BNY

iFlow
WEEK AHEAD

June 16, 2024

Heat Waves

“Heat makes the essence of things rise to the surface.” – Mahatma Gandhi
“If you saw a heat wave, would you wave back?” – Steven Wright

Summary:
Somewhere between the FOMC and the BOJ inaction and the lower-than-expected US CPI and PPI markets moved from worrying about the heat of higher prices to the cold of slowing growth. The fear of uncertainty from politics showed up and put fuel to the fire of change with French President Macron’s surprise snap election call driving EU shares and bonds lower along with the EUR. The US consumer sentiment fell to 7-month lows, while investors showed up to buy the US bond supply happy to own duration and buy stocks. The shift from fear of inflation to fear of slow growth dominates risk markets into the week ahead with focus on whether the central bank decisions from the RBA, BOE, Norges Bank and SNB will add to global divergence. Carry as a factor driving markets is in reverse, falling from positive to slightly negative this last week. This has broad implications on rate policy supporting FX ahead. Like an a 4-stroke engine firing on 2 pistons, the overheating of prices battles the need for more fuel. Notable, that energy price relief matters to many of the CPI reports but its noisy, calls of a commodity super-cycle continue linked back to growth forecasts. Oil prices shot higher on the last week as did EU natural gas, but industrial metals lagged. Growth of future demand remains the forecast with US soft-landing hopes dominant even as the rest of the world seems stuck in stalled growth doubts. This is the summer of discontent, and we await the first heat wave of the season with trepidation as investors will want to greet the start of Summer and the end of half-year with new ideas rather than old suppositions.

Key Themes :

- **Politics trump economics.** The investor uncertainty over ballot boxes shows up again – with the last two weeks highlighting the risks of volatility despite expectations for governmental changes – start with South Africa, continue to Mexico and now throw in Europe with the surprise French election. In the next month, fears are rising about snap election risks in Japan and Germany given the weak government support showing up in polling there, while the UK Tories seem destined for a loss on July 4th. Meanwhile the June 30 and July 7 French vote becomes a barometer for EUR risk. Polls from IFOP show Le Pen's RN at 35% and Macron's Renaissance at 19%, while the left Popular Front at 26% and Republicans at 7%. Fears of democracy failing to govern and all leading to financial crisis are on the rise.
- **Half-year, credit and liquidity**. German yields rarely lead the US but when they do investors turn risk averse, now the world is watching EU bonds again. The spread of French and Italian bonds to the German Bunds have returned to 2017 levels where the last French election spooked markets. This time, the lack of spreads in other credit markets makes such stories more threatening as investors question growth over inflation and wonder when the credit cycle starts to matter. Cash needs into month-end and half-year end are beginning to become a signal for trouble. The FOMC high for longer costs are likely to be questioned.
- **Growth over Inflation**? While the US GDPnow casts vary from 0.9% from St.Louis to 2.1% for Atlanta Fed – the 2Q growth in the US is likely better than 1Q but hardly as hot as 4Q. The sustainable growth rate in the US still is seen at 1.8%-2.0% while that of other nations is lower in the G10 – making the USD bid hold even if Fed rate cuts come into play in September. The role of growth in driving markets is back in play but hasn't yet shown up in all markets, notably equities.
- **USD and Oil**. The role of gold as a key part of central bank reserves remains in focus as gold rallied back this week despite the US Fed holding rates. The role of the USD as the key currency also has to do with oil. Last week, Saudi Arabia became a full member of mBridge allowing CBDC payments cross-border. When this is used to sell oil, the CNY will rise in use over other currencies in competition with the USD. The other part of the USD is wrapped around Swift and the lack of other viable payments platforms. Project mBridge was launched in 2021 by the Bank for International Settlements' Innovation Hub, the Bank of Thailand, the Central Bank of the United Arab Emirates, the Digital Currency Institute of the People's Bank of China, and the Hong Kong Monetary Authority. The role of trade over asset flows linked to USD will be important going forward as investors consider holding FX. The challenge to the USD will require more than oil or gold to dethrone it.

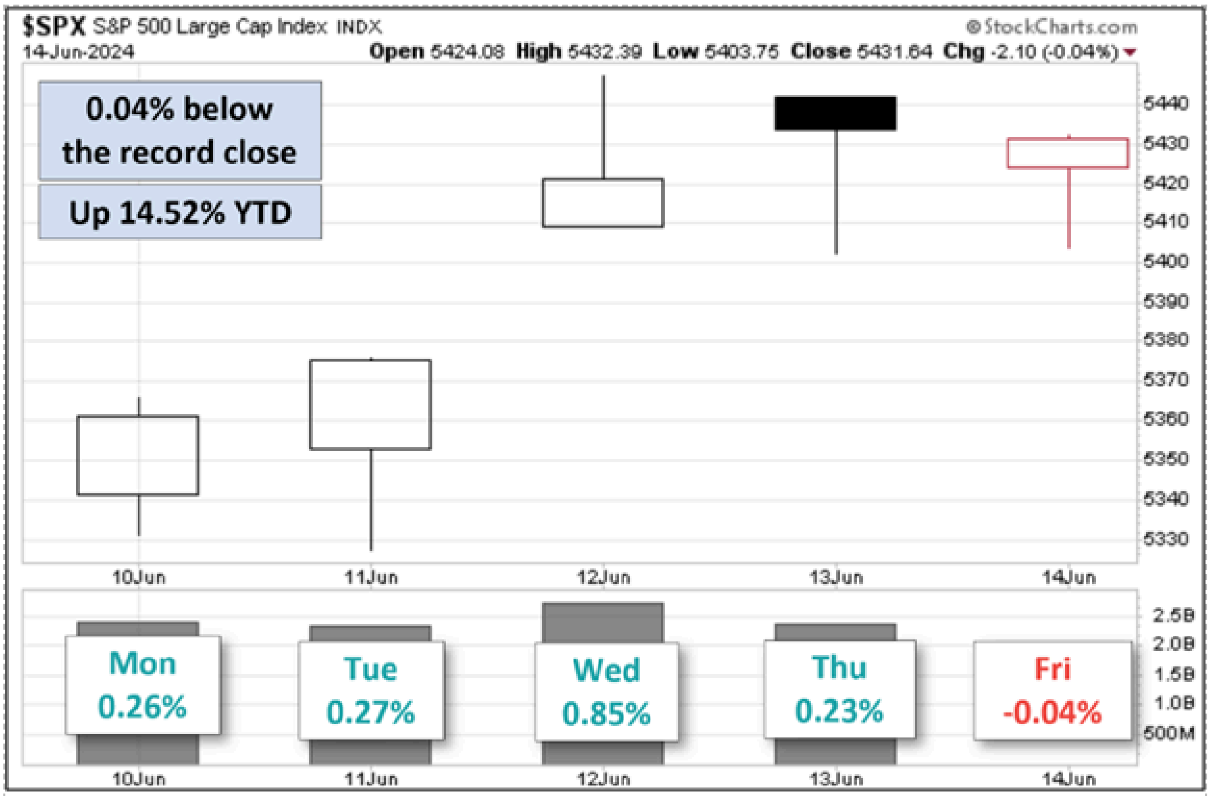
What are we watching:

