US Market Wrap

11th January 2023: Stocks and Bonds rally in quiet newsflow ahead of CPI

- **SNAPSHOT**: Equities up, Treasuries up, Crude up, Dollar flat.
- **REAR VIEW**: Collins leaning towards 25bp in Feb; Mixed ECB speak; Stong 10yr auction; Russia to resume FX intervention; Mega EIA crude stocks build; Airlines grounded after eerie system outage.
- **COMING UP**: **Data**: Chinese CPI, US CPI, IJC, **Speakers**: Fed's Barkin, Bullard, Harker, **Supply**: Spain, Italy & US. **Earnings**: TSM (overnight).

MARKET WRAP

Stocks extended their gains on Wednesday with the fall in yields lending to relative outperformance in tech names (NDX +1.75% vs. SPX +1.3%). Catalysts were on the light side with no major data either, while participants very much cast their attention to Thursday's CPI print. Treasuries bull-flattened (10yr -8bps at 3.53%) in sympathy with EGBs and were supported by a strong 10yr auction with eyes to Thursday's CPI and 30yr auction. There was particularly greater strength seen in EGBs with a strong Bund auction and perhaps more crucially, ECB's Holzmann hinting at no haste in terms of QT. Despite the EGB outperformance, the FX landscape was little changed with the DXY flat, whilst EUR/USD and USD/JPY were marginally firmer, albeit, O/N implied volatility has surged higher to account for US CPI. Meanwhile, oil prices ripped higher with global growth prospects and mean reversion cited despite the massive US crude stock builds and evidence of muted Russian sanction impacts. Nat Gas was also firmer, shaking off Reuters reports that the Freeport LNG export terminal may once again delay the plant restart until February.

US

CPI PREVIEW: The consensus expectation is for headline CPI growth to be unchanged on a month-on-month basis in December (vs a previous rise of +0.1% in November), although the annual measure is expected to ease to +6.5% Y/Y in December from +7.1% the prior month. There is a feeling that traders have fully discounted the 'peak inflation' narrative, and are now refocussing on the deteriorating growth dynamic – as evidenced by the market reactions to last week's ISM reports (where headline and new orders for both services and manufacturing have tilted into contraction) and nonfarm payrolls data (that shows a trend of declining wage pressures). That said, the Fed has not yet seen the 'substantial progress' that it has been seeking. In December, Fed Chair Powell said that although the declines in prices pressures in October and November was welcome, core CPI was still running three times above target, and policymakers would still need to see substantially more evidence to give it confidence that inflation was on a sustained downward path. For a full preview, please click here.

FED

COLLINS (non-voter), in a NYT interview, said either a 25 or 50bp hike looks reasonable in February, but she is leaning towards a 25bps hike at the February 1st meeting although the data will help guide her decision. Collins is the first among the FOMC to express she is leaning towards 25bp, with others just noting it will be 25 or 50bp, depending on the data. Collins said she sees the terminal rate above 5% (median view is 5.1%) and expects rates to be held at the terminal through 2023. On the rate path, Collins says she is favouring three more 25bps hikes to get to terminal.

HSBC expects the Fed to hike a final 50bps in February, with rate cuts expected in 2024.

FIXED INCOME

T-NOTE (H3) FUTURES SETTLED 14 TICKS HIGHER AT 114-14

Treasuries bull-flattened in sympathy with EGBs and were supported by a strong 10yr auction with eyes to Thursday's CPI and 30yr auction. 2s -3.8bps at 4.220%, 3s -5.0bps at 3.920%, 5s -7.1bps at 3.661%, 7s -7.5bps at 3.605%, 10s -7.6bps at 3.543%, 20s -7.9bps at 3.840%, 30s -8.3bps at 3.671%.

Inflation breakevens: 5yr BEI +0.8bps at 2.241%, 10yr BEI -0.1bps at 2.224%, 30yr BEI -1.3bps at 2.293%.

THE DAY: Gradual bull-flattening was seen through the APAC session seeing T-Notes find peaks of 144-13+ in the London morning, with EGBs leading strength on relatively dovish ECB comments and a strong Bund auction, but Treasuries struggled to extend gains ahead of US supply. T-Notes chopped along in tight ranges for the remainder of the session despite the continued ascent in EGBs. There was little data to dig into ahead of supply and Thursday's CPI. The futures contracts managed to eke out session highs of 114-15 in wake of the solid US 10yr auction, with an eye to Monday's YTD peak of 114-23+ going into CPI and the 30yr bond auction on Thursday.

10YR AUCTION: The USD 32bln reopening saw a 3.575% high yield, marking a 0.5bps stop-through, night and day vs the prior since-2015 record 3.7bps tail and the six-auction avg. 2bps tail, and also the first stop-through since Aug. 2022. The 2.53x bid/cover ratio exceeded the prior 2.31x and avg. 2.35x. The takedown saw Dealers (forced surplus buyers) left with 15.1%, with Indirects participation surging to 67% from 59.5% in Dec., indicative of strong end-user demand. Overall, a solid offering from the Treasury, particularly given the recent record in the 10yr sector and the lack of concession, where a combination of disinflation momentum ahead of Thursday's CPI, a softer Dollar, and new year liquidity likely offset the valuation concerns.

