BNY

iFlow
WEEK AHEAD

July 28, 2024

Alternative Universe

"Think of it as a parallel universe. But maybe it's the real one, and we're in a dream." - Joe Haldeman

"There are two things you should remember when dealing with parallel universes. One they're not really parallel, and two, they're not really universes." - Douglas Adams

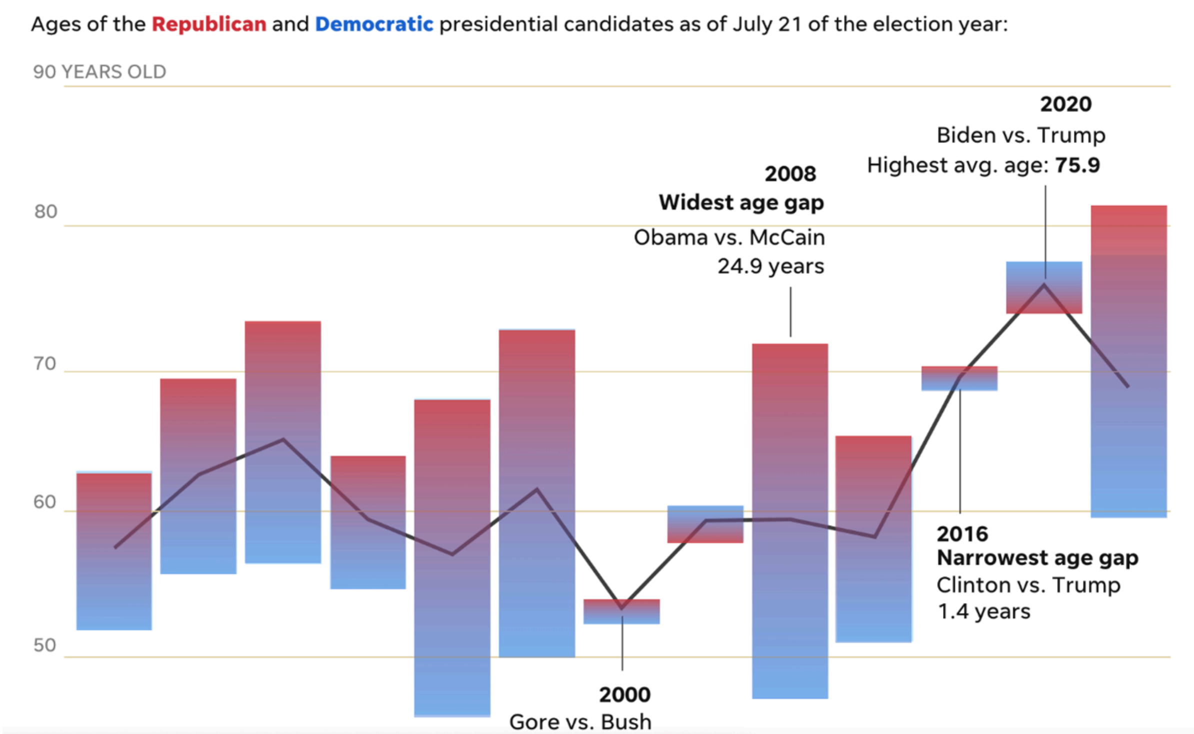
Summary:

The week ahead may best be described by the parallel universe risk to the last week with hopes better outcomes for risk linked to FOMC guidance on easing, on 2Q earnings especially in big tech names confirming value, and with the global economic data confirming growth with special focus on US jobs and EU PMIs. However, confirming the dream to reality will require getting over the month-end rebalancing. Our iFlow rebalancing index makes clear that India, Mexico and Swiss assets have outperformed their FX moves making selling of those currencies something to watch. The carry trade across markets disappointed last week but could continue. The trend factors slowed but are still positive. The Risk mood indicator hold positive but has slid and the peak of such could augur ill for August. Markets have in just two weeks flipped from bullish to bearish views across stocks and bonds and the USD. Some of this comes from the telescope of politics where the Trump trade led to curve steepening, some from the weak China data and rate cuts there, while much gloom continues in Europe where Germany and France lag. The 2.8% 2Q GDP flash in the US was the pivot for many in views the alternative universe of US soft landing and US asset exceptionalism. The need for alternative

thinking stands out as the fears from July have made the month ahead look even more daunting for investors.

Themes for the week ahead:

- **2Q Earnings and the Rotation Trade** – Mixed results from 2Q earnings dominate the risks for the week ahead. According to FactSet with 41% of the S&P500 reporting, 78% are above EPS estimates – that is better than the 5 and 10-year averages but revenues are just 4.4% above estimates which is below both averages. By sector industrials and communications led while health care lagged. The S&P500 fell for the second week and the rotation trade continues.
- **BOJ hiking vs. FOMC guiding toward easing – Divergence trades - with USD focus.** The risk of USD/JPY breaking 150 and moving further towards the 140 zone has implications across markets with bonds at risk from the BOJ expected bond roll-off plans and with the FOMC expected to be clear about September rate cut risks. The divergence of policy in G10 has delivered little in the last year for FX volatility but this week ahead should be a turning point.
- **US Politics and the Harris trade** – The Trump trade is well defined – starting this weekend with a push for crypto – implying a weaker USD – while also seen as sparking higher tariffs, less comfort with allies in Europe, more tax cuts and larger deficits leading to higher US rates and inflation. The Harris trade is less obvious – as many see her tracking the policies of Biden but there are twists and that could lead to more focus on her VP pick and cabinet changes. The week ahead in politics will be measure by the polls continuing to narrow – particularly for the democrats in the Congress while the market watches US curves. The media will be watching for what sticks out for new Presidential candidate as Harris ties together the factions of the democratic party and attempts to win over undecided independents. Age will be one of those factors in play countered with experience. The spread between Trump and Harris is 18 years while the government service split is wider at 28 years for Harris.



