

Financial Market Weekly

28 August 2017

Economic Commentary

Earlier this month, the Bureau of Labor Statistics released its readings on consumer prices for July. Based on the year over year change, headline and core CPI came in at 1.73 and 1.69 percent, respectively, compared to 1.64 and 1.71 percent in June. The core measure of CPI which excludes food and energy, continued to decelerate, as measured on a year over year basis. In fact, it was the sixth consecutive month for core prices to decelerate since peaking in late 2016. On the other hand, headline CPI for the month, showed a modest acceleration from June although inflation levels remain near year-to-date lows.

Rates Commentary

Rates were mostly unchanged with the longer end seeing modest pressure to the downside compared to two weeks ago. The U.S. 10-Year Treasury continues to trade in a range with 2.6 percent seeming to be the top end while the 2.2 percent level has been support over recent months. As of this morning, the 10-year is at the lower end of the range. Compared to two weeks ago, the 10-Yr was down 2 basis points while the 2-Yr was flat. In late summer trade, the Treasury will auction off 2- and 5-year notes later today and 7-year notes tomorrow. Ahead of the holiday weekend, we will get a reading on home prices from S&P Case-Shiller, July's PCE price index, revisions to second quarter GDP and to round out the week the employment report for August.

Outlook

The Amazon-effect may be closing in on supermarket chains across the U.S. The e-commerce giant's acquisition of Whole Foods was completed earlier this morning. The company announced it would begin to slash prices on popular items such as bananas, eggs and ground beef to gain market share and shed its reputation for being overly costly.

The price cuts come at a time when the Fed is struggling to find evidence to support its tighter monetary policy regime. Looking under the hood at the trends in food items measured by the CPI shows that while food prices have been in decline for nearly the past two years, the July reading was modestly higher from the prior year. Depending on the magnitude of the Whole Foods price declines and response by its competitors, the likelihood of additional rate hikes this year seems rather distant against a backdrop of decelerating prices.

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Interest Rate Swap

Rate Market (vs. 2 weeks ago)

2y Swap: 1.58% (-1 bp)
5y Swap: 1.84% (-3 bps)
7y Swap: 1.98% (-1 bp)
10y Swap: 2.14% (-2 bps)
30y Swap: 2.42% (-3 bps)

Source: Bloomberg, FRED