US Market Wrap

12th September 2022: Risk on sees stocks, commodities, and high-beta FX gain but bonds dip after poor auctions ahead of CPI

- **SNAPSHOT**: Equities up, Treasuries down, Crude up, Dollar down.
- **REAR VIEW**: Poor 3y and 10yr auctions; NY Fed consumer inflation expectations see chunky declines; GS preparing for layoffs; US planning to broaden curbs on chip sales to China; AXP and BAC sanguine on consumer spending; Weak UK data.
- **COMING UP**: **Data**: UK jobs, German ZEW, US CPI **Supply**: Italy, US.
- **WEEK AHEAD PREVIEW**: Highlights include US CPI; China activity data; Shanghai meeting; UK data dump. To download the report, click here.
- **CENTRAL BANKS WEEKLY**: Reviewing ECB, BoC, RBA. To download the report, please click here.

MARKET WRAP

Stocks were firmer on Monday as participants position into Tuesday's CPI, accompanied by a softer Dollar and broader risk appetite. There was an earlier outperformance towards tech stocks (NDX > SPX) amid the fall in yields, although that unwound into the close as bonds dipped back lower after very-poor 3yr and 10yr auctions from the Treasury. Aside from the poor auctions, traders very much have their eyes on the inflation data due Tuesday, with some hopes that another soft print could be further evidence towards a downward trend. While some Fed officials have said the August CPI won't alter the Fed's decision on a 75bps September hike, any upside prints do risk skewing the distribution of outcomes towards more aggressive tightening paths going into year-end. Meanwhile, policymakers will have cheered to see the latest NY Fed consumer inflation expectation gauges Monday falling to 10-month and two-year lows in the 1yr ahead and 3yr ahead gauges, respectively - an incremental assurance of 'anchored' inflation expectations. For corporates, reports suggested Goldman Sachs (GS) is set to resumed layoffs amid a slowdown in dealmaking, although commentary on regional banks was more sanguine after US Bancorp (USB) announced positive revenue/NIM trends, although warned its mortgage revenue was down Y/Y. Meanwhile, American Express (AXP) and Bank of America (BAC) both gave positive commentary on the state of the consumer, with the former saying it isn't seeing any significant signs of weakness across its business.

GLOBAL

SHANGHAI COOPERATION ORGANIZATION (SCO) SUMMIT PREVIEW: The Shanghai Cooperation Organization (SCO) members include China, Russia, India, Kazakhstan, Kyrgyzstan, Pakistan, Tajikistan, Uzbekistan, and Iran. The group accounts for around a third of the world’s land, with exports in the trillions of Dollars. Several themes will be eyed as “anti-West” leaders gather in Uzbekistan, namely the theme of de-dollarisation alongside sideline meetings between Chinese President Xi and Russian President Putin, whilst Iranian bilateral and multilateral talks will also be eyed as its nuclear deal talks with the West have seemingly been less constructive. For a full Newsquawk preview, please click here.

FIXED INCOME

T-NOTE (Z2) FUTURES SETTLED 4 TICKS LOWER AT 115-19+

Treasuries bear-steepened Monday after poor 3yr and 10yr auctions reversed earlier strength ahead of CPI and 30yr. At settlement, 2s +0.2bps at 3.574%, 3s +0.3bps at 3.613%, 5s +1.5bps at 3.461%, 7s +2.6bps at 3.440%, 10s +4.3bps at 3.364%, 20s +4.9bps at 3.756%, 30s +6.1bps at 3.517%.

THE DAY: T-Notes traded in a thin range during the APAC session Monday (115-27+/115-18) with participants from China, Hong Kong, and South Korea all on holiday. There was gradual buying through the European morning, with particular spillover from UK Gilts after weak economic data. Session highs were hit in T-Notes at 116-06 in the NY morning before attention turned to the approaching Treasury supply, accentuated by the pick-up in corporate issuance (including USD 3bln deals from both T-Mobile and Home Depot). There was some temporary support after the fall in the NY Fed consumer inflation expectations. But downside momentum picked up after the poor 3yr auction (details below) weighed on the curve ahead of the 10yr, and those fears proved warranted as the latter also saw a big auction tail (details below), taking the contracts within a fraction of their Tokyo/London handover session lows at 115-18 heading into settlement. The 30yr auction on Tuesday will be eyed for stability, although it will come just hours after the CPI report. Note that the cash 30yr yield is now at new cycle peaks above the prior 3.49% peak in June, while the 10yr cash yield is approaching its June 3.50% peak.

