US Market Wrap

31st August 2022: Stocks and bonds sold into month-end; hot EZ inflation boosts 75bps calls from ECB

- **SNAPSHOT**: Equities down, Treasuries down, Crude down, Dollar flat
- **REAR VIEW**: Hot EZ CPI; New series ADP prints beneath expected; Mester reiterates rates needs to rise somewhat above 4% by early next year, and hold it there; Taiwan fires further warning shots to fend off civilian drones; Kashagan oil output four times beneath normal output levels; STX cuts guidance; BBBY lowers outlook; Chicago PMI slightly beats expectations; OPEC+ JTC revised surplus forecasts and expects 2022 oil market surplus of 400k BPD; NS1 at 20% capacity due to anti-Russia's sanctions; GS, CS and BofA see 75bp hike from ECB next week.
- **COMING UP**: **Data**: Chinese, Australian, EZ, UK & US Manufacturing PMIs, German Retail Sales, Swiss CPI, EZ Unemployment, US ISM Manufacturing, Construction Spending **Speakers**: Fed's Bostic **Supply**: Spain, France & UK.

MARKET WRAP

Stocks continued their sell-off into month end with losses widespread with the majority of sectors closing in the red, other than Communication Services which were supported by strong gains in Meta (FB) which found tailwinds on the Snap (SNAP) restructuring/cost cutting update which buoyed the sector. However, Tech was predominantly lower, particularly hardware names after the guidance slash from Seagate Technologies (STX). Treasuries sold off in the morning in wake of hot eurozone inflation metrics before paring ahead of the US equity open, with some support seen after a worse than "forecasted" newly revised ADP report, ahead of the official BLS report on Friday. Elsewhere on data, the Chicago PMI was a touch better than expected while Fed speak was quiet, with just Mester on the wires repeating her call for rates above 4% and to be held there. Energy prices also saw renewed selling pressures tracking risk sentiment lower while the latest OPEC+ JTC revised their surplus forecasts and expects a 2022 oil market surplus of 400k BPD (prev. 900k) due to under production by members, while it now sees a deficit in 2023 of 300k BPD. In FX, the Yuan firmed vs the buck on better than expected PMI data and a firmer PBoC fixing than expected which helped offset any geopolitical woes with Taiwan sending more warning shots at drones. The Euro outperformed after the hotter than expected Eurozone CPI in the morning, which also weighed on fixed income before Treasuries pared somewhat after the US data, although selling resumed in the afternoon, particularly into the settlement while futures extended the decline post-settlement. With the ECB now heading into the blackout period ahead of next Thursday's meeting, several banks are forecasting a 75bp hike based on recent commentary and the hot inflation data. The highlight now turns to Friday's US NFP report.

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FED: **Mester (2022 voter)** reiterated rates needs to rise somewhat above 4% by early next year, and hold it there, and again remarked that the size of rate increments at each meeting depends on the inflation outlook. Furthermore, Mester noted we cannot yet be precise on the level of the Fed's terminal rate, (June SEP shows terminal at 3.75-4.0%, with markets also currently pricing in the 3.75-4% range). On inflation, Mester noted it is too soon to say inflation has peaked and wage pressures show little sign of abating, while the fight against inflation will be a long one. Additionally, Mester noted risks of recession have moved up and the Fed must be resolute in bringing demand into better balance with supply. Finally, the Cleveland Fed President said balance sheet reduction could take three years or so.

CHICAGO PMI: Chicago PMI printed 52.2, slightly above the expected 52.0 and the prior 52.1. Regarding the release, Pantheon Macroeconomics note, “the rebound in China’s Caixin PMI and rising orders for Boeing aircrafts, pointed to a stronger reading, so this is a bit of a disappointment.” Looking ahead to manufacturing ISM, Pantheon adds “Chicago PMI does not always move in line with the national ISM manufacturing index, but it is the final component of our model.” As such, Pantheon now expect the ISM to dip to 51, from 52.8, although a bit of this fall will be due to a further drop in the supplier deliveries index. The index is declining due to supply chains improving, reversing the squeeze which allowed margins to rise massively last year. As such, looking ahead, the consultancy hopes to see a modest uptick in all the regional surveys and the ISM over the next couple months, lagging the upturn in the China Caixin PMI. However, PM concludes, “the US numbers did not fall as far as the Caixin earlier this year, when China imposed widespread lockdowns, so they won’t rebound as much, either.”