- **Economic Data: Monday** – Singapore and India Holiday, US Empire Manufacturing; **Tuesday** - Indonesia Holiday, Eur CPI, US Retail Sales/Ind Prod; **Wednesday** - US Holiday, BoJ Minutes, UK CPI, Gre/Ger Supply; **Thursday** - Eurogroup Meeting, ECB Econ Bulletin/Council Meeting, China 1/5y LPR, Ger PPI, Housing Starts/Building Permits/Philly Fed; **Friday** - UK Retail Sales/PSNB, flash global PMI, Can Retail Sales, US PMI Services/Existing Home Sales/Leading Index,.
- **Central Banks: Monday** – Fed Harker, ECB Lane/Lagarde/Guindos; **Tuesday** - RBA Rate, Fed Cook, Barkin, Collins, Logan, Kugler, Musalem, Goolsbee, ECB Knot/Cipollone/Guindos/Villeroy, RBNZ Conway; **Wednesday** – ECB Centeno, Brazil BCB rate decision; **Thursday** - SNB Rate decision, Norges Rate decision, BoE Rate decision and Gov Bailey news conference, Fed Barkin; Friday - ECB Nagel.
- **US Issuance**: Near term cash flow (next four weeks) is negative at -**$49bn**, and equal to the size of issuance being settled on Jun 28th. **Tuesday -** $13bn of 20Y bonds; Thursday -$21bn in 5Y TIPS
- **EU Issuance**: This week cash flow is negative at **-€13.41bn**, as €16.15bn of expected issuance being settled will offset €2.49bn of total C&Rs being paid. **Monday - Belgium:** OLOs: 5Y 2.70% Oct29, 10y 2.85% Oct34 for total €2.0-2.5bn; **Tuesday - Germany:** 5Y Bobl 2.10% Apr29 for €4bn; **Wednesday - Germany:** 30Y Bund 2.50% Aug54 for €2bn, **Greece:** GGBs for €0.4bn (expected); **Thursday - Spain** SPGBs**:** 5Y 3.50% May29, 8y 0.70% Apr32, 10Y 3.45% Oct34 for €5ebn, **France** OATs**:** 3Y 2.75% Oct27, 5Y 5.50% Apr29, 6y 2.75% Feb30, 8Y 0.00% May32 total €8.0-10.5bn.

What changed last week:

- **In Equities, the US S&P 500 rose for a second straight week**, finishing up 1.58% from last Friday. The index is currently up 14.52% year to date and has recorded a new all-time high 29 times this year. Notably the DJIA fell 0.54% on the week as blue chips lagged while the focus on tech and AI remained with NASDAQ up 3.24%. In the other big 8 bourses, France suffered the most with CAC40 off 6.23% while Italy MIB fell 5.76% and EuroStox 50 fell 4.20%. In Asia, Japan Nikkei rose 0.34% while the Hong Kong Hang Seng fell 2.9% in holiday shortened week. In iFlow – all global equity sectors saw outflows on the week dominated by financials while by region EM Americas were slightly positive flow and APAC was mixed.

