US Market Wrap

17th May 2022: Stocks bounce and Dollar dips as hot retail sales data adds to Shanghai-induced risk on

- **SNAPSHOT**: Equities up, Treasuries down, Crude down, Dollar down.
- **REAR VIEW**: Powell says Fed to tighten until "convincing" evidence of lower inflation; ECB hawk Knot touts potential 50bps hike; WMT profits suffer from inflation; Potential Chinese easing on big tech; Strong US retail sales and industrial production; US reportedly to ease Venezuelan sanctions; US Treasury set to block Russian debt payments; Strong UK jobs report.
- **COMING UP**: **Data**: UK CPI, EZ CPI (Final), US Building Permits/Housing Starts, Candian CPI **Speakers**: Fed's Harker **Supply**: Germany & US **Earnings**: Aviva, easyJet; Cisco, Target.
- **WEEKLY US EARNINGS ESTIMATES**: [WED] LOW, TGT, ADI, TJX, CSCO; [THURS] AMAT; [FRI] DE. To download the full report, please click here.

MARKET WRAP

Stocks were firmer Tuesday (SPX +2%, NDX +2.6%, DJIA +1.3%, R2K +3%) with a pro-risk bias after hot US retail sales data and industrial/manufacturing production data added to the positive COVID tone out of Shanghai. High-beta currencies outperformed, with the DXY down over 75bps, a factor that added weight to the cyclically-levered Russell 2k small cap index. Treasuries bear-flattened (2s30s -6bps) as hawkish ECB (Knot touted a 50bps hike; Bunds saw heavy losses) and China optimism was complemented by the strong US data and a net hawkish Powell and Kashkari. Powell largely echoed prior comments but the Fed Chair was a touch more resolute in his stance that the Fed would not be pausing hikes at neutral if inflation hadn't showed "convincing evidence" of coming down; Kashkari (2023 voter and Fed's dove) said he is wondering if the Fed needs to do more than it is currently suggesting. Bullard (voter, hawk) was on wires but didn't say anything new/surprising, and even came off a bit more dovish. Oil prices were ultimately lower as earlier strength out of Europe was unwound amid reports of a proposed global cap on Russian oil prices and that the US is set to approve negotiations with producers and Venezuela. In stocks, Colgate-Palmolive (CL) made noteworthy comments at a GS conference that it is seeing signs of supply chain pressures abating, United Airlines (UAL) raised its guidance with demand continuing to improve, while Walmart (WMT) posted a profit miss as inflationary pressures offset its strong top-line results. Housing Starts data is on watch Wednesday after the US NAHB Housing Market Index for May saw a notable decline to 69 from 77.0, with early signs for a housing dip being gauged given the dramatic rise in mortgage rates.

FED

Chair Powell said there is broad support on the FOMC for having 50bps on the table at the next two FOMC meetings, saying the Fed will probably reach more "normal" rate levels in Q4 this year. Although, Powell stressed that is not a stopping point and they do not know where neutral is or where 'tight' is as they will be looking meeting by meeting at financial conditions and economic health. Furthermore, adding to his net-hawkish position on Tuesday, he said if the Fed has to move above neutral, it would not hesitate, alongside noting the Fed would continue raising rates until it sees "convincing evidence" inflation is coming down. Powell warned this is a time for the Fed to be tightly focused on getting inflation down, and not one for nuanced takes on inflation. (For full Powell remarks please click here)

Bullard (2022 voter, hawk) reiterated the most pressing issue for the Fed is inflation but his base case is to see continued above-trend growth in the US for the next 18 months at least, but the largest risks to the US outlook are what will happen to European and Chinese economies. Bullard believes the Fed has a good plan in place to bring inflation down and reiterates 50bps rate hikes at coming meetings are a good base case for now. The St Louis Fed President added that financial market tightening should already be lowering inflation but that means broad asset repricing and more volatility; market volatility reflects policy outlook re-pricing. On the balance sheet, he said it is not exactly clear what effect of shrinking the balance sheet will be in the US or globally and he reiterated that MBS sales are a possibility for the Fed, but that would be far into the future. The hawk added increases in market rates for Treasuries and home mortgages show the Fed is not as far behind the curve as might have been thought, noting the Fed should be prepared to manage inflation on its own but if the pace of prices moderate naturally then the Fed can do less.

Kashkari (2023 voter) largely gave familiar commentary, but he did say he is wondering if the Fed will need to do more than what is currently being suggested, which is a step in the hawkish direction for him.

