US Market Wrap

21st November 2022: Risk off with new China restrictions while oil whipsaws on OPEC+ reports

- **SNAPSHOT**: Equities down, Treasuries mixed, Crude down, Dollar up
- **REAR VIEW**: China makes fresh COVID restrictions; Saudi deny production increase reports; Soft German PPI; Mixed Fed speak; Decent 2yr auction followed by weaker 5yr supply; Former DIS CEO Iger reinstated as CEO, ousting Chapek
- **COMING UP**: **Data**: EZ Consumer Confidence Flash, Australian PMIs Flash **Speakers**: Fed's Bullard, George, Mester; ECB's Rehn **Supply**: Germany & US.
- **CENTRAL BANK WEEKLY**: Previewing Fed and ECB minutes, PBOC LPR, RBNZ, Riksbank, BoK, and CBRT rate decisions. To download the report, please click here.
- **WEEK AHEAD PREVIEW**: Highlights include: Fed & ECB mins, PBOC, RBNZ, Flash PMIs. To download the report, please click here.
- **Newsquawk Thanksgiving Schedule**: Please click here.

MARKET WRAP

Stocks were lower Monday with broad Dollar strength and commodity weakness with Chinese COVID woes hitting the global demand outlook. Industrial metals and activity currencies saw particular weakness as new lockdown restrictions were introduced in China. Oil prices were lower, but well off their troughs after earlier WSJ reports about impending OPEC+ production increases were swiftly denied by Saudi. Euro weakness was aided by a surprisingly soft German PPI print, although Lane was out saying that the ECB December hike would not be the last. Across the pond, Fed's Bostic and Mester gave the nod to a downshift to 50bps at the December FOMC, although Daly said she wasn't taking anything off the table. Treasuries saw curve flattening and the front-end sold with the hawkish Fed Speak adding to the Treasury auctions, which saw a decent 2yr offering followed by a weak 5yr; long-end supported by softer German PPI and commodity (ergo inflation) weakness. Disney (DIS) soared after former CEO and Chairman Bob Iger was reinstated as CEO after the board ousted Bob Chapek.

FED

Bostic (2024 voter) over the weekend said he is ready to move away from 75bps hikes at the December meeting and believes that another 75bps-100bps tightening will be warranted (taking FFR to 4.75-5%, beneath market pricing of 5.00-5.25%) and that will be sufficient to rein in inflation over a reasonable time horizon.

Daly (2024 voter) spoke several times on Monday where she suggested financial conditions are tighter than what is suggested by Fed rates, saying financial markets are priced like the FFR is at 6%, not 3.75-4.00%. She also said the Fed must be mindful of overdoing rate hikes but there is still more work to be done but inflation is moving in the right direction. She noted policy is in modestly restrictive territory but she sees it peaking at around 5%, saying 4.725-5.25% is reasonable. She later said she is not ready to say what the Fed will do in December, but nothing is off the table. At some point, said it will be right for the Fed to slow rate hikes but the Fed can hike beyond 5% if inflation data does not cool. Daly said she sits on the hawkish spectrum of her colleagues.

Mester (2022 voter) said it makes sense to slow down the pace of rate hikes and believes they can slow down from 75bps in December. She added they can be very deliberate in setting policy and the Fed needs to be more judicious in balancing risks but they are not anywhere near to stopping rate hikes. Mester is beginning to see the Fed's actions work but they need more, sustained good news. She thinks the Fed is just barely there in regards to restrictive territory, adding they need to get there. Looking ahead, the economy will tell us the pace of rate hikes but if they do not see meaningful progress on inflation next year, the Fed will need to react. She does not have a recession in her forecast but with below-trend growth there are risks of an unexpected shock that could send the US into a recession, stressing the focus is on bringing inflation down and there will be some pain involved on the journey back to 2% inflation. On the balance sheet, Mester said she is monitoring the impact of the runoff impact on financial market functioning adding they will be flexible if conditions change but so far that is not necessary.