ADP: The ADP's new gauge of its National Employment report showed that 132k private payrolls were added to the economy in August (expected 288k, July's reading was stated as 270k). ADP said that the data suggests a shift toward a more conservative pace of hiring, possibly as companies try to decipher the economy's conflicting signals; "we could be at an inflection point, from super-charged job gains to something more normal," it wrote. Within the release, ADP noted that the median change in annual pay (ADP matched person sample) was +7.6% Y/Y for Job-Stayers, and +16.1% Y/Y for Job-Changers. Capital Economics said that "with only limited details as to how they arrived at that number, we have little confidence that this new survey will prove to be any more accurate a guide to the official payrolls tally than the previous incarnation," adding that "according to the ADP, the new measure is not designed to 'forecast' the official non-farm payroll series, but is intended to be 'complementary' to the government data -- the limited history means that it contains only one full business cycle of data, so it will be of limited use for gauging turning points." OxEco add the new series paints a markedly different picture of employment than both the official household and establishment surveys.

FIXED INCOME

T-NOTE (Z2) FUTURES SETTLED 5+ TICKS LOWER AT 116-29

Treasuries were steeper amid a slowdown in Fed speak and a soft ADP print. 2s -1.2bps at 3.454%, 3s -0.5bps at 3.470%, 5s +2.1bps at 3.296%, 7s +3.7bps at 3.256%, 10s +3.4bps at 3.144%, 20s +4.8bps at 3.533%, 30s +4.6bps at 3.266%. 5yr BEI -9.2bps at 2.712%, 10yr BEI -6.6bps at 2.502%, 30yr BEI -4.5bps at 2.339%.

THE DAY: T-Notes (Z2) had an uneventful APAC Wednesday session with better-than-expected Chinese PMI data offsetting Taiwan/China angst. The contracts bounced slightly into the London handover, marking session highs of 117-07+ before the latest above-forecast inflation data in the EU saw better selling, taking them back down to session lows of 116-22+ before the US session got going. It was gradual loss paring from there, with Fed's Mester's reaffirmations of hawkish remarks doing little to sway tape action. The below forecast, new methodology ADP employment print added marginally to the support, although given the historical lack-of correlation to NFP, it didn't garner too much attention - neither did the beat on the Chicago PMI soon after. T-Notes hit resistance at 117-04+ in the later NY morning, which they failed to break above again through into settlement with Treasuries selling off throughout the afternoon.

STIRS:

- EDU2 +2.5bps at 96.620, Z2 +3.5bps at 95.930, H3 +1.0bps at 95.865, M3 +1.0bps at 95.895, U3 +0.5bps at 96.065, Z3 +1.0bps at 96.255, H4 +1.0bps at 96.450, M4 +1.5bps at 96.605, U4 +2.0bps at 96.705, Z4 +1.5bps at 96.775, Z5 -2.5bps at 96.915.
- Little major option flow aside from some (likely) profit taking in EDZ2 put spreads; 19k SR3U2 futures sold in blocks.
- US sold USD 30bln of 119-day CMBs at 3.100%, covered 3.54x.

CRUDE

WTI (V2) SETTLED USD 2.09 LOWER AT 89.55/BBL; BRENT (X2) SETTLED USD 2.82 LOWER AT 94.49/BBL

Oil prices were lower Wednesday, but well off their European session troughs, with risk aversion in the driving seat and bullish US inventory data in the back. The oil futures hit their peak at the Tokyo/London handover before risk assets saw pressure, no doubt aided by the latest hot EU inflation data. Prices hit their troughs for WTI (V2) and Brent (X2) in the late London morning at USD 88.27/bbl and 94.40/bbl, respectively. Prices then pared somewhat into the NY afternoon alongside stocks. The 6.4mln bbl US crude draw (which includes a 3.1mln bbl SPR release) didn't cause much of a notable reaction; the products saw a net 1.1mln bbl draw.

IRAN: US Department of Defense spokesperson Kirby said the administration is still optimistic about reaching an Iran nuclear deal. Meanwhile, Al Jazeera cited EU foreign policy chief Borrell saying he is hopeful on a nuclear deal in "days". That followed Iran Foreign Minister, speaking in Moscow, saying Tehran seeks stronger guarantees from the US for the revival of the deal.

RUSSIA & KAZAKHSTAN: Gazprom's head said Siemens (SIE GY) has no possibility to hold regular maintenance of equipment for Nord Stream 1 gas pipeline, Interfax reported. Said NS1 works at 20% capacity due to anti-Russian sanctions, and not possible to hold major maintenance. Meanwhile, Kazakhstan's Kashagan oil output was around 100k BPD on August 29-30th, four times beneath normal output levels, Reuters sources reported. Production will stay reduced at least until the end of September due to repairs for a gas release on August 3rd.