3YR AUCTION: Despite the latest auction cuts and the highest yielding 3yr offering since 2007, the USD 41bln worth of notes were sold at a sizeable 1.4bps tail at 3.564%. That is opposed to Aug.'s 0.3bps stop-through and the six-auction avg. 0.1bps tail. However, it's worth highlighting that 3yr yields had already fallen 5bps ahead of the auction, taking away some of their appeal to the valuation-sensitive. The takedown saw Dealers (forced surplus buyers) with 23.6%, up from the prior 19.6% and avg. 23.4%, although that was largely a reflection of a large fall in Indirect participation (54.6% from 63.1%), where Directs saw a step-up to 21.9% from Aug.'s 17.3%.

10YR AUCTION: The second poor auction Monday, where the USD 32bln 10yr offering saw a massive 2.7bps tail, stopping at 3.330%, the highest yield since 2011 and still failing to benefit from auction size cuts. For reference, the six-auction avg. was a tail of 1.2bps, while the Aug. offering saw a much better 0.8bps stop-through. The 2.37x bid/cover ratio was worse than the prior 2.53x and avg. 2.45x. The takedown, similar to the 3yr, saw a step-up in Dealer participation to 19.8% from Aug.'s 9.9%, where that was due to a fall in Indirects participation to 62.3% from 74.5%, with a milder increase in Directs.

STIRS:

- EDU2 +1bps at 96.593, Z2 +3bps at 95.825, H3 +1.5bps at 95.795, M3 +2.5bps at 95.86, U3 +1bps at 96.00, Z3 +0.5bps at 96.18, H4 +0.5bps at 96.37, M4 flat at 96.51, Z4 -0.5bps at 96.665, Z5 -2bps at 96.755.
- Block activity saw 10k EDX2 95.50 puts for 3.25 (vs u/l EDZ2 at 95.83).
- Note that with EDU2 expiring on Monday, Sept 19th, which is now a UK bank holiday, the final settlement price will be based on the Friday, Sept. 16th 3m Libor fixing.
- NY Fed RRP op. demand at USD 2.219tln (prev. 2.210tln).
- US sold USD 46bln of 6-month bills at 3.465%, covered 3.03x; sold USD 59bln of 3-month bills at 3.075%, covered 2.74x.

CRUDE

WTI (V2) SETTLED USD 0.99 HIGHER AT 87.78/BBL; BRENT (X2) SETTLED USD 1.16 HIGHER AT 94.00/BBL

The crude complex saw gains on Monday as WTI and Brent printed highs of USD 89.10/bbl and 95.17/bbl, respectively, but settled well off these levels. Newsflow was thin to start the week, although macro themes remain in play, despite updates regarding Iranian nuclear deal and Ukraine/Russia being pretty sparse, as oil benefited from the softer Dollar and broader risk-on environment. Nonetheless, Bloomberg announced some reported internals regarding the EU’s draft energy plan. Looking ahead, market participants will remain cognizant of European energy updates, but there is the key macro event of US CPI on Tuesday, followed by private US inventory data later on.

EU: EU draft energy plan includes mandatory power demand cut, according to Bloomberg sources. Elsewhere, EU proposal for cap on revenue from non-gas fuelled power generators will see countries recovering the surplus revenues from non-gas generators after their power transactions are settled. On this, the revenues gathered by the EU must be used to support energy consumers exposed to high power prices. Additionally, it is to propose a solidarity contribution for the fossil fuel industry, based on taxable surplus profits made in FY22.

OUTPUT: Kazakhstan oil output fell 13% in August from July to 1.2mln BPD amid maintenance on Kashagan and Tengiz oilfields, according to Reuters. As a reminder, Reuters reported on Aug 31st Kashagan’s oil output was around 100k BPD between August 29-30th, four times beneath normal output levels, as oil production was shut down on August 3rd due to a gas release.

UKRAINE/RUSSIA: IAEA Chief Grossi stated he has seen signs that Russia and Ukraine are interested in a protection zone around Zaporizhzhia nuclear power plant; both sides are engaging with IAEA and asking questions.

