

The Fed Can't Stop, Won't Stop

WATCH LIST

Date		Period	Consensus		Previous
U.S.					
Mon 6/20	Markets Closed for Juneteenth		--		--
Tue 6/21	Existing Home Sales	May	5.41 M	▼	5.61 M
Thu 6/23	S&P Global Manufacturing PMI (Prelim. Est.)	Jun	56.4	▼	57.0
Thu 6/23	S&P Global Services PMI (Prelim. Est.)	Jun	53.9	▲	53.4
Fri 6/24	New Home Sales	May	608 K	▲	591 K
Europe					
Wed 6/22	EA Consumer Confidence (Advance Est.)	Jun			-21.1
Wed 6/22	U.K. Consumer Price Index	May	9.1% Y/Y	▲	9.0% Y/Y
Thu 6/23	EA S&P Global Manufacturing PMI (Prelim. Est.)	Jun	53.7		54.6
Thu 6/23	EA S&P Global Services PMI (Prelim. Est.)	Jun	55.5		56.1
Thu 6/23	U.K. S&P Global Manufacturing PMI (Prelim. Est.)	Jun			54.6
Thu 6/23	U.K. S&P Global Services PMI (Prelim. Est.)	Jun			53.4
Fri 6/24	U.K. Retail Sales	May	-0.6% M/M	▼	1.4% M/M
Asia Pacific					
Sun 6/19	People's Bank of China Policy Rates	Jun	--		--
Tue 6/21	South Korea Exports 20 Days	Jun			24.1% Y/Y
Thu 6/23	Jibun Bank Japan Mfg. PMI (Prelim. Est.)	Jun			53.3
Thu 6/23	Jibun Bank Japan Services (Prelim. Est.)	Jun			52.6
Fri 6/24	Japan Consumer Price Index	May	2.5% Y/Y	-	2.5% Y/Y

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

U.S.

- **Preliminary S&P Global PMIs** for June will help gauge the extent to which higher prices are impacting demand and margins.
- We will watch **housing data** to see how much rising interest rates and falling affordability are weighing on demand.

Europe

- We are monitoring continuing developments in **the Ukraine-Russia conflict** as economic and financial effects are felt across the world.
- **EA and U.K. June Flash PMIs** will signal the likelihood of a stagflationary environment developing in the coming months.
- Expect **U.K. inflation** to rise further.

Asia Pacific

- The **PBOC** is expected to keep loan prime rates steady following an earlier decision to make no changes to medium-term lending facility rates.
- **Japan PMIs** should help gauge momentum in the economic reopening, while **Japan CPI** could remain elevated on high commodity prices.

What This Week Means For Markets

The FOMC turned even more hawkish this week, forecasting higher rates, slower growth, and a rise in the unemployment rate. This has translated into a risk-off tone in markets. The S&P 500 trended lower and global core yields surged—with the U.S. 10-Year Treasury yield approaching new YTD highs. While the market had fully priced in the 75bp-hike ahead of the meeting, it also remains well ahead of the Fed, pricing in a more hawkish path through year-end 2022. Elsewhere, the ECB held an emergency meeting to address concerns of fragmentation, leading to a tightening of euro periphery spreads, as the central bank announced it will create a new tool to help address the uneven transmission of monetary policy normalization. We remain with our Stagflation Shock scenario, though given the continued hawkish pivot, rates could top out higher through our 18-month outlook. Please see our latest [Macro Dashboard](#).

IN REVIEW
The FOMC Embraces its Inner Hawk

Following an upward surprise in the May CPI data and a move higher in longer-term consumer inflation expectations, the FOMC turned more hawkish, hiking the Fed Funds rate by 75bps at its June meeting. Inflation is high and broad-based, and upward pressure likely remains for necessities such as food, energy, and shelter which raises further risks to consumers' expectations and the path ahead for interest rates. FOMC language suggests that the Fed is far more concerned with price stability than maximum employment, with its updated Summary of Economic Projections calling for a move higher in the unemployment rate and slower GDP growth. If inflation data continues to surprise to the upside—which we think it will—it is likely that the median dot could move higher from here. Given the more hawkish reaction function, we think that the Fed Funds rate could top out at a higher rate before edging lower through the end of our 18-month Stagflation Shock outlook. Risks of a recession late next year are rising as a result.

