US Market Wrap

21st July 2022: Duration/tech rally after poor US data offsets ECB's hawkish hike

- **SNAPSHOT**: Equities up, Treasuries up, Crude down, Dollar down.
- **REAR VIEW**: ECB hikes 50bps, approves TPI, abandons forward guidance; BoJ keeps policy settings unchanged; Nord Stream says gas delivery resumed on Thursday morning; Poor Philly Fed and jobless claims; Italian President dissolved Parliament; SARB unexpectedly raised rates by 75bps; TSLA beat on profit but Musk warned high car prices could hurt demand; MSFT to slow hiring; T warned customers having difficulties paying phone bills.
- **COMING UP**: **Data**: Australian, EZ, UK & US Flash PMIs, UK Retail Sales **Events**: ECB SPF, CBR Policy Announcement **Earnings**: American Express, Verizon; Danske Bank, Swedish Match.

MARKET WRAP

Stocks were firmer in the US with a tech bias (SPX +1%, NDX +1.4%; RTY +0.4%) as US Treasuries went on a big rally after the weak US data. However, an after-hours SNAP earnings report which noted a hiring freeze has spooked market sentiment heading into APAC Friday. The highlight of the session was the ECB which went ahead with a chunky 50bps liftoff to take the main Depo rate to 0%; ECB also confirmed the new fragmentation tool, but it is not as supportive/active as some doves might have liked. There was initial kneejerk bond selling but the big fall in the July US Philly Fed and rise in initial jobless claims put dampeners on the growth outlook, and thus the Fed hiking cycle, lifting government bonds through the rest of the session, with growth stocks taking impetus from the fall in yields. There was also an inflationary angle to consider with the confirmation of resuming, reduced flows via Nord Stream 1 saw energy prices decline as the risk premia of Russian supply was reduced. The ECB hike saw EUR/USD rally while the Dollar declined. Elsewhere, EZ periphery debt felt the double-edged sword of Italian President Mattarella dissolving parliament ahead of an election scheduled for September 25th. In US earnings, the highlight in the pre-market was AT&T (T) which spooked participants after warning that customers were having difficulties paying their phone bills, particularly in the last six weeks. Attention now falls on the Flash PMIs on Friday ahead of next week's FOMC.

GLOBAL

ECB REVIEW: Despite expectations for a 25bps hike across the ECB's three key rates, policymakers opted to "go big" and deliver 50bps worth of tightening, taking the deposit rate to 0% and therefore drawing a line under the Bank's NIRP. Alongside this, the Bank refrained from providing explicit guidance for the September meeting and is instead adopting a meeting-by-meeting approach. The Governing Council was also able to agree on an anti-fragmentation tool named the Transmission Protection Instrument (TPI) aimed at ensuring that the monetary policy stance is transmitted smoothly across all euro area countries. That said, PEPP remains the first line of defence to counter risks to the transmission mechanism related to the pandemic. At the follow-up press conference, as part of the economic assessment, President Lagarde noted that risks to the inflation outlook continue to be to the upside and have intensified. In terms of the decisions taken today, Lagarde said that the Governing Council rallied around the consensus of a 50bps hike and that the ECB is accelerating the normalisation process, but not changing the ultimate point of arrival. With regards to TPI, Lagarde said the decision on the new tool was unanimous. In terms of the details of TPI, Lagarde noted that all nations are eligible, the ECB is capable of "going big" on the instrument, whilst the activation of TPI is at the discretion of the Governing Council. Lagarde later clarified that the four conditions for TPI are as follows: 1. Compliance of EU fiscal framework, 2. Absence of severe macro imbalances, 3. Fiscal sustainability, 4. Sound and sustainable macro policies. Some commentators were quick to suggest that Italy might fail to satisfy such criteria and as such, the IT/GE 10yr spread was unable to narrow from the levels prompted by the recent resignation of Italian PM Draghi. Furthermore, the follow-up press release noted that purchases under TPI could be suspended if it is judged that persistent tensions are due to country fundamentals. Overall, despite delivering a larger than expected hike, EUR/USD erased all of the upside seen on the initial announcement as the potential hurdles for Italy being able to utilise the TPI appear to be high. Furthermore, although the ECB delivered 50bps instead of 25bps, the central bank is likely to see its window of opportunity for raising rates narrow ahead of a difficult winter amid energy supply disruptions. In terms of market pricing, a 50bps move in September is now priced in, with the deposit rate seen rising to 1.25% by year-end vs. 1% pre-announcement. Given the aforementioned headwinds facing the ECB it is unclear whether such a rate path will be realised. Accordingly, ING expects a further 50bps of rate hikes before winter starts with no hikes to follow thereafter.

