US Market Wrap

20th December 2022: Yen and yields surge after BoJ widens YCC band

- **SNAPSHOT**: Equities mixed, Treasuries down, Crude up, Dollar down.
- **REAR VIEW**: BoJ makes surprise, early widening in yield target band; Falls in US housing starts & building permits; Keystone pipeline files reopening plans; explosion on Ukraine gas pipeline; WFC fined USD 3.7bln; AMZN avoids hefty EU fines.
- **COMING UP**: **Data**: Canadian CPI, US Consumer Confidence, Existing Home Sales **Event**: BoJ Minutes **Supply**: US.

MARKET WRAP

Major US stock indices saw mild gains on Tuesday in the aftermath of the BoJ catching participants offside with an early widening in its yield curve targeting policy after many had not expected the adjustment to occur until 2023. Treasuries bear-steepened in sympathy with JGBs, with the US 10yr yield up 10bps, trailing the Japanese 10yr surging 16bps to 0.42%, the largest rise since 2003 according to Refinitiv data. The FX story was non-surprisingly a Yen-driven one with USD/JPY posting one of its largest declines on record. Other catalysts were light with US data showing further dips in November housing starts and building permits, while EU consumer confidence flash reading for Dec. saw a marginal rise. Elsewhere, in stocks, Wells Fargo (WFC) was sold after the CFPB fined the bank USD 3.7bln, while Amazon (AMZN) was cleared of paying hefty fines by the EU Commission.

GLOBAL

BOJ: The BoJ unexpectedly tweaked its Yield Curve Control (YCC) barometer, widening the 10yr yield band to +/-0.5% from +/-0.25% and unexpectedly announced it is to increase bond purchases to JPY 9tln/m (prev. JPY 7.3tln/m) in Q1. The BoJ kept its benchmark rate unchanged at -0.10% and maintained its 10yr JGB yield target of around 0% as expected. The decision on YCC was unanimous. The statement noted the adjustment is intended to “improve market functioning and encourage a smoother formation of the entire yield curve while maintaining accommodative financial conditions". BoJ said it is to make nimble responses for each maturity by increasing the amount of purchases even more and conducting fixed-rate purchases operations when deemed necessary. The central bank also maintained its rate guidance. The YCC adjustment was seen as a shock and analysts had expected changes to come after Governor Kuroda's term expires in April 2023. In the press conference, Kuroda on the YCC policy change said market functionality was decreasing and the domestic market was hit by volatility abroad. He clarified the decision is not an exit of YCC or a change in policy and the BoJ still finds it appropriate to continue easing policy, while also adding there is no need to further expand the allowance band as he expects volatility in global financial markets to gradually decrease. On broader policy, Kuroda said it is too early to debate the exit to current policy, noting Tuesday's decision is not a rate hike but strategies and tools for monetary easing exit should be discussed at policy meetings if they are close to reaching their inflation target but he also added the BoJ will not hesitate to ease policy further if necessary. Kuroda stressed there is no intention to hike rates or tighten policy and they are not thinking about revising the 2013 joint statement between the BoJ and government. Looking ahead, analysts at Danskebank expect the BoJ to hike its policy rate to 0% in Q2 followed by a 25bp increase in the yield target taking it to 0.25%, seeing the allowance band at -0.25-0.75%, maintaining 50bps of leeway around the target.

BUILDING PERMITS/HOUSING STARTS: Housing data for November was mixed, as building permits disappointed, which is the more forward-looking indicator, while housing starts were a touch stronger than expected. The former fell 11.2% to 1.342mln, well beneath the prior 1.512mln and the expected 1.485mln. Meanwhile, starts fell 0.5% to 1.427mln (prev. 1.434mln), but above the consensus of 1.4mln. Into the report, Oxford Economics highlight a fall in multi-family permits drove the overall decline, but single-family permits continued their slide as well. Ox Eco notes “the drop in permits, along with pessimistic homebuilder sentiment, point to further weakness in housing construction in the months ahead as high interest rates side-line many buyers.” Regarding starts, there was a 4.1% decline in single-family starts mostly offset by a 4.8% rise in multi-family starts and the consultancy adds “starts were mixed at the regional level, with sharp declines in the Northeast and the Midwest, little change in the South and an increase in the West.”

FIXED INCOME

T-NOTE (H3) FUTURES SETTLED 19+ TICKS LOWER AT 113-17

Treasuries bear-steepened Tuesday after the BoJ's hawkish surprise. 2s +1.0bps at 4.272%, 3s +3.4bps at 4.031%, 5s +8.1bps at 3.792%, 7s +10.2bps at 3.779%, 10s +10.9bps at 3.692%, 20s +12.2bps at 3.941%, 30s +11.8bps at 3.742%.

