US Market Wrap

27th July 2022: Stocks rally as Powell tilts dovish

- **SNAPSHOT**: Equities up, Treasuries mixed, Crude up, Dollar down.
- **REAR VIEW**: Fed hikes 75bps, as expected; Sept. meeting will be based on data and it is time to go meeting-by-meeting; Mixed US data, decent durable goods but poor pending home sales; Constructive MSFT guidance; GOOGL beat on advertising & search components solid; Larger EIA crude draw than expected; Kremlin says Gazprom is supplying as much gas to Europe as possible; Slight upward revision to Q2 Atlanta Fed GDPnow model.
- **COMING UP**: **Data**: EZ Economic Sentiment, German CPI (Prelim.), US GDP Advance, PCE Prices Advance, IJC **Supply**: Italy & US **Earnings**: Amazon, Apple, Comcast, Intel, Pfizer, Merck, Altria, Southwest Airlines, Mastercard; Clariant, Nestle; Anglo American, Barclays, BAE; EDF, Euronext, L'Oreal, Sanofi.

MARKET WRAP

Equities took encouragement from Microsoft's earnings report, released after hours on Tuesday, with the tech giant offering constructive guidance. Traders were also encouraged by Alphabet's latest numbers (also released after hours Tuesday), where the advertising and search components were solid. Tuesday's data docket was mixed, with durable goods orders surprising to the upside, while pending home sales disappointed to the downside. These data points resulted in a slight upward revision to the Atlanta Fed's GDPnow model, which is now tracking growth of -1.2% in Q2 (from -1.6% previously). The Q2 advance GDP report will be released Thursday; analysts expect the data to print +0.5%, which would avoid two consecutive quarters of negative growth; nevertheless, the Atlanta Fed's tracking, and the fact that many analysts have forecast a negative print, will keep growth concerns alive. It is worth noting that policymakers have been keen to impress that two-quarters of negative growth does not always imply a recession, especially when the labour market is as solid as it is, and consumers continue to spend. The FOMC rate decision and statement was in line with expectations, although Chair Powell was dovish at the post-meeting press conference and suggested that the Fed had now moved onto a data-dependent, meeting-by-meeting basis, rather than flagging the size of a rate hike increment that the Committee would debate; the pivot was likely a result of the cooling of some macro indicators and rising risks of recession (See our analysis below). Equities rallied in wake of the dovish Powell, with the S&P 500 reclaiming the 4,000 handle. Meanwhile, in Europe, analysts have been casting a great deal of scepticism regarding this week's deal to reduce reliance on Russian energy; exemptions/opt-outs and the impact to growth were cited by many. Gazprom itself continues to squeeze the supply of European energy; flows to Europe via NS1 have already declined to 20% of capacity today, and there are indications that flows could be reduced further, according to Italy's Eni.

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FED: The Fed's rate decision and statement was in line with expectations, acknowledging some of the downside seen in recent; the post-meeting press conference was dovish, with Chair Powell essentially impressing that the Fed was going to be taking a data-dependent, meeting-by-meeting approach, rather than flagging the increment of rate hikes that the Committee would debate. The FOMC lifted rates by 75bps to 2.25-2.50%, as was expected, taking rates back to neutral for the first time since 2019. The only major tweak to the statement was its reassessment of the economy; the Fed now acknowledges that "recent indicators of spending and production has softened" (recall, it previously said that "overall economic activity appears to have picked up after edging down in the first quarter"). This change was to be expected given the softening in many key macro indicators. Going in to the rate decision, a very small minority of analysts were suggesting that the Fed could slow the pace of its balance sheet normalisation, but the central bank has opted against doing so. The statement offered no clues about what the Fed would do at its September meeting, but at his post meeting press conference, Chair Powell was more explicit, stating that over the coming months, the Fed was looking for compelling evidence that inflation is coming down, and the pace of future rate hikes would depend on incoming data and the outlook for the economy. This essentially suggests that the Fed will be data-dependent, and act on a meeting-by-meeting basis, rather than flagging policy in advance. Powell did, however, say that another large rate hike could be appropriate at the next meeting, and argued that the Committee wanted to get rates to moderately restrictive territory, which he suggested was between 3.0-3.5%. According to the June SEP, rates will be at this level by the end of this year (these forecasts will be updated in eight weeks' time, but Powell referred journalists to the June SEP when asked about his economic views); money market pricing, which had expected rates at 3.4% by end-2022 before Powell spoke, had eased to around 3.3% as the Fed Chair was speaking, implying that a rate rise to 3.25% was fully priced, with around 20% probability that rates would be lifted to 3.25-3.5%. Money markets are however pricing a degree of rate cuts next year; Powell was asked if his view of the terminal rate has changed (the June SEP implies this sits at 3.75-4.00%), and he responded that it had evolved for all participants on the Committee, and added that the Fed will have more data by September. Naturally, Chair Powell was quizzed on whether the US economy was in a recession; Powell seemed reticent to use the phrase, but reiterated that it was necessary to slow growth in order to create some slack in the economy, to allow the supply-side to catch-up; Powell also said that the slowdown in Q2 was notable, but the economy was still on track to grow this year, and demand was strong.

