WEEKLY UPDATE

Federal Reserve: A pause while waiting for a better inflation climate

The Federal Reserve (Fed) has decided to keep its interest rate policy unchanged while moderating its pace of balance sheet reduction. The Fed's caution is in response to the upward inflation surprises in the first quarter of the year, which has been slower than expected to converge towards 2%. However, we continue to expect the Fed to begin a very gradual rate cut cycle in the third quarter, with inflation and activity expected to moderate gradually.

The Fed is keeping the pause. As anticipated by the markets, the Fed kept its monetary policy range at 5.25%-5.50%, thus maintaining its key rates at this level since August 2023. The small surprise of the meeting came from its balance sheet policy, as the Fed decided to reduce its Treasury runoff pace from USD 65 billion per month to USD 25 billion. While markets were expecting a change in tone from the Fed given the acceleration of inflation in the first quarter and a potential talk of a scenario of renewed rate hikes, Mr. Powell maintained a balanced or even slightly dovish tone. Indeed, while acknowledging that the latest inflation figures show "it's going to take longer to gain confidence" that inflation is converging towards the 2% target, Powell specified that his three scenarios are those of i) a rate cut due to lower inflation, ii) a rate cut due to a deterioration in employment and iii) rates remaining at current levels. He reiterated that financial conditions remain restrictive.

Inflation surprises linked to housing prices and micro factors. While markets were expecting a sharp rate cut cycle in January, the acceleration of core inflation in the first quarter to 3.7% QoQ effectively pushed back the timing of rate cuts and called into question the possibility of such cuts. However, we believe that this figure does not call into question the disinflationary dynamic. Indeed, on the one hand, the acceleration in inflation corresponds to the sharp increase in January, the result of strong seasonal adjustments. Inflation in February and March showed a slow normalisation. On the other hand, housing prices continue to help keep inflation high. This market remains tight due to demographics and low pressure to sell in a fixed-rate environment. Nevertheless, we do not expect a further acceleration in prices in this sector.

A rebalancing of the labour market and a slowdown in activity support the rate cut scenario. Mr. Powell's press conference, and our scenario of a gradual slowdown in inflation and activity, maintain our scenario of the beginning of the rate cut cycle in Q3-24. First, the labour market continues to rebalance, with the number of unfilled positions and of resignations decreasing and now close to their 2019 levels. On the other hand, wage growth continues to moderate, including in the services sector, pointing to a further moderation in inflation and consumption. Finally, in a context of a real rate of 2.8% and the Fed's dual employment-inflation mandate, a start of the easing cycle seems justified.

Inflation continues to slowly moderate

Wage pressures are also moderating

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Past performance should not be seen as a guarantee of future returns.
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Our Macro Comments

Events of the week

Activity in the Euro area surprised the consensus on the upside in Q1, with euro area GDP rising by 0.4% over the year and 0.3% over the quarter, against expectations of 0.2% and 0.1% respectively. This slight improvement was mirrored in the continent's main economies, which all beat expectations, with French, German, Italian and Spanish GDP rising by 0.2%, 0.2%, 0.3% and 0.7% respectively over the quarter - even if the details in terms of growth drivers were more mixed. Overall, these data confirm the slow recovery in activity in the Euro area.

Meanwhile, inflation data for the euro area confirms that the return to the 2% target will be slow. Headline inflation was 2.4% over the year in April, unchanged from March, as the fall in energy prices slowed. Core inflation eased to 2.7% over the year (against 2.6% expected), from 2.9% in March, thanks to the continued fall in non-energy goods inflation (0.9% over the year) and the first weakening in five months in services inflation (to 3.7% from 4% previously). Inflation is not falling at the same rate in all Euro area economies, with prices rising by 2.2% in France and Germany, compared with 0.9% in Italy and 3.3% in Spain. This data puts the ECB in a comfortable position to consider cutting rates in June.

The week in data

Country	Data	Actual	Last	Forecast
Germany	Unemployment Rate APR	5,90%	5,90%	5,90%
Germany	GDP Growth Rate YoY Q1	-0,20%	-0,20%	-0,20%
United States	ISM Manufacturing PMI APR	49,2	50,3	50
United States	Fed Interest Rate Decision	5,50%	5,50%	5,50%
United States	Unemployment Rate APR	3,90%	3,80%	3,80%
United States	Average Hourly Earnings YoY	3,90%	4,10%	4,00%
France	GDP Growth Rate YoY Q1	1,10%	0,80%	0,90%
France	Inflation Rate YoY APR	2,20%	2,30%	2,10%
Switzerland	Inflation Rate YoY APR	1,40%	1,00%	1,10%
Euro Area	GDP Growth Rate YoY Q1	0,40%	0,10%	0,20%
Euro Area	Inflation Rate YoY APR	2,40%	2,40%	2,40%
Euro Area	Core Inflation Rate YoY APR	2,70%	2,90%	2,60%

Source : Macrobond, on the 3rd May 2024

Colors in 'Actual' column represent the difference with previsions.