Inflation Breakevens: 5yr BEI +7.1bps at 2.311%, 10yr BEI +8bps at 2.247%, 30yr BEI +8.3bps at 2.291%.

THE DAY: The bulk of the downside in duration came in wake of the BoJ decision to double the band for its 10yr JGB yield curve target to +/- 50bps from +/-25bps. T-Notes fell from 114-03+ to lows of 113-11+ in wake of the decision. Contracts then made an attempt to recover but couldn't muster any higher than 113-24+ in the London morning, before fresh selling in NY trade saw session lows eked out at 113-10. The session was otherwise on the light side for catalysts, barring some soft housing data, with the front-end little changed on the session.

STIRS:

- EDZ2 -0.5bps at 94.93, H3 +0.5bps at 94.925, M3 +0.5bps at 95.09, U3 -2bps at 95.40, Z3 -4.5bps at 95.815, H4 -6.5bps at 96.19, M4 -7bps at 96.455, U4 -7.5bps at 96.595, Z4 -7.5bps at 96.67, Z5 -11bps at 96.72, Z6 -14.5 bps at 96.595.
- 20k Fed Funds Jan'23 futures seller seen, touted to be position closing after an even larger buyer seen last Tuesday.
- NY Fed RRP op demand at 2.159tln (prev. 2.135tln) across 98 bidders (prev. 95).
- US announced its next 1-month, 2-month, and 17-week bill auctions where all sizes were left unchanged.

CRUDE

WTI CRUDE FUTURES (G3) SETTLED USD 0.85 HIGHER AT 76.23/BBL; BRENT (G3) SETTLED USD 0.19 HIGHER AT 79.99/BBL

Oil prices were choppy on Tuesday with a combination of supply factors and risk appetite swinging the benchmarks. Aside from the weaker Dollar and broader stock and commodity appetite, easing supply risk was in focus after Reuters reported TC Energy (TRP) has submitted a restart plan to regulators for the Keystone pipeline (622K BPD) after the Kansas oil spill, easing storage depletion concerns for the WTI delivery hub, Cushing, Oklahoma. Meanwhile, Saudi's Energy Minister jawboned to SPA Tuesday that it would not come as a surprise if the issue of missing barrels re-emerges in early 2023, keeping up with the same pattern of underestimating demand yet again. While any hopes of an Iran nuclear deal were further disintegrated, and resulting Iranian (legal) supply after President Biden said "it is dead" to a reporter when asked, whilst also saying "we're not going to announce it".

EUROPE: Dutch TTF found losses capped after a blast occurred on Russia's Urengoi-Pomary-Uzhgorod gas pipeline (32BCM) that runs via Siberia to Western Ukraine to Europe. The fire was later reported to be extinguished and a local branch of Gazprom said gas was being supplied in full to consumers via parallel pipelines despite the damage. Meanwhile, European Energy Exchange, EEX, warned that upon activation of the EU gas price cap it will no longer be in the position to allow for order entry or trade.

EQUITIES

CLOSES: SPX +0.1% at 3,822, NDX -0.1% at 11,072, DJIA +0.3% at 32,850, RUT +0.5% at 1,748

SECTORS: ENERGY +1.52%, COMMUNICATION SVS +0.72%, MATERIALS +0.65%, FINANCIALS +0.31%, TECHNOLOGY +0.16%, INDUSTRIALS +0.14%, UTILITIES +0.06%, CONS STPL -0.02%, HEALTH -0.06%, REAL ESTATE -0.27%, CONS DISC -1.13%.

EUROPEAN CLOSES: EURO STOXX 50 -0.23% at 3,802, FTSE 100 +0.13% at 7,370, DAX 40 -0.42% at 13,884, CAC 40 -0.35% at 6,450, FTSE MIB +0.15% at 23,718, IBEX 35 +0.59% at 8,185, SMI -1.04% at 10,660.