Source: USA Today, BNY

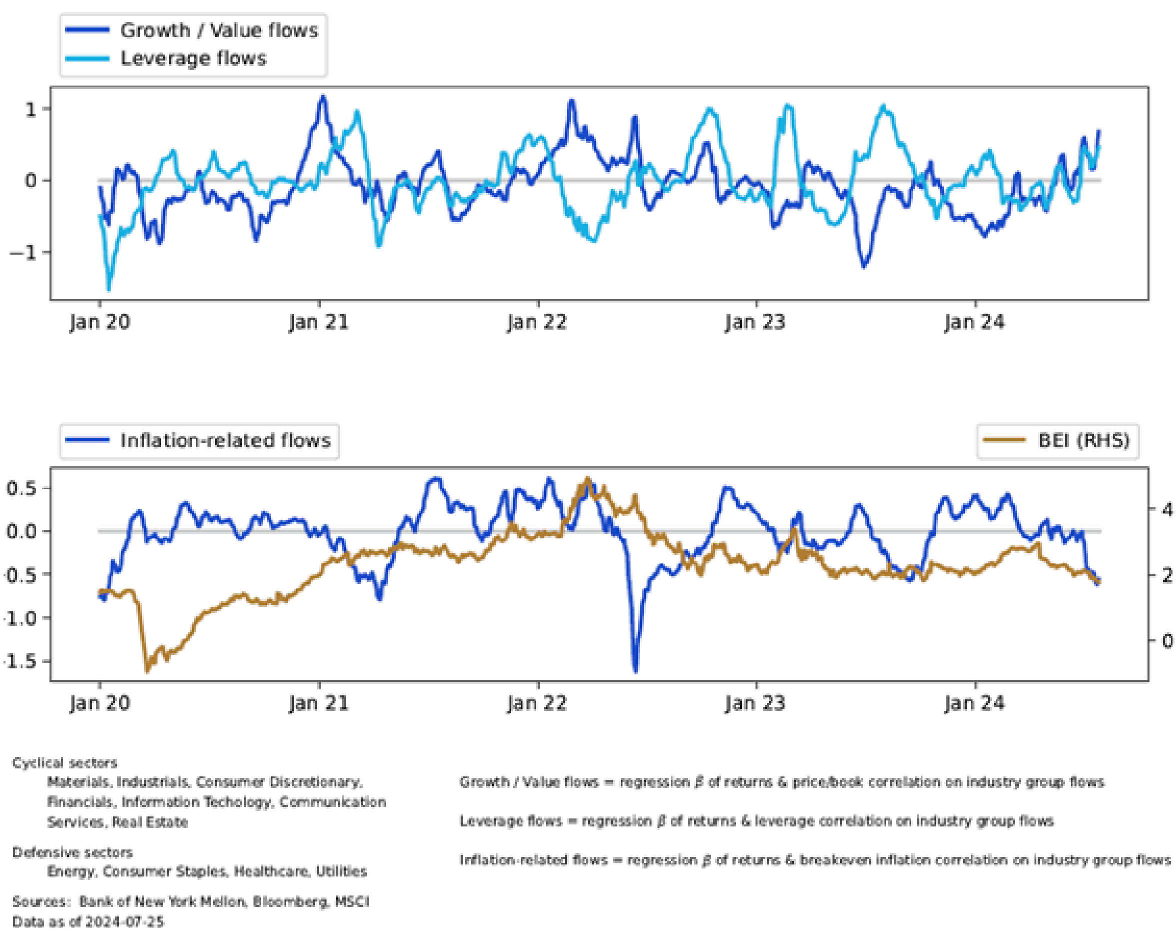
What are we watching:

- **Economic Releases: Monday** – UK consumer credit, Brazil CPI**; Tuesday** – Japan jobs, German CPI flash, EU flash GDP and economic sentiment, US home prices, JOLTS, consumer confidence; **Wednesday** – Korea and Japan industrial production, retail sales, Australia CPI, China NBS PMI, flash EU inflation, German jobs, US ECI; **Thursday** – Korea trade, global PMI manufacturing, Australia trade, Indonesia CPI, EU jobs,
- **Central Banks**: **Wednesday** – BOJ, FOMC, BCRC, BCC, COPOM; **Thursday** – ECB economic bulletin, BOE and CNB decisions.
- **Issuance**: **US has no coupon issues**, but with weekly cash flow -$45.7bn with $183bn from last week offset by $137.3bn in coupons paid Wednesday. On Monday 3Q treasury refunding estimates; Wednesday – US Treasury refunding announced. **UK has GBP3.75bn of 10Y Gilts** sold Tuesday. **EU has E25.5bn in issues** from Italy, Germany, Spain, France and Belgium along with E2bn in linkers from Italy and Spain. **Tuesday** – Italy sells E3bn in 5Y, E4bn in 11Y and E1.5bn in 8Y CCTeu; **Wednesday** – German sells E3bn in 6Y Bunds; T**hursday** – Spain sells E6bn in 3-10-20Y SPGB and E1bn in 3Y SPGei; while France sells E10.5bn of 10-14-19 and 31-year OATs. **Friday** – Belgium sells E1bn of ORI

What changed this week:

- **US S&P500 fell for the second week off 0.83%** with its worst day since 2022 on Wednesday. The rotation trade continued with DJIA up 0.75% on the week while Nasdaq 100 fell -2.08%. The rest of the world did better with UK FTSE up 1.59%, German Dax up 1.35% while the biggest loser was Japan Nikkei off 5.98% and China with the CSI 300 off 3.67%. The focus of our flows continues to be negative in G10 and positive in EM. From a style perspective the notable drop in July has been around inflation fears dropping in equities with our index below October 2023 levels.

