US Market Wrap

14th December 2022: SPX falls sub 4k after hawkish dot plots but Bonds disagree

- **SNAPSHOT**: Equities down, Treasuries up, Crude up, Dollar down.
- **REAR VIEW**: Fed lifts rates 50bps, sees terminal rate at 5.1%; Chair Powell maintains hawkish stance; DAL raises current quarter forecast with upbeat 2023 outlook; GS cuts TSLA price target; Unexpected sizeable EIA crude build
- **COMING UP**: **Data**: Australian Employment, Chinese Retail Sales/Industrial Output, US IJC, Retail Sales, Industrial Production, Australian Flash PMIs **Events**: BoE, ECB, Norges Bank, SNB & Banxico Policy Announcements; European Council Meeting (1/2) **Press Conferences**: ECB's Lagarde, Norges Bank's Bache & SNB's Jordan.

MARKET WRAP

Stocks ultimately finished the day lower after a big rally since the cash open into the FOMC completely reversed. The FOMC gave a hawkish revision to the dot plots taking stocks to lows with SPX falling sub 4k after the start of Powell's presser. The Fed Chair started out with a hawkish tone noting there is still some ways to go and the Fed needs to see substantially more evidence to have confidence inflation is on a sustained downward path back to target, seeing stocks and bonds hit lows while the dollar hit highs. Nonetheless, Powell later stated he thinks policy is getting to a pretty good place and close to sufficiently restrictive, which supported bonds, particularly the belly. Stocks were also off the lows but still closed in the red with SPX closing sub 4k, while the Dollar index finished the day at lows. Money markets aren't buying the Fed's hawkish expectations in the dot plots, in wake of cooling inflation data, with the peak rate being priced in at 4.87% at the time of close, implying an FFR of 4.75-5.00%, despite the dot plots implied FFR of 5.00-5.25%. Attention now turns to the plethora of central bank activity on Thursday, including the BoE, ECB, SNB, & Norges Bank rate decisions, previews available below.

FED

FOMC STATEMENT REVIEW: The Fed voted unanimously to lift the Federal Funds Rate target by 50bps to 4.25-4.50%, as expected, downshifting the pace of rate hikes. The Committee, however, raised its expectation of where rates will peak, now seeing the terminal rate at 5.1% (in the 5.00-5.25% bracket) vs the 4.6% (the 4.50-4.75% bracket) it was projecting in September. That implies 75bps of more tightening in this cycle, which will be seen in 2023; after that point, the Fed expects to cut rates, and projects the Federal Funds Rate target at 4.1% by the end of 2024. The updated rate forecasts suggest the central bank wants to keep rates elevated for longer as it battles above target inflation (historically, it has remained at terminal for between 3-15 months, on average 6.5 months). Its statement was little changed, although it still guides for “ongoing increases” in interest rates; some had flagged an outside risk of this language being tweaked to something on the lines of “some further” rate increases. Elsewhere, the growth profile was upgraded a little for 2022, but was lowered for 2023 and 2024; the inflation forecasts were raised across the horizon, though it still sees long-term PCE at 2.0%. On the jobs front, the central bank has revised its unemployment projection a little lower for this year (3.7% vs 3.8%), although has nudged its view higher for 2023 and 2024, where unemployment is seen peaking at 4.6%, before falling to 4.5% in 2025. The market reaction was hawkish, trading off the higher expected terminal rate. That said, market pricing has still not shifted into the 5.00-5.25% bracket (money markets currently imply a peak of 4.908% in May 2023), remaining just under that range as we head into the post-meeting press conference. At the press conference, traders will be curious to hear how long Chair Powell envisages rates staying at terminal, and the conditions the central bank would need to see in order to begin lowering interest rates.