OPEC+: Initially, Reuters reported the OPEC+ JTC upgraded its 2022 oil market surplus forecast by 100k BPD to 900k BPD and said it expects the market surplus to rise to 1.4mln BPD in November from 0.6mln BPD in October, but later it was reported the JTC revised 2022 oil surplus to 0.4mln bpd from earlier 0.9mln due to underproduction by its members, in fitting with a Bloomberg report. BBG noted the OPEC+ panel tightened its oil market outlook for this year and next; and as such cuts estimate of 2022 surplus in half to 400k BPD and flips forecast for 2023 to deficit of 300k BPD. Elsewhere, JTC report said rising energy costs "may lead to a more significant reduction in consumptions towards year-end". Additionally, according to Argus media sources, JTC outlook assumes that OPEC+ members produce at their latest quotas for the remainder of the year, and a formal proposal to lower crude output quotas has yet to be put forward. Lastly, a Reuters survey sees OPEC oil output rising 690k BPD M/M in August to 29.58mln BPD, the highest since April 2020, with the survey suggesting oil output rise will be led by return of Libyan production, increases in Saudi Arabia and other Gulf members under OPEC+ deal.

EQUITIES

CLOSES: SPX -0.78% at 3,954, NDX -0.57% at 12,272, DJIA -0.88% at 31,511, RUT -0.89% at 1,836.

SECTORS: Materials -1.21%, Consumer Discretionary -1.05%, Technology -0.96%, Energy -0.94%, Financials -0.88%, Industrials -0.77%, Utilities -0.68%, Health -0.63%, Consumer Staples -0.58%, Real Estate -0.35%, Communication Services +0.01%.

EUROPEAN CLOSES: Euro Stoxx 50 -1.25% at 3,517; FTSE 100 -1.05% at 7,284; DAX -0.97% at 12,834; CAC 40 -1.37% at 6,125; IBEX 35 -1.17% at 7,886; FTSE MIB -1.22% at 21,559; SMI -0.39% at 10,842.

STOCK SPECIFICS: **Bed Bath & Beyond (BBBY)** tumbled after it announced a stock offering and strategic update where it lowered guidance. Moreover, BBBY is exiting a third of owned of owned brands and closing 150 stores. **Seagate (STX)** cut its guidance with revenue and EPS view beneath expectations due to worsening macroeconomic conditions. **Snap (SNAP)** lost two executives to **Netflix (NFLX)**, who are joining to develop its global advertising strategy. Elsewhere, SNAP confirmed it is laying off 20% of its roughly 6,400 employees and shuttering several projects to cut costs, according to WSJ, adds it is aiming to generate FCF in low growth scenarios. **Apple (AAPL)** Chief Privacy Officer to leave the co. to take on a role at a law firm, according to Bloomberg citing sources. **Boeing's (BA)** CH-47 Chinook helicopters have been grounded by the US Army due to risks of engine fires, according to WSJ citing US officials said, with the engines manufactured by **Honeywell (HON)**. Elsewhere, Boeing was awarded a USD 5.02bln Missile Defense Agency contract. **JPMorgan (JPM)** offices in Frankfurt, Germany were searched as part of a "cum-ex" probe, according to a JPM spokesperson. **Visa (V)** August US payments volume +11% Y/Y, but flat M/M. **Toyota (TM)** announced it is to spend USD 2.5bln to scale up production at its North Carolina plant. **Walmart's (WMT)** Sam's Club raises annual membership fee for the first time in nine years, according to CNBC. Elon Musk reportedly wants a longer **Twitter (TWTR)** trial delay over whistle-blower claims. **Tesla (TSLA)** is reportedly facing an “unprecedented demand,” according to a Wall Street analyst after a visit with management at Gigafactory Berlin cited by Electreck. It also shortened its delivery waiting time for some Model Y cars in China. Arm said it sued **Qualcomm (QCOM)** for licensing and trademark violations; says it filed suit against Qualcomm in US court and says it used technology without permission, according to Bloomberg. **Global smartphone** shipments expected to decline 6.5% in 2022 to 1.27bln units, amidst global inflation and softer demand, according to IDC. **CrowdStrike (CRWD)** beat on EPS and revenue alongside raising guidance. **HP (HPQ)** was lower after revenue missed alongside cutting its FY adj. EPS forecast and reiterating revenue growth forecast. Note, EPS was inline. **PVH (PVH)** beat on EPS but missed on revenue. Looking ahead, PVH cut its FY outlook and announced it plans to cut its workforce by 10%.

