US Market Wrap

27th September 2022: Bond rout continues but stock sales lose momentum

- **SNAPSHOT**: Equities mixed, Treasuries down, Crude up, Dollar up.
- **REAR VIEW**: BoE's Pill pushes back on inter-meeting BoE action, touts significant November action; Evans optimistic terminal rate the Fed has set out will be restrictive enough; Kashkari and Bullard tout party line; Strong US data as consumer confidence, durable goods and new home sales all top expected; Prelim results show Donbass, Kherson and Zaporizhia agree to join Russia; Russia will likely propose 1mln BPD OPEC+ output cut at next meeting; Weak US 5yr auction; EU poised to adopt new sanctions on Russia; TSLA to keep Shanghai output beneath maximum.
- **COMING UP**: **Data**: German GfK **Speakers**: Fed's Daly, Bostic, Bullard, Bowman, Barkin; ECB's Lagarde, Elderson; BoE's Cunliffe, Dhingra **Supply**: US.

MARKET WRAP

Another rollercoaster session as far as fixed income was concerned, although the selling in stocks lost some momentum as major indices close little changed. The moves were framed as a natural bounce amid short-covering/tired tape. Bonds had entered the US session on the front foot, although renewed heavy selling on both sides of the pond was observed again. BoE's Pill spoke, essentially pushing back further on the prospect of any inter-meeting action, but alluded to a major BoE reaction at the next meeting (Nov 3rd), the UK 10yr and 30yr Gilt yields rose above 4.5% and 5%, respectively. Meanwhile, better than expected US data across consumer confidence, new home sales, durable goods, and Richmond Fed survey kept the pressure on USTs, where a poor 5yr auction saw the curve hit lows of the session, with the cash 10yr coming within earshot of 4% **-** the 7yr auction is due Thursday. Despite the heavy Gilt selling, Cable held onto its gains, albeit well of highs, with Sterling selling hitting near-term limits. Oil prices were firmer with Russia touted by Reuters to be flirting with a 1mln BPD OPEC+ production cut proposal.

CENTRAL BANKS

BOE: **Chief Economist Pill** broke the silence after the recent Sterling market turmoil. Pill echoed Governor Bailey's statement on Monday, saying that the MPC is relying on communication in the run-up to the November meeting, pushing back on expectations of inter-meeting action further; said monetary policy has limitations for fine-tuning short-term developments. He countered that hesitancy by saying it's hard not to draw conclusions that a significant monetary policy response will be required in November (money markets are pricing in over 125bps of hikes by the next meeting on Nov 3rd). The official was also keen to express the need for orderly and well-functioning markets, but insulated that current market moves have been a repricing to economic fundamentals. Said BoE will not sell Gilts into a dysfunctional market, but as long as the market is orderly repricing of fundamentals, QT can continue. Note the first active BoE Gilt sales are scheduled for Monday.

FED: **Kashkari (2023 voter)**, in an interview with WSJ, noted markets understand what the Fed is doing and Fed policymakers are united and are committed to bringing down inflation, but he is not sure policy is tight enough. Kashkari reiterated that the Fed needs to keep tightening policy until it sees compelling evidence that underlying inflation has peaked and is heading down. The Minneapolis Fed President also said a soft landing is still possible, but whether that is realised or not is a lot out of the Fed's control. **Bullard (2022 voter)** said the US has a serious inflation problem and the credibility of the inflation targeting regime is at risk. **Evans (departing, non-voter, dovish)** is optimistic the terminal rate the Fed has set out (4.6% median in Dot Plot) will be restrictive enough. **Mester (2022, 2024 voter)**, after market on Monday, said further rate hikes will be needed and will need a restrictive stance for some time; can be better to act more aggressively in an uncertain environment and pre-emptive action can prevent worst-case outcomes. Additionally, she added this is the time to be decisive. Mester believes the Fed policy rate may be right below restrictive levels; not at neutral yet and need to get above that. **Harker (2023 voter)** said the Fed is working to stabilise inflation; getting shelter inflation under control will require action not just by the Fed, but also by federal, state, and local governments.