POWELL PRESSER REVIEW: Fed Chair Powell maintained a hawkish stance repeating guidance that the Fed expects ongoing rate hikes are appropriate to get to a sufficiently restrictive level and they are committed to bringing inflation back to target, and the Fed still has some ways to go. On inflation, he acknowledged the welcome downturn in the October and November inflation reports, while inflation expectations remain well anchored but that is not grounds for complacency. He added the Fed wants to see substantially more evidence to have confidence that inflation is on a sustained downward path. He does not see the Fed cutting rates in 2023 but for them to consider cuts they would have to be confident inflation is moving down in a sustained way, without elaborating what that would entail. However, Powell noted that he thinks policy is getting to a pretty good place and is close to a sufficiently restrictive level. He did however stress the largest pain is the Fed does not raise rates high enough and noted history cautions against prematurely loosening policy, and the Fed will stay on course until the job is done. On future rate hike increments, he said he cannot tell today what size the next rate hike will be but he repeated having moved so quickly the Fed thinks the appropriate thing to do is to move to a slower pace of rate hikes, as they did today. He also noted earlier in the year it was important for the Fed to move quickly on rates, but now the pace is not so important, the ultimate level of rates is most important but soon it will be how long the Fed keeps rates sufficiently restrictive. On the SEP's, he towed his usual post-SEP line that projections are the best assessment of where Fed policy rate will be at this current time, he did note that at each subsequent SEP this year, we have increased our estimates of peak rate, and he could not tell us confidently the Fed won't upgrade, or even downgrade, the peak at next SEP meeting as it depends on the economic data. On the recent loosening of financial conditions, Powell said it is important financial conditions reflect the Fed's policy constraint; but their focus is not on the short-term changes in financial conditions, he said they are seeing effects on demand in interest rate sensitive sectors, but it takes more time for the rest of the economy. Looking ahead on inflation, Powell expects a very large drop in inflation next year but with a higher "jump off point" at the start of 2023. By the middle of next year, Powell said we should see lower inflation from the housing services sector and there is "a ways to go on" on core services ex-housing.

CENTRAL BANK PREVIEWS

ECB: Despite a softer-than-anticipated headline November Eurozone Y/Y HICP print of 10% (exp. 10.4%), the release was overshadowed by an unexpected increase in the core metric (ex-food to 6.6% (exp. 6.3%, prev. 6.4%). As such, the ECB is expected to pull the trigger on another rate hike despite the uncertain economic outlook. A step down from a 75bps to a 50bps increment is expected by 45/62 economists surveyed by Reuters, whilst market pricing assigns a circa 87% chance to such a move. Chief Economist Lane has laid the groundwork for a potential slowdown in the cadence of rate increases by noting that he would be reasonably confident in saying that "it is likely we are close to peak inflation". That said, the GC does not appear to be unanimous in stepping down to a 50bps pace of tightening with Austria's Holzmann backing another 75bps increase, whilst the influential Schnabel of Germany stated that incoming data thus far suggests that slowing down the pace of rate adjustments remains limited. For several weeks, analysts at ING have been of the view that an "earlier and more significant" form of QT could be the compromise required by hawks in order to back a slower pace of rate hikes. Accordingly, ING expects the ECB to "announce a gradual reduction of the reinvestments of its bond holdings under the Asset Purchase Programme (APP) at the December meeting, with the aim to stop the reinvestments by end-2023." Looking beyond the December meeting, a further 75bps of tightening is fully priced in for 2023 which would take the deposit rate to 2.75% and into restrictive territory with policymakers broadly of the view that rates are "close to neutral". For a full Newsquawk preview, please click here.

BOE: The MPC is expected to return to a 50bps adjustment, according to 52 of the 54 analysts surveyed by Reuters, whilst market pricing assigns around a 74% chance of such an outcome. The decision to move on rates is expected to be unanimous, however, given dissent at the November meeting – where Swati Dhingra voted for a 50bps hike, and Silvana Tenreyro for 25bps – it is likely that the decision on the magnitude of the hike will not be unanimous. Capital Economics notes that there is a risk that Tenreyro could opt for an unchanged rate given remarks she made in a recent speech, where she said that “in the most likely scenario, we had already done enough”; she also published a central scenario where rates peak at 3% (current level). Thus, it is likely that the bulk of the focus will centre around the vote split and any adjustment to forward guidance. For a full Newsquawk preview, please click here.