GLOBAL

US INDUSTRIAL PRODUCTION: Industrial production was strong, rising 1.1% from 0.9% and above the expected 0.5%, meanwhile manufacturing output rose by 0.8% above the 0.4% expected and above the prior 0.8% (revised lower from 0.9%), capacity utilisation rose to 79% from 78.2%, above the 78.6% consensus. Analysts at Pantheon Macroeconomics note the headline was supported by a rise in vehicle output, which returned above the pre-COVID trend line for the first time but the backlog of lost output is large, although rising output will boost inventory and increase sales which will recompress dealers' margins, and help to tackle inflation. The consultancy adds that there is no impact from China disruptions so far, but the disappointing China PMIs suggest trouble ahead, although how much of the disruptions in China will filter through is not clear. However, it will be less than is implied by the usual relationship between China PMI and US production, but nonetheless, it is still an unfavourable development.

US RETAIL SALES: Headline retail sales rose by 0.9%, although slowed from the prior revised 1.4%, in line with analyst expectations, the ex-autos beat at 0.6% (exp. 0.4%) but slowed from the prior revised 2.1%. Ex-gas and autos rose by 1% from a prior revised 1.2%. The Retail Control was strong, rising 1% in April from a prior revised +1.1% in March from the initial print of -0.1%, and above the 0.5% expected. The Retail Control can be used to gauge consumer spending (a large component of GDP), thus a positive sign for Q2 GDP amid global growth concerns. ING highlights that the report points to a willingness from households to spend their savings to maintain their usual lifestyle when inflation is hitting real income growth and the report fully supports "the case for a sharp recovery in GDP growth in the second quarter and a series of 50bp rate hikes from the Federal Reserve". On growth, ING adds the retail sales, along with Google mobility data, surging restaurant dining and recovery in air passengers, gives them more confidence in their Q2 GDP forecast of 3.0-3.5%.

GEOPOLITICS: Russian Foreign Ministry said that there are no talks in any form going on with Ukraine, according to Interfax, where Russia said Ukraine has "practically withdrawn" from the negotiations, while Kyiv blames Moscow for failing to compromise. On NATO applications, Swedish PM Andersson said Sweden and Finland will hand over their NATO applications on Wednesday, and they are ready to discuss/work out any issues with Turkey. As a reminder, to join NATO all existing members, currently 30, must agree, but Turkey has intimated it would not be willing to admit nations which impose restrictions/sanctions against them, in the context of multiple Scandi nations having arms embargoes on Turkey. However, Russian Foreign Minister Lavrov said that there is no large difference if Finland or Sweden join NATO given they had long participated in NATO military drills.

FIXED INCOME

T-NOTE (M2) FUTURES SETTLED 26 TICKS LOWER AT 118-27+

Treasuries bear-flattened as hawkish ECB and China optimism was complemented by strong US retail sales and a net hawkish Powell. 2s +13.2bps at 2.700%, 3s +14.0bps at 2.887%, 5s +13.1bps at 2.951%, 7s +11.6bps at 2.998%, 10s +9.2bps at 2.971%, 20s +6.6bps at 3.372%, 30s +7.7bps at 3.161%.

TOKYO/LONDON: Treasuries were sold through the APAC Tuesday session in gradual, light futures activity amid some optimism around Shanghai reopening. Some stability for T-Notes was found at the London handover, but as stocks extended to the upside and ECB's Knot touted the potential for 50bps hikes, the bear-flattening extended, not to mention the overhang of an abysmal German Schatz auction that aided the spillover pressure from EGBs.

NEW YORK: Support in T-Notes was broken after the beat in April US retail sales, seeing the contracts hit support at 119-00. Fed hawk Bullard (voter) was on wires at the time but didn't provide many surprises (reiterated 50bp hike base case). The super-strong US industrial and manufacturing production data for April kept the pressure on to see 119 break on the contracts, but the dive in the NAHB housing index capped the upside in yields. Choppy trade through into late session Powell, who at the WSJ event, stressed the Fed's desire to keep tightening until there is "convincing" evidence of inflation coming down and that the Fed would not hesitate to rise above neutral if not. His comments saw T-Notes leak to session lows of 118-24.

AHEAD: The US session Wednesday sees the 20yr bond auction as the highlight, however, housing starts data and Fed's Harker are also on the schedule.

STIRS:

- Selling across the Eurodollar strip with reds weakest.
- EDM2 -0.3bps at 98.175, U2 -6.5bps at 97.325, Z2 -11.0bps at 96.805, H3 -15.0bps at 96.63, M3 -16.5bps at 96.565, U3 -16.5bps at 96.66, Z3 -16.5bps at 96.75, H4 -16.5bps at 96.835, M4 -16.0bps at 96.895, Z4 -14.5bps at 96.945, Z5 -10.0bps at 97.02.
- NY Fed RRP op demand at USD 1.877tln across 90 bidders (prev. USD 1.833tln across 92 bidders).