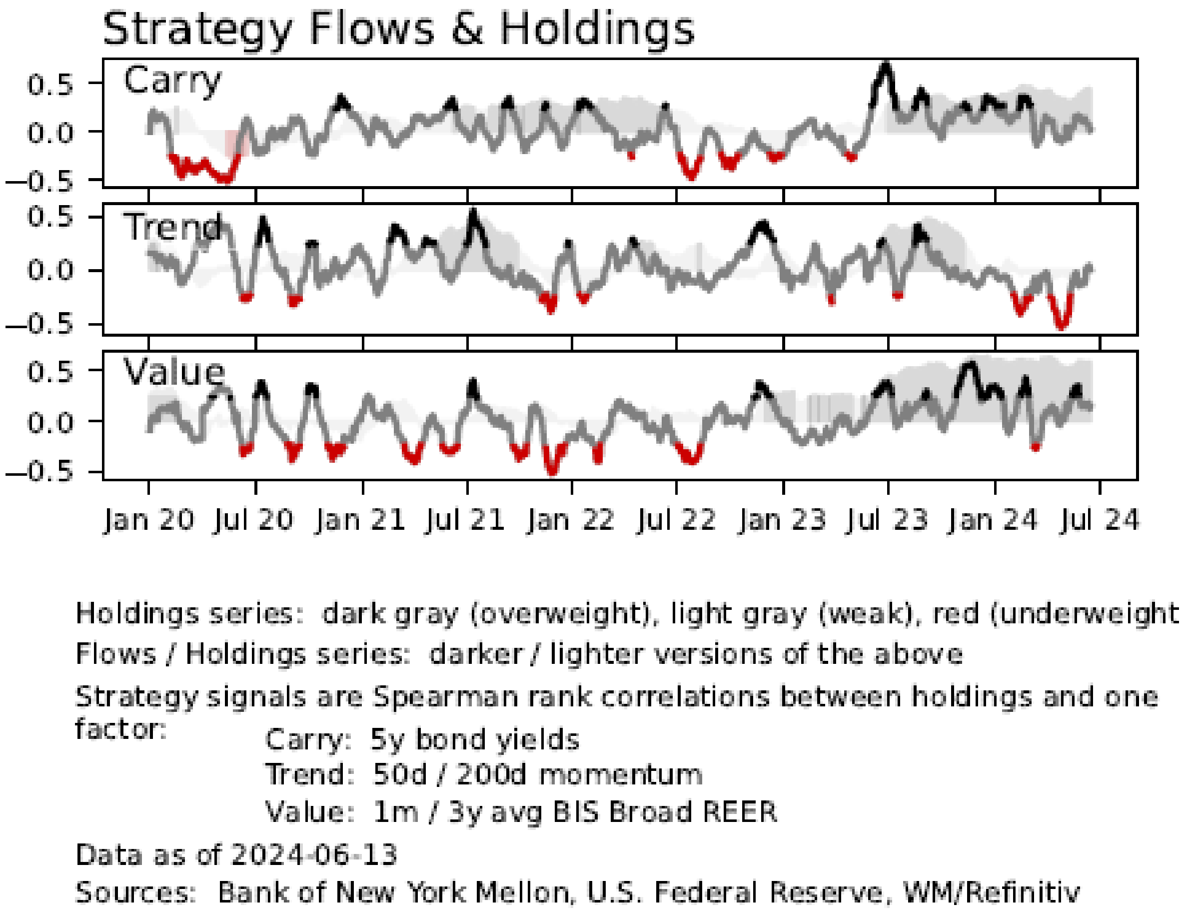
US markets outperform, up for second week led by AI/Tech



Source: Bloomberg, BNY Mellon

- **In Foreign Exchange**, t**he last week saw the USD rally 0.55% on the narrow index** with focus on EUR weakness while CHF, AUD and SEK gained. The role of carry shifted back towards value with ZAR gaining while COP and HUF, CLP and TRY all lost. In iFlow the APAC region remains the most likely to see movement given flows to cover shorts are notable in KRW, HKD, PHP and MYR, while JPY is oversold. In LatAm, Peru is the only standout with MXN and BRL and CLP all long and seeing selling with losses. In the G10, CHF and SEK remain the most likely to see further unwinding of short positions.

FX carry trade drops out



Source: Bloomberg, iFlow, BNY Mellon

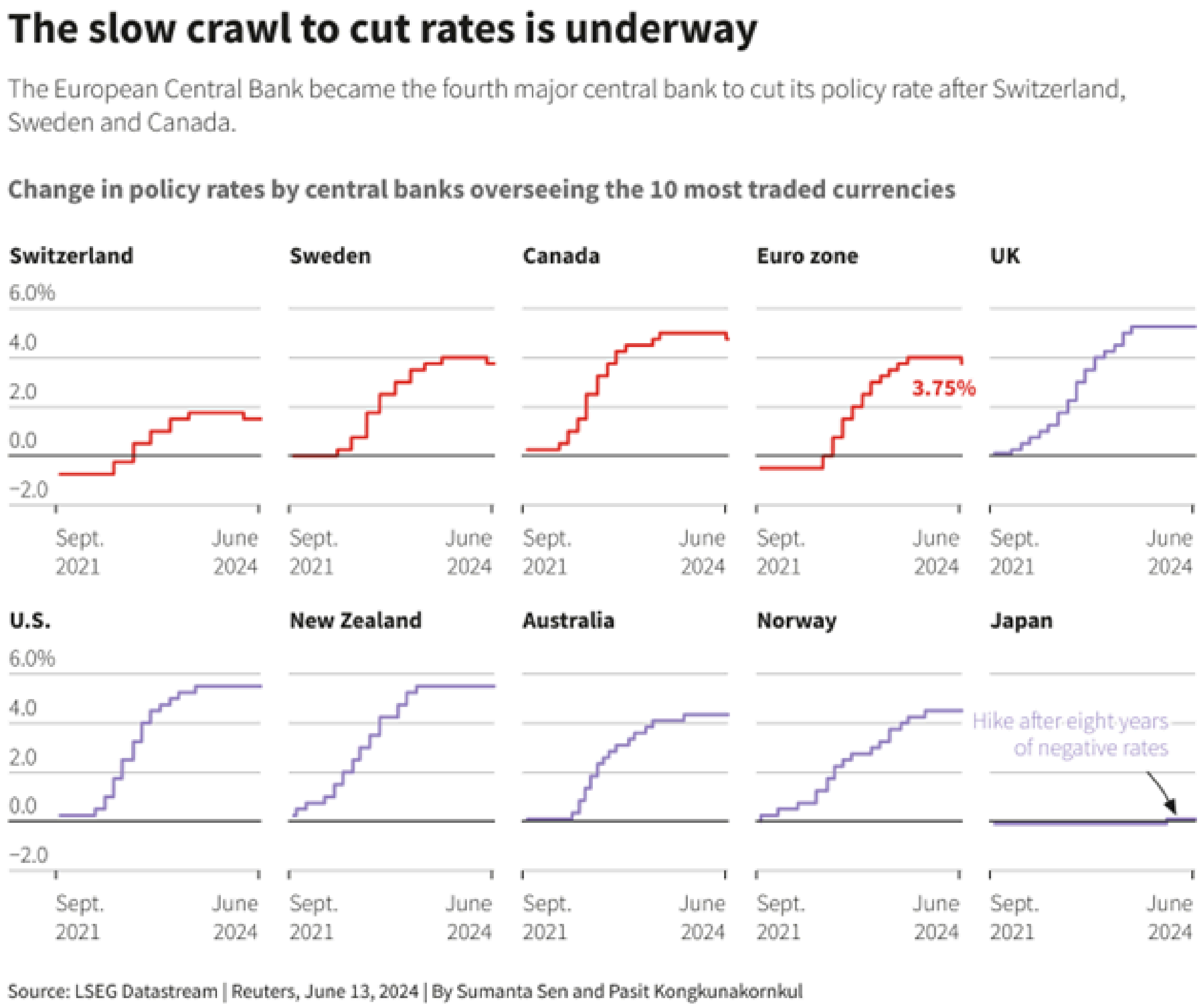
- **In Fixed Income**, US bonds extended the rally from last week, with CPI, PPI and an as expected FOMC delivering enough to push yields towards the lower end of the yearly range with 4.20% a key psychological level. The 25bps drop in 10-year yields didn't provide the relief to EM markets where Chile saw local bond yields 10Y rise 7.5bps, Indonesia 5bps and Turkey jump 42bps. The EM winners were Korea off 15.5bps to 3.28% 10Y along with India off 5bps. In iFlow, the cross-border buying of US bonds stood out beating domestic demand for the first time since August 2023. Flows out of Canada bonds both corporate and domestic stood out as did the reversal of buying in Argentina and Turkey while Korea saw outsized selling with modest corporate buying while China outflows of corporate bonds continued.