US DATA

DURABLE GOODS: US durable goods orders in August fell 0.2%, less than the expected 0.4% fall but still a deeper decline than July's 0.1% fall. The ex-transport orders rose 0.2%, as expected after the decline in aircraft orders was well telegraphed going into the print. There was also another big 0.7% rise in headline shipments. Oxford Economics opine, "The high inflation environment means these nominal data overstate the real strength of durable goods, but it's nonetheless encouraging to see factory activity remaining fairly resilient given the grim economic backdrop." Meanwhile, the core nondefense capital goods orders excluding aircraft rose a chunky 1.3%, above expected 0.2%, with the prior revised up to +0.7% from +0.3%, a positive trend for business spend. Oxford Eco adds, "Also encouraging was that core shipments - our preferred business investment gauge - climbed 0.3%, pointing to reasonable equipment spending growth in Q3." The consultancy notes the outlook sees a "dwindling pipeline", offering minimal growth impulse for manufacturing going into 2023. Things are ok for now, but higher rates, higher inflation, weaker demand, and downbeat sentiment will weigh on durables next year, but on an aside, "softening activity will lead to a better balance between supply and demand and reduce stress in supply chains."

CONSUMER CONFIDENCE: US consumer confidence for September rose to 108.0, above the expected 104.5 and the prior, revised higher, 103.6. The Present Situation and Expectations indices both rose to 149.6 (prev. 145.3) and 80.3 (prev. 75.8), respectively. Elsewhere, the assessment of the labour market improved as 49.4% (prev. 48.0%) said jobs were plentiful and a slight fall to 11.4% (prev. 11.6%) noted jobs hard-to-get. Meanwhile, 1yr consumer inflation expectations declined to 6.8% (prev. 7.0%). Looking into the survey, consumer confidence improved for the second consecutive month and was supported, in particular, by jobs, wages, and declining gas prices, while Expectations also improved from summer lows, but recession risks nonetheless persist. The report notes, “purchasing intentions were mixed, with intentions to buy automobiles and big-ticket appliances up, while home purchasing intentions fell. The latter no doubt reflects rising mortgage rates and a cooling housing market.” Looking ahead, the report adds, “the improvement in confidence may bode well for consumer spending in the final months of 2022, but inflation and interest-rate hikes remain strong headwinds to growth in the short term.” Overall, it is a steady report but is still low compared to the pre-pandemic level, suggesting consumers are still worried about the economic outlook.

RICHMOND FED: US Richmond Fed composite manufacturing index rose to 0 in September, against the prior -8. Within this, two of the three component indices significantly improved as shipments and volume of new orders jumped to 14 (prev. -8) and -11 (prev. -20), respectively. Although, the third component, the employment index dropped to 0 (prev. 11) highlighting hiring challenges still remain. Additionally, the wage index rose notably to 40 (prev. 27) and surpassed its July and August levels, and local business conditions index rose but remained negative in September, as did firms’ expectations of conditions over the next six months. Meanwhile, the report details, there was not much indication of supply chain relief, as indices for vendor lead time and backlog of orders remained steady, although both have improved dramatically since earlier this year. Lastly, on the inflationary footing, the average growth rate of prices paid and prices received both decreased markedly in September, as expectations for both over the next 12 months changed little from August.

NEW HOME SALES: US new home sales rose to the strong pace of sales since March to 685k in August, above the expected 500K and prior, revised higher, 532k. Meanwhile, supply of homes edged up 0.4% to 461k units, and that amount of inventory translated to 8.1 months' worth of supply (prev. 10.4 months). Regarding the release, Oxford Economics note, “lower prices may have helped support home sales, with median new home prices declining 6.3%”, and looking ahead OxEco “don't expect the August pace of sales to be sustained in the months ahead, as the latest rise in mortgage rates will take an added toll on homebuying affordability.” However, the consultancy concludes, “further price declines may bring in buyers... keeping a floor under activity”.