SNB: Expected to hike by 50bp, taking the Policy Rate to 1.00%. A move that is merited by inflation remaining above target, however, given the Q4 figures looks set to be comfortably below the SNB’s earlier forecast, outsized hawkish action is not likely to be deemed necessary by the Governing Board. This view is also supported by ongoing signs /forecasts of an economic slowdown, albeit a recession is not expected; taken together, these factors have sparked some calls for a 25bp increase. Currently, market pricing looks for 50bp, but around 10% chance of a 25bp hike is implied. Further out, the release will be scrutinised to see if further tightening is expected, with the statement in September saying that “It cannot be ruled out that further increases in the SNB policy rate will be necessary to ensure price stability over the medium term.” Elsewhere, we look for any updates to the language on the CHF and willingness to engage in two-way intervention as required alongside any further tweak to the tiering system, as the Policy Rate moves further into positive territory. For a full Newsquawk preview, please click here.

NORGES BANK: Expected to hike by 25bp to 2.75%, in a continuation of the pace from November’s meeting given the balancing act between above-forecast CPI and ongoing signs of an economic slowdown, particularly the Regional Network Survey indicating that the labour market is expected to plateau in the near-term. Rates aside, attention will turn to the peak policy level, of 3.10% at September’s MPR, for guidance as to how the Norges Bank sees the balancing act between inflation and the broader economy playing out in the meetings ahead. Particularly, after the Bank indicated a more gradual approach to rate setting may be required, in the context of a tightening effect beginning to become evident from the policy decisions taken thus far. For a full Newsquawk preview, please click here.

FIXED INCOME

T-NOTE FUTURES (H3) SETTLED 2 TICKS LOWER AT 114-23

Pre-FOMC steepening turned to post FOMC flattening after the hawkish dot plots although Powell's presser wiped out Treasury losses with outperformance in the belly. 2s -0.9bps at 4.220%, 3s -3.3bps at 3.922%, 5s -4.2 bps at 3.611%, 7s -3.4bps at 3.557%, 10s -4.0bps at 3.463%, 20s -2.4bps at 3.712%, 30s -1.8bps at 3.509%

Inflation breakevens: 5yr BEI -5.3bps at 2.287%, 10yr BEI -5.9bps at 2.191%, 30yr BEI -6.5bps at 2.210%.

THE DAY: Ahead of the FOMC the curve steepening continued in wake of the cool CPI Tuesday and woeful 30yr auction Tuesday evening. The immediate reaction to the statement and dot plots was hawkish, Treasuries sold off across the curve and the earlier steepening turned to flattening. The hawkish reaction was seen in the wake of the dot plots, the Fed's peak dot is seen rising to 5.1% in 2023 from 4.6% in the September SEPs, higher than what markets were pricing in. The selling pressure across the curve however reversed during the press conference, with markets seemingly not buying such a high terminal rate given the recent progress on inflation, with money markets still implying a peak FFR of 4.75-5.00%, moving marginally higher from 4.8% pre FOMC to 4.87% post FOMC. Further upside in Treasuries was seen, particularly in the belly after Powell suggested policy is getting close to a sufficiently restrictive level. Attention now turns to more central bank decisions on Thursday, particularly from the BoE and ECB.

STIRS

- EDZ2 +0.3bps at 95.258, H3 -0.5bps at 94.960, M3 -2.0bps at 94.930, U3 +0.5bps at 95.115, Z3 +2.0bps at 95.475, H4 +2.5bps at 95.925, M4 +2.5bps at 96.325, U4 +2.0bps at 96.595, Z4 +3.0bps at 96.745, Z5 +3.5bps at 96.915, Z6 +3.0bps at 96.865.
- NY Fed RRP op demand at USD 2.193tln (prev. 2.181tln) across 97 bidders (prev. 98 bidders).

CRUDE

WTI (F3) SETTLED USD 1.89 HIGHER AT 77.28/BBL; BRENT (G3) SETTLED USD 2.02 HIGHER AT 82.70/BBL

The crude complex was firmer throughout Wednesday, as prior to the FOMC rate decision, WTI and Brent trundled higher throughout the session amid thin newsflow and light liquidity as market participants awaited the aforementioned meeting. Nonetheless, WTI and Brent saw brief dip in wake of the weekly EIA report, which saw an unexpected sizeable build, both from a headline crude perspective and the all stocks (incl. SPR) metric. Note, this was in-fitting with the private inventory data on Tuesday night. In wake of the FOMC, little reaction was seen in crude benchmarks. Elsewhere, CPC blend oil loadings resumed following a storm, however, Urals and Siberian Light Black Sea exports remain suspended, according to traders cited by Reuters. Moreover, TC Energy (TRP) is anticipating an update on Keystone pipeline (622k BPD) restart later on Wednesday, while Freeport LNG's natgas export terminal still plans to restart by year-end after receiving an extensive list of demands from US regulators, according to Bloomberg.