News Agenda and Weekly Themes – US retail sales, Central Banks, China Data

In the United States, key economic indicators such as retail sales, manufacturing and services PMI, industrial production, housing starts, building permits, and existing home sales will be closely watched. Additionally, speeches by several Federal Reserve officials will garner significant attention given the wide dispersion of rate paths shown in the SEP. Globally, central bank decisions in Australia, Brazil, China, Norway, Switzerland, and the United Kingdom will be of paramount interest. Manufacturing and Services PMI data will be published for Australia, Japan, India, France, Germany, the Eurozone, and the United Kingdom. In the UK, critical data releases include the inflation rate, consumer confidence, and retail sales figures. Germany's ZEW economic sentiment index will also be a key focus. China will release a slew of important economic data, including industrial production, retail sales, house prices, the unemployment rate, and fixed assets investment. Finally, in Japan, the trade balance and inflation rate will be closely monitored.

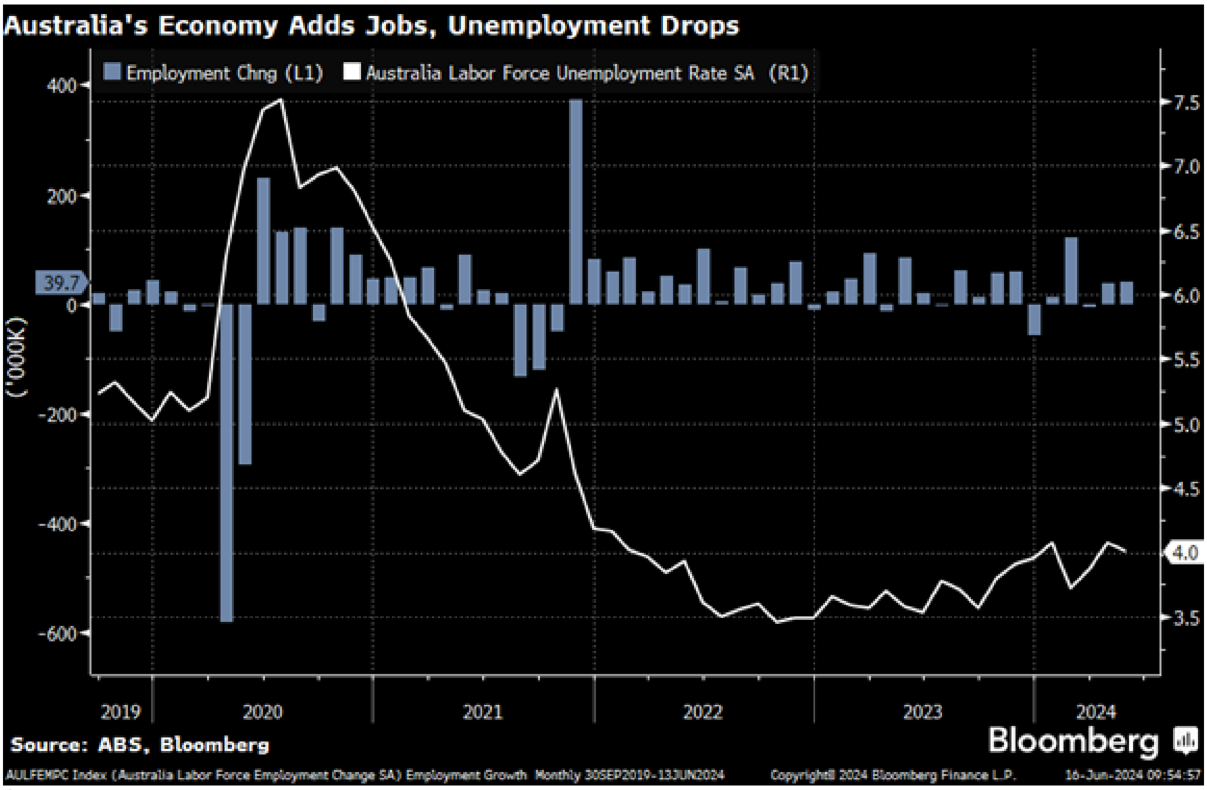
1. More European Central Bank Decisions: Britain, Switzerland and Norway hold central bank meetings on Thursday. The Bank of England will likely dash any hopes the ruling Conservative party had of a pre-July 4 election rate cut – they canceled on the election call any speeches and are pushing to remain neutral in politics. Markets now expect easing later rather than sooner, pricing a roughly 40% chance of an August quarter point move and a 70% chance in September with pay and services inflation sticky. The Swiss National Bank kicked of rate cuts in March. Another cut on Thursday is seen as 50-50 after steady March inflation – many would expect them to hold rather than cut given the push of CHF gains on EU politics. Norway, in no rush to cut rates with core inflation around 4%, releases new economic projections which could make clear an Autum easing start. Australia's central bank meets on Tuesday and is not expected to ease for some time with markets concerned about inflation remaining sticky despite slowing growth.

