US Market Wrap

15th June 2022: Fed hikes 75bps, but Powell does not out-hawk expectations

- **SNAPSHOT**: Equities up, Treasuries up, Crude down, Dollar down.
- **REAR VIEW**: Fed hikes by 75bps, revises dot plots higher, & adjusts language around inflation returning to target; Powell does not expect 75bps hikes to be common; ECB to apply flexibility in PEPP reinvestments, to accelerate work on fragmentation tool; NY Fed manufacturing & retail sales disappoint; Gazprom halted additional compressor; BoJ announced another emergency bond-buying operation; F seeing auto-loan delinquencies increasing; GM inline with targets to raise vehicle production 25-30% Y/Y; Surprise crude DoE build.
- **COMING UP**: **Data**: Japanese Trade Balance, US IJC, New Zealand Manufacturing PMI **Events**: BoE Policy Announcement; SNB Policy Announcement & Press Conference **Speakers**: ECB's de Guindos & Panetta **Supply** : Spain & France.

MARKET WRAP

Stocks, bonds, and precious metals rallied while the Dollar tumbled after Fed Chair Powell indicated that 75bps hikes are not going to be common, but did suggest the July meeting could be 50bps or 75bps. The pushback on 75bps being the norm helped the S&P reclaim 3,800, albeit still remaining in technical bear territory. To summarise the Fed decision, the bank hiked its target range by 75bps to 1.50-1.75% in a 10-1 vote split (George dissented for just 50bps), substantially revised higher its dot plots, and adjusted language on reaching its inflation goal (full summary below). Treasuries bull flattened to see 2yr yields tumble 20bps from recent peaks, still substantially elevated to levels just a week ago. Note inflation breakevens rallied as investors demanded greater inflation risk premium in wake of the dovish (vs expectations) guidance. The Dollar initially hit fresh YTD peaks in wake of the announcement at 105.79, although the buck sold off heavily during the press conference to see a low of 104.69. Ahead of Fed, stocks and bonds had been trending higher amid a flurry of short-covering in anticipation of the ECB special meeting on bond market fragmentation and in wake of the BoJ entering the market with more unlimited bond purchases (see ECB section below for more details). Crude prices were lower despite the weaker buck post-Fed, while Biden demanded an explanation from oil companies on why they are refraining from putting additional supply on the market and wants ideas on how supplies can be increased. Meanwhile, the EIA inventory data saw a surprise build with production rising to 12mln from 11.9mln, while distillates posted a larger build than expected but gasoline stocks saw a surprise draw.

CENTRAL BANKS

FOMC STATEMENT: The Federal Reserve hiked rates by 75bps as was touted heavily in wake of the hot May CPI and inflation expectations surveys. The dot plots have all been revised higher by a substantial amount seeing year-end rates at 3.4% (FFR target range of 3.25-3.50%), with increases continuing to a terminal rate of 3.8% in 2023 before rate cuts occur in 2024 back to 3.4%; longer-run (neutral) rate revised modestly higher to 2.5% from 2.4%. Core PCE forecasts were revised higher for 2022 and 2023 but were left unchanged in 2024, but PCE was revised higher for 2022 but revised 0.1% lower for 2023 and 2024, before returning to target in the long run at 2.00% - unchanged from March forecasts. GDP was revised lower and the unemployment rate revised higher from 2022 to 2024, but was left unchanged in the long run, reflecting the expected impact of ramped monetary tightening (full SEPs available here). Within the statement, the Fed removed language "the Committee expects inflation to return to its 2 percent objective and the labor market to remain strong" and replaced it with a more forceful "The Committee is strongly committed to returning inflation to its 2 percent objective." Elsewhere, the FOMC maintained language it is highly attentive to inflation risks and noted "The Committee would be prepared to adjust the stance of monetary policy as appropriate if risks emerge that could impede the attainment of the Committee's goals" and it views that ongoing increases in the target range will be appropriate. Balance sheet plans were left unchanged.