IEA MOMR: Raised 2022 oil demand growth estimate by 140k BPD to 2.3mln BPD and 2023 raised by 100k BPD to 1.7 mln BPD. Furthermore, world oil supply fell 190k BPD in November to 101.7mln BPD, breaking a five-month uptrend, after Saudi Arabia and other Gulf countries curbed supply in line with lower OPEC+ output targets. A steeper drop is expected next month as the EU ban on Russian crude imports and the G7 price cap take effect. For Newsquawk’s more thorough piece, please click here.

BANK COMMENTARY: Goldman Sachs cut its Q1 and Q2 2023 Brent forecasts to USD 90/bbl and USD 95/bbl, respectively, from USD 110/bbl. The bank sees an oil surplus of 1.7mln BPD in Q4 2022 and 1.3mln BPD in Q1 2023, diminishing the risk of a winter price spike. Meanwhile, Morgan Stanley expects Brent oil to rally back to USD 110/bbl by mid-2023 and sees post winter downside to US Henry Hub and a more manageable, but still tight, outlook for global LNG. MS added the oil market should return to a deficit by mid-2023, skewing price risks to the upside.

EQUITIES

CLOSES: SPX -0.60% at 3,995, NDX -0.79% at 11,740, DJIA -0.42% at 33,996, RUT -0.65% at 1,820.

SECTORS: Financials -1.29%, Materials -1.11%, Real Estate -1.01%, Technology -0.86%, Communication Services -0.86%, Consumer Discretionary -0.73%, Energy -0.64%, Industrials -0.19%, Utilities -0.16%, Consumer Staples -0.07%, Health +0.14%.

EUROPEAN CLOSES: EURO STOXX 50 -0.29% at 3,975, FTSE 100 -0.09% at 7,495, DAX 40 -0.26% at 14,460, CAC 40 -0.21% at 6,730, FTSE MIB -0.26% at 24,573, IBEX 35 +0.40% at 8,360, SMI +0.22% at 11,160.

STOCK SPECIFICS: Goldman Sachs lowered its price target for **Tesla (TSLA)** to USD 235 (prev. 305); new estimates reflect softer supply and demand. GS also lowered its FY23 and FY24 EPS estimate; said that if TSLA can show that its demand levers and the US Inflation Reduction Act can drive strong growth and margins, the stock could rise to around USD 300 (vs current USD c.160). **Delta Airlines (DAL)** issued an upbeat forecast; raised current quarter forecast with upbeat 2023 outlook. Expects to deliver strong topline growth and significant operating leverage. **ABM Industries (ABM)** marginally beat on the top and bottom line; exec said it will continue to face labour-related pressures in the near term. FY23 adj. EPS guidance was light. For **TSMC (TSM)**, Taiwanese officials said it has not yet received an application from TSM to increase its investment in Arizona to USD 40bln to build a second fab, according to DigiTimes. **Braze (BRZE)** posted a surprise loss per share but beat on revenue; guided an expected profit loss for the next quarter, but FY EPS and revenue view topped the consensus. **Paccar (PCAR)** was upgraded at Morgan Stanley; said it is among the industrial stocks poised to benefit from a sector recovery. **Best Buy (BBY)** was downgraded at BofA Securities; cited a challenging environment for achieving earnings growth. **United Airlines (UAL)** expects over 8.3mln (prev. 8mln Y/Y) people to fly with it during the year-end holiday travel period. Sees over 480k people to fly with it on January 2nd (post COVID record was 460k passengers in one day). For **Apple (AAPL)**, "Side-loading and alternative app stores won't affect Apple's bottom line by much, and in fact, could improve its stock thanks to regulatory backoff", according to Appleinsider citing commentary from Morgan Stanley. **Goldman Sachs (GS)** is reportedly considering a bonus cut of at least 40% for the investment bank, according to FT.