ECB SOURCES: ECB sources followed the conclusion of the meeting, where Bloomberg reported some officials initially preferred a quarter-point rate hike and agreement on transmission tool convinced officials that they could afford a half-point move, and the proposal for 50bps hike was put forward by Chief Economist Lane. Elsewhere, Reuters sources said the ECB's internal metrics do not currently show unwarranted fragmentation in any EZ country, and the ECB does not expect TPI to be triggered imminently. Moreover, Reuters sources said ECB did not discuss any particular country on Thursday, while ECB staff will look at a complex set of metrics and alert GC if they show unwarranted fragmentation. Lastly, sources said all EZ countries currently eligible for ECB's TPI based on conditions outlined on Thursday, but ECB governors currently see PEPP reinvestments as sufficient to contain fragmentation.

NORD STREAM 1: As touted, flows through the Nord Stream 1 pipeline resumed at reduced capacity (40%) on Thursday after the ten-day maintenance period. The focus now falls on getting the pipeline further back to full capacity to fill storage levels in Europe. Germany said on Thursday that if Russian supplies remain at the current low levels, the 90% storage level by November will hardly be reachable without additional measures. Economy Minister Habeck said Russia is blackmailing Germany and Europe and that they have the impression Russia does not want to take back the turbine serviced in Canada. Reuters reported later that the turbine was still stuck in transit in Germany due to Russia not giving approval to transport it back, noting it is currently unclear when the turbine can be returned. The reports suggested it could take days or even weeks.

US

PHILLY FED: Philly Fed printed -12.3, way beneath the expected 0.0 and the prior -3.3. Looking at the subcomponents, 6month view fell dramatically to -18.6 (prev. -6.8), while employment dropped to 19.4 (prev. 28.1) and new orders to -24.8 (prev. -12.4). However, the inflation gauge of prices paid notably dropped to 522.2 from 64.5. The fall in the Philly Fed contrasts the fall in the Empire State index, although divergence is not uncommon between the two. Pantheon Macroeconomics, while they have a view that the US surveys will start to track the Chinese ones firmer in the next few months, caveat that "the continued drop in the Philly Fed’s measure of capex plans for the next six months, down 7.3 points to a nine-year low, is disconcerting." The analysts hope and expect this will be a bottom. Meanwhile, Pantheon highlight the further improvement in the supply chain measures after the supplier delivery times index fell a sizeable 20.1 points and the order backlog dipped 3.4 points, "both are now below normal levels but still trending down." On the inflation measures, prices paid and received both dropped sharply too. PM expands, "These moves are consistent with a host of other evidence signalling that supply constraints are rapidly morphing into supply gluts, which mean that the current hugely elevated level of margins across the goods distribution chain cannot possibly be sustained." Most interestingly, "This is the single strongest argument for expecting core inflation to fall faster than the Fed and markets expect over the next year."

JOBLESS CLAIMS: Initial jobless claims rose to 250k, above the expected 240k and prior 244k, whilst continued claims printed 1.384mln (exp. 1.34mln, prev. 1.333mln). On the report, Pantheon Macroeconomics note, “we doubt the increase in claims is significant; numbers are still being distorted by the annual automaker retooling shutdowns, which cause problems for the seasonal adjustment because the timing and extent of the shutdowns varies from year to year.” As such, moving forward the underlying trend will re-emerge when the distortions fade, in early August. Lastly, the consultancy adds, “we expect to see only a small increase from the 230K trend before the auto shutdowns, with the level of claims remaining very low by historical standards.”

FIXED INCOME

T-NOTE (U2) FUTURES SETTLED 1 POINT & 4 TICKS HIGHER AT 118-29

Treasuries bull-steepened after the hawkish ECB was offset by soft US data and energy supply risk abating, triggering short-covering and chasing into next week's FOMC. 2s -15bps at 3.100%, 3s -17.5bps at 3.074%, 5s -17.1bps at 3.006%, 7s -15.7bps at 2.994%, 10s -13bps at 2.906%, 20s -9.3bps at 3.339%, 30s -9.5bps at 3.075%. Inflation breakevens: 5yr BEI -9.7bps at 2.624%, 10yr BEI -7.9bps at 2.266%, 30yr BEI -7bps at 2.146%.

THE DAY: T-Notes had been leaking lower into the NY handover, dipping further in sympathy with EGBs after the ECB hiked by 50bps to print session lows of 117-14+, at a cash 10yr yield high of 3.08%. Flows reversed after a double-dose of growth concerns were piqued on the big fall in the Philly Fed survey and another rise in weekly initial jobless claims. The bid then continued to grind from there, aided by block activity with a notable 40k buy in the FVU2 future, followed by further block buys in the belly. IFR noted real money was in a chase with CTAs covering shorts. There was a brief pause in the bid as Europe closed shop, but after the strong 10yr TIPS auction passed, fresh highs were made into the settlement, with the 10yr cash yield approaching 2.90% and T-Notes towards resistance at 119-00. Traders now look to Friday's Flash PMIs while otherwise book squaring into next week's FOMC and Treasury auctions...