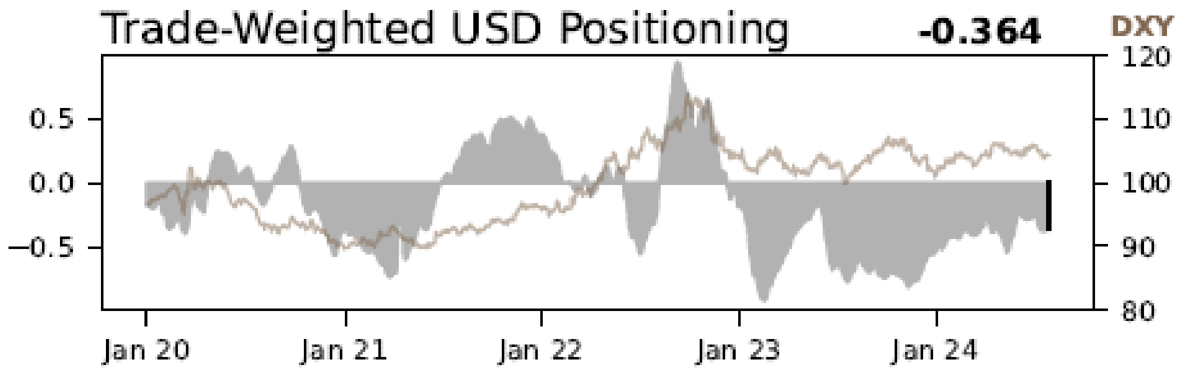
Exhibit #1: Growth and Inflation back in play in US shares

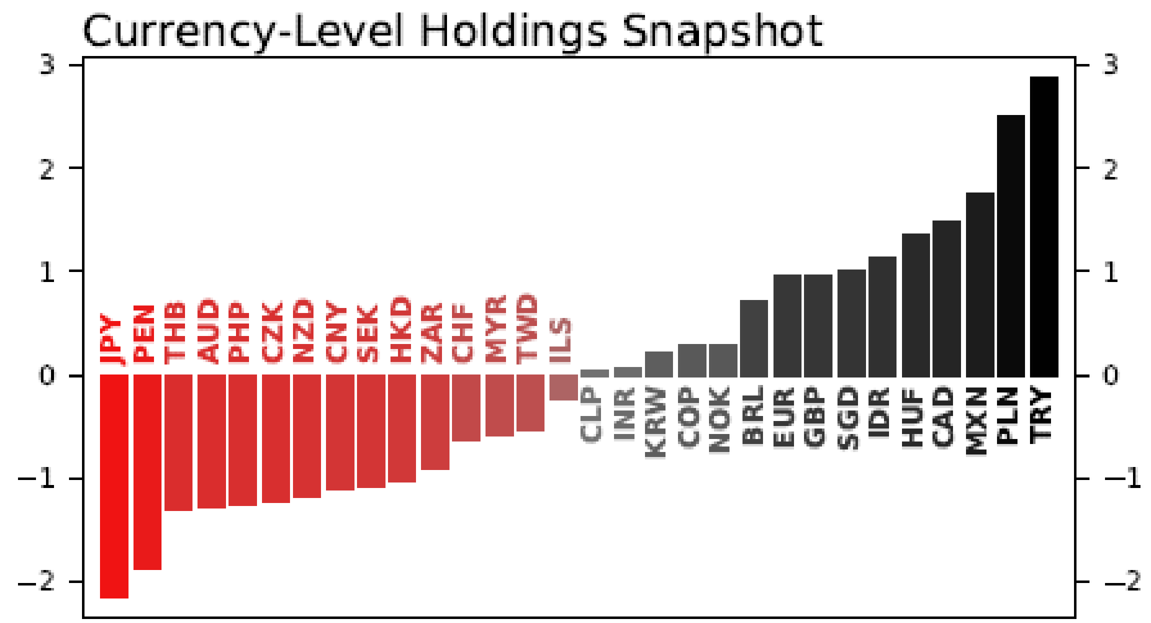


Source: iFlow, BNY

- **Bonds continued to rally globally except in Japan.** The US curve was positive 2/10Y and 2/30Y with closes Friday at 2Y 4.383%, 5Y 4.075%, 10Y 4.195% and 30Y 4.452%. The better GDP was offset by lower PCE price index and markets in the US price a FOMC September cut. The rest of the world is less sure – with China cutting rates (1Y MLF off 0.2%) and South Korea benefitting with bonds off 8bps to 3.08%. The BOJ decision ahead leave 10Y there up 1.5bps to 1.055%. The BNY iFlow data shows inflows into US bonds but selling elsewhere with foreigners not involved in the US market while appetite for credit has returned modestly from lows set early in July.
- **FX markets continued to be mixed with USD flat on the week** while JPY gained 2% and MXN fell 2.75%. The NZD and AUD fell 1.4% and reflect ongoing rate/growth pains over policy outlooks and China while CHF, KRW and CNY all were slightly positive given the JPY and Carry unwinds. The iFLow data highlighted that TRY, PLN, MXN and HUF remain overheld while the JPY, PEN, THB and AUD lead the least. The carry factor fell back to negative while trend holds positive.

Exhibit #2: FX USD holding JPY and MXN focus





Source: iFlow, BNY

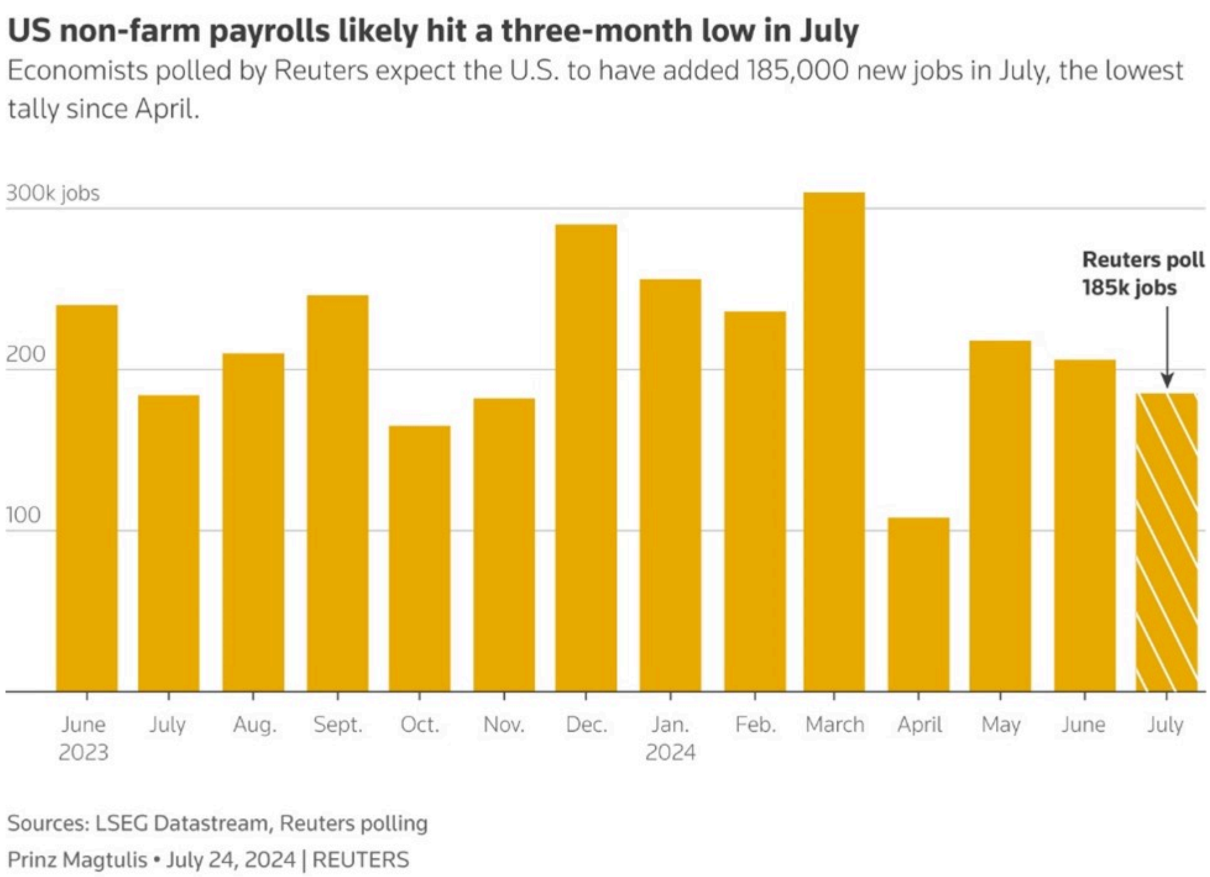
News Agenda and Weekly Themes – FOMC, BOJ, BOE, US jobs, PMIs and more 2Q earnings