GAS COMMENTARY: Goldman Sachs sees TTF prices declining sequentially through winter, dropping from EUR 215 /MWH this summer to below EUR 100/MWH in Q1 2023. Meanwhile, GS raises summer 2023 TTF prices to EUR 235 /MWH (prev. EUR 153/MWH, vs. forwards at EUR 184/MWH). Additionally, GS adds NW European gas storage will reach over 90% full this summer even as Russian supplies halt, and the bank expects high storage levels at the beginning of the season to accommodate larger-than-average storage withdrawals.

OSP'S: Echoing Saudi Aramco last week, Iraq saw big cuts to its OSPs, especially to Asia highlighted by the fact Iraq sets October Basrah medium crude price to Asia at plus USD 1.40/bbl vs Oman/Dubai average (prev. plus 5.10).

EQUITIES

CLOSES: SPX +1.09 at 4,111, NDX +1.20% at 12,739, DJIA +0.72% at 32,383, RUT +1.22% at 1,905.

SECTORS: Energy +1.83%, Technology +1.64%, Consumer Discretionary +1.35%, Utilities +0.97%, Materials +0.89%, Financials +0.88%, Real Estate +0.86%, Health +0.66%, Industrials +0.61%, Communication Services +0.45%, Consumer Staples +0.43%.

EUROPEAN CLOSES: EURO STOXX 50 +2.14% at 3,646, FTSE 100 +1.66% at 7,473, DAX 40 +2.40% at 13,402, CAC 40 +1.95% at 6,333, FTSE MIB +2.33% at 22,610, IBEX 35 +2.01% at 8,194, SMI +0.85% at 10,993.

STOCK SPECIFICS: Bloomberg reported that **Intel (INTC)** is targeting a lower valuation for its Mobileye IPO to USD 30bln from over USD 50bln and may delay it to 2023 amid the stock rout. **Amazon (AMZN)** sellers are bracing for a bleak holiday shopping season, according to Bloomberg, and many merchants will be forced to cut prices to move unsold inventory. **Disney (DIS)** CEO said he has rejected calls by activist investor Dan Loeb to sell or spin off the ESPN sports television network, FT reports, vowing to restore the business to its one-time status as a growth engine of the company. **Bristol-Myers Squibb (BMY)** had the US FDA approve Sotyktu oral treatment for adults. **Berkshire Hathaway (BRK.B)** raised its stake in **Occidental Petroleum (OXY)**, again, to 26.8% from 20.2% after last month receiving approval from US regulators to buy as much as half of the Co. **General Electric (GE)** targets the spin-off of GE HealthCare in the first week of January 2023. **Adobe (ADBE)** was downgraded at Mizuho, which said this quarter was indicative of a more difficult environment than expected and wouldn't be surprised by a guide down for Q4. Note, Adobe reports earnings on Thursday. **Oak Street Health (OSH)** was downgraded at Goldman Sachs as it noted a more cautious outlook reflects the cos. growth-profitability constraints. **US Bancorp (USB)** said the expectation is that NIM will continue to expand and NII will grow into 2023 at a more moderate level; said it was seeing positive revenue growth apart from in its mortgage business. **Goldman Sachs (GS)** is reportedly preparing for layoffs as dealmaking slows, according to the NYT. GS typically revisits its headcount every year, but it paused that during the pandemic, and it typically lays off 1-5% of workers, but this is expected to be at the lower end of that range. **Yum! Brands (YUM)** announced USD 2bln share buyback programme. **Gilead Sciences (GILD)** announced it settled a patent case over its HIV therapies with five generic drugmakers. **Carvana (CVNA)** was upgraded at Piper Sandler, who called the stock “grossly undervalued” and believes Carvana could double from current levels. **American Express (AXP)** CFO said Co. feels "even better" about its multi-year outlook it provided back in January; don't see any "significant signs of weakness" anywhere in the parts of the economy Co. covers. **General Dynamics (GD)** upside attributed to remarks made at Barclays conference that implies FAA approval for G500/600 software fix appears imminent.