STIRS:

- EDH3 +0.5bps at 94.925, M3 flat at 94.865, U3 +1bps at 95.01, Z3 +3.5bps at 95.395, H4 +6.5bps at 95.90, M4 +8.5bps at 96.35, U4 +9.5bps at 96.65, Z4 +9.5bps at 96.795, H5 +8bps at 96.85, H6 +7bps at 96.895, H7 +6.5bps at 96.795.
- There was a burst of high-volume selling seen across SOFR whites on exchange in the NY morning, with a 45k Dec'23 SOFR block sale not long after, but losses quickly unwound.
- NY Fed RRP op demand at USD 2.199tln (prev. 2.193tln) across 99 bidders (prev. 102).
- US sold USD 36bln of 17-week bills at 4.680%, covered 2.79x.

CRUDE

WTI (G3) SETTLED USD 2.29 HIGHER AT 77.41/BBL; BRENT (H3) SETTLED USD 2.57 HIGHER AT 82.67/BBL

Oil prices ripped higher Wednesday with global growth prospects and mean reversion cited despite the massive US crude stock builds and evidence of muted Russian sanction impacts. Oil prices were subdued during APAC hours, with bearish private inventory data applying pressure, but found bullish momentum in the European morning alongside other risk assets. WTI and Brent front-month futures kept on rising, with even more bearish EIA inventory data struggling to cap strength with storm-related factors at play, and ultimately printing session highs at midday in NY at USD 77.84/bbl and 82.91/bbl, respectively, then hovering near highs into settlement.

US INVENTORIES: Crude stocks built 18.96mln bbls in the latest week, a massive surprise against the analyst consensus for a 2.2mln bbl draw, and even greater than the private data indicated build of 14.9mln bbls, with the fallout from the winter storm playing out, seen via a +15mln bbl build in the Gulf Coast alone. The SPR released a relatively small 800k bbls. Cushing, Oklahoma delivery hub stocks saw a build of 2.5mln bbls. Crude production rose 100k BPD to 12.2mln BPD. In the products, refinery utilisation rebounded 4.5% after last week's 12.4% tumble, with gasoline stocks building 4.1mln bbls (exp. +1.2mln, private +1.8mln) and distillates drawing 1.1mln bbls (exp. -0.5mln, private +1.1mln).

RUSSIA: WSJ reported that the US and allies are preparing the next round of sanctions on Russian oil, intending to cap the sales price of Russian exports of refined petroleum products. However, the effectiveness of the existing sanctions is coming into question after Reuters reported, citing traders, that oil loadings from Russia's Baltic ports between Jan. 1st to 20th are expected to rise by c. 50% vs. the same period in December. Russian Kremlin also said today, in reference to possible losses from oil price caps, that there have been hardly any cases of the caps yet.

EQUITIES

CLOSES: SPX +1.28% at 3,970, NDX +1.76% at 11,403, DJIA +0.80% at 33,973, RUT +1.17% at 1,844.

SECTORS: Real Estate +3.6%, Consumer Discretionary +2.68%, Technology +1.75%, Materials +1.61%, Communication Svs. +1.34%, Industrials +0.96%, Utilities +0.86%, Financials +0.86%, Health Care +0.57%, Energy +0.36%, Consumer Staples +0.06%.

EUROPEAN CLOSES: EURO STOXX 50 +1.04% at 4,100, FTSE 100 +0.40% at 7,725, DAX 40 +1.17% at 14,948, CAC 40 +0.80% at 6,924, FTSE MIB +0.72% at 25,547, IBEX 35 +0.16% at 8,726, SMI +0.75% at 11,246

AIRLINES: US flights were grounded due to an outage of the FAA pilot notification system, albeit the grounding has since been lifted. An investigation is underway but as it stands there is no evidence of a cyber attack. Note, there was also an outage in Canada, where the Air Traffic Controller announced the Canadian NOTAM system is experiencing an outage too, albeit there were no flight delays. Note, **Southwest Airlines (LUV)** were downgraded today at Susquehanna given their recent travel woes in December, while today's events will only add to the troubles.