In the United States, key highlights will include the Fed's interest rate decision and the nonfarm payrolls report. Other important events will feature JOLTs job openings, CB Consumer Confidence, ISM Manufacturing PMI, factory orders, S&P Case-Shiller House Price Index, pending home sales, and the employment cost index. Earnings season will enter one of the busiest weeks, with megacaps Microsoft, Meta, Apple, and Amazon taking center stage. Globally, Bank of England, Bank of Japan, and Central Bank of Brazil will provide updates on their monetary policy. Inflation rates will be released for Spain, Germany, Australia, Netherlands, France, Poland, the Euro Area, Italy, South Korea, and Switzerland. Additionally, GDP growth rates will be announced for France, Spain, Germany, Italy, the Euro Area, and Mexico. In China, manufacturing and services PMIs will be closely watched.

Manufacturing PMIs will also be published for South Korea, Russia, Spain, Italy, and Canada.

US Jobs and the FOMC Easing Hopes - US employment data due August 2 will give investors the opportunity to assess whether the gradual signs of slowing that bolstered rate cut expectations have continued in July. Economists polled by Reuters expect the U.S. to have created 185,000 jobs in July, compared with 206,000 in the prior month. Prior to that data, the FOMC July 30-31 meeting will likely be watched for any signal of easing bias ahead. Most analysts see that as unlikely, and that Chair Powell will wait until the Jackson Hole speech to spell out the plan for any easing with a focus on the neutral rate and path ahead. However, signs of economic concern from the Fed Statement or Powell press conference could give investors - already unnerved by turbulence in U.S. tech stocks - yet another reason to worry. As it is, investors believe the time to ease monetary policy is swiftly approaching as futures tied to the Fed funds rate show investors pricing in a more than 90% chance for September.

Exhibit #3: US unemployment over 4.1%?



Source: Reuters, BNY

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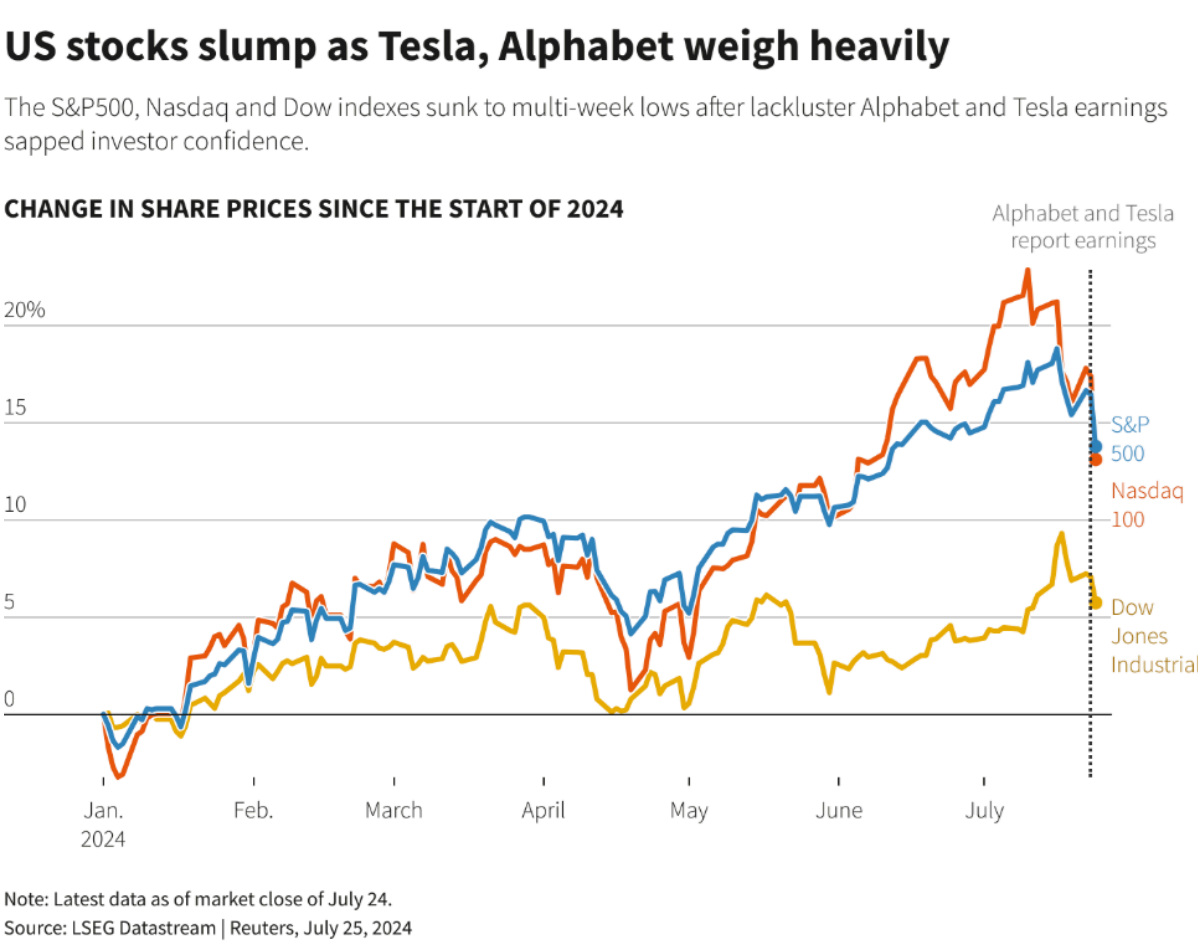
2. 2Q Earnings and the Tech Rotation – Microsoft is scheduled to report earnings on Tuesday, followed by Facebook-parent Meta on Wednesday and Apple and Amazon on Thursday. Disappointing numbers could re-ignite the worries that caused a crushing selloff in U.S. stocks on Wednesday, when both the S&P 500 and Nasdaq suffered their worst day since late 2022. Google-parent Alphabet, whose earnings were one of the triggers for the recent selloff, actually reported better-than-expected revenue, but investors grew wary that rising spending on AI infrastructure could squeeze margins, sending the shares 5% lower.

