr	1.9% Y/Y	▲	1.5% Y/Y

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

U.S.

- **CPI for April** is expected to remain elevated amid broad-based price pressures. However, the jump in oil prices in March from the war in Ukraine is not expected to be repeated in the April data.
- We will watch preliminary **consumer sentiment for May,** notably longer-term consumer inflation expectations.

Europe

- **Military and economic responses** to Russia's war in Ukraine remain in focus, particularly following the EU's proposal of a complete ban on Russian oil by year-end.
- **U.K. GDP for Q1** should give some clarity on how the economy there is reacting to war in Eastern Europe and the offsetting effects of receding COVID.

Asia Pacific

- **China lockdowns** continue to be in focus as cases remain elevated. Authorities in Beijing have deployed an increasingly intense response to contain COVID.
- **China credit growth** will likely show the impact of monetary policy loosening, including the reserve requirement ratio cut and window guidance.

What This Week Means For Markets

The FOMC tightened policy Wednesday, as expected. However, comments by Fed Chairman Jerome Powell indicated the committee is not considering 75bp hikes, which led markets to reprice rate hike expectations lower this year—pricing in seven hikes through year-end, compared with 10 prior to the meeting. This dovish surprise initially drove yields lower, the curve steeper, and equities higher. However, stagflation fears re-emerged Thursday, retracing some of those moves. S&P 500 1Q22 earnings are on track to grow 9.1% Y/Y, better than expected. But despite the solid beat, corporate guidance and earnings revisions have plummeted to the lowest level since 2020. Across the Atlantic, the Bank of England (BoE) hiked rates by 25bps, as expected, though it pushed back on market rate hike expectations, flagging risks of a recession. This led the pound to decline 2%. With the EU eyeing a Russian oil ban, commodity prices edged higher over the week, which should keep upward pressure on prices across the globe. Given elevated inflation and tightening monetary policy, we remain with our central Stagflation scenario. Please see our latest Macro Dashboard.

IN REVIEW

Powell Puts a Cap on Rate Hikes and QT

The FOMC raised the target range for the Fed funds rate by 50 bps to 0.75%-1% and announced that quantitative tightening (QT) will begin June 1. While Fed Chairman Jerome Powell signaled that 50 bps hikes are to be expected in the next couple of meetings, a 75 bps hike "isn't actively being considered." This caused market-implied rate hike expectations to fall, now pricing in seven hikes through year end, compared with 10 prior to the meeting. However, the FOMC will remain data-dependent, so a 75 bp hike could always be put back on the table. The path outlined for QT was as expected, with a phase-in over three months, and then letting the balance sheet run off subject to monthly caps of $60 billion for Treasuries and $35 billion for MBS, to be adjusted if needed. Powell emphasized concerns over elevated inflation and a tight labor market but signaled he believes a "soft-ish" landing can still be achieved.

Rising Wages Support Spending and a Hawkish Fed

A tight labor market, rising wages, and fairly resilient consumer demand should keep the FOMC on track for an aggressive tightening cycle. The 1Q22 Employment Cost Index (ECI)—our and the Fed's preferred measure of wage growth—rose at the fastest pace since 1990, with wage growth broad-based across sectors. Leisure and hospitality, retail, manufacturing, and health care—where the imbalance between supply and demand for labor is stark—saw the fastest gains. With job openings reaching a record high and the quits rate edging higher in March, a tight labor market should keep upward pressure on wages in the near-term. Rising wages drove the 0.5% M/M increase in nominal personal income in March; together with excess savings, this supported an upward surprise in consumer spending, up 1.1% M/M (cons: 0.6%). In real terms, elevated inflation weighed on real income, though spending still rose 0.2% M/M. This supports further 50 bp hikes by the Fed at upcoming meetings.

Investment Compensates for Weak EA Trade & Consumption

Euro area (EA) GDP rose 0.2% Q/Q, in line with expectations. Notwithstanding easing mobility restrictions, growth momentum slowed marginally compared to 4Q21 (0.3% Q/Q), likely due to high inflation and greater uncertainty from the war in Ukraine hurting consumer purchasing power and confidence, as well as slowing global growth.