Will central bank decisions matter?



Source: Reuters, BNY Mellon

2. The RBA and the long wait ahead. June 18th, Tuesday the RBA is expected to leave rates steady at 4.35%. The OIS market has nothing priced and the balancing act of the central bank for jobs vs. CPI is seen as difficult. The government budget for 2024-25 was expansionary adding to RBA troubles with energy relief seen adding to the consumer spending but perhaps temporarily easing energy costs. Non-tradable CPI is still 5.4% - and that is 60% of the total – making the RBA path to easing higher for longer like the Fed. The difference maybe in the guidance as the RBA seems stuck with a longer wait and so no guidance on the path ahead seems most likely. What this does to AUD is not clear as growth seems to matter more than rates given the stall in carry.



Source: Reuters, BNY Mellon

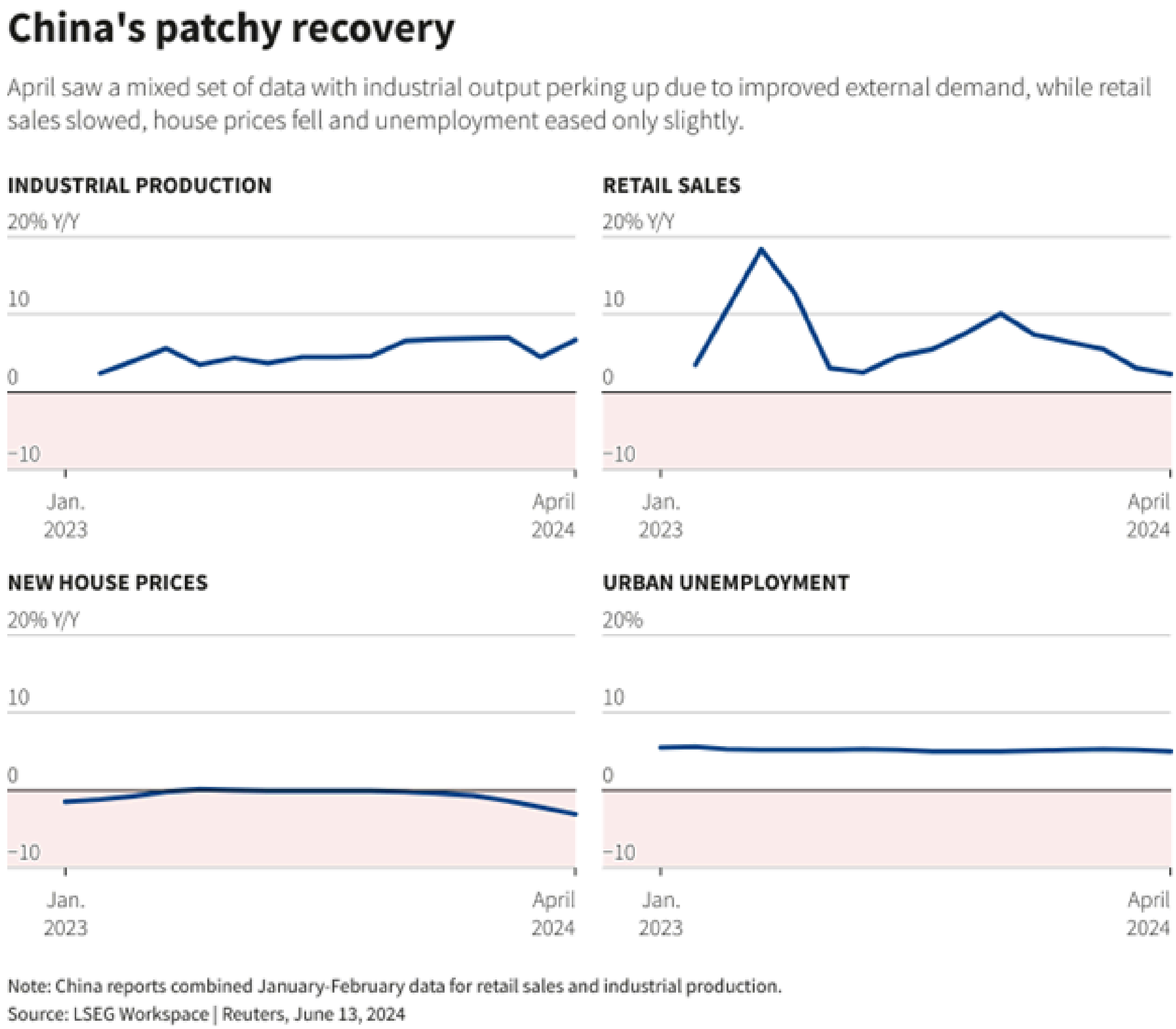
3. **US Retail Sales and the Consumer** - Retail sales are expected to have risen 0.3% in May, according to a Reuters poll of economists, after they were unexpectedly flat in April. This data took on a larger role for investors after the 7-month lows in consumer sentiment shown Friday by the University of Michigan Survey. Many see the slowing US consumer as a warning sign for future trouble rather than a soft-landing necessity. Given the economic data surprises are to the downside, risk of any upside may tilt markets back to higher rates and that might hurt risk more than help it.