CRUDE

WTI (N2) SETTLED USD 2.19 LOWER AT 109.63/BBL; BRENT (N2) SETTLED USD 2.31 LOWER AT 111.93/BBL

Oil prices were ultimately lower Tuesday as earlier strength on the incrementally improved China situation was unwound later amid reports of a proposed global cap on Russian oil prices and that the US is set to approve negotiations with producers and Venezuela. July futures prices hit peaks of 113.20/bbl and 115.69/bbl in WTI and Brent, respectively as NY players arrived, before dipping through into the futures settlement, closing at lows.

RUSSIAN OIL: US Treasury officials are to discuss pricing caps and tariffs on Russian oil with G7 nations as an alternative to embargoes. Meanwhile, amid the EU-Hungary embargo dispute, Reuters reported that Budapest has indicated that about EUR 750mln of EU investment in a Hungary-Croatia pipeline expansion, in addition to converting refineries off Russian crude blends, would be adequate in the short term for an agreement, although the EU is hesitant to convert private refineries over concerns of a breach of the bloc's competition rules.

VENEZUELA: AP reported that the US is to ease a few economic sanctions against Venezuela, according to AP Limited, where changes will allow Chevron (CVX) to negotiate its license with PDVSA, but not to drill or export any petroleum of Venezuelan origin. In exchange, a former PDVSA official will be removed from a US list of sanctioned individuals.

OPEC: OPEC+ production was 2.6mln below quotas in April, according to a report cited by Reuters, with Russian production 1.28mln below the required level in April. Total OPEC+ compliance now stands at 220% up from the prior month's 157%.

EQUITIES

CLOSES: SPX +2.02% at 4,089, NDX +2.62% at 12,564, DJIA +1.34% at 32,655, RUT +2.99% at 1,839.

SECTORS: Technoloy +2.91%, Materials +2.87%, Financials +2.69%, Consumer Discretionary +2.68%, Industrials +2.28%, Communication Services +1.83%, Health +1.39%, Energy +1.14%, Real Estate +1.04%, Utilities +1.03%, Consumer Staples -1.15%.

EUROPEAN CLOSES: Euro Stoxx 50 +1.52% at 3,741; FTSE 100 +0.72% at 7,518; DAX +1.59% at 14,185; CAC 40 +1.30% at 6,430; IBEX 35 +1.46% at 8,475; FTSE MIB +1.12% at 24,301; SMI +0.50% at 11,730.

EARNINGS: **Walmart (WMT)** posted its biggest one-day decline since 1987 after it missed on EPS as the Co. noted inflationary pressures offset the positive impact of better-than-expected sales. Looking ahead, WMT cut its Q2 and FY23 EPS view, but raised FY revenue view. **Home Depot (HD)** issued a strong report, highlighted by beating on top and bottom line and raising FY22 guidance. **Take-Two (TTWO)** surpassed Wall St. consensus on top and bottom line. Although, TTWO missed on its key booking metric and issued weaker guidance for Q1 and FY. However, analysts have pointed to a history of conservative guidance from TTWO, and are also expecting a more upbeat outlook once its pending acquisition of Zynga (ZNGA) closes. **JD (JD)** topped expectations on EPS and revenue, while annual active customer accounts increased by 16.2% Y/Y. JD saw increased demand amid new COVID-related lockdowns. Separately, JD was also among tech stocks benefiting from hopes for relaxed regulatory curbs on tech companies. **Sea Limited (SE)** posted a shallower loss per share than expected and also beat on revenue.

STOCK SPECIFICS: **United Airlines (UAL)** raised its current quarter revenue forecast, as the demand environment has continued to improve, resulting in a higher unit revenue outlook for Q2. Moreover, UAL expects its busiest summer since before the pandemic began. **Caterpillar (CAT)** board approved USD 15bln share buyback programme and is expecting higher long-term sales growth. **Q2 (QTWO)** reportedly weighing options after takeover interest. Black box data in the China Eastern crash points to an intentional nosedive as the cause; Chinese authorities have not identified problems with **Boeing (BA)** plane involved in the crash, according to WSJ sources. **Twitter (TWTR)** lost three more senior employees (all VPs) ahead of Elon Musk's buyout, according to Bloomberg. **Colgate-Palmolive (CL)** said it's seeing supply-chain pressures abate; some costs are rising but others are moving down. Moreover, consumers are accepting price increases and elasticity is about as expected, maybe a bit better. In H2 it sees higher prices for fats and oils. **AMD (AMD)** saw gains after Piper Sandler upgraded the stock to 'Overweight' from 'Neutral' and said shares could rally nearly 50% after dipping this year. **Lordstown Motors (RIDE)** ability to stay in business for another year remains in doubt until the company secures more funding and raises its market value.