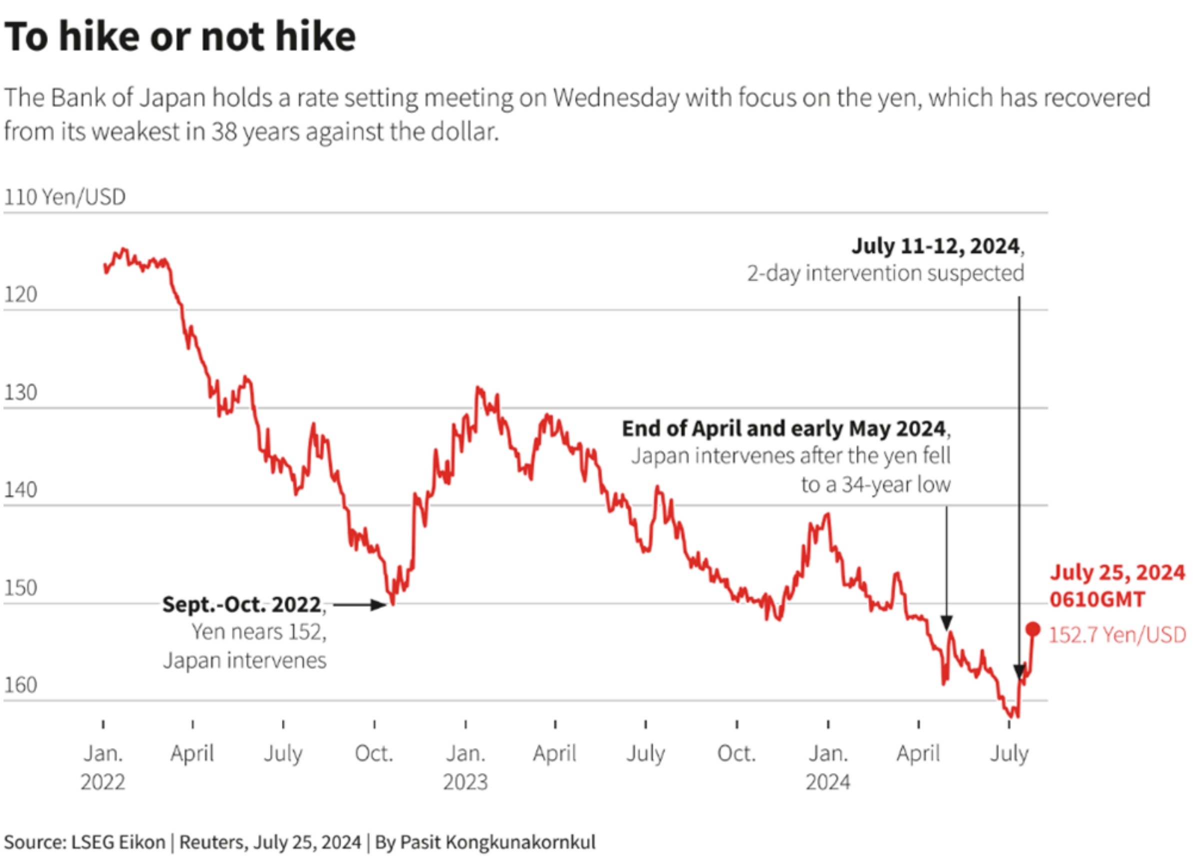
Exhibit #4: Tech rotation trade



Source: Reuters, BNY

3. BOJ and the Rate Hike Risk – Our call is for a 10bps hike from the BOJ putting the 0.1%-0.2% band for O/N rates for August and then another 10bps in September. While the BOJ would like to argue this is a normalization process after nearly a decade of negative rates, the JPY issues are the dominant concern of the consumer and government. The weak yen's choking effect on households and businesses turns the exchange rate into a central issue for the ruling Liberal Democratic Party's leadership convention in September. The fact that the currency has rebounded by a staggering 10 yen per dollar from three-decade lows at the start of the month hasn't deterred some from predicting a July hike. Many argue the BOJ can get the most bang for its buck by hiking into a rallying yen. Others worry a fragile economy and weak consumer sentiment couldn't weather higher borrowing costs, with slowing U.S. growth set to have a knock-on effect already.