REFUNDING: US to sell USD 45bln of 2yr notes on July 25th; USD 46bln of 5yr notes on July 26th; USD 38bln of 7yr notes on July 28th; all to settle on August 1st.

STIRS:

- EDU2 +5bps at 96.565, Z2 +13.5bps at 96.205, H3 +18.5bps at 96.385, M3 +19.5bps at 96.55, U3 +20.5bps at 96.74, Z3 +21bps at 96.885, H4 +21.5bps at 97.005, M4 +22bps at 97.115, Z4 +21bps at 97.225, Z5 +16.5bps at 97.225.
- US sold USD 58bln of 1-month bills at 2.120%, covered 2.44x; sold USD 53bln of 2-month bills at 2.230%, covered 2.71x.
- NY Fed RRP op. demand rises to USD 2.272tln from 2.240tln.

CRUDE

WTI (U2) SETTLED USD 3.53 LOWER AT 96.35/BBL; BRENT (U2) SETTLED USD 3.06 LOWER AT 103.86/BBL

Oil prices were lower again on Thursday after Europe hit the bid hard from the get-go with some renewed optimism around Russian supply after Nord Stream 1 flows resumed. The losses picked up into the NY handover, where WTI and Brent (U2) hit lows of USD 94.59/bbl and 101.50/bbl before finding some mild support through into the close, likely part a function of the further strength in stocks. Aside from the Nord Stream 1 decision, there wasn't many major energy catalysts, with overarching themes such as China's COVID and Libya's return to production being touted for the losses. On an aside, note the Kremlin said today that President Putin and Saudi Crown Prince spoke by phone and discussed the global oil market situation, although not much more was revealed apart from a statement underlining the importance of further cooperation within the OPEC+ framework.

EQUITIES

CLOSES: SPX +0.97% at 3,998, NDX +1.44% at 12,619, DJIA +0.51% at 32,036, RUT +0.40 % at 1,834.

SECTORS: Consumer Discretionary +2.25%, Health +1.51%, Technology +1.41%, Materials +1.4%, Real Estate +1.01%, Industrials +0.68%, Financials +0.64%, Consumer Staples +0.36%, Utilities +0.29%, Communication Services -0.21%, Energy -1.69%.

EUROPEAN CLOSES: Euro Stoxx 50 +0.31% at 3,596; FTSE 100 +0.09% at 7,270; DAX -0.27% at 13,246; CAC 40 +0.27% at 6,201; IBEX 35 -0.20% at 8,012; FTSE MIB -0.71% at 21,196; SMI +0.79% at 11,147.

EARNINGS: **Tesla (TSLA)** beat on EPS but missed on revenue alongside shrinking profit margins as it dealt with higher costs and supply chain disruptions. Elsewhere, it converted ~75% of Bitcoin purchases into fiat currency. In commentary, exec does not see major supply problems for chips and batteries, whilst Musk said prices for its cars are “embarrassingly high” and could hurt demand. **AT&T (T)** surpassed consensus on the top and bottom line, as well as raising mobility service revenue guidance after reporting a rise in Q subscriber additions. T stated people are taking longer to pay their bills, and couple this with higher CapEx, gives the reason why T lowered FY FCF guidance to USD 14bln (prev. 16bln). **Dow (DOW)** beat on top and bottom line, but looking ahead Q3 revenue view was light. **Travelers (TRV)** had a strong report where it beat on all major metrics, such as EPS, revenue, and net premiums written. TRV positive results came despite higher catastrophe losses and a drop in investment income. **CSX (CSX)** topped Wall St. consensus on profit and revenue. CSX added it is seeing flying demand but it is having difficulties hiring because of a tight labour market. **Danaher (DHR)** exceeded streets view on EPS and revenue, with higher sales helping offset a rise in expenses. **Nucor (NUE)** had a stellar Q, where top and bottom line beat. NUE said demand remains stable and resilient. Looking ahead, Q3 seen decreasing from the record-setting Q2, but expect another strong Q of profitability. **Phillip Morris (PM)** beat on EPS and revenue, while cigarette shipping volume posted a surprise rise against an expected decline. **United Airlines (UAL)** reported poor earnings, illustrated by missing on EPS and revenue. UAL warned of the impact of higher jet fuel prices and a possible economic slowdown. **D.R. Horton (DHI)** reported better-than-expected profit, but revenue fell. DHI cut its FY sales guidance on moderating demand. **Alcoa (AA)** topped on EPS and revenue alongside announcing a USD 500mln share buyback programme.

