Goldman Sachs The Markets
A market friendly data print— for now
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Sam Grobart, Host
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Sam Grobart: The latest inflation data just came in. And it has everyone wondering, what will the Fed do next? This is The Markets.

Hi, I'm Sam Grobart. Today I'm joined by Anshul Seghal, head of US interest rate products trading in Global Banking & Markets. Anshul, thanks so much for joining us today.

Anshul Seghal: Thank you for having me.

Sam Grobart: So, at the time we're recording, we just heard the recent consumer price index number, it came in as expected, 3.4, down from 3.5 percent in March. The core number, 3.6, down from 3.8. What's your big takeaway from this latest data?

Anshul Seghal: I think it was as very helpful data print for market and the Fed. Going into this number, what the market was worried about is after a string of three really hot CPI prints earlier this year, if you were to get another hot print, it would put into question if or when the Fed would actually embark on a cutting cycle.

Sam Grobart: Or a hiking cycle.

Anshul Seghal: Exactly. There were voices on the committee that basically thought that the next Fed move should be a hike. The fact that this number was friendly for what the Fed's trying to achieve, essentially was very helpful for markets as well. So, you saw all assets do well. And again, it's just one data print. And one data print doesn't make a trend. So, we'll see where this goes. But so far, so good.

Sam Grobart: Well, I want to ask you about the market reaction. Of course, markets have been sort of champing at the bit for this kind of number to come in. Now that it has arrived, how are they responding to that data?

Anshul Seghal: As I said, there's a sense of relief. Again, one print does not make a trend. And we did have three hot prints. So, Powell spoke yesterday. He was very clear you want to see a string of lower CPI prints or low PCE inflation prints for the Fed to basically get comfortable with the idea of cutting rates.

The problem that markets had going into this print, which made everything all the more jittery, was that late last year, in Q4 of last year you had very, very low CPI prints and PCE prints. So, the year-on-year inflation with the passage of time, as those prints drop out of the year-on-year computation, it's entirely conceivable that the trajectory of inflation might actually look like it's going up again.

So, the Fed does not cut in the summer months, the window for them to cut sort of shrinks materially. And therefore, the market really wanted a weak print. Or at least not a strong print on inflation this time. And the market got that.

Now, if this continues, I think everything's fine, everything's on track. Market and the Fed feel like we have a handle on the economy. And you should see risk assets being supported. You should see the Fed cutting two to three times this year. All of that.

Should that not happen, then the Fed has to make an assessment whether the next move is a hike or a cut. Today's print, obviously, nudged us away from the next move being a hike. Only time will tell where we end up.

Sam Grobart: So, alongside that we've been seeing some movement this week in treasury yields. And I wanted to know what's behind those moves and where do you see yields headed?

Anshul Seghal: The million-dollar question. Let's see. So, again, when we got the hot CPI print and the hot data earlier this year, treasury yields actually went up a lot. Now the perception in markets was that the tightening of monetary policy hadn't really had as much of an impact on the real economy as people, including the Fed, had hoped.

Sam Grobart: Job markets stayed hot.

Anshul Seghal: Job markets. Hot.

Sam Grobart: Consumer spending was hot.

Anshul Seghal: U rates very low.

Sam Grobart: Right.

Anshul Seghal: The unemployment rate's very low. All of it. And it put to question, like, exactly is the US economy completely interest rate insensitive? If that's the case, the Fed could take rates any way, it just wouldn't have much of an impact. Obviously, we've all spent the last three years dusting off what happened in the early '80s and late '70s when Volcker hiked all the way to 11 percent. The question was, like, are we on a similar path at this point in time?

And markets were very anxious about that. So, you got a big sell off in rates. And all that's happened in the last month or since the beginning of May, it's still a very robust number, but we got a relatively weaker payroll print. Sentiment data. The ISM surveys were on the weaker side. If you look at consumer staples earnings, at least the guidance was on the weaker side. Like, the market was expecting that the consumers' excess savings have eroded and at this point in time that, like, maybe we're coming more into balance, which is our view, which is Goldman's view, that the economy was offsides. It was very hot. And we're on the soft-landing approach.

Sam Grobart: Trajectory.

Anshul Seghal: Trajectory. And we're moving along that direction. Though other people were more worried about the tail risk of a recession.

But all said, like, the rally in rates we've seen over the last three to five weeks has been mainly driven by that market getting comfortable that there wasn't as much of an imbalance. Or if there was, we're moving back to a more equilibrium state.

Sam Grobart: We're talking about the US, and as far as rates, that remains a bit of a guessing game. It looks like there's increasingly likelihood that the Bank of England may cut rates as soon as June. What's going on in that country that's driving that earlier move?

Anshul Seghal: So, it's really fascinating. It's not just the Bank of England. If you look, the Bank of Canada wants to start a cutting cycle. The ECB wants to start a cutting cycle. And, of course, as you highlight, the BOE wants to start a cutting cycle in June.

If you look at global growth over the last 12 months, the United States in DM economies, developed market economies, the United States sticks out. United States has had off the charts real growth.

Sam Grobart: Ridiculous performance.

Anshul Seghal: But everyone else has had very middling real growth. It's an open question where the divergence is coming from. It's likely some combination of a lot of fiscal expansion in the US relative to these other domains. Immigration being very high in the US, which actually leads to higher nominal growth, higher real growth as well versus all of these domains. The US economy being relatively interest rate insensitive, that's probably a big part of this.

The situation in the UK is it's just a very difficult market to read at this point in time. They've had very forward unemployment rates. The unemployment rate actually went up by more than the market expected. But at the same time, wage growth was very high. It's north of 5 percent. So, it's hard to reconcile that. It's hard to reconcile how the consumer is doing in the current environment.

The fact that the Bank of England hiked as much as it did, that their funds rate is higher than what it is in the United States essentially makes them a little nervous and they want to basically be ahead and start a cutting cycle for fear that if they don't, they might be too late. So, it's very difficult to get a read.

Sam Grobart: Final question. What's going to be on your radar for next week?

Anshul Seghal: It should be a quiet week in terms of market data. We have auctions in the US treasury market. You have the twenties and then the TIPS auction. But by and large, the next big data print that the market's looking to is the next payrolls report. We had a relatively weaker payrolls report, it's up 200K job gains, followed by two ISM surveys that were weaker and a retail sales report today that was quite meaningfully weak.

The big question is, is the consumer rolling over? Is the consumer much weaker today than he or she was as little as six months ago? So, if the consumer is, indeed, weaker, then there are follow through effects. That lack of consumption can feed into essentially corporates not doing well and therefore job losses and then it feeds off of itself.

Are we at the precipice of that cycle starting? And I think the jobs number matters a lot for the market to basically establish whether that's the case or not? So, the next big data print's going to be early next month. And then it's about the next CPI print.

Sam Grobart: Anshul, thank you so much. This was great.

Anshul Seghal: Thank you for having me.

Sam Grobart: That does it for another episode of The Markets. Be sure to find us on Apple Podcasts, Spotify, or wherever you get your podcasts.

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