STOCK SPECIFICS: **Merck's (MRK)** COVID-19 drug Molnupiravir is expected to enter the Chinese market on Friday 13th January, according to local media citing Sinopharm executives. **Apple (AAPL)** is reportedly planning to start developing its own displays for mobile devices, according to Bloomberg, which adds AAPL is looking to reduce reliance on partners like **Samsung (SSNLF)**. Meanwhile, an ITC Judge ruled AAPL violated US trade laws by infringing on **Masimo (MASI)** pulse oximeter patent. **Wells Fargo (WFC)** announced plans to streamline its residential mortgage business, exit its correspondent business and plans to reduce the size of its servicing portfolio. **WWE (WWE)** elected Vince McMahon as Executive Chairman; Stephanie McMahon resigned from her roles as Chairwoman and Co-CEO. Nick Khan will serve as WWE CEO. There were also vague reports that WWE had been sold to the Saudi Arabia Public Investment Funds. **Tesla (TSLA)** is nearing a preliminary deal to set up a factory in Indonesia, according to Bloomberg, it is said to target an output of 1mln cars/yr. Of note for **Whirlpool (WHR)**, **Electrolux (ELUXB SS)** gave a dire update, posting a Q4 EBIT of SEK -2bln. It also noted a negative impact from non-recurring items of around 1.4bln adding business in North America was the main contributor to weaker-than-expected Q4 earnings. **Ubisoft (UBSFY)** cut its booking guidance in a dire update. **Homebuilders (LEN, PHM, DHR)** were upgraded at Bank of America. **Meta (META)** was downgraded at OTR Global to mixed from positive. **Sotera Health (SHC)** was double upgraded at Barclays to overweight. **Universal (CMCSA)** plans to open two new attractions in Texas & Las Vegas; the Vegas attraction will be a year-round horror-focused destination. **Blackrock (BLK)** is cutting up to 500 jobs, according to Business Insider. Elliott is reportedly a top 10 investor in **PPL Corp. (PPL)** and is helping shape PPL's updated business plan but discussions are said to be cordial, according to Bloomberg. **Illumina (ILMN)** is to face an EU fine of 10% of turnover over its Grail takeover, according to Reuters sources. **Google (GOOGL)** parent Alphabet filed a redacted version of the motion to dismiss the US DoJ lawsuit against it, according to a court document. **Salesforce (CRM)** CTO, Taher Elgamal, has reportedly left the Co. following the departures of other execs in recent months. **Kroger (KR)** CEO McMullen said the Co. expects some inflation moderation later in the year.

US FX WRAP

The Dollar was flat Wednesday with all eyes on Thursday's CPI data, a full Newsquawk preview of the data can be found here. DXY held above 103 throughout the session within parameters of 103.480 and 103.100. With the Dollar flat, options implied volatility data show a huge risk premium on overnight USD expiries as the market braces for the CPI report on Thursday. Analysts at Reuters highlight the option pricing shows a doubling of actual volatility risk premium to levels that were last seen ahead of the December FOMC meeting. There was little US data Wednesday but we did hear some comments from Fed's Collins (non-voter), who expressed she is leaning towards a 0.25% hike in February, but she still sees terminal above 5% and could see the Fed's rate hike path to terminal being through three more 25bp hikes. Collins also towed the Fed line that a 50 or 25bp hike in Feb. is reasonable, but she will be guided by the data.

The Euro was marginally firmer on Wednesday with EUR/USD trading either side of 1.0750. There was a slew of ECB speakers, Villeroy noted rates will be raised more in the coming months but the peak rate should be reached by the summer, he also noted French inflation is likely to peak in H1. Holzmann noted rates will need to rise significantly further to reach a sufficiently restrictive territory, a view echoed by ECB's Rehn later.

The Yen also saw marginal gains vs the flat Dollar with USD/JPY trading between highs of 132.87 and lows of 132.07. Attention turns to the BoJ next week but traders will also be looking for direction from Thursday's US CPI report and how it impacts policy differentials between the Fed and BoJ. Looking ahead to the March BoJ meeting, analysts at BNP Paribas expect to widen the yield curve control range by 50-to-100bps either side of 0%. although they do see a risk of an action as early as the January meeting.

The Franc was the clear underperformer with notable losses vs both the Dollar and the Euro in lack of specific swiss catalysts although technicians highlight swiss FX pairs crossed several technical levels. USD/CHF trade within a range of 0.9206 and 0.9331, rising above the 5, 10 and 20dma and the psychological 0.9300. EUR/CHF traded between 0.9899 and 1.0021, rising above the psychological parity level, as well as the 200dma at 0.9936.

Cyclical currencies were primarily flat. NZD, CAD & GBP were flat vs the buck while GBP saw mild losses vs the Euro with the activity currencies failing to reap many benefits from the upside in equities, albeit traders are likely sitting on the sidelines ahead of US CPI. AUD was bid vs the buck, however, thanks to strength in iron ore prices while the region reported stronger than expected retail sales data for November, while CPI was in line with expectations, but hotter than the prior month at 7.3%.

The Yuan was firmer for both onshore and offshore currencies against the buck despite reports overnight in China Securities Journal that analysts say there is room for China to cut RRR and interest rates this year. Meanwhile, the commerce ministry issued a notice on further supporting foreign trade companies to expand cross-border Yuan usage.

EMFX was generally firmer. ZAR saw gains despite weakness in gold prices with USD/ZAR remaining sub 17.000. USD/MXN fell sub 19.000 for the first time since early 2020 while technicians at SocGen wrote this morning "USD/MXN has resumed its down move after struggling to reclaim the 200-DMA (19.95). Holding below the daily Ichimoku cloud at 19.50, the pair is expected to head lower towards 19.00 and 2020 levels of 18.60/18.50." BRL also saw gains despite weaker-than-expected retail sales while MXN saw stronger-than-expected industrial output data. The Rouble strengthened after Russia announced it would resume forex intervention, starting with a sale of the Chinese Yuan.