FIXED INCOME

T-NOTE (Z2) FUTURES SETTLED HALF-A-TICK HIGHER AT 112-10

Treasuries chopped around Monday alongside OPEC-induced oil volatility and mixed demand at 2yr and 5yr auctions. 2s +4.4bps at 4.554%, 3s +3.9bps at 4.319%, 5s +2.3bps at 4.021%, 7s +1.9bps at 3.941%, 10s +1.8bps at 3.836%, 20s +0.0bps at 4.147%, 30s -1.1bps at 3.916%.

Inflation breakevens: 5yr BEI +9.4bps at 2.405%, 10yr BEI +6.1bps at 2.328%, 30yr BEI +4.7bps at 2.404%.

THE DAY: Weekend Fed Speak saw Bostic (non-voter) strike a more dovish tone than his colleagues last week alongside surging Chinese COVID cases, seeing T-Notes rally to resistance at 112-17+ in APAC Monday trade. There was some fleeting, spillover demand from the German long-end after surprisingly soft PPI figures in the region, only for T-Notes to dip to session lows of 112-04 later in the London morning. Upside momentum for Treasuries was reignited in the NY morning, coinciding with losses in the oil complex after WSJ suggested OPEC+ was considering a production increase in December, taking T-Notes to session highs of 112-23. The combination of corporate and Treasury supply - decent 2yr and average 5yr auctions - alongside the reversal higher in oil prices after Saudi denied the WSJ reports saw T-Notes pare back lower into the NY afternoon. Treasury traders now look to Tuesday's 7yr ahead of FOMC minutes on Wednesday and the Thanksgiving holiday, with futures participants looking to roll into the March'23 contracts.

2YR AUCTION: A solid USD 42bln 2yr auction that adds to the chorus of decent Treasury offerings so far in November. The 4.505% high yield was marginally cheaper than last month's 4.460% and marked a 0.8bps stop-through the WI, better than the prior 1.1bps tail and avg. 0.5bps tail. The 2.64x bid/cover ratio was also better than the prior and averages. Dealers were left with 20.6%, just beneath avg. 21%, with Indirects stepping up to 57% from last month's below-average 50.5%.

5YR AUCTION: A mixed 5yr offering and disappointing when compared against the strong November auctions beforehand. The USD 43bln auction stopped at 3.974%, marking a 0.7bps tail which is in line with the six-auction average but disappointing vs last month's 1.8bps stop-through. The 2.39x bid/cover ratio was better than average but a step down from the prior. Dealers (forced surplus buyers) were left with 15.1%, which was on the small side against the prior 16.5% and average 19.4%, although it's worth a caveat that Dealers were reported to be net long over USD 30bln in the 3yr to 6yr sector as of November 9th, which IFR note as the longest since August 2020. While the tail is a disappointment, it's worth contextualising that the 5yr sector is trading acutely rich on the curve from a relative value perspective, with the 2s5s10s fly at its richest in nearly a decade which will have been a headwind for the auction. Furthermore, with the 2s auction earlier Monday and the 7yr ahead on Tuesday, valuation-sensitive buyers could easily be reallocating to those sectors.

STIRS:

- EDZ2 -0.5bps at 95.01, H3 -2.5bps at 94.725, M3 -3.5bps at 94.67, U3 -5.5bps at 94.840, Z3 -5bps at 95.135, H4 -4bps at 95.51, M4 -3bps at 95.845, U4 -2bps at 96.08, Z4 -3bps at 96.23, Z5 -4bps at 96.505, Z6 -1bps at 96.47.
- US sold USD 50bln of 6-month bills at 4.520%, covered 3.03x; sold USD 60bln of 3-month bills at 4.220%, covered 2.64x.
- NY Fed RRP op. demand USD 2.125tln (prev. 2.113tln), across 93 bidders (prev. 95).