The US consumer mood may not match spending?

Source: Bloomberg, BNY Mellon

4. China and the recovery - Data on China's home prices is due on Monday - the first such release after Beijing announced "historic" steps to stabilize the property market last month, though to limited effect so far. Further plans to stabilize property markets seem unlikely. **May** industrial output, urban unemployment rate and retail sales data are all due Monday as well, with hopes the latter could point to a stronger uptick after April's disappointment. Still, recent releases continue to underscore the need for further stimulus from policymakers with the loan prime rate decision due on Thursday. The slowing M2 and weak loan growth are signs of ongoing trouble. Souring trade relations add to the woes, with Europe set to slap extra duties on imported Chinese electric cars.

Will China data surprise to upside?



Source: Reuters, BNY Mellon

Economic Data and Events Calendar June 17-21:

Central Bank Decisions

- **Australia RBA (Tuesday, June 18) –** We expect the RBA to hold rates and the market will remain on edge for a hawkish outcome as the labour market is performing very strongly, led by a surge in full-time jobs growth in May. Considering this happened with higher participation, wage growth risks are clearly to the upside and this has been reflected in upside surprises to CPI figures as well. Markets for now are only expecting the first cut around Q1 next year and there will be little from the RBA tod dispel that.
- **Hungary MNB (Tuesday, June 18) –** The MNB is expected to reduce rates by 25bp to 7%, but as the ECB has already cut rates and the EUR struggling due to idiosyncratic factors, there will be enough room to ease this time around and maintain a comfortable real rate buffer. CEE currencies for now are not under pressure, but markets will probably remain nervous about financial conditions

becoming excessively loose, especially with wages still growing at double-digits on an annualised basis.

- **Chile BCC (Tuesday, June 18) –** A further 25bp cut is expected by the BCC but as this will bring the real rate cushion to around 200bp, we believe the market will start to become wary of further moves, especially if the Fed continues to show deep reluctance towards cutting rates. Furthermore, there is still significant uncertainty over the outlook for commodity prices and terms-of-trade, especially as risk aversion is showing signs of picking up again.
- **Brazil COPOM (Wednesday, June 19) –** No change is expected from COPOM. Given the recent travails of key emerging market currencies, even if it has been due to idiosyncratic risk, we expect central banks in the region to remain extremely cautious, especially with the current Fed path and renewed risk aversion. Brazilian inflation is currently holding at adequate levels – regular prints of 4% or lower should ensure confidence regarding real rate levels. Even so, we doubt COPOM will be counting on strong currency appreciation or better balance of payments support in the near term.
- **Indonesia BI (Thursday, June 20) –** Our biased is for BI to maintain status quo but remain ready to hike again if IDR depreciation momentum were to escalate. Asset volatility and rupiah valuations would be the top focus for the policy meeting, as the central bank recently reiterated the need to give a “strong response” to address uncertainty, though they did refrain from a hike at the May meeting. Heightened vigilance would be needed if there are spillover signs from risk aversion in Europe.
- **Swiss SNB (Thursday, June 20) –** We believe the June SNB decision is finely balanced. The recent pressure on the euro due to esoteric issues will probably just about tip the scales in favour of a cut, but the guidance will certainly be hawkish. This will be reflected in the conditional inflation forecast, which should show significant upward reversions to 1.5% or higher for the coming years, supporting outgoing SNB President Jordan’s recent comments hinting at higher equilibrium rates.
- **Norway Norges (Thursday, June 20) –** The surprise dip in headline CPI for May should not alter expectations too much for Norges to remain on hold for the rest of the year. The currency remains the best-held currency by cross border investors within our flow monitor, though we believe that the central bank will probably leave the door open to easing this year if data continues to soften. Underlying inflation is still running at relatively robust levels and the volatility in inflation and wage figures have made it difficult for Norges to establish a clear trend for policy.
- **UK BoE (Thursday, June 20) –** Due to the upcoming general election, we don’t expect any change in monetary policy. Unlike the last decision during

campaigning season in 2019, a monetary policy report is not due so new inflation is likely to be kept at a minimum. However, a vote will be needed nonetheless, and it would give some indication as to the likelihood of a cut in the first meeting after the vote on August 1st, where there is still an even chance of a cut.