FIXED INCOME

T-NOTE (Z2) FUTURES SETTLED 15 TICKS LOWER AT 110-28+

Treasuries bear-steepened amid renewed Gilt selling, strong US data, and another weak Treasury auction. 2s -0.2bps at 4.308%, 3s +0.1bps at 4.397%, 5s +5.3bps at 4.212%, 7s +7.9bps at 4.145%, 10s +8.8bps at 3.968%, 20s +13.9bps at 4.159%, 30s +15.1bps at 3.848%.

Inflation breakevens: 5yr BEI +5.3bps at 2.404%, 10yr BEI +3.3bps at 2.356%, 30yr BEI +1.8bps at 2.234%.

THE DAY: T-Notes found support through the APAC session and into the London morning alongside the recovery/short-covering in UK Gilts, taking the T-Note to session highs of 112-01+ at the NY handover. But, renewed selling resumed with an eye toward BoE's Pill and the US 5yr auction. Fed's Evans and Bullard were on the wires at the time but neither said anything surprising on Fed comms (in short, reaffirming the hawkishness), instead, the action came again from the Gilt complex as BoE's Pill expressed interest for waiting until the next BoE meeting in November to take any action whilst saying a "significant" response would be required. The UK 30yr yield later hit fresh peaks above 5%. Meanwhile, adding to the Treasury selling, was the bounce in US confidence, new home sales, Richmond Fed survey, and core durable goods orders. T-Notes ultimately hit session lows of 110-22 in wake of the poor 5yr auction (more below), with cash 10yr yield peaking at 3.992%. Attention now moves to the 7yr auction on Wednesday alongside another Fed speak deluge.

5YR AUCTION: Another weak Treasury auction with the vol-ridden market seeing the USD 44bln 5yr offering tail by 2.6 bps, well above both the prior 1bps tail and six-auction average at 0.6bps. The 4.228% stop marked a material cheapening from August's 3.230%, and the already 4+ bps concession Tuesday wasn't enough to see meaningful demand. The low 2.27x bid/cover ratio reflected the poor demand reception. The takedown saw Dealers with a chunky 21.7%, above the prior 20.6% and average 19.1% amid a step down in Indirects participation.

STIRS:

- EDZ2 +4.0bps at 95.30, H3 +10.5bps at 95.21, M3 +13bps at 95.205, U3 +12.5bps at 95.27, Z3 +7bps at 95.33, H4 +3bps at 95.495, M4 +1.5bps at 95.665, U4 flat at 95.785, Z4 -0.5bps at 95.89, Z5 -6.5bps at 96.05.
- NY Fed RRP op. demand USD 2.327tln (prev. 2.299tln).
- Heavy Treasury short base sees market repo rates pressured lower.

CRUDE

WTI (X2) SETTLED USD 1.79 HIGHER AT 78.50/BBL; BRENT (X2) SETTLED USD 2.21 HIGHER AT 86.27/BBL

Oil prices were firmer Tuesday despite the risk aversion amid a slew of supply updates ranging from OPEC production cut proposals to Hurricane Ian. WTI and Brent front-month contracts hit session highs of USD 79.51/bbl and 87.15/bbl in the NY morning after Reuters reports Russia will likely propose OPEC+ reduces output by around 1mln BPD at the next meeting. The selling momentum in stocks and bonds took commodities off their highs although the oil benchmarks did reapporach the peaks in later trade as the broader risk aversion lost momentum.

IAN: The latest US offshore regulator update announced 190,358 barrels of oil (11% of offshore) and 184mln cubic feet of gas (8.6%) were shut in on Tuesday in the Gulf of Mexico due to Hurricane Ian. However, BP (BP/ LN) said on Tuesday afternoon that it has determined hurricane Ian no longer poses a significant threat to its Gulf of Mexico assets and is looking to redeploy personnel, which likely means other major producers will follow suit.