FX WRAP

The Dollar was notably lower on Monday, hitting lows of 103.230 in contrast to early highs of 104.230. For the Buck, albeit not resulting in a market reaction, there was strong retail sales and industrial production data, as well as a slew of Fed speak, with the highlight being Chair Powell. On this, Powell said broad support on FOMC for having on table for 50bps at next two meetings, and if there is a need to move above neutral, they would not hesitate as they will continue raising rates until there is "convincing evidence" inflation is coming down. Nonetheless, the Dollar weakness appeared to be a function of the GBP and EUR strength on the back of supporting factors, as opposed to any notable negative headlines for the Buck.

GBP was the G10 outperformer and saw significant gains against the Buck, which started in the European morning following a very strong UK jobs report. On this, unemployment rate was lower than expected, and hit a 48-year low, but the clear standout was earnings which notably beat expectations. As such, Cable hit a high since May 5th of 1.2498, just falling short of the pivotal 1.25 resistance level, where technicians note a close above the 10dma, 1.2347, would facilitate a test of 21dma resistance by 1.2522 and help pause a slide exacerbated by the BoE's dovish shift in March. Looking ahead, market participants await the key UK CPI on Wednesday and then retail sales on Friday, as well as ongoing Brexit rhetoric, where UK Foreign Secretary Truss confirmed the UK has proposed what it believes is a "comprehensive and reasonable" solution, which requires changes in the Northern Ireland protocol itself.

EUR was the next best performer and firmed about a percent against the Greenback. The first catalyst for the single-currency strength was comments from ECB hawk Knot, as while he said a 25bps hike in July is realistic, he appeared to be the first ECB member to discuss a 50bps move. On this, he added a 50bps rate hike should not be excluded if data in the next few months suggests that inflation is broadening and accumulating. In terms of data, Eurozone Q1 GDP topped expected, but more attention resides around EZ Final April CPI on Wednesday. Regarding key levels, EUR/USD hit a high of 1.0555, but analysts note gains are likely to be short-lived due to strong US retail sales and industrial production reports on Tuesday that increased Fed rate hike pricing, making major resistance at 1.0636-42 more daunting.

CAD was flat, as the USD/CAD cross traded within a tight range, highlighted by 1.2854-07, with the Loonie gleaning little impetus from the crude complex, which saw losses heading into settlement. Note comments from Alberta's Premier that Canada could add 300k BPD of oil pipeline exports and 200k BPD of oil exports by rail this year; adding that if midstream companies make technical improvements to pipelines, could add another 400k BPD of export capacity over the next year.

Antipodes were firmer with AUD boosted by less-dovish RBA talk after the RBA Minutes noted a 40bps hike was among the options the central bank considered earlier this month, and highlighted an argument for 40bps increase could be made given the upside risks to inflation and current very low level of interest rates. Additionally, the Antipodes were boosted on broad Dollar weakness and commodities higher amid easing of COVID lockdowns, as the APAC region's COVID situation improves. AUD/USD and NZD/USD hit highs of 0.7040 and 0.6375, respectively.

JPY was the underperformer and only G10 currency to see losses vs the Buck. USD/JPY rose to a high of 129.77 following the strong US retail sales and also fell victim to the general risk on sentiment. Nonetheless, analysts note, Treasury-JGB yield spreads remain the primary driver of the cross as JGB yields remain isolated to tiny ranges by BoJ yield curve control. In terms of key levels, technicians note USD/JPY needs to close above the 10DMA at 129.65 to target its recent 20-year high of 131.35. There are a few key risk events scheduled, namely Japanese Q1 GDP Wednesday, export data on Thursday, and finally CPI Friday.

CHF saw gains and was a beneficiary of the broader Buck sell off, as USD/CHF broke back beneath parity to highs of 0.9919.

EMFX was predominantly firmer, with the TRY and RUB the underperformers and sitting in the red against the DXY. CNH/CNY saw gains, and derived encouragement from signs of further progress on the COVID situation in Shanghai plus speculation about the easing of crackdowns on the tech sector spurred by a meeting between senior Chinese officials and industry heads. PLN and HUF had better than expected GDP data which supported as well as NBP and HUF comments signalling more tightening. Meanwhile, TRY and RUB lagged, with the former hindered amid Turkey's resistance to Sweden and Finland joining NATO, whilst the latter continues to be weighed upon by sanctions, and as such remains impossible to tell the true value. Nonetheless, according to Interfax, the Russian economy ministry sees Russia's 2022 GDP down 7.8% (prev. down 8.8%) and 2022 inflation at 17.5% (prev. 20.7-22.6%). Be aware of

Bloomberg reports that the US Treasury is set to block Russian debt payments, raising odds of default, where the Biden admin. will not extend the carveout (which let Russia pay coupons in Dollars) that ends May 25th.

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