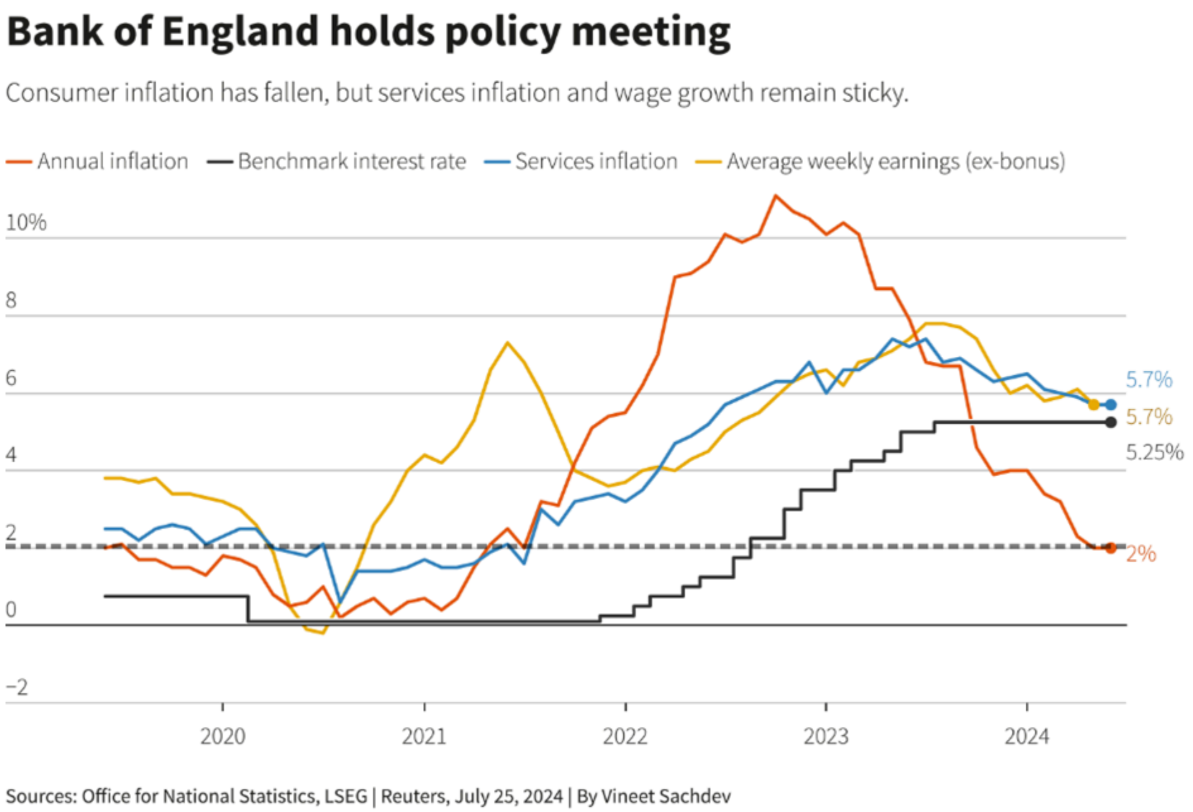
Exhibit #5 BOJ rate hikes and bond roll-off key



Source: Reuters, BNY

4.The UK consumers, banks and the BOE – The markets price in just 48% chance for a August 1 hike. Clare Lombardelli, the new Deputy Governor of the Bank of England, may hold the deciding vote, as the other eight Monetary Policy Committee members are split evenly on whether to hold or cut. The tie breaker could also be the plans of the New Labour Government and the balance tax and spend implied budget. British consumers are feeling the pain of high for longer interest rates – staying at more than 14-year highs, but banks have clearly reaped the benefits. Markets will watch results from HSBC, Barclays and Standard Chartered to get a sense of how well they are likely to fare when borrowing costs, and the profit they make on them, start to fall.

Exhibit #6: BOE cut our call



Source: Reuters, BNY

Weekly Calendar – July 29-Aug 2

Central Bank Decisions

- **Japan BoJ (Wednesday, July 31) –** The market is looking at the strong prospect of a rate hike by the BoJ but conditions remain highly variable. The strong appreciation in the JPY of late is itself disinflationary and we believe it is incumbent upon the BoJ to act more with regard to the balance sheet as to affect the direction and scale of cross-border flows. Inflation numbers also remain mixed and all central banks globally will be mindful of external circumstances, especially with market expectations for the Fed also adjusting towards a less hawkish narrative.
- **Colombia BCRC (Wednesday, July 31) –** Unfortunately for the BCRC, their policy announcement will be simultaneous with the Fed so some guesswork will be needed for external conditions. On balance we believe that all LatAm central banks deciding this week will err on the side of caution and not count on a dovish FOMC, and despite weak growth conditions, BCRC will not move

beyond 50bp, keeping nominal rates well above double-digits. Columbian inflation is softening on s sequential basis but realistically until annualized rates fall below 5%, BCRC cannot move more aggressively.

- **US FOMC (Wednesday, July 31) –** We don't expect any policy action at Wednesday's FOMC meeting. We will be watching the statement as well as Powell's press conference for potential signs of the Fed's openness to easing in upcoming months – we think September will feature the first rate cut in this cycle.
- **Brazil COPOM (Wednesday, July 31) –** The Selic rate is expected to remain at 10.5% though there could be some additional room for manoeuvre depending on how the Fed decision transpires with respect to their policy path. For now, given the positioning and fiscal risks surrounding LatAm, we don't see much scope additional moves and market pricing for additional cuts has all but stalled. Budgetary pressures continue to loom large in Brazil and across the region, and this is inhibiting additional inflows, irrespective of the Fed's stance.
- **Chile BCC (Wednesday, July 31) –** The market is split on a cut in Chile. With nominal rates approaching Fed levels, but inflation running at close to 4%, there is very little room for the central bank to move further without risking further currency weakness. As terms of trade have deteriorated for Chile with the drop in copper and lithium prices, valuations probably need to adjust but there is no guarantee that demand will also show the requisite contraction, especially with real wages growing at 2-3%y/y.
- **UK BoE (Thursday, August 1) –** We believe the Bank of England will take the plunge and opt to start their easing cycle, but it will be an extremely close call. The spread between headline inflation and services inflation is widening aggressively, and the BoE also faces additional delays in an updated version of labour market figures to assess the true state of slack or general tightness. The chancellor may also announce a new round of public-sector pay increases while admitting to a larger-than expected fiscal gap, which would also complicate the demand outlook. The new government has generated a 'stability premium' for GBP, but market tolerance for fiscal largess is very limited.
- **Czech CNB (Thursday, August 1) –** The repo rate is expected to drop by an additional 25bp to 4.5%, which now puts Czech rates within distance of some G10 peers in Europe. However, inflation has fallen to normal levels and was manufacturing in the region continues to contract, the CNB may have enough

confidence that domestic demand will continue to weaken – retail sales figures are still relatively high but generally surprising to the downside.