POWELL PRESSER/Q&A: The highlight of Powell's Press conference was his rate guidance, where he suggested the July hike could be either 75bps or 50bps, but crucially, he does not expect 75bps hikes to be common, instead just a tool to get to 'neutral' faster. Powell justified the larger 75bp hike after the hot May CPI data and the "quite eye-catching" UoM inflation expectations print (as the WSJ article had suggested on Monday). Powell said the Fed thought strong action was needed at this meeting and they decided they needed to do more frontloading. He maintained the Fed will take a data-dependent view but they want to see policy at a modestly restrictive level at year-end, which he said is generally seen within a 3.00-3.5% range. Powell said the continued approach of expeditiously raising rates will help ensure longer-term inflation expectations remain well-anchored (note the lack of suggestions that expectations have become unanchored). On inflation, he noted the worst mistake the Fed could make is failing to get inflation down, saying it is not an option. Powell was eager to stress that the Fed does not think current inflation is affecting longer-term expectations in any way, and that the Fed is not seeing a wage price spiral. On their economic targets, he said the Fed wants to see a series of declining inflation readings and a moderating demand with the labour market in a better market balance. Powell also leant into the academic framework that Waller introduced a few weeks ago, saying that if unemployment rose to 4.1% (a big rise from 3.6% currently) that is still historically low and if it rises to that it would be deemed successful (setting the bar for perhaps an even bigger rise in unemployment). Powell reiterated that the Fed thinks it can achieve a softish landing, but did say recent events have raised the degree of difficulty. Furthermore, said that if data goes in a different direction, the Fed would adapt policy accordingly.

ECB: The ECB held an ad-hoc Governing Council meeting and decided that it will apply flexibility in reinvesting redemptions coming due in the PEPP portfolio, and instructed the relevant Eurosystem Committees to accelerate the completion of the design of a new anti-fragmentation instrument for consideration by the Governing Council. Within the statement, ECB noted the pandemic has left lasting vulnerabilities in the euro area economy which are indeed contributing to the uneven transmission of the normalisation of our monetary policy across jurisdictions. Moreover, the ECB meeting came amid renewed focus on action in the EGB space, particularly the periphery, with the BTP-Bund yield spread once again in heightened focus as it peaked at 252bp on Tuesday. Regarding the statement, one potential take is that although committees have been told to accelerate the creation of an anti-fragmentation tool and a tool will likely be forthcoming, given the timeframe in which committees tend to take to decide on such measures, it appears that the new tool will not be deployed in the immediacy, but we could get more details in July. Following the meeting, President Lagarde spoke at the LSE and noted the ECB cannot just be bold, they must be consistent too, while crises are never the same twice, and they must have the courage to act when facts are not clear. Following the US cash close, Reuters ECB sources said ECB bond scheme to come with loose conditions, such as compliance with commission's recommendations and it is to stress the scheme aims to bring yield in line with fundamentals. Finally, sources add the conditions will likely be achieved through quantitative benchmarks, such as historical spreads, which may then be turned into a "traffic light" system to instruct staff on which country's bonds to purchase and at what frequency.