STOCK SPECIFICS: **Microsoft (MSFT)** is to slow hiring in some groups and is eliminating open jobs, according to Bloomberg. **Carnival (CCL)** filed to sell USD 1bln worth of its stock; to use proceeds for general purposes and debt maturities. **Ford (F)** released new battery capacity plan and raw materials details to scale EVs; F is on track to ramp to 600k run rate by 2023 and 2mln+ by 2026. **Amazon (AMZN)** is to buy **1Life Healthcare (ONEM)** for USD 18/shr in an all-cash deal valued at USD 3.9bln. Note, ONEM closed Wednesday at USD 10.18/shr. Upside for **Akamai (AKAM)** attributed to StreetInsider chatter that a private-equity firm is lining up a bid. **Altice (ATUS)** reportedly considers a sale of Suddenlink for up to USD 20bln, according to Bloomberg.

FX WRAP

The Dollar was choppy on Thursday, but at pixel time it is lower having traded between a high of 107.330 and a low of 106.390. The main risk event from Thursday was the ECB rate decision, where the central bank unexpectedly raised rate by 50bps, alongside approving the Transmission Protection Instrument (TPI) and abandoning forward guidance. In an immediate reaction, EUR/USD rallied but throughout the rest of the session the move was somewhat faded. Moving to before the meeting, the single currency had already marked out a decent range on Italian political developments and a steady flow of Nord Stream headlines, but the cross extended the top side following the aforementioned ECB rate decision. The pair hit new highs circa 1.0278 and seemed destined to break even higher having picked off Wednesday's session high, probed a Fib retracement level and the 21 DMA. However, momentum waned by the time Lagarde revealed some details of the anti-fragmentation tool that the ECB has chosen to call the Transmission Protection Instrument, and it became clear that the bar for utilisation is high. Looking ahead, there is earnings from American Express (AXP), Verizon (VZ), and Twitter (TWTR) on Friday, as well as global PMIs.

Activity currencies were predominantly flat, with only the AUD seeing mild strength against the Buck. Cable saw highs of 1.2203, in contrast to lows of 1.1891 after the aforementioned ECB rate decision. On this, the Pound managed to settle flat after the whipsaw post-ECB surprise 50bps hike faded. Moreover, the ECB boost to GBP was only fleeting as inflation and growth risks remain, alongside the political turmoil. Aussie and Kiwi traded in tight ranges against the Buck, highlighted by the former between 0.6916-0.6860 and the latter pivoting either side of 0.6200, with a peak of 0.6242 and a trough of 0.6186. For the Kiwi, there was poor trade data, which continued to weigh, as the trade balance fell into a deficit from the prior surplus, accompanied by exports declining and imports rising. Meanwhile, the Aussie did have a rise in NAB business conditions, and the gains seen in equities alongside the bounce off lows in copper provided tailwinds for the antipode. Nonetheless, looking ahead market participants eye Friday's Australian PMIs as the next risk event. Lastly, the Loonie was not helped by the crude complex, highlighted by WTI and Brent seeing losses in excess of USD 3/bbl, and couple that with inflation and growth concerns it was not an appealing cocktail for the Loonie. Continuing, the cross traded between 1.2937-1.2861 and technicians note it was held firm by the 55DMA at 1.2868 after the second consecutive test fails.

Safe havens, CHF and JPY, firmed against the Buck with the Yen the G10 outperformer. Starting with the Yen, BoJ continued with its ultra-loose policy after it keeps policy unchanged, as expected, with rates at -0.10% and QQE with yield curve control maintained to target 10yr JGB yields at around 0%. Although, do note, USD/JPY was choppy in immediate reaction to the BoJ policy announcement but returned to preannouncement very quickly after the decision. Elsewhere, the disappointing US data in the form of jobless claims and Philly Fed dragged Treasury yields and the USD /JPY lower as the Yen saw some haven demand post-ECB. Swissy pivoted 0.9700 and leaned on some traction from the softer US Treasury yields amidst swings in broad risk sentiment.

EMFX was predominantly lower, with only the ZAR seeing gains and hence the outperformer. The ZAR was buoyed by a couple of factors, which was first the larger than expected SARB hike, as the central raised rates 75bps to 5.5% (exp. 5.52%). Additionally, the upside in gold also supported the Rand, as the yellow metal made a clean break above USD 1,700/oz to highs of ~ USD 1,718/oz. Aside from the RUB, TRY was the EM underperformer after the CBRT maintained rates and delivered almost identical forward guidance.