Key data/releases

Date	BST	EDT	Country	Event	Period	Cons.	Prior
07/30/24	00:30	19:30*	JN	Jobless Rate	Jun	2.60%	2.60%
07/30/24	00:30	19:30*	JN	Job-To-Applicant Ratio	Jun	1.24	1.24
07/30/24	02:30	21:30	AU	Building Approvals MoM	Jun	-2.50%	5.50%
07/30/24	08:00	03:00	CZ	GDP YoY	2Q A	--	0.30%
07/30/24	10:00	05:00	EC	GDP SA QoQ	2Q A	0.20%	0.30%
07/30/24	10:00	05:00	EC	GDP SA YoY	2Q A	0.50%	0.40%
07/30/24	13:00	08:00	GE	CPI YoY	Jul P	2.20%	2.20%
07/30/24	13:00	08:00	GE	CPI MoM	Jul P	0.40%	0.10%
07/30/24	15:00	10:00	US	Conf. Board Consumer Confidence	Jul	99.7	100.4
07/31/24	00:50	19:50*	JN	Industrial Production MoM	Jun P	-4.50%	3.60%
07/31/24	02:30	21:30	CH	Manufacturing PMI	Jul	49.3	49.5
07/31/24	02:30	21:30	AU	Retail Sales MoM	Jun	0.20%	0.60%
07/31/24	02:30	21:30	AU	CPI QoQ	2Q	1.00%	1.00%
07/31/24	02:30	21:30	AU	CPI YoY	2Q	3.80%	3.60%
07/31/24	08:00	03:00	TU	Trade Balance	Jun	--	-6.50b
07/31/24	09:00	04:00	PD	CPI YoY	Jul P	--	2.60%
07/31/24	10:00	05:00	EC	CPI MoM	Jul P	-0.20%	0.20%
07/31/24	12:00	07:00	US	MBA Mortgage Applications	Jul-26	--	-2.20%
07/31/24	13:00	08:00	SA	Trade Balance Rand	Jun	22.3b	20.1b
07/31/24	13:15	08:15	US	ADP Employment Change	Jul	168k	150k
08/01/24	01:30	20:30	JN	Jibun Bank Japan PMI Mfg	Jul F	--	49.2
08/01/24	02:45	21:45	CH	Caixin China PMI Mfg	Jul	51.5	51.8
08/01/24	07:00	02:00	UK	Nationwide House PX MoM	Jul	--	0.20%
08/01/24	07:00	02:00	UK	Nationwide House Px NSA YoY	Jul	--	1.50%
08/01/24	07:30	02:30	SW	Swedbank/Silf PMI Manufacturing	Jul	--	53.6
08/01/24	08:00	03:00	TU	S&P Global/ICI Turkey Manufacturing PMI	Jul	--	47.9
08/01/24	08:00	03:00	PD	S&P Global Poland Manufacturing PMI	Jul	--	45
08/01/24	08:30	03:30	CZ	S&P Global Czech Republic Mfg PMI	Jul	--	45.3
08/01/24	08:55	03:55	GE	HCOB Germany Manufacturing PMI	Jul F	42.6	42.6
08/01/24	09:00	04:00	EC	HCOB Eurozone Manufacturing PMI	Jul F	--	45.6
08/01/24	09:00	04:00	NO	DNB/NIMA PMI Manufacturing	Jul	--	47.7
08/01/24	09:30	04:30	UK	S&P Global UK Manufacturing PMI	Jul F	--	51.8
08/01/24	13:30	08:30	US	Initial Jobless Claims	Jul-27	--	235k
08/01/24	14:00	09:00	BZ	S&P Global Brazil Manufacturing PMI	Jul	--	52.5
08/01/24	14:30	09:30	CA	S&P Global Canada Manufacturing PMI	Jul	--	49.3
08/01/24	14:45	09:45	US	S&P Global US Manufacturing PMI	Jul F	--	49.5
08/01/24	15:00	10:00	US	ISM Manufacturing	Jul	49	48.5

08/02/24	07:30	02:30	SZ	CPI YoY	Jul	1.30%	1.30%
08/02/24	07:30	02:30	SZ	CPI MoM	Jul	-0.20%	0.00%
08/02/24	13:00	08:00	BZ	Industrial Production YoY	Jun	--	-1.00%
08/02/24	13:30	08:30	US	Change in Nonfarm Payrolls	Jul	175k	206k
08/02/24	13:30	08:30	US	Unemployment Rate	Jul	4.10%	4.10%
08/02/24	15:00	10:00	US	Factory Orders	Jun	0.50%	-0.50%
08/02/24	15:00	10:00	US	Durable Goods Orders	Jun F	--	-6.60%

Key events/speeches

Date	BST	EDT	Country	Event			
07/31/24			*JN*	*BoJ Governor Kazuo Ueda press conference*			
07/31/24	*19:30*	*14:30*	*US*	*Fed Chair Jerome Powell press conference*			
08/01/24	*12:30*	*07:30*	*UK*	*BOE Governor Andrew Bailey press conference*			
07/31/24	*19:00*	*14:00*	*CO*	*Overnight Lending Rate*	*Jul-31*	*10.75%*	*11.25%*
07/31/24	*19:00*	*14:00*	*US*	*FOMC Rate Decision (Upper Bound)*	*Jul-31*	*5.50%*	*5.50%*
07/31/24	*22:30*	*17:30*	*BZ*	*Selic Rate*	*Jul-31*	*10.50%*	*10.50%*
07/31/24	*23:00*	*18:00*	*CL*	*Overnight Rate Target*	*Jul-31*	*5.63%*	*5.75%*
08/01/24	14:00	09:00	UK	BOE decision maker panel survey			
08/01/24	*12:00*	*07:00*	*UK*	*Bank of England Bank Rate*	*Aug-01*	*5.00%*	*5.25%*
08/01/24	*13:30*	*08:30*	*CZ*	*Repurchase Rate*	*Aug-01*	*--*	*4.75%*
08/01/24	17:00	12:00	UK	BOE's Huw Pill speaks			
08/02/24	12:15	07:15	UK	BOE Chief Economist Huw Pill speaks			

Conclusions: Politics in the Americas – why the Venezuela election matters?