BOE PREVIEW: Policymakers are expected to continue with the rate hiking cycle by delivering another 25bps rise, taking the Bank Rate to 1.25%. The decision to move on rates is expected to be unanimous, however, the split of views regarding the magnitude of the move remains to be seen, given that there were three dissenters at the May meeting. The need to continue raising rates was underscored by the jump in April's CPI metrics, which printed 9.0% from 7.0%. With further increases in inflation likely in the months ahead, the MPC expects consumer prices to average a little over 10% at its peak in Q4 2022. From a growth perspective, the recent survey data from S&P Global highlighted the difficult economic backdrop in the UK, and the likelihood of a stagflationary environment going forwards, with the services metric slipping to 53.4 in May from 58.9. Accompanying commentary from S&P Global noted "the monthly loss of momentum for business activity expansion was a survey record outside of lockdown periods." That said, policymakers will have found some comfort in the latest government support measures aimed at addressing the cost-of-living crisis, which could boost nominal GDP by around 0.7% in H2 2022. In terms of guidance from the MPC itself, Governor Bailey has flagged concerns that pay growth will feed into inflation and is prepared to raise rates again if needed. Furthermore, Chief Economist Pill has stated that when it comes to lifting interest rates, "further work needs to be done." Note, current market pricing has continued to pick up since the prior meeting and now looks for around another seven 25bps hikes by year-end. This continues to remain at odds with guidance from the MPC, which at the May meeting noted that the implied market path would see inflation firmly below target in three years time, at around 1.3%. Therefore, as the year progresses, desks are still widely of the view that some of this exuberant pricing will need to be taken out of the market. For full Newsquawk preview, please click here.

SNB PREVIEW: Overall, a June hike is a possibility but is not the base case, evidenced by 24/26 respondents polled by Reuters expecting an unchanged Key Rate at -0.75%, with the other two calling for a 25bp hike. The SNB is likely to await confirmation of the ECB lift-off in July and then hike at the next scheduled meeting, which occurs in September. However, the timing of the September meeting being one week after the ECB, where theoretically we could have had 75bp of total ECB tightening by that point, raises the argument for an interim-meeting move post-July given the implications for interest differentials. Reminder, the SNB's most recent rate alterations came via unscheduled announcements. Thus, a post-ECB move in July cannot be ruled out but, as mentioned, September/December are the focal points. For the June gathering, focus points include the CHF classification (currently "Highly Valued"), inflation forecasts, particularly the 2023 rate (currently 0.9%) compared to the 2.0% target and the attached Key Rate assumption. Finally, the tiering multiplier (currently 30x) will garner focus, particularly if we see a hike, as this was designed to offset the impact of negative rates on the domestic banking sector. For full Newsquawk preview, please click here.

US DATA

RETAIL SALES: May retail sales disappointed expectations, while the April readings were all revised down. The headline fell by 0.3% M/M in May (exp. +0.2%), the ex-autos metric rose +0.5% M/M, short of the +0.8% analysts were expecting, while the ex-gas and autos measure rose +0.1%. The Control Group was unchanged in the month at 0.0% (exp. +0.5%). Capital Economics said that the data suggested that "surging prices might finally be taking their toll on real consumption," but added that "the latter still on course for solid growth of 3% annualised in Q2," but CapEco says this is still unlikely stop the Fed from its aggressive pace of policy tightening.

NY FED MANUFACTURING: The NY Fed manufacturing survey was expected to strongly rebound in June. The headline rose from the May downside but still did not manage to rise back into positive territory. The headline printed -1.2 (exp. 3.0, prev. -11.6), while the New Orders sub-index printed 5.3 from -8.8, Prices 78.6 from 73.7, Employment picked up to 19.0 from 14.0, and the Six-Month Business Conditions measure pared back to 14.0 from 18.0. Although the headline missed expectations, Pantheon Macroeconomics said it was still a relief given the continued weakness in China's PMI, which tends to lead the US surveys. "The Empire State reports a rebound in orders and employment, and further declines in delivery times and order backlogs; the latter are now back to normal," the consultancy says, adding that "the average level of the key subindexes appears to point to an uptick in the national ISM index, but it has been too optimistic over the past year or so and we need to see what the other regional surveys say," and "on the face of it, though, this is a better survey than the low headline print." NOTE: The manufacturing ISM data is scheduled for release on July 1st.