CRUDE

WTI (F3) SETTLED USD 0.35 LOWER AT 79.73/BBL; BRENT (F3) SETTLED USD 0.17 LOWER AT 87.45/BBL

The crude complex was initially notably lower on account of a higher dollar and China COVID concerns before being further accentuated by WSJ sources noting Saudi Arabia and other OPEC members are reportedly considering a production increase. However, the weakness was unwound and more after Saudi officials denied reports of talks increasing OPEC+ oil output. The China COVID concerns sparked more demand fears after three COVID-related deaths were reported in Beijing over the weekend, the first reported since May, on top of the total rise in the number of cases while more regions enacted virus restrictions. Regarding the WSJ sources piece, it noted OPEC+ are considering a production rise of up to 500k BPD at the December 4th meeting, leading to notable downside in the crude complex. The move would reverse part of their decision in October to cut production by 2mln BPD, at which point the schedule for gatherings switched from monthly to bi-monthly (once every two months). The Journal added the move could also assist in healing a rift between Saudi and US President Biden's admin. However, Saudi officials later disputed these claims seeing the move unwind and more. The Saudi official said the current cut of 2mln BPD continues until the end of 2023, but if there is a need to take further measures by reducing production to balance supply and demand, we will always remain ready to intervene. There were also remarks out of Russia on the oil price caps, Deputy PM Novak reiterated Russia will not sell oil to nations that implement a price cap adding it will trigger lower supply, adding Russia may also cut oil production in the event of the price cap which helped Crude settle just marginally lower. Note, just after the settlement UAE also denied it is in talks with other OPEC+ members to change the last OPEC+ agreement.

BANK COMMENTARY: Goldman Sachs cut its Brent oil outlook by USD 10/bbl to 100/bbl due to China's COVID concerns and sees elevated oil flows from China ahead of EU curbs and price caps. Separately, UBS forecasts Brent to recover to 110/bbl in 2023 and sees oil demand to increase at an above-trend rate of circa. 1.6mln BPD in 2023.

EQUITIES

CLOSES: SPX -0.39% at 3,950, NDX -1.06% at 11,554, DJIA -0.13% at 33,700, RUT -0.57% at 1,839

SECTORS: Consumer Discretionary -1.41%, Energy -1.39%, Technology -1.13%, Communication Svs. -0.81%, Health Care +0.05%, Financials +0.34%, Industrials +0.37%, Materials +0.38%, Utilities +0.5%, Real Estate +0.72%, Consumer Staples +0.98%.

EUROPEAN CLOSES: EURO STOXX 50 -0.40% at 3,909, FTSE 100 -0.12% at 7,376, DAX 40 -0.36% at 14,379, CAC 40 -0.15% at 6,634, FTSE MIB -1.29% at 24,356, IBEX 35 +0.00% at 8,188, SMI +0.36% at 11,085.

STOCK SPECIFICS: **Disney (DIS)** former Chairman and CEO Bob Iger is returning as chief executive, replacing Bob Chapek. **Imago BioSciences (IMGO)** is to be acquired by **Merck (MRK)** for USD 36/shr in a 1.35bln deal. IMGO closed Friday at USD 17.40/shr. **J M Smucker (SJM)** beat on profit and revenue; raised FY23 guidance on both top and bottom line. **Broadcom's (AVGO)** proposed USD 61bln **VMware (VMW)** acquisition scrutinized by UK regulators in a phase 1 investigation. **Jacobs (J)** topped consensus on EPS and revenue; backlog increased 5% Y/Y. **Carvana (CVNA)** is facing a cash crunch from high debt and interest rates; could run out of cash in a year, according to WSJ. **TSMC (TSM)** founder said the **Apple (AAPL)** supplier will build 3nm chips at its USD 12bln factory in Arizona, though final plans are not ready yet. China stocks listed in the US, such as **Alibaba (BABA), Baidu (BIDU), JD (JD), and Pinduoduo (PDD)** were pressured after three COVID-related deaths were reported in Beijing over the weekend, the first reported since May. The overall number of cases in China is on the rise as well. **Williams-Sonoma (WSM)** was downgraded at Barclays; pointing to the negative impact of a weakening housing market. **Apple (AAPL)** extended wait time for popular iPhone 14 models beyond Christmas as **Foxconn (FXCOF)** scrambles to resume full production in Zhengzhou, according to SCMP. **DraftKings (DKNG)** users were reportedly hacked, with their accounts drained and unable to log in, via ActionNetwork, although DKNG responded to the hack saying they are aware of the irregular activity on accounts and intend to make whole any customer was impacted. DKNG identified less than USD 300k of customer funds were affected and believes login information was compromised on other websites and they found no evidence DraftKings' systems were breached to obtain information. A US appeals court decertified class action against **Boeing (BA)** and **Southwest Airlines (LUV)** for allegedly concealing a defect in a MAX-8 plane and has ordered the lawsuit be dismissed, according to a court ruling cited by Reuters. **Amazon (AMZN)** reportedly mulled investing several hundred million dollars in **Argo (ARGO)**, according to Bloomberg, but decided against it due to high AI tech costs which also prompted **Volkswagen (VOW3 GY) and Ford (F)** to abandon the co.

