US Market Wrap

22nd June 2022: Recession squeals weigh on Dollar and commodities as money markets ramp hard landing pricing

- **SNAPSHOT**: Equities down, Treasuries up, Crude down, Dollar down.
- **REAR VIEW**: Recession a coin toss over the next year, according to Fed research paper; Powell will never take anything off the table, incl. 100bps hike; Evans notes need to raise rates 'a good deal more'; Harker undecided on 50 or 75bps hike in July; Canadian inflation above exp. across all metrics; Jordan says SNB may need to hike again; Mixed 20yr bond auction; Biden calls on Congress to suspend federal gas tax; BA expects supply chain woes through '23; CMCSA and GOOGL among frontrunners to partner NFLX in ad-supported tier.
- **COMING UP**: **Data**: Australian, EZ, UK & US Flash PMIs, US IJC **Events**: Norges Bank, CBRT & Banxico Policy Announcements, US Bank Stress Test Results **Speakers**: Fed's Powell (House Finance Committee).

MARKET WRAP

Stocks were choppy Wednesday as losses in Europe pared into the NY session, only to fade again into the black into the close. There were a few factors to consider, rather than clear catalysts, with the losses in oil (down over USD 6/bbl in the benchmarks at their worst) becoming the cross-asset driver as bonds ripped higher. Aiding the soured risk tone was a Fed research paper showing the US economy facing elevated risks of a recession over the next one to two years, with just over a 50% chance of a recession over the next year. Meanwhile, headlines drew attention to Chair Powell refusing to rule out a 100bps hike when pressed on it in his Senate hearing, amplifying concerns over a hard landing. Note that money markets are seeing the Dec'22/Mar'23 futures start to flirt with inversion, while 2yr and 10yr yields are back down to levels not seen since the May CPI release on June 10th. On oil, the earlier losses seemed not much more than momentum, while desks are split on the implication of Biden's proposed removal of the federal fuel tax; considered immediately bullish for oil, but perhaps indicative of further price suppressing actions to follow from the administration. In FX, the DXY sold as bonds surged and risk tumbled, favouring havens (CHF, JPY).

US

FED: **Chair Powell** testifying to the Senate reiterated much of his usual tone, but he did say he will never take anything off the table when asked about a 100bps rate hike, reaffirming his hawkish remarks that the policy rate is still at a relatively low level and wants it up to a more "neutral-ish" level. Moreover, the Chair added additional rate increases are priced in and this is appropriate, and reiterated ongoing rate hikes will be appropriate with the pace dependent on data with decisions made "meeting by meeting". On the June meeting, Powell added he was persuaded that it was important that a 75bps hike was made. **Harker (2023 voter)** said the Fed needs to get to a neutral rate of 2.5% quickly and should be above 3% by year-end, whilst a 75bps hike helps Fed get to neutral. On the July meeting, Harker added he is not yet ready to decide whether to back 50bps or 75bps. **Evans (non-voter; departing)** spoke heavily again, and stated the Fed will need to raise interest rates "a good deal more" over coming months, whilst noting there are many risks to the downside and must be ready to adjust its policy stance. Lastly, Evans later remarked 100bps hike isn't necessary, and 75bps hike in July would be in line with continued concerns that inflation isn't slowing. However, by year-end he thinks the Fed will be doing 25bps hikes.

FIXED INCOME

T-NOTE (U2) FUTURES SETTLED 1 POINT & 5 TICKS HIGHER AT 116-30+

Treasuries rallied across the curve, led by the belly, as oil tumbled and growth concerns amplify; 20yr auction was average. 2s -14.4bps at 3.054%, 3s -16.4bps at 3.191%, 5s -15.6bps at 3.223%, 7s -15.7bps at 3.236%, 10s -15.5 bps at 3.151%, 20s -15.6bps at 3.485%, 30s -15.4bps at 3.236%. inflation breakevens: 5yr BEI -8.5bps at 2.770%, 10yr BEI -5.7bps at 2.509%, and 30yr BEI -3.7bps at 2.445%.

THE DAY: T-Notes were already finding sympathy strength out of APAC and into the London morning as stocks and oil came under pressure. The lift for govvies extended through the mixed UK inflation print for May - perhaps the fact some metrics even missed can be viewed as a positive in this environment. Stock futures bottomed out as NY trade got underway, although the bid for bonds extended, taking cues from the relentless selling in oil. Aiding the move was attention to a Fed research paper that noted recession odds had increased. T-Notes topped out for the session at 117-06, with cash 10yr yields printing a low of 3.124%, the lowest since June 10th when the May US CPI and UoM inflation survey ignited the Fed's hawkish pivot; interestingly, the 2yr is also at levels not seen since then, coming as hard landing outcomes become more likely, with forwards pricing an inversion as soon as Mar'23. There was some mild paring from highs into the 20yr auction, aided by an 8.7k Ultra 10yr block sale and some concern when Fed Chair Powell said in the Senate he cannot rule out a 100bps hike.