JUNE FOMC SUMMARY OF ECONOMIC PROJECTIONS

Variable	2022	2023	2024	Longer run
GDP	1.7%	1.7%	1.9%	1.8%
Unemployment Rate	3.7%	3.9%	4.1%	4.0%
PCE Inflation	5.2%	2.6%	2.2%	2.0%
Federal Funds Rate	3.4%	3.8%	3.4%	2.5%

Source: Federal Reserve. As of June 16, 2022.

Shoppers Spend More on Gas, Less on Goods

U.S. retail sales surprised to the downside in May as consumers divert money toward necessities and away from goods. Retail sales fell 0.3% M/M, led by declines in autos, electronics, furniture, and online orders. Adjusting for inflation, real retail sales fell over the month. While retail sales remain well-above pre-COVID levels, momentum is clearly slowing.

GASOLINE AND FOOD SHARE OF U.S. RETAIL SALES


Source: Bloomberg. As of June 16, 2022.

Retail sales largely reflects spending on goods. The sole services component in the retail sales data—food services and drinking places—increased modestly in May, suggesting consumers are shifting spending toward services. We will watch broader May personal spending data to gauge the shift. Looking ahead, the pace of consumer spending should continue decelerating given rising prices of necessities and tightening monetary policy.

China's May Rebound Points to Bumpy Road Ahead

May activity in China, consistent with the latest PMI report, showed a better-than-expected rebound. Industrial production grew 0.7% Y/Y (from -2.9% prior), driven partially by the export sector. Fixed Asset Investment also remained robust, growing 6.2% Y/Y (from 6.8% prior), with notable strength in manufacturing and infrastructure investment. Growth in aggregate credit coincided with the rebound in activity and came in better than expected. Continued easing of pandemic restrictions and further untangling of logistical disruptions should support the growth momentum. The property and services sector and the labor market remain under pressure, however, with 70-city average house prices continuing to contract, the service production index falling 5.1% Y/Y (from -6.1% prior), and the surveyed unemployment rate staying elevated at 5.9% (from 6.1% prior). Downside risks remain high, given the need for more policy support that may under-deliver. With the Fed and the ECB pushing more hawkish policy, it may prove increasingly difficult for the People's Bank of China to substantially lower policy rates from here. Nonetheless, incremental support, via window guidance or targeted fiscal support on consumption or infrastructure spending, will likely continue to be the primary tool for policymakers.

BoE Posts Another Rate Hike as Inflation Worsens

The Bank of England raised interest rates by 25bps to 1.25% at its June meeting (in line with market expectations), as it tries to fight soaring inflation. This is a fifth-consecutive rate hike; three policymakers preferred an increase of 0.5 percentage points. On top of effects from the Russia-Ukraine war, pandemic restrictions, and a tight labor market, U.K. inflation suffered from the government being the only major European entity that did not cap energy prices. The U.K. now suffers the highest inflation rate in the G-7 (9% Y/Y in April). Utility prices will increase again in October, which could push headline inflation up again. The BoE expects inflation to peak slightly over 10% in the last quarter of 2022 before returning to around 2% in two years. This implies more hikes despite the British economy showing signs of slowdown: U.K. monthly GDP was estimated to shrink by 0.3% M/M in April, missing market expectations.