STOCK SPECIFICS: **General Mills (GIS)** earnings saw a beat on both EPS and revenue, while it raised its organic net sales view and it is to lift prices again in early 2023. However, commentary from executives noted inventory reductions at some key retailers was an unexpected headwind while headwinds were felt across its pet business, they've been particularly acute on our dry dog food and treats sub-segments. The European Commission accepted **Amazon's (AMZN)** commitments to address competition concerns and end two EU antitrust investigations; avoided fines of up to 10% of its global sales. JPMorgan lowered its **Apple (AAPL)** iPhone volume forecasts for the December quarter to around 70mln (prev. forecast ~74mln). **Netflix's (NFLX)** new ad-supported plan was reportedly the least popular tier of its service in November, the first month in which the service was offered, according to subscription analytics firm Antenna being cited by WSJ. The CFPB ordered **Wells Fargo (WFC)** to pay USD 3.7bln over consumer abuses. CPFB added the Wells Fargo order does not provide immunity to executives; need to consider whether to apply additional limitations on WFC beyond existing asset cap. **Boeing (BA)** won backing from Congress to lift a looming deadline imposing a new safety standard for modern cockpit alerts for 737 MAX aircraft. **Walmart (WMT)** reached opioid settlement agreements with all 50 states and surpassed the first threshold required for finalizing the co.'s USD 3.1bln nationwide settlement announced on Nov 15th. **Lucid Group (LCID)** announced a successful capital raise of approximately USD 1.515bln in a series of stock sales. **3M (MMM)** will stop making forever chemicals, and is to discontinue use in 2025; expects to book pretax charges between USD 1.3-2.3bln. **Hertz (HTZ)** being investigated by the NHTSA over whether it rented certain vehicles without having performed required recall repairs. Of note for **GoGo (GOGO)** and **Viasat (VSAT)**, **Delta Air Lines (DAL)** is expected to begin rolling out free wireless Internet for its passengers as soon as early 2023, according to WSJ citing sources. DAL also issued a weather waiver ahead of the widespread winter storm, noting there wil be flight cancellations this week.

FX WRAP

The Dollar was weaker Tuesday as a result of the pronounced Yen strength in wake of the BoJ YCC band adjustment. DXY hit a low of 103.77 from highs of 104.790 and the Yen strength kept the pressure on the buck despite the pronounced upside in US yields too. The Dollar did finish off lows, fixating around 104. Regarding US data, November housing starts declined 0.5%, but that was better than feared, although building permits tumbled 11.2%, beneath expectations.

The Yen at one point saw its strongest gain vs the buck since 1998, taking USD/JPY to lows not seen since August. The BoJ made an unexpected tweak to its YCC programme, although the target was maintained at 0% it widened its tolerance band to 50bps either side vs 25bps previously. Kuroda stressed in the press conference the decision is not an exit of YCC or a change in policy and reiterated it is appropriate to continue easing policy.

The Euro was relatively flat trading either side of 1.06 but did hold above the level headed into the US close with little of note for the currency with all the attention on the Yen. There was some commentary from ECB's Villeroy, just noting France should be able to avoid a recession, but if it didn't, it would only be a temporary one. Meanwhile, the December Eurozone consumer confidence flash data saw a marginal improvement to -22.2 from -23.9, but still missed expectations of -22.0.

Cyclical currencies were volatile in wake of the BoJ and choppy risk tone with underperformance in the Antipodeans. AUD/USD saw little reaction to the RBA minutes but was volatile post-BOJ. The latest RBA minutes revealed the board considered several options for its 25bp hike in December, including a 50 or 25bp hike, or no change at all. In New Zealand, the business outlook deteriorated in December to -70.2 from -57.1 while the activity print also tumbled. The Dollar weakness from the BoJ saw AUD/USD hit a peak of 0.6743 while NZD/USD tested 0.6400 to the upside, the antipodeans then trundled lower throughout the rest of the session with Aussie falling sub 0.6700 while the Kiwi tested support at 0.6300 multiple times. The Pound traded sideways after extreme volatility overnight when Cable peaked around 1.2223 and troughed near 1.2086. CAD saw mild strength against the Dollar on the move higher in crude prices and the weaker greenback.

Scandi's were weaker vs the Euro but NOK outperformed its Scandi counterpart on the Brent gains with NOK/SEK rising above 1.05 again.

EMFX was mixed. The Rouble continued to tumble, adding to the steep losses seen Monday on fears of Russia/Ukraine escalation. The Real saw notable gains vs the buck with USD/BRL hitting a low of 5.1764 after Bloomberg reported Brazilian President Lula's transition bill may be voted in the Senate on Tuesday, and will still cost BRL 145bln; to be valid for one year after the agreement. The Rand was weaker despite gains in gold prices but did see notable gains on Monday and remains around those levels. Meanwhile, Eksom announced stage 6 loadshedding will be implemented Tuesday night before returning to stage 4 Wednesday morning. The Forint saw some strengthening after the NBH, after keeping rates unchanged, added to its statement that it was ready to take appropriate action if needed on rates, while Deputy Governor Virag later called for patience on any adjustments to the O/N 18% quick depo rate amid speculation that could soon be cut towards the base rate 13%.

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