FIXED INCOME

T-NOTE (U2) FUTURES SETTLED 24 TICKS HIGHER AT 115-05

Treasuries bull-steepened after Powell attempted to guide away from further 75bps hikes, excluding July. 2s -20.7bps at 3.229%, 3s -21.2bps at 3.381%, 5s -19.1bps at 3.407%, 7s -16.9bps at 3.416%, 10s -13.8bps at 3.345%, 20s -6.9bps at 3.648%, 30s -4.8bps at 3.384%.

INFLATION BREAKEVENS rallied amid Powell's cautiousness on further 75bps hikes: 5yr BEI +7.7bps at 3.032%, 10yr BEI +6.6bps at 2.683%, 30yr BEI +6.4bps at 2.540%.

TOKYO/LONDON: T-Note volumes were healthy again through APAC and Europe Wednesday, albeit flows favoured short-covering ahead of FOMC as the contracts climbed both in Tokyo and then more acutely in Europe (in sympathy with EGBs) as the ECB's impromptu meeting regarding asset purchases for periphery members was revealed. T-Notes hit highs of 115-15 at the NY handover, losing momentum in wake of the ECB announcement holding less bite than some had expected.

NEW YORK: The US data had little sway for Treasury trade after both weak retail sales (May) and a surprise slip intro contractionary for the June Empire State mfg. survey. T-Notes instead trundled lower to the 115-00 area ahead of FOMC. The 75bps hike to 1.50-1.75% with hikes in the median 2022 and '23 dots to 3.4% and 3.8%, respectively, confirmed the hawkish shift and T-Notes slid to lows of 114-20+, although that was within earlier ranges. The contracts instead bounced back in the Powell presser after the Fed Chair said 75bps would not be common, while the July hike would likely be 50bps or 75bps. That less-hawkish guide saw T-Notes rally to session highs of 115-25+, although it was the front-end that drove the action, steepening the curve, as 2yr yields richened over 10bps lower from pre-FOMC levels and 20bps lower on the day.

AHEAD: Data Thursday sees housing starts, Philly Fed, and jobless claims, while we also get next week's FRN, TIPS, and 20yr bond announcement. Otherwise, the Fed blackout period ends Friday with Powell set to be speaking at a conference in the morning, while we can expect some other speakers to come out of the woodwork.

STIRS:

- Eurodollars saw a big rally as some of the most hawkish outcomes were taken off the table.
- EDU2 +14.5bps at 96.72, Z2 +21.0bps at 96.065, H3 +25.5bps at 95.955, M3 +28.5bps at 96.03, U3 +28.5bps at 96.20, Z3 +28.0bps at 96.34, H4 +28.0bps at 96.435, M4 +26.5bps at 96.505, U4 +25.0bps at 96.56, Z4 +24.5bps at 96.605, Z5 +18.5bps at 96.68.
- NY Fed RRP op demand fell to USD 2.163tln across 96 bidders; decline comes amid a large Treasury settlement.
- SOFR as of June 14th fell further to 0.69% from 0.73%, but GC opened firmer Wednesday at 0.70%.
- US sold USD 30bln of 119-day CMBs at 2.090%, covered 3.20x.

CRUDE

WTI (N2) SETTLED USD 3.62 LOWER AT 115.31/BBL; BRENT (Q2) SETTLED USD 2.66 LOWER AT 118.51/BBL

Oil prices were lower Wednesday amid demand uncertainty, with prices dipping through the session amid a bearish IEA report, mixed inventories, and weak retail sales data ahead of FOMC. WTI (N2) and Brent (Q2) futures made session highs of USD 119.61/bbl and 121.88/bbl in the APAC session, before flurries of selling pressure in the European and NY session brought prices into the red.

US INVENTORIES: The EIA report saw crude stocks build 2.0mln bbls in the latest week, larger than the indicated +0.7mln in the private data, and against expectations for a 1.3mln bbl draw; Cushing stocks drew by 0.8mln bbls, however. Crude production rose 100k BPD on the week to 12mln BPD, the highest level since the onset of COVID. In the products, gasoline saw a surprise 0.7mln bbl draw (no gasoline builds seen since March now), while distillates saw a build of the same size. Refinery utilisation saw a surprise 0.5% decline.

