



US Market Wrap

11th July 2022: China's COVID and European gas woes sees global risk off as Dollar trumps all

- **SNAPSHOT:** Equities down, Treasuries up, Crude down, Dollar up
- **REAR VIEW:** China COVID woes; EUR/USD flirts with parity; NY Fed 1yr inflation expectations rise, 3yr fall; Bullard & Bostic in favour of 75bp in July, George spoke on risks of moving too fast; Decent 3yr auction.
- **COMING UP: Data:** German ZEW **Event:** OPEC MOMR **Speakers:** Fed's Barkin; BoE's Bailey & Cunliffe **Supply** : UK, Germany & US.
- **WEEK AHEAD PREVIEW:** Highlights include US CPI, retail sales; US-Saudi meeting, BoC, RBNZ. To download the report, [please click here](#).
- **WEEKLY US EARNINGS ESTIMATES:** [TUES] PEP; [THURS] JPM, MS; [FRI] UNH, BLK, WFC, C. To download the full report, [please click here](#).

MARKET WRAP

A global, risk-off Monday as the China COVID flare-up and European gas woes were touted catalysts in an otherwise quiet, summer session. All major indices were lower with quality/defensives the relative outperformers, while the more speculative sectors were hardest hit: DJIA, SPX -1.2%, NDX -2.2%, and RUT -2.3%. That was seen particularly in crypto with Bitcoin -6% (20.5k) and Ethereum -8% (1.14k). The Dollar was king as the DXY surged to levels not seen since 2002 as EUR/USD flirts with parity, USD/JPY hits new 24yr peaks, and activity currencies and EMFX suffer broadly. A 10bps fall in the US 10yr might cause for a double-take on a day where the DXY rises over 1%, although that ignores the even greater (relative) rally in EGBs. Ahead of Tuesday's US 10yr auction, the US 3yr auction went well and marked the first auction above 3% since 2007. Fed speak saw George (2022 voter; 50bps dissenter) reiterate her concerns about the Fed moving too fast, while Bostic (non-voter) and Bullard (2022 voter) reiterated calls for 75bps in July. Bostic was encouraged by the fall in longer run inflation expectations after the NY Fed consumer survey saw 3yr inflation expectations decline, although the 1yr expectations rose to a series high. In commodities, all felt the pressure of the Dollar bid, although oil did rise off lows into the settlement given stock indices found some earlier paring, only then to dip back to lows into the close, although oil failed to follow suit.

US

FED: George (2022 voter, 50bp dissenter) stated the speed at which rates should rise is an open question, but noted moving too fast risks oversteering. She added communicating the path for rates is "far more consequential" than the speed of policy change. The Kansas City Fed President said recession projections suggest to her that rapid rate hikes risk tightening faster than both the economy and markets can adjust, adding it is remarkable that there is growing discussion of recession risk just four months after the Fed began raising rates. Further on rates, she noted abrupt changes in could create strains in the economy, while the pace of rate increases needs to be "carefully balanced" against the state of the economy and financial markets. Lastly, on the economy, George added with GDP still 2.5% below pre-pandemic trend suggests the pandemic did "long-lasting damage" to the supply side, particularly the service sector and the nature of inflation suggests a "tight economy" rather than specific supply disruptions are driving prices. **Bullard (2022 voter, hawk)** stated the solid US economy can handle rising rates and he reiterated support for a 75bps rate hike in July, according to AP interview. Bullard added he doesn't believe the economy has been in a recession. **Bostic (2024 voter)** spoke once again where he reiterated support for a 75bps hike in July noting he is comfortable the economy can withstand such a move. Bostic added M/M inflation readings have not been as encouraging as he would have liked but movements in the longer run inflation expectations is encouraging, indicating the public and markets have confidence in the Fed. Bostic was also dismissive of a recession, stating the action of the jobs market right now does not feel like a recession.