Key events next week

Monday	
China	Caixin Composite PMI APR
Italy	HCOB Composite PMI APR
Euro Area	PPI MAR
Tuesday	
United Kingdom	BRC Retail Sales Monitor APR
Euro Area	Retail Sales YoY MAR
Wednesday	
Germany	Industrial Production MAR
Thursday	
United Kingdom	BoE Interest Rate Decision
Friday	
United Kingdom	GDP Growth Rate Q1
United Kingdom	Industrial Production MAR
Saturday	
China	Inflation Rate APR

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Market Performances

Interbank rates	Last.	-1W	-3M	YTD	-12M
€STER O/N	3,89	3,91	3,89	1,90	2,90
USD SOFR O/N	5,32	5,31	5,32	4,31	4,81
JPY TONAR O/N	0,08	0,08	-0,01	-0,02	-0,07
GBP SONIA O/N	5,20	5,20	5,19	3,43	4,18
CHF O/N	1,34	1,36	1,62	0,00	0,80

Long term sov. rates	Last.	-1W	-3M	YTD	-12M
10Y OAT	3,08	3,11	2,65	2,90	2,83
10Y Bund	2,58	2,58	2,15	2,39	2,25
10Y BTP	3,92	3,97	3,72	4,49	4,12
10Y JGB	0,87	0,88	0,70	0,41	0,40
10Y Bonos	3,36	3,38	3,14	3,44	3,31
10Y Swiss	0,69	0,72	0,83	1,46	1,03
10Y Gilt	4,36	4,32	3,87	3,63	3,69
10Y USTnote	4,63	4,65	3,99	3,79	3,38

Credit & EM	Last.	-1W	-3M	YTD	-12M
EUR Corporate Aaa	3,27	3,24	2,81	3,12	3,22
EUR Corporate Baa	4,07	4,04	3,76	4,65	4,41
GBP Corporate Baa	4,99	4,94	4,54	4,59	4,75
USD Corporate Aaa	5,12	5,14	4,55	4,62	4,19
USD Corporate Baa	5,88	5,90	5,33	5,70	5,34
USD EM aggregate	7,42	7,40	7,14	7,52	7,26

Commodities	Last.	-1W	-3M	YTD	-12M
Brent, USD/BL	83,55	-5,1%	3,6%	-2,8%	16,3%
Or, USD/oz	2 318	0,1%	13,7%	26,9%	13,7%
Copper, USD/metric ton	9 894	1,1%	14,8%	17,8%	16,2%
Platinium, USD/oz	936	1,8%	1,0%	-12,1%	-12,5%
Palladium, USD/oz	938	-8,3%	-4,6%	-47,5%	-34,7%
Silver, USD/oz	26,48	-2,4%	14,7%	10,6%	4,9%

FX rates	Last.	-1W	-3M	YTD	-12M
EUR/USD	1,07	0,3%	-1,1%	0,3%	-2,9%
EUR/CHF	0,98	0,5%	5,3%	-0,5%	0,1%
USD/GBP	0,80	-0,4%	1,9%	-3,6%	0,3%
USD/JPY	157,66	1,7%	7,8%	20,5%	16,7%
USD/BRL	5,20	0,6%	5,1%	-2,7%	3,7%
USD/CNY	7,24	-0,1%	2,1%	5,0%	4,8%
USD/RUB	93,51	0,4%	4,2%	28,1%	17,6%

Equity indices	-1W	-3M	YTD	-12M
Developped markets	-0,9%	2,7%	11,5%	11,3%
Euro area	-1,4%	5,9%	26,8%	14,2%
Germany	-0,9%	6,1%	26,4%	13,4%
France	-1,3%	4,3%	20,5%	7,8%
United Kingdom	1,0%	6,4%	7,5%	4,3%
Switzerland	-1,0%	-0,6%	2,6%	-2,1%
United States	-1,0%	3,6%	31,2%	22,7%
Japan	0,7%	7,0%	44,3%	31,5%
Brazil	0,9%	-1,4%	20,9%	23,7%
Hong Kong	3,3%	14,7%	-11,8%	-9,8%
India	0,9%	3,8%	21,5%	21,7%
China	2,4%	12,1%	-7,3%	-10,5%

Source: Bloomberg, on 03 May 2024, 1W = 1 week change, 3M = 3 month change, 12M = 12 month change, YTD = year to date change. Equities; total return in local cu rrency. Government bonds = 10 year returns. Figures are rounded..

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