IEA: The monthly IEA report leaned on the bearish side after it cut its Q3 demand forecast by 0.2mln BPD whilst adding 1.6mln BPD to its prior non-OPEC supply forecast, a result of Russian production exceeding expectations despite sanctions.

EUROPEAN GAS: Eni (ENI IM) announced that Russia had cut gas deliveries to Italy by 15%. Bloomberg separately reported that Gazprom had halted an additional compressor, squeezing flows to Europe; reports noted the halt had brought flows via the Nord Stream 1 to just 40% of capacity. Later on, more Bloomberg headlines hit that Germany's Uniper (UN01 GY) had received 25% less gas than had been agreed to with Russia.

EQUITIES

CLOSES: SPX +1.46% at 3,789, NDX +2.49% at 11,593, DJIA +1.00% at 30,668, RUT +1.35% at 1,731.

SECTORS: Consumer Discretionary +3.02%, Communication Services +2.36%, Real Estate 2.33%, Technology +2.17%, Financials +1.24%, Health +1.02%, Industrials +1.01%, Utilities +0.68%, Consumer Staples +0.08%, Materials +0.03%, Energy -2.13%.

EUROPEAN CLOSES: Euro Stoxx 50 +1.69% at 3,533; FTSE 100 +1.16% at 7,271; DAX +1.39% at 13,489; CAC 40 +1.35% at 6,030; IBEX 35 +1.37% at 8,177; FTSE MIB +2.88% at 22,476; SMI +0.87% at 10,792.

STOCK SPECIFICS: **Baidu (BIDU)** is in talks with potential suitors to offload a 53% stake in **iQIYI (IQ)**. **Boeing (BA)** is to meet US and European officials next week regarding the 777X that is awaiting certification. Separately, BA exec said engineering test flight program for 737 MAX 10 nearly complete and working through certification activities to eventually get type inspection authorisation from FAA. Although, BA is unsure if 737 Max 10 will be certified by the end of the year and is mulling plans if MAX 10 is not certified by the year-end deadline. **Zendesk (ZEN)** is discussing a truce with activist Jana Partners that could involve the CEO stepping down, and other changes to the board, according to the WSJ. **Qualcomm (QCOM)** won the fight against a USD 1.05bln fine imposed by EU antitrust regulators four years ago for paying Apple to use only its chips and blocking out rivals such as Intel. **MicroStrategy (MSTR)** CEO told investors not to be concerned about a potential margin call on a Bitcoin-backed loan, adding that MicroStrategy had ample collateral that it could pledge if needed. **Hertz (HTZ)** announced a new USD 2bln share buyback programme. **Nucor (NUE)** expects to record Q2 2022 earnings above expectations at USD 8.75-8.85 (exp. 8.26). **Robinhood (HOOD)** fell after it was downgraded to “Underweight” from “Neutral” at Atlantic Equities, which cited the cos. revenue trends. Meanwhile, the continued crypto collapse is also weighing. **Wheels Up (UP)** surged after Goldman began coverage with a “Buy” rating, saying Wheels Up is a leading company in an established and growing end market. **Ford (F)** CFO said they are seeing auto-loan delinquencies are increasing; caveats that it's coming from very low levels and are reverting back more towards the mean. **Charter Communications (CHTR)** CFO expects to lose 60-70k broadband customers in Q2 (exp. net adds +132k), with churn out for those in subsidy programmes; "we still expect to have positive broadband net adds”. **Aptiv (APTV)** is beginning to see some supply chain tightness on semiconductors and is impacting production while it expects its earnings will probably in the bottom half of the guidance range. **McDonald's (MCD)** settled a French tax case for USD 1.3bln, according to WSJ. **General Motors (GM)** CFO stated GM is still in line with targets to increase vehicle production 25-30% Y/Y and is on track for its EBIT target. GM has not seen signs of weakening consumer demand and noted it can offset USD 5bln in higher costs with higher prices and cost cutting. **Nio (NIO)** launched the ES7 sports utility vehicle on Wednesday as competition with **Tesla (TSLA)** intensifies in China. **Spotify (SPOT)** CEO intends to slow hiring by 25% but plans to keep growing. **Moderna (MRNA)** FDA vaccine advisory panel unanimously recommended granting EUA for Moderna’s COVID-19 vaccine for children aged 6-17yrs as did the 6month-5year COVID shot receiving unanimous FDA adviser backing.

