

MBS & TREASURY MARKETS

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The Day Ahead: Bonds Rallying Despite Higher Core PCE

After yesterday's quarter over quarter core PCE price index came in 0.2% higher than expected, we knew today's monthly PCE data would have to include higher numbers divided across the months of April, May, and June in some unknown proportion. If April and May were not revised, it suggested an unrounded monthly core PCE of 0.37 today, which would have rounded to a 0.4% headline versus the 0.1% forecast. But that would be very uncommon, so markets split the difference and figured the extra inflation would be spread more evenly across the quarter. Forecasters who updated their predictions changed to 0.2% for the m/m core number, and that's exactly what we got.

The more we drill down, the better the news gets. After all, 0.2 is a rounded number. The unrounded version was 0.182... even better! Perhaps just as important was the fact that the housing component of the PCE data fell to its lowest level since it was first on the way up in 2021.

Housing Inflation in PCE
% Chg, m/m



The following heat map shows another way to visualize the progress:

% change (M/M) in selected PCE Categories (from table 2.8.4 on 7/26/2024)

| | FEB | MAR | APR | MAY | JUN | JUL | AUG | SEP | OCT | NOV | DEC | JAN | FEB | MAR | APR | MAY | JUN |
|--------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|---------|--------|--------|--------|--------|--------|--------|--------|
| Core PCE | 0.359% | 0.336% | 0.307% | 0.288% | 0.172% | 0.120% | 0.098% | 0.329% | 0.144% | 0.089% | 0.152% | 0.505% | 0.257% | 0.334% | 0.261% | 0.127% | 0.182% |
| Core PCE ex Housing | 0.287% | 0.304% | 0.256% | 0.241% | 0.113% | 0.047% | 0.034% | 0.283% | 0.085% | 0.007% | 0.096% | 0.505% | 0.217% | 0.314% | 0.231% | 0.064% | 0.163% |
| Core Services ex Housing | 0.363% | 0.333% | 0.316% | 0.187% | 0.237% | 0.293% | 0.063% | 0.473% | 0.111% | 0.166% | 0.267% | 0.754% | 0.175% | 0.423% | 0.287% | 0.177% | 0.190% |
| Housing | 0.711% | 0.485% | 0.550% | 0.517% | 0.450% | 0.469% | 0.402% | 0.544% | 0.427% | 0.476% | 0.417% | 0.515% | 0.442% | 0.431% | 0.406% | 0.421% | 0.271% |
| Market-based PCEs | 0.357% | 0.129% | 0.276% | 0.096% | 0.098% | 0.148% | 0.376% | 0.397% | 0.083% | -0.008% | 0.082% | 0.321% | 0.325% | 0.309% | 0.198% | 0.014% | 0.047% |
| Core Market-Based PCE | 0.415% | 0.383% | 0.275% | 0.308% | 0.092% | 0.144% | 0.076% | 0.334% | 0.220% | 0.108% | 0.106% | 0.398% | 0.239% | 0.299% | 0.180% | 0.126% | 0.162% |

The main takeaway is really the same in that it shows significant cooling in what has been the most problematic sector. It also serves to remind us that there are months like January that will continue to distort 6 month and 1 year metrics.



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Bottom line to all this: the market knew the previous 0.1% forecast for today's core PCE was a long shot after yesterday. That's why we sold off yesterday instead of today. Now that today's PCE came out with what was probably the softest possible realization of yesterday's warning, bonds are breathing a small sigh of relief, moving to the stronger end of this week's range.