FX WRAP

The Dollar was choppy but ultimately flat on Wednesday at month end with equities adding to this week's weakness while there was mixed data from the US. The latest Chicago PMI data was marginally above expectations, for August, while the return of the ADP National Employment report was worse than expected, albeit analysts are cautious comparing to expectations given the methodology was not known beforehand. Fed speak saw Mester reiterate rates need to rise somewhat above 4% by early next year and to be held there, and she does not anticipate the Fed cutting the target rate next year based on her current economic outlook.

The Euro was the outperformer on Wednesday and held above parity throughout the afternoon, but it did print a low in the morning of 0.9972. EZ inflation came in above expectations with the HICP rising 9.1% Y/Y with core rising 5.1%, both above street expectations. Despite hot inflation, the upside for the Euro was limited by ongoing energy jitters after

Nord Stream 1 shut off the taps for three days due to maintenance. ECB speak saw Villeroy note the next rate move must be carried out with determination but in an orderly and predictable way. Meanwhile, Goldman Sachs, Credit Suisse and Bank of America are all out with fresh ECB forecasts and are calling for a 75bp hike next week.

The Yen was flat against the buck, weaker against the euro but firmer against cyclical currencies with the Euro supported by the aforementioned EZ CPI while cyclical currencies are hit on the stock rout. US Treasury yields were mixed across the curve in a steeper manner while overnight BoJ's Nakagawa spoke stating BoJ's policy response is having its intended effects and called for a continuation of easing to achieve its price target in a stable manner. However, Nakagawa added the BoJ decided to maintain easy policy bias in July and hopes to discuss that at the September meeting whether it should continue doing so based on data. Note, the July Industrial Production data was better than expected, as were Japanese retail sales. **CHF** was weaker against the Euro but firmer than the Yen and flat against the buck ahead of Swiss CPI Thursday morning.

Cyclical currencies were weaker across the board, in fitting with the downbeat risk sentiment into month-end although the antipodes were flat vs the Dollar, at pixel time. The Aussie outperformed peers throughout the European session on the back of better-than-expected Chinese official PMI metrics – which in turn bolstered copper prices. However, the turnaround in risk appetite later weighed, with AUD/USD flat intraday in a 0.6843-0.6904 range, and the pair sees its 10 and 50 DMAs at 0.6898 and 0.6909 respectively. NZD/USD sat in a 0.6111-0.6154 range, with the 10 DMA seen at 0.6177 today. AUD/NZD fell back under 1.1200 after finding some support at its 10 DMA (1.1164) earlier in the session. GBP was weaker and Cable tested 1.16 to the downside with the latest Citi/YouGov poll providing more worry on the inflation outlook. UK public inflation expectations for 5-10yrs jump to 4.8% from 3.8%; 1yr ahead jump to 6.3% from 6.1%. CAD was also weaker with USD/CAD trading between 1.3064 and 1.3140 with little reaction around the Canadian GDP metrics which were in line with expectations growing 0.1% in June and 0.8% in Q2 while StatsCan estimates July GDP most likely declined 0.1%. Meanwhile, oil prices tumbled again on Wednesday weighing on the Looney as well as the risk sentiment.

CNH firmed against the Dollar and as did CNY overnight. The PBoC overnight again opted for a firmer CNY fix, setting the mid-point at 6.8802 vs exp. 6.9076 (prev. 6.8698), and reports citing traders also suggested China's state-owned banks are seen selling US Dollars in the onshore spot market. USD/CNH looks to end the session around 6.9000. Meanwhile, the China PMI's were better than expected.

Scandi's saw NOK predominantly weaker on the downbeat risk tone and falling Brent crude prices, while SEK outperformed its Scandi peer, by quite a bit. Moreover, Riksbank's Breman is not ruling out a 50 or 75bps hike at the September 20th meeting.

EMFX was mixed, BRL saw pronounced weakness while MXN was relatively flat. There were several Banxico speakers on Wednesday, Esquivel interestingly noted Fed rate hikes do not automatically and necessarily mean hikes from Mexico, a different tone to Heath earlier in the week while Governor Rodriguez also said the Fed is an important element the Banxico follows but there is no pre-defined objective of following Fed rate hikes. In Brazil, Presidential Candidate Lula is looking for a gradual boost to the welfare programme, while the latest data saw the jobless rate drop to 9.1% in July, in line with expectations. Meanwhile, it posted a primary budget surplus of 20.44bln from a prior deficit of 32.99bln while the nominal budget balance was a deficit of 22.5bln from a prior deficit of 66bln Reals. Elsewhere in LatAm, CLP was weaker following weaker copper prices while the latest manufacturing output data declined more than the prior with copper output also falling. ZAR was weaker also in fitting with metal prices although the latest trade balance rose to 27.76bln Rand from 24.23bln.