DURABLE GOODS: June's durable goods report surprised to the upside, with the headline rising +1.9% M/M (exp. -0.5%, prev. +0.8%); the ex-transport measure rose by 0.3% M/M (exp. +0.2%). "Durable goods activity continues to hold up in the face of strong headwinds, increasing for the fourth straight month in June," Oxford Economics notes, "while the strength was concentrated in transportation, durable goods orders excluding transportation notched a gain, indicating continued positive momentum beneath the surface." The non-defense capital goods ex-aircraft component rose +0.5% (exp. +0.2%). OxEco notes that it was the second consecutive rise, while the core shipments measure, which is its preferred gauge of business investment, was up 0.7%, which OxEco says offers a sturdy handoff for Q3. "The June data suggest that nominal equipment spending rose solidly in Q2, but with producer prices running hot over the past three months, real equipment spending growth – which will be reported tomorrow as part of the Q2 GDP report – is likely to show a more muted performance." Ahead, the consultancy says that slowing demand for durable goods from consumers, along with high inflation and rising interest rates, and the recession fears that these are bringing, will lead to slowing manufacturing activity. "Tighter financial conditions will make capital expenditure projects more expensive, but higher interest rates in line with what we're forecasting won't completely derail business investment prospects."

PENDING HOME SALES: The June pending home sales data disappointed to the downside, falling 8.6% M/M (exp. -1.5%). "The plunge in pending home sales is just tracking the extended rollover in mortgage applications, with the usual lag," Pantheon Macroeconomics writes, "both series are erratic month-to-month, but the trends are clear: Pending home sales capture contract signings for existing home transactions, which then usually close within a month or so." PM says that this suggests that we can also see a fall in July's pending home sales data too; "activity is now in free-fall, inventory is rocketing, and prices have started to fall. They have some way yet to go; we expect a total drop of 10-to-20%."

FIXED INCOME

T-NOTE (U2) FUTURES SETTLED 18 TICKS HIGHER AT 120-13+

The Treasury complex was drifting higher into the FOMC meeting, looking through mixed economic data (durable goods much better than expected, pending home sales were weak). The Atlanta Fed GDPnow tracker was revised higher in wake of the data, but given that the advance look at US Q2 GDP is due on Thursday, traders seemed happy to look through the update ahead of the FOMC. The Fed’s rate decision and statement were in keeping with expectations, although Powell was far more dovish in his post-meeting press conference; he said the Fed was moving to a data-dependent, meeting-by-meeting approach. That resulted in a Treasury rally, with 10yr yields falling to 2.73% (vs highs of around 2.82% earlier in the session). Powell reiterated that the Fed wanted to get rates higher than the current neutral levels into moderately restrictive territory, which he flagged was somewhere between 3.0-3.5%; he was also asked if his view of the terminal rate had changed, to which he referred back to the June SEP (which envisages terminal at 3.75-4.0% next year). Powell said his views had evolved, as had other Committee members’. In combination with the Fed statement now acknowledging the softness in some of the recent indicators, market pricing for the Fed rate hike trajectory narrowed. For the September meeting, markets are pricing a 50bps rate rise, and through to the end of the year, markets have fully priced a move to 3.0-3.25%, with around 20% probability of 3.25-3.5%. The profile in 2023 was modestly marked lower, but not by a great deal. The data-dependent approach makes Thursday’s GDP data, as well as the Friday’s employment cost index key.