EUROPE: Gazprom warned there’s a risk Moscow will sanction Ukraine’s Naftogaz, which would prevent it from being able to pay transit fees, and therefore put at risk gas flows to Europe via Ukraine. There was a move higher seen in Dutch TTF futures in wake of the legal threats. Meanwhile, Danish and Swedish authorities have attributed the major gas leaks on the Nord Stream 1 and 2 pipelines to large explosions, coming amid claims it was sabotage. However, there is not much imminent market impact given the pipelines are not currently being used, although the situation does highlight the geopolitical fragility. Meanwhile, WSJ had a sources piece that said EU officials need further time to agree to the fix which would allow an international price cap on Russian oil (echoes recent reporting about internal disagreements).

EQUITIES

CLOSES: SPX -0.17% at 3,649, NDX +0.16% at 11,271, DJIA -0.43% at 29,134, RUT -0.17% at 1,661.

SECTORS: Consumer Staples -1.76%, Utilities -1.7%, Real Estate -1.28%, Communication Services -0.72%, Industrials -0.31%, Financials -0.3%, Health -0.21%, Technology +0.22%, Materials +0.23%, Consumer Discretionary +0.29%, Energy +1.16.

EUROPEAN CLOSES: EURO STOXX 50 -0.42% at 3,328, FTSE 100 -0.52% at 9,984, DAX 40 -0.72% at 12,139, CAC 40 -0.27% at 5,753, FTSE MIB -1.16% at 20,961, IBEX 35 -0.84% at 7,445, SMI +0.52% at 10,112.

STOCK SPECIFICS: **Tesla (TSLA)** is planning to hold Shanghai production beneath the maximum output, at around 93%, throughout the end of the year despite the recent upgrade, according to Reuters sources. **Synnex (SNX)** EPS printed inline and beat on revenue, but looking ahead it cut next Q EPS and revenue view. **Jabil (JBL)** beat on the top and bottom line estimates; next quarter EPS and revenue view surpassed Wall St. expectations and announced a USD 1bln share repurchase programme. **Goldman Sachs (GS)** has begun laying off workers across the US and is focused on cutting mid-level investment bankers amid a downturn in dealmaking as the economy slows, according to Business Insider. **TSMC (TSM)** has seen its major fabless customers start cutting back wafer starts for 2023, and may prompt the Co. to revise its sales outlook at an investor conference in January, according to DigiTimes citing sources. **US Silica (SLCA)** announced price increases of between 9-20% on industrial and specialty products. **Nio (NIO)** warned energy crisis and tight labour market is slowing its European expansion; rising battery costs, driven by increases in the price of raw materials, delaying the target of becoming profitable, according to an executive talking to the FT. **Keurig Dr Pepper (KDP)** was downgraded at Goldman Sachs; said it sees increased risk to Co.'s margins as commodity inflation, especially related to coffee, remains elevated. **Just Eat (JTKWY)** said adj. EBITDA is to be profitable in H2 2022 and profitability is now expected to come earlier than anticipated. **Velodyne Lidar (VLDR)** announced a multi-year agreement to provide its lidar sensors to Stanley Robotics for an automated valet parking solution. **Avidity Biosciences (RNA)** announced FDA partial clinical hold on trial enrollment due to a serious adverse effect reported in a single participant. **Tesla (TSLA)** CEO Musk's deposition by **Twitter (TWTR)** has been rescheduled to October 6th-7th, according to a court filing. While CNBC's Faber added he is hearing nothing suggesting signs of settlement talks on the horizon between Musk and Twitter. **Intel (INTC)** CEO said GPUs are too expensive and announced flex data centre graphics cards. Arc A770 GPU to sell for USD 329, beginning in October. **Ryder (R)** being eyed up by **Apollo Global (APO)** for a potential takeover; other suitors could emerge, according to Bloomberg. **Disney (DIS)** to closing Florida theme parks Wednesday and Thursday ahead of Hurricane Ian.