FX WRAP

The Dollar eventually settled lower on Wednesday in wake of the FOMC rate decision and the following Chair Powell press conference. On the initial announcement, where the central bank hiked FFR by 50bps to 4.25-4.50%, as expected, with terminal rate seen at in 5.1% 2023 (prev. 4.6%), markets saw an immediate hawkish reaction. The move was accentuated taking DXY to session highs of 104.18 after early in the press conference Chair Powell said “it will take substantially more evidence to have confidence that inflation is on a sustained downward path.” The Dollar pared its gains through the Q&A, and markets saw a dovish reaction after the Chair said he thinks policy is getting to a pretty good place and policy is getting close to sufficiently restrictive. Just for reference, heading into the meeting the Dollar was contained in thin liquidity and newsflow. Looking ahead, there is a slew of central bank decisions on Thursday, such as ECB, BoE, SNB, and Norges Bank, as well as a plethora of US data by way of Philly Fed, Retail sales, jobless claims, amongst others.

GBP was firmer on Wednesday, but Sterling saw initial weakness on the FOMC rate decision, but later pared this to end the US session firmer vs the buck and marginally firmer against the Euro. Cable tested a double top of 1.2444/45 during the press conference just below the important 1.2451 major fib retracement level. Elsewhere, UK CPI data came in cooler than expected at 10.7% and cooled from the prior 11.1%, seeing a cooler than expected 0.4% M/M gain. Core CPI was also beneath expectations at 6.3% Y/Y and 0.3% M/M.

YEN: The Yen was bid on the session but off best levels in wake of the FOMC statement, but also off worst levels after the presser. Elsewhere, in Japan, Bloomberg sources suggested the BoJ sees the possibility of conducting a policy review in 2023, but would be unlikely to occur before Governor Kuroda leaves his position in April. The sources follows commentary from BoJ's Tamura who called for a policy review at the right moment, although other officials, including Kuroda, had pushed back on it. Overnight, saw the latest Tankan survey come in above expectations for the manufacturing and services index while the outlook was in line with expectations for manufacturing, but the outlook for services missed expectations.:

The Euro saw gains in wake of the FOMC with a choppy Fed rate decision ahead the key ECB rate decision on Thursday. Although, do note Reuters source reports said the new ECB forecasts will put inflation comfortably above 2% in 2024 and just above in 2025.

The Yuan was bid thanks to the ultimate dollar selling post Fed, but elsewhere in China, reports on COVID are mixed. China is to offer a second booster for the high risk people while noting vaccine production capacity is over 7bln doses. It also decided against postponing its key economic policy meeting and is expected to take place between 15-16th December, denying reports on Tuesday.

Cyclical currencies were mixed with the aforementioned GBP outperforming its cyclical peers, while AUD saw mild gains and CAD was flat vs the buck but NZD lagged despite commentary overnight from the RBNZ. The RBNZ said actual and expected inflation is too high and needs to be reduced, while it expects spending to slow and unemployment levels to increase as more people join the workforce over the coming year, adding it expects the level of employment will remain high. Meanwhile, RBNZ Deputy Governor Hawkesby has seen little impact of higher rates so far and the level of neutral OCR has drifted higher.

Scandi's were weaker vs the Euro but firmer against the buck. Note, Swedish inflation data came in in line with expectations on the headline while Riksbank's Floden spoke today, noting November inflation was roughly as expected and was a pretty good outcome for the CPIF ex-energy print, adding there are a number of indicators internationally that inflation is going in the right direction.

EM: EMFX was mixed, with gains in BRL, ZAR but weakness in MXN, RUB, & TRY once the dust settled post Fed. Aside from the Fed, South Africa's CPI was cooler than expected Y/Y but slightly hotter M/M, while the CEO of Eskom is to resign at the end of March. In Brazil, Incoming Finance Minister Haddad noted they received an official letter from the government, ordering the removal of 2.5mln Brazilians from Auxilio Brasil, the social welfare programme, adding they will be announcing measures in 2023 and many will need to be reassessed as money is being wasted. In Turkey, Lira and Turkish assets saw pronounced weakness after President Erdogan's rival was convicted by the Turkish court ahead of elections.