FX WRAP

The Dollar was bid on Monday with strength forming in APAC and throughout the European session on ongoing COVID woes in China with cases rising and several areas seeing fresh virus-related restrictions. There was also a slew of Fed Speak, Bostic over the weekend said he is ready to move away from 75bps hikes at the December meeting and believes that another 75bps-100bps tightening will be warranted (taking FFR to 4.75-5%, beneath market pricing of 5.00-5.25%) and that will be sufficient to rein in inflation over a reasonable time horizon. Fed's Daly suggested financial conditions are tighter than what is suggested by Fed rates and that the Fed must be mindful of the risk of overtightening. However, she did repeat she sees the peak rate at around 5%, saying between 4.75-5.25% is reasonable, and that she is not taking anything off the table for the November meeting. Mester said it makes sense to slow down a bit the pace of rate hikes but they are nowhere near to stopping rate hikes. The remarks from officials do not appear as hawkish as the likes of Collins and Bullard at the end of last week. The upside in the DXY over the last week is helping pare back some of the post-October CPI losses albeit still well off the pre-CPI highs north of 114 with DXY trading in a 106.89 to 107.99 range on Monday.

The Euro was pushed lower by the buck with EUR/USD falling from 1.0333 at the highs to lows of 1.0224 with the much weaker than expected producer prices data in Germany helping with the Euro weakness given prices dropped 4.2% in

October, despite expectations for a 0.9% rise. Meanwhile, when ECB's Lane was questioned on the increment of upcoming hikes, he dismissed it suggesting what matters is the level the ECB arrives at but he does not think December is going to be the last rate hike.

The Yen saw notable weakness with USD/JPY rising above 142.00 due to the Dollar strength, albeit, the Yen was a notable underperformer with rates still set to rise to "around 5%" in the US despite the cool October inflation report. Further direction will be gauged from the Fed's November meeting minutes on Wednesday.

In antipodes, AUD was a notable underperformer with a downbeat risk tone weighing on the activity currency with Australia susceptible to follow-through effects from China with COVID cases on the rise sparking more concerns about stricter restrictions. NZD was lower in sympathy with AUD, a stronger buck and risk appetite, but did fare better than its antipodean counterpart, albeit AUD/NZD managed to hold on to 1.08 while attention turns to the RBNZ rate decision on Wednesday.

The Loonie was weaker on the broader stronger buck and risk sentiment, but USD/CAD saw highs as oil prices hit their lows on reports OPEC+ are mulling a 500k BPD production increase in December, however, oil prices pared losses on the swift denial from Saudi Arabia, supporting the Looney from its weakest levels.

EMFX was mixed with BRL finding strength with a risk on tone in Brazil after an alternative proposal to Lula's was filed by a Senator that reduces the spending ceiling from BRL 198bln to BRL 70bln, but still guarantees the maintenance of the BRL 600 under the social programme, Auxilio Brasil. IF reports also suggest an alternative Finance Minister being mulled to the internal candidate Haddad. ZAR saw weakness in fitting with precious metals while MXN was lower on weaker oil prices, as well as the stronger Dollar.