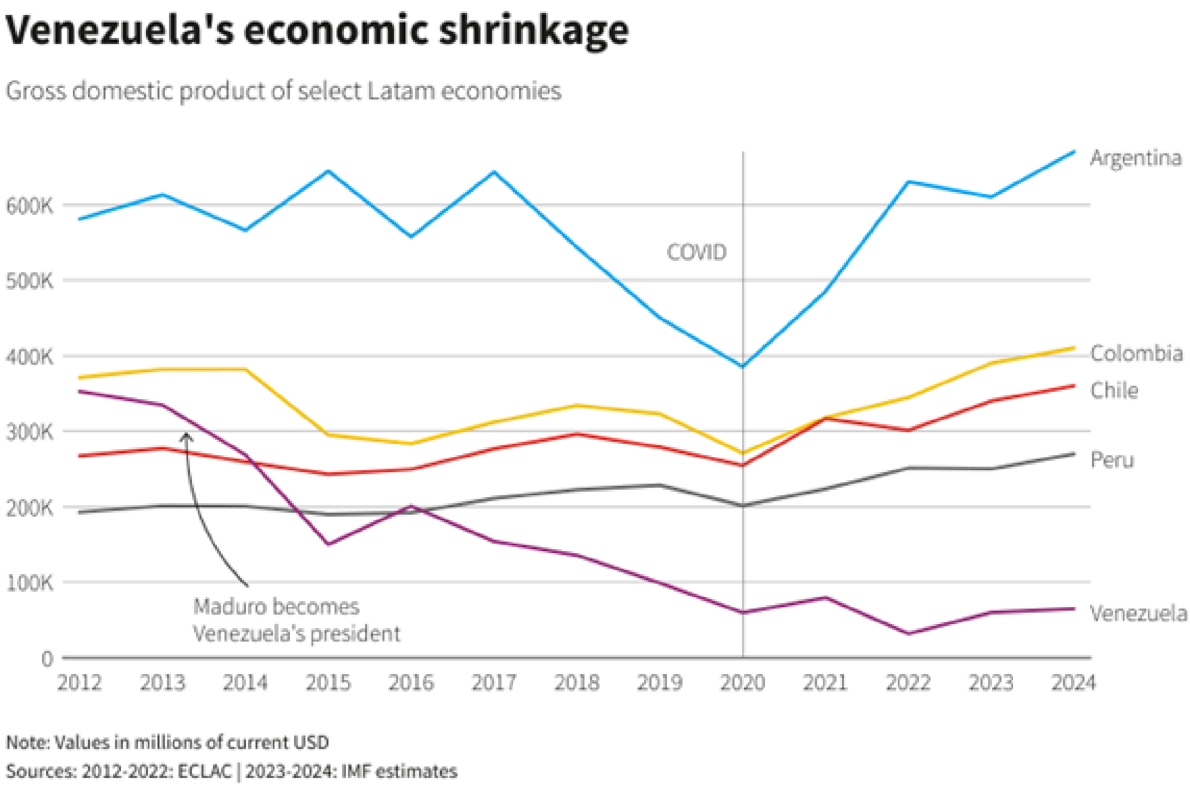
The simple answer is oil and credit. Investors are watching to see if the Maduro government will relent and pass to another, and that process matters to the US and EU. The implication for the US election is in the mirror as foreign money flows into and out of the US could hinge on the outcome.

Venezuelans will elect a president on Sunday. Opposition candidate Edmundo Gonzalez leads polls by 20 points over incumbent Nicolas Maduro, who has pledged the election will be transparent, but forced the winner of the opposition primary, Maria Corina Machado, out of the race. The reason investors should care is that a peaceful transfer of power from Maduro to Gonzalez could reset US foreign policy and relieve energy markets globally. The results and handling of the vote is one half of the issues for future U.S. sanctions on Venezuela - the US election between Harris and Trump for the White House is the other half – as policy on foreign trade in energy will be key.

Current US curbs include a ban on buying bonds directly from Venezuela's government which effectively prevents any restructuring of the $60 billion in international bonds owed by the government and state-owned oil firm PDVSA. Venezuela's and PDVSA'S defaulted bonds trade at deeply distressed levels of 13-22 cents but have rallied sharply from late last year's single-digits 5-10 cents. Investors are watching Maduro's handling of the election very closely along with the actual outcome.

Bottom Line: US markets have become obsessed with politics and that won't change unless the telescope shifts directions - perhaps 2Q earnings or the FOMC/BOJ divergence will matter - but for the USD and US rates the focus ahead is on trends and what has been started over the summer continuing. For equities risk on and off has been mild, and the cost of fear too little to change the programs that have left US exceptionalism in play.

Exhibit #7: Politics matter to growth long term



Source: FactSet, BNY

Please direct questions or comments to: iFlow@BNY.com

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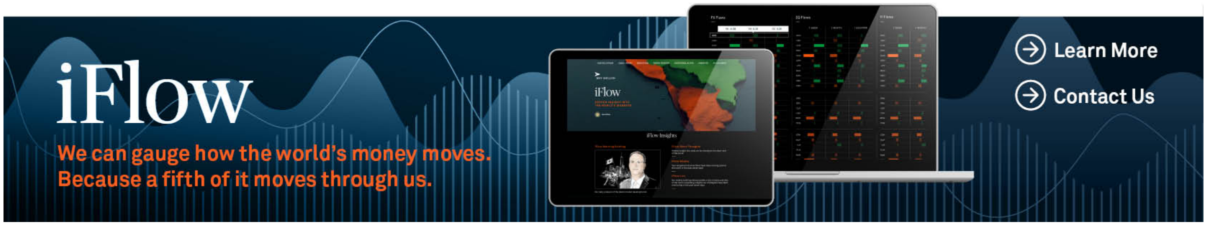

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