CRUDE

WTI (U2) SETTLED 2.28 HIGHER AT 97.26/BBL; BRENT (U2) SETTLED USD 2.22 HIGHER AT 106.62/BBL

The crude complex saw gains throughout the NY afternoon, with WTI and Brent printing highs of USD 98/bbl and 106.95/bbl, respectively. In terms of the day, following the EIA data, where there was a larger crude draw than expected, the complex saw continued upside into settlement. After the Federal Reserve statement, which was in line with expectations, WTI and Brent were little changed. Moreover, on the weekly EIA data, production rose, whilst refining utilisation surprisingly printed -1.500% (exp. 0.4%), while gasoline also had a larger draw than consensus.

NORD STREAM 1: On the key NS1, nothing materially changed on the Russian gas front, aside from the Russian Kremlin noting Gazprom is supplying as much gas to Europe as possible, but it cannot guarantee supplies if foreign equipment cannot be serviced due to sanctions. Meanwhile, Siemens Energy (ENR GY) said from its side, the transportation of NS1 turbine could begin immediately and has provided with all the necessary documents.

GLOBAL OIL: A key Nigerian oil pipeline that exports Bonny Light crude oil has been empty since mid-June due to theft, according to Reuters sources. On this, Reuters highlight that earlier in July the SPDC MD said two of Nigeria's most important pipelines were shut due to theft but he did not name them. Elsewhere for Nigeria, the cabinet assumes 1.6mln BPD crude production for 2023 budget, according to Finance Minister. Lastly, Atyrau Oil Refinery in Kazakhstan halted processing due to an emergency power outage, while the Caspian Pipeline Consortium stated there is a power outage at two pumping stations in Kazakhstan due to bad weather; incident has not impacted July loading schedule.

US/EUROPE: US Deputy Treasury Secretary Adeyemo met with European counterparts to discuss a price cap on Russian oil.

EQUITIES

CLOSES: SPX +2.54% at 4,020, NDX +4.26% at 12,601, DJIA +1.37% at 32,197, RUT +2.06% at 1,842.

SECTORS: Communication Services +5.11%, Technology +4.29%, Consumer Discretionary +3.85%, Energy +2.2%, Industrials +1.58%, Financials +1.54%, Materials +1.25%, Consumer Staples +0.78%, Health +0.65%, Real Estate +0.54%, Utilities +0.11%.

EUROPEAN CLOSES: Euro Stoxx 50 +0.91% at 3,607; FTSE 100 +0.57% at 7,348; DAX +0.53% at 13,166; CAC 40 +0.75% at 6,257; IBEX 35 +0.68% at 8,124; FTSE MIB +1.52% at 21,480; SMI -0.41% at 11,056.

EARNINGS: **Alphabet (GOOGL)** missed on profit and revenue, but advertising revenue was strong. In commentary, the CFO said the FX impact is to be even greater in the current quarter. **Microsoft (MSFT)** missed on EPS and revenue, and saw its slowest earnings growth in two years amid a slowdown in its cloud business, but issued an upbeat outlook, saying currency-adjusted sales and operating income will increase by a double-digit percentage this Q. **Boeing (BA)** missed on the top and bottom line, but posted a surprise positive operating cash flow and unlike in prior Qs, did not see any charges related to the production of its 737 MAX jet. Boeing later announced it expects MAX deliveries to be closer to the low 400s for 2022, short of what was discussed earlier in the year. **Visa (V)** beat on EPS and revenue and noted it is seeing no evidence of a pullback in consumer spending and does not see any slowdown in spending by lower-income consumers. **Texas Instruments (TXN)** saw gains after a strong report, highlighted by surpassing consensus on top and bottom line alongside raising Q3 guidance. **T-Mobile (TMUS)** reported a surprise loss per share alongside missing on revenue, but it did raise guidance across the board. Additionally, postpaid net customer additions surpassed St. expectations. Moreover, CFO said they are seeing a slight increase in bill payment delays. Reminder, last week AT&T (T) said it is seeing late bill payments, which was in contrast to Verizon (VZ) saying it is not. **Sherwin-Williams (SHW)** saw notable losses following a poor report. Profit and revenue missed alongside cutting FY EPS view as it sees a negative 2% impact on Q3 sales due to unfavourable FX environment. **Spotify (SPOT)** missed the St. consensus on EPS but revenue and MAUs beat. Looking ahead, SPOT guidance was strong, as MAUs, revenue, and total premium subscribers were all lifted. **Hilton (HLT)** was up following a stellar report where it topped on EPS and revenue alongside raising its FY outlook. **Shopify (SHOP)** posted a wider-than-expected loss and said losses will increase in the current quarter. Shopify said inflation and rising interest rates will hurt consumer spending.

