Natasha Tiwana: The ECB says its policy path is wide open, so what does that mean for investors? This is The Markets. I'm Natasha Tiwana with Goldman Sachs Research, and I'm joined by Gurpreet Garewal, a macro strategist on the Fixed Income team in Goldman Sachs Asset Management.

Let's start with the ECB decision. After a rate cut in June, they're keeping the benchmark at 3.75%, and ECB President Lagarde says the data will determine what they do in September. So what do you make of her comments?

Gurpreet Garewal: Hey, Natasha. First of all, great to be with you. And yeah, like you said, as expected, the ECB kept policy unchanged, but what was really key from this meeting is what clues we could gain for the prospect of a second ECB rate cut in September, following the initiation of the easing cycle back in June. And on that front, we think the ECB's assessment of the economy is consistent with a September cut. The central bank thinks data is evolving as expected. They noted that the board process of disinflation is still on track. They also seem to downplay recent strength in inflation and wage growth and also emphasize that the catch-up that we've seen in wage

growth through the new inflation regime should start to subside going forward.

Now, they didn't explicitly commit to cutting in September, but today's assessment of the economy aligns with what our European economist Federico Torracchi has also been saying. And he's highlighted a couple of other things that I would note that are supportive of steady easing. For example, inflation expectations are still anchored, the breadth of price rises is narrowing, and energy fuel and goods inflation are still in check as well.

Natasha Tiwana: And focusing in on that inflation question, what do you expect for inflation data through the rest of the year? As we know, some prints tend to be quite volatile. Do you see any risks for upside surprises to distort the rates path from here?

Gurpreet Garewal: Yeah, that's a great question. In investing and economic forecasting, there is no absolute certainty. Variables that impact the economy and inflation can change, and we're always thinking in scenario terms. And right now, one risk scenario that we're particularly attentive to is persistence in services inflation, and that

could impact the overall inflation reading and delay the next ECB cut. And broadly speaking, there's two key reasons for that. The first is tourism, and the second quite simply is Taylor Swift.

So on the tourism front, we may have seen investors being a bit more cautious on European assets around political uncertainty, but consumers are still very constructive or bullish on Europe's beaches holiday spots. And that's pushing up prices for things like hotels.

And then on the Taylor side, we've seen a new sort of Taylor Rule of late. The conventional Taylor Rule in economic thinking guides policy rates based on what's happening in inflation and economic conditions. But lately we've seen this concept of Swiftonomics, so the influence of concerts on activity due to direct spending on tickets and merchandise but also indirect spending on things like hotels, dining, and retail. And that holds true in economies like the UK as well as the euro area. And we are very mindful and attuned to the fact that tourism and live events like concert tours but also sporting events could keep services inflation elevated. And I think the key question to monitor and the key thing to watch is are these

impacts persistent or are they temporary, meaning central banks can shake it off as a summer blip?

Natasha Tiwana: I like that. Digging into what we're seeing in early market reactions, the euro's showing some weakness. What do you make of this? And how do you think investors are interpreting the meaning?

Gurpreet Garewal: Yeah, like you said, the euro is a bit low. We've also seen rates rally a bit. And that seems intuitive with raised confidence in prospects for a September ECB rate cut. But I'd also note some of those news may reflect softer labor market data that we've had come out of the US today with jobless claims ticking higher.

In terms of what this means for markets more broadly, I would emphasize that the fact that we are in an easing path for the euro area policy does lead us to stay underweight the euro. And then against that backdrop of easing, we think it still opens up interesting opportunities in European credit markets. We see opportunities in investment [UNINTEL] but also the European high-yield bond market, which is higher quality today than it was in

the past. And there's lots of dispersion there, which is fertile investing ground for active investors like us.

Natasha Tiwana: And on a more general longer term view for the outlook for the markets, how are you thinking about monetary policy paths across DMs and how that will influence risk assets?

Gurpreet Garewal: Yeah, look, big picture, I'd say bonds are still in their comeback era. And if you stick to Europe a few years ago, billions of dollars of bonds were trading with negative yields, meaning investors had to pay certain governments and certain companies to lend to them. Today, that backdrop is materially different, and it's significantly promising for investors. So easing means bond yields lower, bond prices higher, so very positive for bond investors.

But it also highlights that there is no one-size-fits-all approach to easing actions. Like we said, the ECB's on track for a course [UNINTEL]. We think the Bank of England is going to begin cutting rates next month considering a softer labor market and disinflation progress, even though it's been bumpy. In the US, we think the

latest jobs, inflation, and policymaker signals all suggest a September cut is on the horizon. Down under in Australia, we've seen actually very hot inflation and labor market prints. That suggests the Reserve Bank of Australia is unlikely to cut rates anytime soon. And this divergence is paving way to really interesting cross-market interest rate opportunities for investors.

Natasha Tiwana: Final question, what's on your radar for next week?

Gurpreet Garewal: There's three key things that we're watching next week -- the economy, the policy picture, and company earnings for the second quarter. On the economy, I'd highlight one notable data point, which is US PCE inflation. This is the Fed's preferred measure of price rises, and it's [UNINTEL] 2.6%. So we'll have to see if it follows in the footsteps of recent CPI data in moving in the right direction.

On the policy front, we get the Bank of Canada meeting. We think that they are on track to become the first developed market central bank to cut rates at consecutive meetings. If it does so, that would benefit how we're

positioned, and this speaks to the earlier point that I made about no one-size-fits-all approach to easing cycles.

And then lastly, on corporate earnings, as credit investors, we're really focused on are companies still in good financial health in order to service their debt?

Natasha Tiwana: Gurpreet, thanks so much for being here today.

Gurpreet Garewal: Of course. Thank you for having me.

Natasha Tiwana: That's it for this week's episode of The Markets. I'm Natasha Tiwana, and thanks for listening.

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