20YR AUCTION: A mixed USD 14bln, 20yr bond auction from the Treasury, although relative to the lack of concession, more impressive than headline numbers suggest. The cut-size offering saw a high yield of 3.488%, cheaper than last month's 3.29% and the highest stop since the tenor's reintroduction in 2020, but still tailed the WI by 0.2bps, as opposed to the prior 0.2bps stop-through. However, the 2.6x bid/cover ratio was strong vs the prior 2.5x and six-auction avg. 2.55 x. The takedown saw Dealers (forced surplus buyers) with 12.4%, better than the prior 13%, which is also the average. That was a result of Directs stepping up to take 20.2% vs the prior 16.4%, while Indirects took a smaller 67.4% vs the prior 70.6%.

STIRS:

- Growth/hard landing concerns sees Dec'22/Mar'23 futures flirt with inversion.
- EDU2 +5.5bps at 96.68, Z2 +14.0bps at 96.175, H3 +19.0bps at 96.185, M3 +19.0bps at 96.28, U3 +19.0bps at 96.425, Z3 +20.0bps at 96.555, H4 +21.5bps at 96.665, M4 +22.0bps at 96.76, Z4 +20.5bps at 96.85, Z5 +15.0bps at 96.88.
- Notable options flow sees 11k EDZ2 96.6250 straddles for 91.5; 10k SR3U2 97.2500/97.1250 put spreads for 8.5; 20k EDU2 put condor strike roll lower.
- US sold USD 30bln of 119-day CMBs at 2.060%, covered 3.00x; sold USD 22bln of 2yr FRNs at high discount margin of -0.003%, covered 3.49x.
- NY Fed RRP op demand new record at USD 2.259tln across 95 bidders; SOFR steady at 1.45%, while 2yr specialness in repo recedes.

CRUDE

WTI (Q2) SETTLED USD 3.33 LOWER AT 106.19/BBL; BRENT (Q2) SETTLED USD 2.91 LOWER AT 111.74/BBL

Oil prices tumbled into the NY Wednesday session before paring with risk assets into the afternoon as traders weigh Biden's proposed federal fuel tax cut. WTI (Q2) and Brent (Q2) futures hit session lows of USD 101.53/bbl and 107.03/bbl, respectively, before better buying developed after the NY cash energy product open. In lack of clear catalysts, many pointed to Biden's latest tax proposals. While US consumers at the pump would pay less under the proposed tax scrap, that would likely add to the global demand pressure for oil/products, although desks point to the measures potentially indicative of further actions to come from the Biden admin. that could be keeping the marginal energy buyer on the sideline. Otherwise, traders look now to the weekly inventory data with the private release due after hours Wednesday (day delayed due to holiday weekend). Current expectations (bbls): Crude -0.6mln, Gasoline -0.5mln, Distillate +0.3mln.

EQUITIES

CLOSES: SPX -0.17% at 3,758, NDX -0.16% at 11,527, DJIA -0.15% at 30,483, RUT -0.55% at 1,689.

SECTORS: Energy -4.19%, Materials -1.29%, Industrials -0.53%, Technology -0.41%, Financials -0.26%, Consumer Discretionary -0.14%, Consumer Staples -0.07%, Communication Services +0.22%, Utilities +1.04%, Health +1.42%, Real Estate +1.55%.

EUROPEAN CLOSES: Euro Stoxx 50 -0.82% at 3,465; FTSE 100 -0.80% at 7,094; DAX -1.10% at 13,145; CAC 40 -0.81% at 5,916; IBEX 35 -1.07% at 8,147; FTSE MIB -1.41% at 21,779; SMI +0.30% at 10,511.

STOCK SPECIFICS: **Boeing (BA)** CEO said that global supply chain constraints would likely continue until at least the end of next year, adding that labour shortages at mid-and sub-tier suppliers remain an issue. **Kohl's (KSS)** saw downside after **Franchise (FRG)** mulls cutting its bid closer to USD 50/shr from 60/shr, according to CNBC. **Comcast's (CMCSA)** NBCUniversal and **Google (GOOGL)** are among the frontrunners to partner with **Netflix (NFLX)** to help create an ad-supported tier, according to WSJ. **La-Z-Boy (LZB)** saw gains after beating on EPS and revenue as it announced record sales whilst next Q revenue view topped consensus. However, expects current macroeconomic and geopolitical uncertainty will likely cause demand trends to remain volatile for the foreseeable future. **Winnebago (WGO)**