FX WRAP

Dollar was flat ahead of the FOMC meeting, but in reaction to the FOMC rate decision, the DXY saw initial weakness but quickly pared and rose to YTD highs of 105.790. Within the meeting, the Fed hiked rates by 75bps and revised its dot plots higher, while signalling ongoing increases will be appropriate. The Fed also adjusted language around inflation returning to target. In the accompanying press conference, when Fed Chair Powell said he does not expect moves of 75bps to be common but either 50bps or 75bps in July seem most likely, the Buck saw immediate weakness and fell to lows of 104.870 from over 105.70 when Powell started speaking, with the losses then accentuated to 104.69 at the lows. Moreover, as Powell said this it was an immediate dovish reaction in wider markets as Treasuries, particularly the short end caught a bid while stock indices bounced. Elsewhere, note there was poor US data as NY Fed Manufacturing fell against an expected rise while US retail sales also disappointed.

Cyclical currencies saw pronounced strength, amid the dovish reaction, against the Buck following Powell's comments against expecting 75bps moves to be common. In terms of individual currencies, the AUD outperforms and is firmer by over 2% against the DXY, having hit session highs of 0.7024, but all cyclical currencies saw notable gains against the Greenback. Cable rose to session highs of 1.2204, above the key round level, as all eyes turn to the key BoE rate decision on Thursday (Full Newsquawk preview available here), where the expectations are for the MPC to hike rates by 25bps to 1.25% via a 9-0 vote, while traders will be looking for signs of the MPC pushing back on market pricing.

JPY firmed against the Buck, and hit lows of c. 133.55, but news for the Yen overnight saw JGBs tumble which spurred the BoJ to announce another emergency bond-buying operation for an unlimited amount of 10yr JGBs on June 16th & 17th at 0.25% to help defend its target. Looking ahead, market participants will be focussed on the BoJ meeting which begins tonight and concludes on Friday.

Euro was the relative G10 underperformer on Wednesday, albeit still firmer against the Buck, which came after the ECB called an emergency ad-hoc meeting. Within this, it saw the ECB instruct committees to prepare a new crisis tool while it will apply flexibility in reinvesting PEPP redemptions, which analysts expect the ECB to shift reinvestment more to the highly indebted countries other than less indebted countries in the EZ. Following this, ECB President Lagarde spoke at LSE and noted the ECB must focus on bringing inflation back to its 2% target and policy must not be dominated by fiscal considerations.

EMs saw a similar reaction to cyclicals following the Chair Powell's remarks regarding future 75bps hikes, and as such firmed against the Greenback. Prior to this, CNH and CNY got traction from much better than anticipated Chinese IP and not as bad as feared retail sales on top of snippets from the Stats Bureau in response, such as the economy shows good recovery momentum, and it expects economic performance to improve further in June due to policy support. ZAR was buoyed by gains in gold in wake of FOMC while the precious metal also saw a bullish gold forecast from SocGen that sees prices averaging USD 1,943/oz in 2022. Looking to tonight, attention turns to the BCB later this evening, where the central bank is expected to hike rates by 50bps taking its key rates to 13.25 (prev. 12.75%), while language on rate guidance will also be eyed, which is expected to show no more hikes through year-end (Full Newsquawk preview available here).