



AFS Insights

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Headline Sweep

- Johnson Moves From Playing G-7 Host to Bearer of Bad Covid News
- G-7 Haggles Over Strong U.S. Push to Counter China's Clout
- Blinken Says Biden-Putin Meeting Isn't 'Light-Switch' Moment
- Putin Sees Chance to Work With Biden at Low Point in Ties

The Week Ahead: the Fed and Putin

- **Unlike the ECB, Wednesday's Fed meeting probably will *not* be a snooze fest and the outcome is certainly no done deal.** We see four moving parts: the QE guidance; the dot plot; technical tweaks to interest rates and/or standing facilities to counter some of the (excessive) downward push on money market rates; and tolerance of inflation.
- **Starting with QE, several Fed-speakers – including key players such as Vice Chair Clarida – have suggested the FOMC ought to “talk about talk about” tapering sooner than later.** Our interpretation of those remarks is that the bar for labor market gains has been lowered a tad so that they can have this conversation this week. We expect language along the lines that if payrolls continue to print around current levels in the next several months (500k), a taper announcement will be likely later this year (in September). Alternatively, Powell & Co could make the taper hint less obvious. Take Chair Powell's guidance from the April press conference: it is going to take “some time” before we see “further substantial progress” in the labor market. Such progress would justify tapering. With different language, Powell & Co could shorten the time frame or simply state that less progress is needed (i.e. further progress instead of further substantial progress). Alternatively, they could decide to keep everything in place. After all, Powell himself didn't join the 'talking about talking about' chorus and there's no majority of Fed-speakers having made remarks along those lines. In any case, we've been making hawkish calls, and expect the aforementioned taper warning. Our reading of the tealeaves is that the market only expects some tinkering with the language (i.e. further progress instead of further substantial progress).
- **The dot plot could be a big headache for Powell, who is loath to discuss rate hikes.** At the March meeting we had 7 dots consistent with a hike in 2023 while 11 were still at zero. The contingent calling for a 2023 has been increasing steadily since the December meeting. Thus, the infamous 'median' dot is in the balance. Powell's heart is definitely not with a 2023 hike, so, it's going to be interesting if he will have to explain away half his contingent of colleagues.

- **Regarding technical tweaks, sell-siders have made countless of calls on the Fed doing something about taking away the risk of overnight rates dipping consistently below zero.** The most obvious candidate is a ‘technical’ hike of the administered rates (overnight reverse repo and the interest on excess reserve rates of 0 and 10bps, respectively). The Fed could also expand the counterparty list for the reverse repo facility, hold term reverse repos, reinstate banks’ reserve requirements or even ‘twist’ its portfolio of bond/bill holdings. However, despite all the doom the Fed’s floor at zero has been holding up remarkably well. Thus, we expect no change here.
- **Finally, on inflation we can be brief.** We’re simply checking for stronger language that the Fed won’t become overly tolerant of inflation. Seeing the recent declines in breakevens and inflation-linked swap rates, things have been going the Fed’s way. However, it’s still something to keep an eye on as it will limit the Fed’s room for maneuver to create a hot labor market like we had on the eve of the pandemic.
- **ECB-speak is also set to resume in full force following Thursday’s snooze fest of a meeting.** From the ubiquitous ECB sources we learned that just three hawks pushed for curtailing pandemic QE purchase volumes at last week’s meeting. By September, they will probably have won enough converts to dial down purchase volumes. But now is just too soon for the ECB to engage in taper talk. In any case, we’ll be scanning ECB-speak for hints about TLTROs, tiering and teaser rates. If we read the tealeaves correctly, some (French Governing Council member Villeroy de Galhau) believe the teaser rate is being misused for arbitrages. But President Lagarde didn’t seem worried when she dubbed arbitrages a “tactical approach” undertaken by Dutch and German banks.
- **Besides the Fed, three other central banks in our universe will announce rates this week: Norges Bank and the Swiss National Bank on Thursday; and the Bank of Japan on Friday.** We can be very brief about the SNB, which is still confronted with the same old problems: an overvalued exchange rate, barely any inflation and unable to match the ECB’s ever-increasing balance sheet. Thus, the meeting should be a hold with no change in tone or guidance.
- **The Norges Bank should be hawkish in the sense that consensus expects the central bank to lay the groundwork for a September hike.** An autumn rate hike should be reflected in the rate path and justified by a stronger than expected bounce-back in the economy.
- **Finally, we can conveniently gloss over the Bank of Japan meeting.** Consensus simply expects no change. But that should surprise no one.
- **Besides central banks, there also much in the way of geopolitics.** President Biden will join his first NATO meeting in Brussels today. On Wednesday he will meet the world’s evil mastermind, Russian President and master strategist Vladimir Putin (that’s sarcasm). Ahead of the meeting both sides have admitted that relations are at their lowest points in decades. And both men have a mutual dislike of each other. And both sides are engaged in asymmetrical warfare (Russia with cyber attacks and other subterfuge, the US with NATO encroachment. And by the way, does the West do cyber-attacks? Inquiring minds want to know). Our reading of the tealeaves is that President Biden at least wants to make sure things don’t get worse from here with the Russians. The US simply can’t afford to be at loggerheads with both of the world’s bogeyman: Russia and China. What will be Putin’s price for freezing the current situation?

Calendar

TIME	REGION	EVENT	PERIOD	CONSENSUS	PRIOR
09:00	Turkey	Current Account Balance	Apr	-2.20b	-3.33b
10:00		SNB Domestic Sight Deposits CHF	Jun-11	--	632.2b
10:00		SNB Total Sight Deposits CHF	Jun-11	--	710.8b
11:00	Eurozone	Industrial Production SA MoM	Apr	0.40%	0.10%
11:00	Eurozone	Industrial Production WDA YoY	Apr	37.30%	10.90%
11:30	Germany	Sells EUR 4 Bln of 182-day Bills (DE0001030328)			
12:00	Portugal	CPI EU Harmonized YoY	Jun F	--	0.40%
14:50	France	Sells Up to 1.7 Billion Euros 154-day Bills			
14:50	France	Sells Up to 2.8 Billion Euros of 91-day Bills			
14:50	France	Sells Up to 1.6 Billion Euros 336-day Bills			
14:50	France	Sells Up to 400 Million Euros 280-day Bills			
15:00		ECB's Schnabel Speaks			
15:00		BOE's Bailey at Conference			
15:00		Riksbank's Floden Speaks on Swedish Financial Stability			
15:45		ECB Weekly QE Overview			
		Bank of France Industrial Sentiment	May	108	107
		NATO Summit in Brussels			

Consensus data: Bloomberg News; All Times Are in Central European Time

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