Key data/releases

Date	BST	EDT	Country	Event	Period	Cons.	Prior
06/17/24	00:50	19:50	JN	Core Machine Orders MoM	Apr	-3.00%	2.90%
06/17/24	03:00	22:00	CH	Industrial Production YoY	May	6.20%	6.70%
06/17/24	03:00	22:00	CH	Retail Sales YoY	May	3.00%	2.30%
06/18/24	***05:30***	***00:30***	***AU***	***RBA Cash Rate Target***	***Jun-18***	***4.35%***	***4.35%***
06/18/24	10:00	05:00	GE	ZEW Survey Expectations	Jun	50	47.1
06/18/24	10:00	05:00	GE	ZEW Survey Current Situation	Jun	-64.7	-72.3
06/18/24	10:00	05:00	EC	CPI YoY	May F	2.60%	--
06/18/24	10:00	05:00	EC	CPI MoM	May F	0.20%	0.20%
06/18/24	***13:00***	***08:00***	***HU***	***Central Bank Rate Decision***	***Jun-18***	***7.00%***	***7.25%***
06/18/24	13:30	08:30	US	Retail Sales Advance MoM	May	0.30%	0.00%
06/18/24	14:15	09:15	US	Industrial Production MoM	May	0.40%	0.00%
06/18/24	***23:00***	***18:00***	***CL***	***Overnight Rate Target***	***Jun-18***	***5.75%***	***6.00%***
06/19/24	07:00	02:00	UK	CPI MoM	May	0.40%	0.30%
06/19/24	07:00	02:00	UK	CPI YoY	May	2.00%	2.30%
06/19/24	07:00	02:00	UK	CPI Core YoY	May	3.50%	3.90%
06/19/24	09:00	04:00	SA	CPI YoY	May	5.20%	5.20%
06/19/24	12:00	07:00	SA	Retail Sales Constant YoY	Apr	1.50%	2.30%
06/19/24	12:00	07:00	US	MBA Mortgage Applications	Jun-14	--	15.60%
06/19/24	***22:30***	***17:30***	***BZ***	***Selic Rate***	***Jun-19***	***10.50%***	***10.50%***
06/19/24	23:45	18:45	NZ	GDP SA QoQ	1Q	0.10%	-0.10%
06/20/24	***08:20***	***03:20***	***ID***	***BI-Rate***	***Jun-20***	***6.25%***	***6.25%***
06/20/24	***08:30***	***03:30***	***SZ***	***SNB Policy Rate***	***Jun-20***	***1.50%***	***1.50%***
06/20/24	***09:00***	***04:00***	***NO***	***Deposit Rates***	***Jun-20***	***4.50%***	***4.50%***
06/20/24	09:00	04:00	PD	Sold Industrial Output YoY	May	0.70%	7.90%
06/20/24	09:00	04:00	PD	PPI YoY	May	-7.00%	-8.60%
06/20/24	***12:00***	***07:00***	***UK***	***Bank of England Bank Rate***	***Jun-20***	***5.25%***	***5.25%***
06/20/24	13:30	08:30	US	Initial Jobless Claims	Jun-15	--	242k
06/20/24	13:30	08:30	US	Housing Starts	May	1375k	1360k
06/21/24	00:30	19:30*	JN	Natl CPI YoY	May	2.90%	2.50%
06/21/24	01:30	20:30*	JN	Jibun Bank Japan PMI Mfg	Jun P	--	50.4
06/21/24	08:30	03:30	GE	HCOB Germany Manufacturing PMI	Jun P	46.4	45.4
06/21/24	09:00	04:00	EC	HCOB Eurozone Manufacturing PMI	Jun P	47.8	47.3
06/21/24	09:30	04:30	UK	S&P Global UK Manufacturing PMI	Jun P	51.4	51.2
06/21/24	14:45	09:45	US	S&P Global US Manufacturing PMI	Jun P	51	51.3
06/21/24	15:00	10:00	US	Existing Home Sales	May	4.10m	4.14m

Key speeches/events

Date	BST	EDT	Country	Event
06/15/24	00:00	19:00*	US	Fed's Cook Gives Speech for AEA Summer Program
06/15/24	10:00	05:00	PO	ECB's Centeno Speaks in Dubrovnik
06/17/24	09:00	04:00	EC	ECB's Lane Speaks
06/17/24	18:00	13:00	US	Fed's Harker Speaks on Economic Outlook
06/18/24	02:00	21:00*	US	Fed's Cook Gives Acceptance Remarks
06/18/24	10:00	05:00	EC	ECB's Knot Speaks in Dutch Parliament
06/18/24	13:00	08:00	EC	ECB's Cipollone Speaks
06/18/24	14:30	09:30	EC	ECB's Guindos Speaks
06/18/24	15:00	10:00	US	Fed's Barkin Discusses US Economy, Fed
06/18/24	16:40	11:40	US	Fed's Collins Gives Keynote Address
06/18/24	17:00	12:00	EC	Villeroy speaks in Paris
06/18/24	18:00	13:00	US	Fed's Logan Speaks in Q&A
06/18/24	18:00	13:00	US	Fed's Kugler Speaks on Economy, Monetary Policy
06/18/24	18:20	13:20	US	Fed's Musalem Gives Speech on Economy, Monetary Policy
06/18/24	19:00	14:00	US	Fed's Goolsbee Speaks in Panel Discussion
06/18/24	22:00	17:00	NZ	RBNZ Chief Economist Paul Conway Speaks on Inflation
06/19/24	00:50	19:50*	JN	BOJ Minutes of April Meeting
06/19/24	09:30	04:30	EC	ECB's Centeno Speaks
06/19/24	18:30	13:30	CA	Bank of Canada Releases Summary of Deliberations
06/20/24	09:00	04:00	SZ	SNB's Jordan Speaks After Rate Decision
06/20/24	21:00	16:00	US	Fed's Barkin Speaks on Economic Outlook
06/21/24	08:00	03:00	EC	ECB's Nagel Speaks

