

Morning Market Tidbits

(Greater) confidence is everything

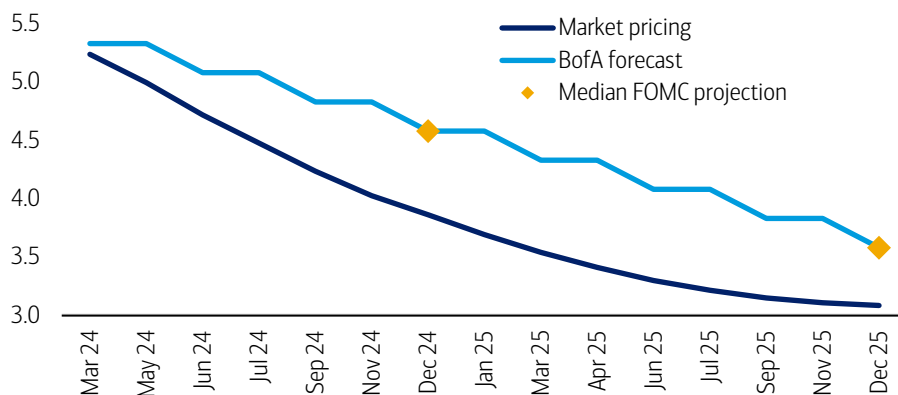
In focus

In our latest [US Economic Weekly](#), we review the recent FOMC meeting and our forecast change for the first rate cut. Chair Powell stated that a March rate cut is unlikely because the Fed probably won't be sufficiently confident that inflation is returning to target. We think the Fed has created considerable ambiguity about its reaction function. Still, we take Powell's message on board: we now expect the Fed to start cutting at a quarterly cadence starting in June instead of March. We also expect the QT taper to start in March. The Fed managed to push back against the timing of the first cut but not the pace of cuts. Markets are pricing a policy error: roughly six cuts this year.

In our latest [Global Economic Weekly](#), we discuss the guidance from the January FOMC meeting and the inflation risks ahead. The Fed's message was clear: we need to see more data to confirm the disinflation process is sustainable. While immaculate disinflation is the baseline scenario for the market, we take a look at upside inflation risks in the US. A reacceleration of inflation is still the most underpriced risk for an economy where final demand grew at 3% in 2H23.

Exhibit 1: Market pricing of Fed policy rates vs. BofA forecasts and dot plot projections

Markets are pricing roughly six rate cuts this year



Source: BofA Global Research, Bloomberg, Tullett Prebon

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(Continued on next page)

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GDP: Gross Domestic Product

FOMC: Federal Open Market Committee

ECB: European Central Bank

BoJ: Bank of Japan

NIRP: Negative Interest Rate Policy

YCC: Yield Curve Control

QT: Quantitative Tightening

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Market Action

The Asian equity markets that we cover closed mostly negative overnight. Looking at individual markets, the Shanghai Composite, the Korean Kospi, the Indian Sensex and the Hang Seng fell 1.0%, 0.9%, 0.5% and 0.2% respectively. On the flipside, the Nikkei rose 0.5%.

As of 7:00 am ET, aggregate European stocks are up 0.3% and S&P500 futures are down 0.2%. In the bond markets, 10-year Treasury yields are up 7bp to 4.09% and German Bund yields are up 4bp to 2.28%. The dollar index is up \$0.34 to \$104.27. WTI crude oil prices are \$0.60 lower at \$71.68/bbl, and gold prices are at \$2027.78/oz.

Data review

Employment Report

Nonfarm payroll employment increased by 353k above both the consensus forecast (+185k) and the highest forecast on Bloomberg (+300k). In addition to the strength of hiring in January, the last two months were revised up by a total of 126k, with most of that increase occurring in December (333k v 216k initially). This broke a trend of downward revisions seen throughout most of last year. Over the last three-months, payroll employment has increased by an average of a staggering 289k compared to 207k in October. In short, the jobs data show little sign of an impending slowdown in activity.

In addition to strong job growth, average hourly earnings rose by 0.6% m/m and 4.5% y/y. This is above what the Fed would see as consistent with 2% inflation outcome if labor productivity is stable at 1.5%. Strong wage growth was driven by the service sector (+0.6%) as the goods-producing sector saw wage growth moderate to 0.2% m/m. We take the acceleration with a grain of salt as hours worked fell two-tenths to 34.1, which could very well be a weather effect. The combination of solid 4Q GDP and January employment is likely to keep the Fed needing "greater confidence". The report is consistent with our outlook that the Fed will likely begin its interest rate cutting cycle in June.