FIXED INCOME

T-NOTE (U2) FUTURES SETTLE 24 TICKS LOWER AT 118-12



Treasuries bull-flattened Monday in sympathy with global risk aversion ahead of US supply and CPI; 3yr auction above 3% for the first time since 2007. Futures volumes were lighter than average. 2s -5.5bps at 3.066%, 3s -5.9bps at 3.100%, 5s -9.5bps at 3.045%, 7s -10.7bps at 3.062%, 10s -11.2bps at 2.989%, 20s -10.8bps at 3.431%, 30s -9.2bps at 3.177%. Inflation breakevens: 5yr BEI -5.0bps at 2.584%, 10yr BEI -4.5bps at 2.289%, 30yr BEI -4.1bps at 2.189%.

THE DAY: T-Notes hugged just above their post-NFP lows (117-18) for the APAC session on Monday, before finding a lift into the European morning as stocks trundled to the downside. 118-00 served as resistance before the US session saw the level breached convincingly in spillover from the global govvie bid, with EGBs in particular well bid amid energy supply/growth concerns front-of-mind; approaching US supply and CPI failed to restrain the paring of NFP losses. There was some chunky bullish T-Note option flow seen into the NY handover too, with high volume September expiry call buying. The shaky cash open for stocks in NY only accelerated the Treasury bid, taking T-Notes to 118-19 (just above their pre-NFP highs) before losing momentum amid a 3.4k Ultra 10yr block sale, paring a few ticks into the later session. The strong 3yr auction (more below) didn't sustain much price action out the curve. Traders now look to Tuesday's 10yr auction ahead of Wednesday's 30yr and CPI data.

3YR AUCTION: The USD 43bln auction was largely strong after the 3.083% high yield - the first stop above 3% since 2007 - stopped through the WI by 0.5bps, better than the prior 1bp tail and six-auction avg. tail of 0.2bps. However, it's worth noting the 2.43x bid/cover ratio was below avg. 2.47x and prior 2.45x. Nonetheless, the 20.3% Dealer takedown was significantly beneath the prior 24.9% and avg. 23.9%, a result of Indirects stepping up to take 60.4% from last month's meagre 51.5%.

STIRS:

- The Eurodollar strip saw low futures activity Monday; whites (1st yr of quarterlies) bull-flattened with Mar'23 the most actively traded.
- EDU2 +0.5bps at 96.68, Z2 +6bps at 96.205, H3 +11.5bps at 96.30, M3 +12.5bps at 96.48, U3 +12bps at 96.685, Z3 +9.5bps at 96.855, H4 +8.5bps at 96.98, M4 +8.5bps at 97.08, Z4 +9.5bps at 97.14, Z5 +13bps at 97.095.
- In options, a NY morning block of 20k EDZ2 96.50/96.00 put spreads for 27 stands out.
- NY Fed RRP op. demand rose to USD 2.164tn from 2.145tn, while SOFR as of Friday fell to 1.53% from 1.54%.
- US sold USD 58bln of 3-month bills at 2.110%, covered 2.49x; sold USD 48bln of 6-month bills at 2.685%, covered 2.67x.

CRUDE

WTI (Q2) SETTLES USD 0.70 LOWER AT 104.09/BBL; BRENT (U2) SETTLES USD 0.08 HIGHER AT 107.10/BBL

Oil prices were subdued Monday but off lows as risk assets recovered, offsetting the demand woes amid China's latest COVID flare-up. The supply backdrop also improved after a Russian appeals court ruled the CPC can pay a minor fine instead of the month-long shutdown initially ordered, keeping Kazakhstan oil exports running from the Novorossiisk port. Elsewhere, JPMorgan's strategists were out calling for oil prices to be in the low USD 100s/bbl for the rest of the year, then falling to high USD 90s in 2023.

RUSSIAN PRICE CAP: Bloomberg reported the US is to urge India and Japan to back the plan for a cap on Russian oil prices. That follows last week's report that US and allies had discussed capping Russian oil at USD 40-60/bbl, something which desks caution could have unintended (bullish) effects.

EUROPE: Nord Stream 1 has commenced its scheduled 10-day maintenance period and officials are already expressing concern that supply might not return. To the point, Reuters reported Germany will decide Wednesday on steps to reactivate coal-fired power plants in order to reduce gas consumption. In Austria, the government is proposing a new release of fuel from its national reserves. While Spain's government called on its utilities to reduce LNG imports from Russia and seek alternatives, noting a gas contingency plan is in the works ahead of winter.