FX WRAP

The Dollar was choppy on Tuesday but eventually firmer, highlighted by the fact the Buck meandered between a peak of 114.480 and a trough of 113.330. US data was pretty strong as consumer confidence and home sales both surpassed expectations as did durable goods, albeit still a decline M/M, but markets paid sparce attention due to the wider macro sentiment. Fed speak was heavy, as Evans (departing, dovish) said he is optimistic the terminal rate the Fed has set out (4.6% median in Dot Plot) will be restrictive enough and Bullard (2022 voter) noted the US has a serious inflation problem with the credibility of inflation targeting regime at risk. Lastly, Kashkari (2023 voter) declared markets understand what the Fed is doing and policymakers are united and are committed to bringing down inflation, but is not sure policy is tight enough. For the rest of the week, aside from a plethora of Fed Speak scheduled, the data highlight is PCE on Friday and the final UoM survey.

GBP was mildly firmer against the Buck, but well-off earlier session highs, as Sterling attempted to reclaim some of the significant losses seen on Monday. As such, Cable reached a high of 1.0838 in contrast to a low of 1.0655, but the cross spent most of the NY afternoon around the 1.07 level, as the Pound could not maintain its earlier strength in the European morning. BoE Chief Economist Pill downplayed prospects of an emergency or interim hike as he said the MPC is relying on communication in the run-up to the November meeting but did note it is hard not to draw the conclusion that a significant monetary policy response is required. Pill later added the BoE is not running faster than elsewhere in reducing its balance sheet, but the process is different; said the bank would not sell Gilts into a dysfunctional market, but as long as the market is orderly repricing the fundamentals, QT can continue. As such, the latter remarks spelt out in more certain terms that there are no plans to alter the current Gilt sales plan (with Gilts expected to be sold from next Monday). Looking ahead, BoE’s Dhingra, 25bps dissenter, is scheduled to make remarks on Wednesday.

Activity currencies, CAD, NZD, and AUD were mixed as the former outperformed with slight gains while the latter saw losses vs the Buck, although all aforementioned currencies retreated from best levels as the Dollar upside in the NY afternoon weighed. Elsewhere, the rebound in the crude complex supported the Lonnie as USD/CAD reached a low of 1.3641, while AUD/USD retreated from 0.6500+ ahead of final retail sales.

Safe havens, JPY and CHF, were more-or-less flat vs the Buck and traded within fairly narrow ranges given the scale of recent moves. USD/JPY traded between 144.90-08 and USD/CHF bounced from 0.9850 to highs of 0.9946. For the Yen, 145 is the pivotal level as technicians note there are major options expiries this week at this level which comes ahead of Thursday's 24-year peak at 145.90 that triggered Japanese intervention.

EUR saw slight losses against the Dollar amid the increasingly bleak outlook for the single currency due to the Ukrainian war, among other factors. On this, the Euro’s outlook is dimmed by the deteriorating prospects for Europe's economy amid rising energy insecurity which threatens notable losses for businesses and soaring costs for consumers and governments trying to subsidise energy costs. There was also a WSJ sources piece noting that fresh EU sanctions are set to be announced on Russian individuals, with the bloc looking at an import ban on the still un-sanctioned Russian steel sector. Elsewhere, there was a slew of ECB speakers with the most notable remark from Villeroy who noted the ECB should reach the neutral rate (largely touted in the 2% region) before assessing. On Wednesday, ECB President Lagarde and Elderson are on the speaker docket, while the data slate is sparse ahead of a range of key data points on Thursday.

EMFX was mixed as ZAR and BRL saw gains and hence outperformed, but RUB, TRY, and CNY/CNH reside in the red vs the Buck. Softer than forecast Brazilian mid-month CPI metrics did not weigh too heavily on the BRL as BCB minutes left the door open to a resumption of tightening without hesitation if the disinflation process does not pan out as anticipated, while the ZAR was encouraged by a recovery in Gold and reports via the SA Government indicating that

Finance Minister Gordhan plans to restructure and reconstitute the Board at Eskom. Elsewhere, the HUF got an unexpected lift and unwind from the NBH following up its above-forecast 125bps rate hike with a statement saying it is ending its rate hike cycle. CNH inched closer to its record low in wake of a sub-forecast PBoC reference rate for the CNY, steeper decline in Chinese industrial profits, and a worrying GDP outlook from the World Bank.