17 June 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	0 bps	75 bps	75 bps	75 bps	75 bps
U.S. SOFR	0.70%	-6 bps	-9 bps	65 bps	65 bps	69 bps	65 bps
3 Month USD Libor	2.03%	34 bps	59 bps	111 bps	181 bps	190 bps	182 bps
3 Month Euribor	-0.18%	12 bps	22 bps	32 bps	42 bps	36 bps	39 bps
3 Month U.S. T-Bill	1.76%	52 bps	80 bps	131 bps	170 bps	173 bps	171 bps
2-Year U.S. Treasury	3.27%	49 bps	68 bps	141 bps	259 bps	311 bps	254 bps
10-Year U.S. Treasury	3.38%	36 bps	45 bps	122 bps	192 bps	188 bps	187 bps
10-Year German Bund	1.61%	26 bps	66 bps	127 bps	198 bps	185 bps	179 bps
10-Year U.K. Gilt	2.43%	19 bps	68 bps	85 bps	170 bps	168 bps	147 bps
10-Year JGB	0.24%	0 bps	0 bps	3 bps	20 bps	20 bps	17 bps
Fixed Income	Yield	OAS	1W Return	1M Return	3M Return	12M Return	YTD Return
Barclays Capital U.S. Government-Treasury	3.37%	N/A	-1.6%	-2.1%	-6.3%	-10.2%	-10.7%
Barclays Capital U.S. TIPS	3.62%	N/A	-2.0%	-1.7%	-6.4%	-4.0%	-7.9%
Barclays Capital U.S. Aggregate	3.96%	53	-2.1%	-2.2%	-6.4%	-11.4%	-11.7%
Barclays Capital Global Aggregate	3.09%	53	-3.0%	-3.2%	-9.5%	-17.0%	-15.0%
Barclays Capital U.S. ABS	4.06%	79	-0.9%	-1.3%	-2.4%	-5.1%	-4.5%
Barclays Capital U.S. MBS	4.05%	48	-2.4%	-2.7%	-6.6%	-10.8%	-10.5%
Barclays Capital U.S. Corporate Investment Grade	4.81%	140	-2.5%	-1.9%	-6.7%	-14.2%	-15.0%
BAML Euro Corporate Investment Grade	3.17%	184	-2.9%	-4.6%	-7.8%	-13.1%	-12.6%
Barclays Capital U.S. Corporate High Yield	8.32%	477	-3.6%	-2.2%	-6.3%	-10.5%	-12.4%
BAML European Currency High Yield Non-Financial	6.92%	541	-3.5%	-3.5%	-6.7%	-11.9%	-12.0%
CS U.S. Leveraged Loans	9.45%	585	-1.1%	-0.7%	-1.4%	-0.9%	-2.8%
JPM CEMBI Broad Diversified	6.88%	353	-2.0%	-1.5%	-4.4%	-13.2%	-13.1%
JPM EMBI Global Diversified	8.27%	488	-3.6%	-2.9%	-9.4%	-20.0%	-19.1%
JPM GBI-EM Global Diversified	7.15%	N/A	-4.1%	-0.3%	-7.3%	-20.4%	-14.7%
Equities	Price	Div Yield	1W Return	1M Return	3M Return	12M Return	YTD Return
S&P 500	3,789.99	1.61%	-7.9%	-5.6%	-10.7%	-9.5%	-19.9%
Euro STOXX 600 (Local)	413.10	2.54%	-6.2%	-4.7%	-5.1%	-10.0%	-15.3%
U.K. FTSE 100 (Local)	7,273.41	3.59%	-4.2%	-2.0%	1.4%	1.4%	-1.5%
Japan Nikkei 225 (Local)	26,326.16	2.10%	-6.8%	-0.4%	3.9%	-10.6%	-8.6%
China Shanghai Composite (Local)	3,305.41	2.21%	1.3%	7.2%	7.9%	-7.1%	-9.2%
MSCI AC World (Local)	600.30	2.29%	-6.9%	-4.1%	-9.6%	-10.8%	-17.1%
MSCI Emerging Markets (Local)	1,020.10	2.86%	-3.8%	2.1%	-2.6%	-18.6%	-12.6%
Commodities/Currencies	Price	1W Change	1M Change	3M Change	6M Change	12M Change	YTD Change
S&P GS Commodity Index	776.47	-5.2%	2.2%	12.0%	44.8%	46.6%	38.4%
WTI Crude (\$/bbl)	115.31	-5.4%	4.3%	19.6%	62.7%	60.0%	53.1%
Copper (\$/lb)	4.17	-6.5%	-0.3%	-7.4%	-0.3%	-4.0%	-6.5%
Gold (\$/oz)	1,823.75	-1.6%	0.7%	-4.7%	3.1%	-2.2%	1.0%
U.S. Dollar Index	105.16	2.6%	0.6%	6.1%	9.0%	16.2%	9.6%
Euro (USD/EUR)	1.04	-3.0%	0.2%	-5.1%	-7.5%	-14.2%	-8.5%
British Pound (USD/GBP)	1.21	-3.9%	-1.3%	-7.7%	-8.7%	-14.3%	-10.9%
Japanese Yen (Yen/USD)	134.58	0.6%	4.0%	13.9%	18.2%	22.2%	16.9%
Chinese Yuan (CNY/USD)	6.72	0.5%	-0.9%	5.3%	5.6%	4.9%	5.4%

Source: FactSet and Bloomberg. As of June 16, 2022.

17 June 2022 | *The Week Ahead*

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