EQUITIES

CLOSES: SPX -1.15% at 3,854, NDX -2.19% at 11,860, DJIA -0.52% at 31,174, RUT -2.11% at 1,732.

SECTORS: Communication Services -2.80%, Consumer Discretionary -2.76%, Technology -1.42%, Energy -0.89%, Financials -0.83%, Industrials -0.67%, Materials -0.27%, Health Care -0.23%, Consumer Staples -0.14%, Real Estate +0.01%, Utilities +0.64%.



EUROPEAN CLOSES: Euro Stoxx 50 -0.99% at 3,471; FTSE 100 +0.00% at 7,196; DAX -1.40% at 12,832; CAC 40 -0.61% at 5,996; IBEX 35 -0.43% at 8,065; FTSE MIB -0.95% at 21,567; SMI +0.05% at 11,020.

STOCK SPECIFICS: **Chinese tech stocks**, such as **Alibaba (BABA)** and **Tencent (TCEHY)**, saw losses after China slapped fines on the aforementioned cos., and others, for failing to comply with anti-monopoly rules on the disclosure of transactions. Regulators released a list of 28 deals that violated the rules, five of which involved units of Alibaba. Casino names, **LVS, MGM, WYNN, MLCO**, were softer following Macau shutting casinos for a week amid another COVID-19 outbreak, according to WSJ. **Twitter (TWTR)** was lower after Elon Musk said he is ending a USD 44bln bid to buy Twitter, alleging it has failed to provide much of the information he requested. Twitter plans to pursue legal action against Musk, stating that it was committed to closing the transaction on the price and terms agreed. **Nio (NIO)** was weaker following a response to a short-seller report from Grizzly Research, as it formed an independent committee to oversee an investigation on allegations made in the report, which accused Nio of exaggerating its revenue and profit margins. **Uber (UBER)** broke laws, duped police and secretly lobbied governments in a global push, according to the Guardian. The article also alleges that Uber used a 'kill switch' during raids to stop police from seeing data. Uber issued a statement saying it had made mistakes in the past and that it is a different company today. **Lululemon (LULU)** and **Qorvo (QRVO)** saw weakness after they were both downgraded. The former was downgraded to "Underperform" from "Hold" at Jefferies who said the co. is noting increased competition and an easing of the COVID-related spike in demand. While the latter, was downgraded to "Market Perform" from "Outperform" at Cowen, who thinks weakness in the Android market will weigh on revenue and profit margins. **EOG (EOG)** anticipates a Q2 net loss of USD 1.38bln of its financial commodity derivative contracts. New York AG said she has uncovered evidence that **Teva (TEVA)** pharmaceuticals lied to evade accountability for Opioid crisis in the state. **Amazon (AMZN)** reportedly considers bidding for Metro India, in a deal which could be valued up to USD 1.2bln, according to Bloomberg. **Smith & Wesson (SWBI)** and **Sturm, Roger & Co (RGR)** saw mild strength after US President Biden noted he is determined to ban assault weapons. **Meta (META)** dropped after Needham downgraded it to "Underperform" from "Hold" and pointed to Meta's heavy investments into the metaverse, which may take too long to pay off. **Netflix (NFLX)** is reportedly interviewing multiple external candidates for new senior role overseeing ad-supported tier, according to WSJ. Chemical giant **BASF (BASF GY)** announced upside preliminary Q2 results, seeing a beat on net income and revenue but it did reaffirm guidance for the time being.