Thanks to solid investment that offset the slowdown in net trade (in Germany and Italy) and in consumption (in France and Spain), a technical recession has been avoided in Germany (where Q4 was negative). That said, all signs points to a slowdown in the coming quarters, when we expect EA growth to be flat-to-negative Q/Q.

Consumer confidence took another dip in April, hitting -22, from -16.9 in March. Last month saw one of the biggest drops ever, due to Russia's invasion of Ukraine. This month's further drop is also broad-based, with economic, industrial, and services confidence indices all turning south yet again.

EA Inflation Stabilizes, but is Broadening

EA CPI rose by 0.1ppt to 7.5% Y/Y in April, in line with consensus. Lower oil prices, tax cuts, and rebates combined to push energy prices down 3.7% M/M. Offsetting this, both core and food inflation showed strong acceleration (+0.5ppt to 3.5% Y/Y and +1.4ppt to 6.4% Y/Y, respectively), likely due to worsening supply chain bottlenecks and rampant food commodities inflation—all of which shows inflationary pressures continue broadening beyond energy.

Markets are starting to price in the first ECB hike in July and five further hikes in the subsequent seven meetings. Given the likelihood of a recession coming, the central bank may remain more cautious and hike gradually. The key risk to this view is rising core inflation and expectations. Should these accelerate further in coming months, they would likely force the ECB to first hike in July and then continue steadily.

China PMIs Reveal Supply Chain Trouble

China PMIs weakened in April, a sign that near-term lockdown pressures intensified for both production and logistics, which could exaggerate global inflationary pressures. The official manufacturing PMI plunged to 47.4, the lowest since February 2020. The decline was broad-based across components, as companies reported shortages in raw materials and inputs for production, in addition to a growing number of logistical problems. The services sector also fell sharply to 40 amid COVID disruptions. While the PMIs imply a significant drag on economic activity, the decline in manufacturing has not been as bad compared to the start of the pandemic. High-frequency data also suggest early signs of relief, particularly on production. The central government announced measures, including the "closed loop" system for factories and health passes for trucker drivers, to address supply chain disruptions. Nevertheless, uncertainty is high given the possibility of additional or rolling lockdowns across the country, which could lead to lasting disruptions between inter-city logistics.