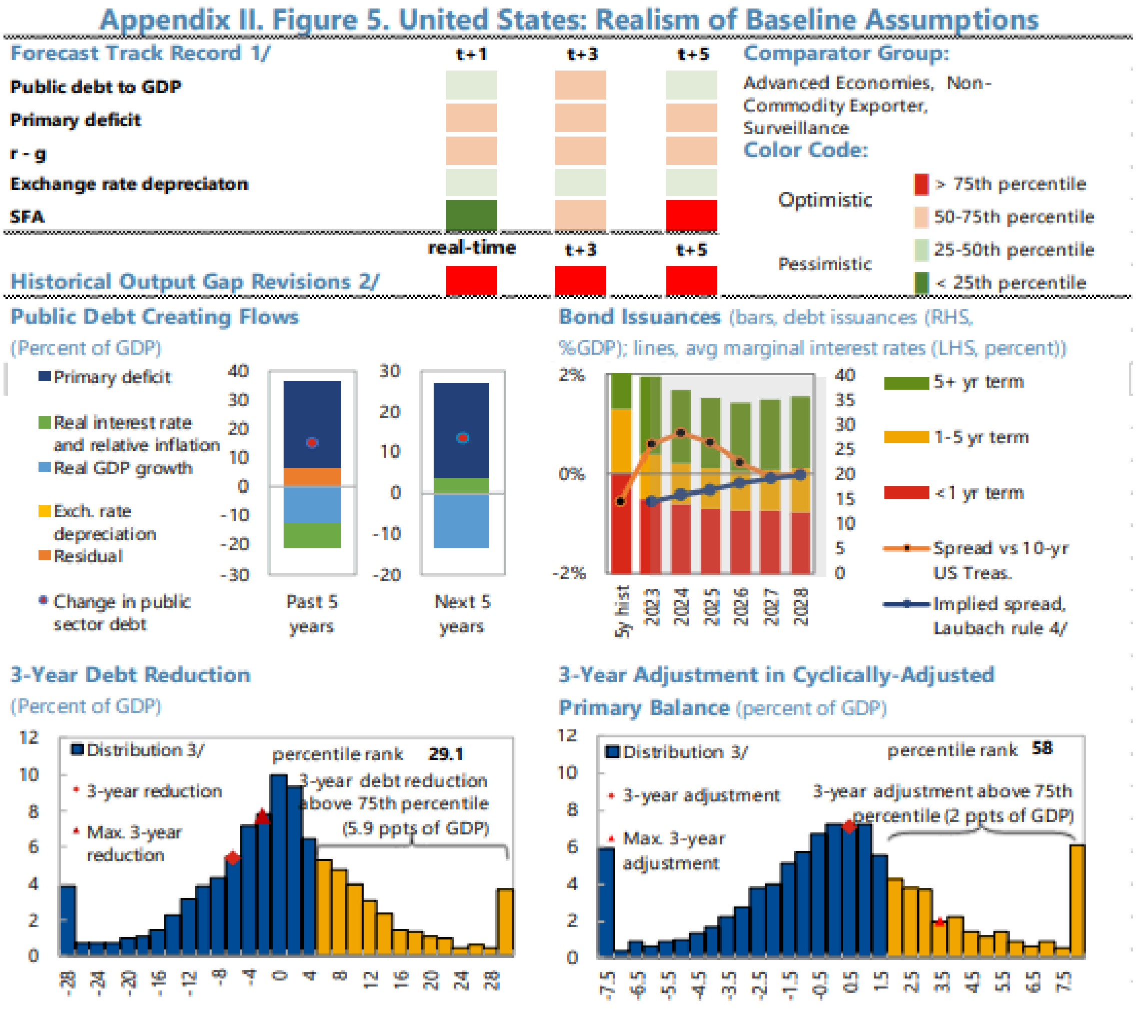
Conclusions: Debt Sustainability?

The IMF article IV review of the US economy found that the US government debt is on a sustainable path. The IMF based its outlook on numerous forecasts including the evolution of inflation, GDP growth, interest rates, and budget deficits. The IMF lack credibility for the accuracy of such forecasts for a period of ten years, much less for thirty years, the horizon over which the US Congressional Budget Office undertakes an analogous exercise and also finds sustainability – which may surprise some of those more doubting about the future. Debt in the hands of the public is currently 100% of GDP – an elevated level by advanced-economy standards, but by no means catastrophic. CBO sees this rising, assuming no changes in prevailing law, to 116% of GDP in 2034, 139% in 2044, and 166% in 2054. Japan has managed to live with such a state for 15-years.

The risks for markets rests as we have seen in the last week around the credibility of the institutions that support debt sustainability – including the central bank, the government finance (Treasury) and the rule of law. The test for the US is around the higher spending on interest payments – driving hard decisions for the government to hike taxes or cut spending or both. The IMF suggestions for fixing the US risks focus mostly on the revenue side – as taxes are seen as low by advance economy standards. One that stands out for the summer ahead is carbon taxes.

The week ahead maybe more about the credibility of governments everywhere in democracies as they face political shifts. The French election made this clear last week, but the risks for Germany and Japan are not yet fully recognized. Similarly, the calm around the US elections seems misguided. Markets are likely to start looking at how the correlation of rates to FX, and how regional FX currencies mix – as the MXN can't weaken over 10% without some effect on CAD and the USD, so too the EUR can't drop without some pressure on NOK, CHF, GBP and SEK. The way markets think about the JPY and KRW and CNY is more organized around their own central bank currency basket approaches. Expect the "safe-haven" status of CHF and JPY and SEK as "low yielder" in the carry trade against "high yielders" like MXN, USD and NZD to be in question as well.

Does the US election matter in the summer trading season?



Source: IMF, BNY Mellon

Disclaimers and Disclosures

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

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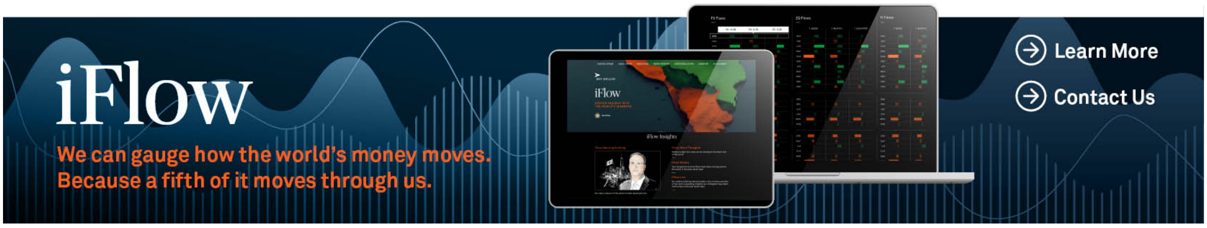

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