FX WRAP

The Dollar sold off to start the week, in what was a risk on day with equities adding to the gains seen late last week. Attention now turns to the US CPI report on Tuesday where expectations are for another cooling on the headline amid the recent downturn in energy prices, although Core CPI is actually seen accelerating slightly. The Fed is on blackout so we will not hear from the Fed themselves after the release, but we may potentially hear from news journalists if the report does alter their thinking. However, it is worth remembering that Fed's Bullard last week suggested a good CPI report this week is unlikely to alter the Fed's thinking for the September 21st FOMC. Consumer inflation expectations saw a marked improvement on Monday, falling to a 10-month low for the 1yr expectations to 5.75% (down from 6.2% in July) and 3yr expectations fell to the lowest in almost two years at 2.8% from a prior 3.2% - a welcome sign for the Fed. Markets are currently implying a 93% probability of a 75bp hike in September, and just a 7% probability for a smaller 50bp move.

The Euro was bid on Monday and tested 1.02 to the upside at its highs, topping out at 1.0197 although the single currency moved off highs as EGB yields pared somewhat while hawkish ECB speak also cooled, with ECB's Scicluna suggesting the central bank will continue with rate hikes but they are unlikely to be as large as the 75bps hike seen last week. Meanwhile, EUR/GBP tested the 2022 peak at 0.8721, printing a high today of 0.8722 - but as the Euro sold off in the afternoon, the cross completely unwound its gains.

The Yen was flat vs the buck trading in between a range of 142.17 and 143.49, but off the near 145 peak seen last week where official verbal intervention has been playing its role in the Yen strength off recent lows. Over the weekend, a Japanese Government spokesperson added to the chorus noting Japan must take steps against excessive declines in the Yen. Meanwhile, reports overnight suggested Japan is eyeing allowing foreign visitors to travel freely without travel agency bookings and is to waive visa requirements, with PM Kishida to make the decision as early as this week, according to FNN. The move to allow more accessible visits to Japan could be a way to help with improving foreign demand for the Japanese Yen at a time of weakness, while the government spokesperson stated a weak yen is most effective in attracting tourism and further steps may be taken to attract more tourists.

The offshore Yuan (CNH) firmed against the buck while there was no trading in CNY overnight due to market holidays. However, COVID remains an ongoing issue in China and Global Times reported a variant of Omicron was discovered in China and poses risks of community transmission. Moreover, the Deputy director of Neijiang Center for Disease Control and Prevention Xu warned that the city is in the most critical moment of the epidemic development and reminded the public to carefully check the itinerary of their movements. Meanwhile, reports suggest Google (GOOGL) is planning its Pixel phone assembly in India, amid the China lockdowns - in a similar move to Apple. Elsewhere on tech, Reuters reported the US is planning to broaden curbs on sales to China of semiconductors used for AI and chipmaking tools, according to sources.

Cyclical currencies tracked the risk appetite and weaker Dollar higher, highlighted by solid gains in GBP which outperformed on Monday, irrespective of disappointing UK GDP, IP and Output. In addition to date, senior officials played down an EU offer to reduce the number of customs inspections at the NI border. Attention in the UK lies on the upcoming fiscal event in September, although no concrete date has been set. NZD/USD briefly rose a bit further above 0.6150 but ultimately returned beneath the level and the Aussie approached 0.6900, but topped out at 0.6899 as it managed to briefly breach the 55dma at 0.6893, but ran out of momentum ahead of the round number. Aussie traders had been eyeing the 10dma at 0.6807 as a level of support, which held well on Monday as it rebounded after hitting a low of 0.6805. AUD/NZD lost momentum from around 1.1235 to lows of 1.1184 awaiting NAB consumer confidence and conditions before NZ current account balances for Q2. CAD also saw gains vs the buck supported by the risk environment and higher oil prices.

EMFX was generally bid across the board, thanks to the weaker greenback and upside in equities. There was strength in ZAR which tracked the decent move higher in gold prices while RUB also saw solid gains vs the buck. CLP found solace in the move higher in copper prices and was the LatAm outperformer while COP and ARS were weaker against the buck, but BRL and MXN saw gains. The HUF underperformed after the European Commission expressed a desire to see more action from Hungary on stepping up anti-corruption safeguards before Brussels agrees to unlock EU funds, according to Reuters sources, and the the Try was undermined by a wider than anticipated Turkish current account deficit.