firmed after it topped consensus on EPS and revenue as it was helped by higher prices and a rise in its gross profit margins. Looking ahead, expects supply chain inconsistencies to continue in Q4 and 2023. **Sonoco (SON)** gained after raising Q2 outlook citing strong April and May results as well as sustained, strong customer demand, particularly in consumer packaging. **Airbnb (ABNB)** was lower after JMP Securities downgraded the stock to “Market Perform” from “Market Outperform,” saying that the post-pandemic jump in travel demand is already reflected in Airbnb’s valuation. **Toyota (TM)** expects it will produce around 800k vehicles globally in July. Note, TM reportedly cut production in June by 100k to 850k units due to semiconductor shortages. **Dow (DOW)** dipped after it was downgraded at Credit Suisse to “Underperform” from “Neutral”, who cited several pandemic-related factors that boosted Dow and its peers could be in the process of reversing. **Warner Music (WMG)** CEO Cooper is reportedly to leave the Co. by the end of 2023, via WSJ. **Meta (META)**, **Microsoft (MSFT)**, **NVIDIA (NVDA)**, and others formed a Metaverse Standards Forum aiming to drive open synergy, making it easier for developers to build across platforms. However, **Apple (AAPL)**, which is eventually expected to become a dominant player in the metaverse, was missing. A group of drivers claimed that **Uber (UBER)** and **Lyft (LYFT)** is engaging in anti-competitive practices by setting the prices customers pay, limiting drivers’ ability to choose which rides they accept without a penalty, according to NYT. **Tesla (TSLA)** is to suspend most production at Shanghai plant in the first two weeks of July to upgrade the site, according to Reuters citing a memo. US FDA is reportedly preparing to order Juul Labs to remove its e-cigarettes from the US market, according to WSJ citing sources. **Altria (MO)** fell on the back of this. **Chesapeake Energy (CHK)** doubles its authorisation for stock and warrant buybacks from USD 1bln to 2bln, and CEO anticipates 10% inflation in 2023 vs. 2022.

FX WRAP

Dollar was lower Wednesday and hit a trough of 103.850 as analysts note a brace for further Fed hikes and the possibility that accelerated monetary tightening could hasten the arrival of lower inflation and possibly a recession, impacting the Dollar. Moreover, technicians flag the Buck as entering overbought territory and EUR/USD, its primary component, is proceeding toward completing a triple-bottom off June and May's 1.3059/49 lows, near 2017's 1.0340 trough, the lowest since 2003. Elsewhere, Fed speak was heavy on Wednesday as Chair Powell testified in front of the Senate and largely reiterated his tone from the June FOMC, but did note he will never take anything off the table, when asked about a 100bps rate hike, reaffirming that the policy rate is still at a relatively low level, and wants it up to a more "neutral-ish". Moreover, Harker (2023 voter) noted he is not ready to decide between a 50bps or 75bps hike in July, while Evans (non-voter) said the Fed will need to raise interest rates "a good deal more" over the coming months, but did say he sees the Fed back at 25bps hikes by year-end and that 100bps isn't necessary. Looking ahead, on the data front, there is S&P Global Flash Manufacturing PMIs Thursday ahead of stress tests after-market.

Activity currencies were lower against the Buck, with Antipodeans the underperformers and GBP the relative outperformer, albeit still in the red. For the Pound, the main risk event, aside from the ever-present macro themes, was the pivotal CPI data, where core M/M and Y/Y printed slightly cooler than expected, but headline M/M was hotter than anticipated while Y/Y was in line. For the Loonie, Canadian CPI was hot across the board, surpassing consensus on all metrics, whilst the USD/CAD recovered from lows coinciding with the recovery in WTI and Brent, albeit still settling noticeable lower, but well off lows. Following the inflation data, BoC's Rogers stated the May inflation data was an unwelcome number, but not totally unexpected, whilst looking ahead said the decision will be made when we get to July, when asked about 75bps hikes. Aussie and Kiwi both saw more pronounced losses, as previously mentioned, but clawed back some of the lost ground as the risk-aversion faded. As such, AUD/USD traded between a range of 0.6973-0.6882, whilst NZD/AUD parameters were 0.6337-0.6245 but both are well off the extremes, at pixel time. On the calendar front, the key for the antipodeans is Australian flash June PMIs on Thursday.

CHF, EUR, JPY, were the clear G10 outperformers, in that order, with the typical ‘safe haven’ currencies seeing gains against the Greenback on Wednesday in a day which started with risk-averse sentiment. As sentiment improved throughout the day the aforementioned crosses faded off best levels, but remain notably firmer. For the Swissy, SNB's Jordan stated inflation data shows the need to tighten monetary policy further, unclear when, while inflation is broader than just energy, and the SNB may need to hike rates again. Meanwhile, the Euro piggybacked the broader macro themes to eke out gains, but did print disappointing consumer confidence data, which fell deeper into negative territory than expected. Yen pulled back some of its losses with analysts citing the pullback in Treasury yields and initially as part of a broader haven Yen rise amid risk-off flows. Moreover, analysts add, because the BoJ remains committed to its ultra-easy policies and the Kishida government is merely warning about the potential drawbacks of rapid Yen weakening, the post-FOMC meeting pullback in Treasury-JGB yields spreads isn't doing much damage to the broader rates-driven uptrend thus far.

EMFX was mixed, with BRL the clear underperformer, whilst MXN outperformed ahead of the Banxico rate decision on Thursday, where the bank is expected to hike by 75bps. Elsewhere, CZK got little impetus from the CNB’s bigger than anticipated 125bps rate hike or follow-up comments pledging further intervention, perhaps on the premise that two members dissented for unchanged yet again and the Bank personnel has turned less hawkish following recent appointments by the Czech President. For the INR, the RBI minutes were released, with members calling for further policy tightening to bring real yields higher.