STOCK SPECIFICS: Two US senators are preparing legislation that would give merchants power to process many **Visa (V)** and **Mastercard (MA)** credit cards over different networks, according to WSJ. Activist Investor Elliott Management reportedly holds a stake in **PayPal (PYPL)**, size unknown, according to WSJ citing sources. **Cassava Sciences (SAVA)** plummeted after the US DoJ opened a criminal investigation into the co. involving whether it manipulated research results for its experimental Alzheimer's drug. SAVA later stated no government agency has filed any charges against the co. **Teva Pharmaceutical (TEVA)** surged after it reached a national settlement worth up to USD 4.25bln over its alleged role in the opioid crisis. **Alphabet's (GOOG)** Google is reportedly planning to delay the deadline for removing tracking cookies until at least 2024, according to Business Insider. Citron Research is short **Agilon Health (AGL)**. **Apple (AAPL)** taps Lamborghini executive to work on its electric car.

FX WRAP

DXY was lower on Wednesday, and after being choppy post the FOMC-rate decision, which was as expected where they hiked by 75bps and maintained its language and guidance on inflation but softened its tone on the economy. The Greenback saw significant softness throughout Fed Chair Powell's press conference, after Powell noted the pace of rate hikes going forward will depend on data and it is time to go to a meeting-by-meeting basis and not provide a clear guide as before. As such, a dovish reaction was immediately seen as DXY fell to session lows of 106.25 and all G10 peers saw gains against the Buck, with many rising to session highs. Additionally, US equities saw upside with all major indices rising to session highs. Regarding the rest of the day, DXY gleaned a little traction from a decent durable goods print, while there was significantly weaker pending home sales data. Looking ahead, following the Fed rate decision we will be on the lookout for any Fed speakers to hit the wires from Friday, whilst on the data docket there is US Q2 GDP on Thursday and US Core PCE for June on Friday.

Activity currencies were firmer across the board, with GBP outperforming and CAD underperforming, albeit still notably in the green. As previously mentioned, high beta FX saw strong gains through Powell's press conference, highlighted by Cable surging through the key 1.21 level to highs of 1.2186, whilst the AUD/USD rose to 0.7012. NZD/USD reached a peak of 0.6277, meanwhile, USD/CAD fell to 1.2809 from above 1.2900. On the moves, market participants picked up on remarks from Powell noting the Fed going forward will be data-dependent and go meeting-by-meeting. Elsewhere on Wednesday, the Aussie saw weakness in the APAC session after Australian CPI disappointed and fell short of expectations. Looking ahead, for Sterling, market participants await next week's BoE meeting, while there is Australian retail sales on Thursday and PPI on Friday.

Safe havens, CHF and JPY, saw gains against the Buck, albeit not as strong as its G10 counterparts. Highlighting this, USD/JPY and USD/CHF hit lows of 136.33 and 0.9585, respectively, in the midst of the Powell press conference. Prior to the Fed, it was choppy trade for the Swissy and Yen mainly amid fluctuations in broad risk sentiment, whilst there was a pick-up in Swiss investor morale, albeit still firmly negative. Regarding the calendar, there is Japanese CPI, unemployment and consumer confidence on Friday. Lastly, EUR gained against the Greenback and the EUR/USD cross even breached 1.02 to the upside, to highs of 1.0220 as the single-currency benefitted from a lift in equities and commodities. On the day, there were no fundamental updates to the European gas situation, but the Russian Kremlin stated Gazprom is supplying as much gas to Europe as possible, and cannot guarantee supplies if foreign equipment cannot be serviced due to sanctions. For the Euro, there is a slew of data in the coming days, such as EU consumer confidence, German CPI, EU GDP, and EU HICP.

EMFX was mixed on Wednesday, as BRL, MXN, and ZAR saw notable gains against the Buck, with the latter being spurred higher on rising gold prices which are at session highs, at pixel time. For the Real watchers, Brazil Presidential Candidate Lula stated he will make a new growth acceleration programme and will resume the housing programme if elected, which comes ahead of the Brazilian election in October. Moreover, Petrobras (PBR) Board has approved changing its fuel pricing policy. TRY and RUB saw losses, with the latter being weighed on by ongoing economic and political uncertainties.