University of Michigan Sentiment

University of Michigan sentiment for January finalized at 79.0 from 78.8, as we anticipated. One year inflation expectations finalized lower at 2.9% from 3.1% by end of December, while long run inflation expectations remaining at 2.9%. Overall solid improvement from December's 69.7 reading as consumers are becoming more optimistic with the economic outlook.

Factory Orders

Factory orders increased by 0.2% m/m in December after a 2.6% print in December. This was in line with consensus expectations. This was largely due to the 0.4% rise in non durable goods. Meanwhile durable goods came in flat this month. There were small increases across the board in electrical equipment manufacturing, metal, machine, computer and electronic products manufacturing. But transportation equipment manufacturing went down 0.9% this month mainly due to a decline in ship and boat building. Hence, excluding transportation, factory orders rose by a higher 0.4% m/m after an upwardly revised print of 0.2%. Durable goods orders ex transportation also posted a higher 0.5%, a tenth lower from the preliminary. Meanwhile capital goods ex-defence and aircraft (core capital goods) orders that feed into our GDP tracking also declined a tenth to 0.2% m/m in the final print.

Factory shipments came in flat in December after a 0.5% m/m in the previous month. This was on the back of a 0.3% decline in durable goods shipments print and a 0.4% rise in non-durable goods. Within non-durable goods, there were small increases across most categories except petroleum and coal products manufacturing shipments which declined by 0.3% m/m. Within durable goods, there were small declines across most categories like transportation, electrical equipment, computer products and machinery manufacturing shipments. Also, core capital goods shipments declined by a tenth to

0.0% m/m after the preliminary report. Overall, the readings are consistent with the current narrative - manufacturing might be slowing down given the unsustainable levels of investment growth especially buoyed by fiscal policy measures. Going forward, business investment might be levelling off in the coming quarters as the fiscal impulse weakens and higher rates becomes a larger headwind.

Data preview

February 5th – February 9th

ISM Services, SLOOS

Date	Time	Indicator	Period	BofA Estimate	Consensus	Previous
2/05/24	9:45	S&P Global US services PMI	Jan F	—	—	52.9
2/05/24	10:00	ISM Services	Jan	51.5	52.1	50.5
2/05/24	14:00	SLOOS results	—	—	—	—

Source: Bloomberg, BofA Global Research

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US GDP Tracking

Exhibit 2: BofA US GDP tracking estimate (% q/q saar)

4Q US GDP tracking is up two-tenths to 3.5% q/q saar largely due to the higher-than-expected construction spending print in December along with the upward revision to November

Date	Data release	GDP	Final Sales	PCE	Res. Inv.	Struct	Equip	IPP	Gov.	Exports	Imports	Net exports (level)	CIPI (level)
1/12/24	PPI	1.3	2.0	1.9	-0.2	3.6	2.8	2.5	2.3	2.2	2.2	-935.5	27.0
1/17/24	Retail Sales	1.4	2.1	2.0	0.2	3.6	2.8	2.5	2.3	2.2	2.2	-935.5	27.0
1/17/24	Industrial Production, Business Inventories	1.3	2.1	2.0	0.2	3.5	2.5	2.5	2.3	2.2	2.2	-935.5	26.3
1/17/24	Import and Export Prices	1.4	2.1	2.0	0.2	3.5	2.5	2.5	2.3	2.4	1.8	-930.8	26.3
1/18/24	Housing Starts and Permits	1.5	2.1	2.0	0.6	3.5	2.5	2.5	2.3	2.4	1.8	-930.8	26.3
1/25/24	4Q (A) GDP	3.3	2.7	2.8	1.1	3.2	1.0	2.1	3.3	6.3	1.9	-908.2	82.7
2/1/24	Construction Spending	3.5	3.0	2.8	1.5	5.8	1.0	2.1	4.1	6.3	1.9	-908.2	82.7
	GDP tracking	3.5	3.0	2.8	1.5	5.8	1.0	2.1	4.1	6.3	1.9	-908.2	82.7
	Contribution to GDP growth (pp)			1.9	0.1	0.2	0.1	0.1	0.7			0.4	0.1
	BofA official GDP forecast	1.5	2.5	2.0	1.0	3.5	2.5	2.5	2.0	2.5	2.0	-929.0	29.5

Source: BofA Global Research. Our GDP tracking estimate reflects the mechanical aggregation of incoming data that directly informs the BEA's GDP calculations. The process is distinct from our official published GDP forecast. Boldface cells indicate where data have implications for tracking estimates.

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Overseas data

Euro Area

January's final services PMI print came in at 48.4, in line with the flash print, while both the German and French prints were revised slightly higher (to 45.4 and 47.7 respectively). Our Europe economists note that the main highlight in this round of surveys is the core/periphery disparity, with French and German services PMI well below the 50-threshold.



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