FX WRAP

The Dollar surged on Monday to print fresh YTD highs at 108.190, a level not seen since 2002. The move in the Dollar was supported by the risk-off tone in markets with equities lower while bonds were bid, albeit the higher yields did little to stop the greenback's rise, likely a factor of a stronger bid for other govies. Risk off had started in Asia on renewed COVID/demand fears out of China where Macau shut all of their casinos and a Shanghai official announced additional areas of high risk areas. Fed speak Monday saw George (2022 voter) warn moving rates too fast risks oversteering and noting communication the rate path is far more consequential than the speed of policy changes. George appeared to lean back on faster tightening once again after she dissented in June voting for a 50bp hike rather than a 75bp move, she also warned that abrupt changes in rates could create strains in the economy. Meanwhile, Bullard reiterated support for a 75bp hike in July, adding the jobs report shows the US economy can handle rising rates. We also saw the latest NY Fed consumer survey which saw one-year ahead inflation expectations rise to a series high of 6.8% from 6.6%, although the 3-year inflation expectations cooled to 3.6% from 3.9% - attention turns to US CPI on Wednesday.

Euro was put in the dust amid the Dollar bid as the cross looks ever closer to parity, touching a fresh low of 1.0042 at pixel time, a level not seen since 2002 as rate differentials, geopolitics, and recession fears continue to weigh on the cross while ING note fears of a Russian gas shutdown, hawkish Fed bets, and risk sentiment in general all argue against a recovery in the cross.

Yen weakened to a 24yr low against the rising greenback at 137.75 with the BoJ's ultra-easy policy settings set to remain as BoJ Governor Kuroda once again signalling the central bank is prepared to ease policy further without hesitation if needed while also warning the economy is showing signs of weakness, reiterating they will maintain their ultra-loose policy to stably achieve its 2% price target. Meanwhile, the BoJ's Osaka branch manager said that rapid and short-term moves in FX, as seen recently, are undesirable. Note, the BoJ raised its economic assessment for seven out of Japan's nine regions and maintained its assessment on the other two, noting many regions saw economies picking up moderately as the impact of the pandemic subsides.

CHF firmed against the Euro on policy divergence and recessionary fears which sparked a bid for the CHF against the Euro although the Dollar remained king and the Swissy was weaker against the buck. Desks have warned previously of Switzerland's exposure to the European gas crisis.



Gold prices took a hit on the Dollar rally, alongside broader metals, coming ahead of US CPI Wednesday before the FOMC's July rate decision on 27th, with the blackout period commencing from Saturday. Gold saw a low of USD 1,731 /oz and analysts are looking at strong support around USD 1,670/oz.

Activity currencies fell victim to the stronger buck with weakness seen in antipodeans on China COVID woes, particularly the AUD which was the underperforming currency on Monday. NZD and GBP saw similar losses, while although the CAD was also weaker vs the Dollar, it was relatively strong in comparison to its activity currency pairs ahead of the BoC on Wednesday which is expected to hike rates by 75bps with attention on guidance for rate hikes throughout the rest of the year.

Scandis were both stronger against the Euro and weaker vs the Dollar, while the NOK outperformed SEK despite lower crude prices, although oil prices were off their lows while although risk assets sold off, they were off extremes. In Sweden, the Riksbank minutes showed an affirmation to prevent high inflation becoming entrenched in price and wage setting. The 50bp hike from the Riksbank was unanimous and the minutes revealed several members emphasised they are prepared to do what is necessary to bring inflation down, even if it were to lead to weaker developments in the real economy in the near term. Meanwhile, for the NOK, Norwegian CPI was hotter than expected rising 0.9% M/M and 6.3% Y/Y although the core metrics were in line at 0.5% M/M and 3.6% Y/Y.

CNH and CNY were weaker on the Dollar strength and renewed COVID concerns. Meanwhile, the latest domestic CPI and PPI data came in marginally hotter than expected.

EMFX was generally weaker, with huge underperformance in BRL amid the Dollar strength while political violence in Brazil has increased. An official from Brazil's leftist opposition Workers' Party was shot dead by a federal prison guard who was shouting support for Bolsonaro. Note, President Bolsonaro also announced they are close to a deal to purchase cheaper diesel from Russia, something which Petrobras said was not surprising but it does raise concerns. The deal could potentially have ramifications for Brazil if it goes against Western Sanctions. MXN saw pronounced weakness also, as did the ZAR with the latter hit by falling gold prices and the former on a rating agency cut from Moody's on Friday, although EM's generally saw pronounced selling. CLP and COP hit all-time lows with weakness stemming from the risk aversion, recessionary fears and weaker commodity prices.

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