KEY FINANCIAL INDICATORS

Rates	Yield	1 W Change	1M Change	3M Change	6M Change	12M Change	YTD Change
Fed Funds	0.50%	0 bps	0 bps	25 bps	25 bps	25 bps	25 bps
U.S. SOFR	0.30%	2 bps	0 bps	25 bps	25 bps	29 bps	25 bps
3 Month USD Libor	1.41%	17 bps	44 bps	107 bps	126 bps	123 bps	120 bps
3 Month Euribor	-0.43%	2 bps	2 bps	12 bps	14 bps	11 bps	15 bps
3 Month U.S. T-Bill	0.89%	8 bps	33 bps	66 bps	85 bps	87 bps	84 bps
2-Year U.S. Treasury	2.62%	5 bps	20 bps	130 bps	221 bps	246 bps	189 bps
10-Year U.S. Treasury	2.91%	10 bps	50 bps	99 bps	139 bps	132 bps	140 bps
10-Year German Bund	1.01%	22 bps	49 bps	78 bps	124 bps	126 bps	119 bps
10-Year U.K. Gilt	2.01%	20 bps	44 bps	59 bps	107 bps	122 bps	104 bps
10-Year JGB	0.23%	-2 bps	2 bps	3 bps	16 bps	13 bps	16 bps
Fixed Income	**Yield**	**OAS**	**1W Return**	**1M Return**	**3M Return**	**12M Return**	**YTD Return**
Barclays Capital U.S. Government-Treasury	2.86%	N/A	-0.5%	-2.8%	-5.9%	-7.5%	-8.5%
Barclays Capital U.S. TIPS	3.07%	N/A	-0.6%	-1.9%	-1.8%	-0.1%	-5.4%
Barclays Capital U.S. Aggregate	3.46%	49	-0.5%	-3.5%	-6.6%	-8.6%	-9.4%
Barclays Capital Global Aggregate	2.60%	49	-0.8%	-5.2%	-9.4%	-13.0%	-11.5%
Barclays Capital U.S. ABS	3.34%	70	-0.1%	-0.4%	-2.6%	-3.8%	-3.5%
Barclays Capital U.S. MBS	3.58%	40	-0.5%	-3.2%	-6.1%	-8.6%	-8.2%
Barclays Capital U.S. Corporate Investment Grade	4.29%	134	-0.6%	-5.3%	-8.5%	-10.5%	-12.6%
BAML Euro Corporate Investment Grade	2.15%	153	-1.0%	-3.0%	-6.9%	-8.7%	-8.2%
Barclays Capital U.S. Corporate High Yield	7.04%	390	-0.8%	-3.8%	-5.5%	-5.4%	-8.4%
BAML European Currency High Yield Non-Financial	5.66%	481	-1.2%	-3.7%	-6.8%	-7.0%	-8.0%
CS U.S. Leveraged Loans	7.77%	472	-0.4%	-0.3%	-0.7%	2.6%	-0.2%
JPM CEMBI Broad Diversified	6.28%	335	-0.6%	-2.3%	-9.6%	-10.1%	-11.0%
JPM EMBI Global Diversified	7.45%	447	-1.3%	-5.7%	-13.4%	-14.8%	-15.4%
JPM GBI-EM Global Diversified	6.80%	N/A	-0.2%	-6.1%	-13.0%	-16.0%	-12.4%
Equities	**Price**	**Div Yield**	**1W Return**	**1M Return**	**3M Return**	**12M Return**	**YTD Return**
S&P 500	4,300.17	1.38%	2.8%	-6.1%	-4.1%	4.7%	-9.4%
Euro STOXX 600 (Local)	441.37	2.38%	-0.7%	-4.5%	-4.5%	1.8%	-9.5%
U.K. FTSE 100 (Local)	7,493.45	3.40%	0.9%	-0.9%	-0.3%	8.2%	1.5%
Japan Nikkei 225 (Local)	26,818.53	2.22%	1.6%	-3.3%	-2.3%	-6.9%	-6.9%
China Shanghai Composite (Local)	3,047.06	3.32%	3.0%	-7.2%	-9.4%	-11.6%	-16.3%
MSCI AC World (Local)	667.08	2.01%	2.2%	-4.8%	-5.8%	1.2%	-8.9%
MSCI Emerging Markets (Local)	1,063.84	2.74%	2.0%	-4.8%	-8.8%	-14.2%	-10.2%
Commodities/Currencies	**Price**	**1W Change**	**1M Change**	**3M Change**	**6M Change**	**12M Change**	**YTD Change**
S&P GS Commodity Index	771.37	2.9%	4.6%	20.0%	34.5%	49.3%	37.5%
WTI Crude ($/bbl)	107.81	5.7%	4.4%	16.8%	36.7%	64.0%	43.1%
Copper ($/lb)	4.33	-2.8%	-9.4%	-3.5%	0.1%	-4.6%	-2.8%
Gold ($/oz)	1,863.65	-1.2%	-3.5%	3.3%	3.8%	3.7%	3.2%
U.S. Dollar Index	102.59	-0.4%	3.6%	7.4%	8.7%	12.4%	6.9%
Euro (USD/EUR)	1.05	0.3%	-4.1%	-7.8%	-8.6%	-12.3%	-7.2%
British Pound (USD/GBP)	1.25	0.0%	-4.7%	-7.6%	-7.3%	-10.0%	-7.7%
Japanese Yen (Yen/USD)	129.98	1.3%	5.9%	12.8%	14.4%	19.0%	12.9%
Chinese Yuan (CNY/USD)	6.59	0.5%	3.6%	3.5%	3.0%	1.8%	3.4%

Source: FactSet and Bloomberg. As of May 5, 2022.

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