US Market Wrap

25th January 2023: Stocks and bonds recover as BoC makes final hike

- **SNAPSHOT**: Equities flat, Treasuries up, Crude flat, Dollar down
- **REAR VIEW**: BoC hikes and pauses; MSFT cloud guidance weak; Stellar US 5yr auction; Australian and New Zealand CPI above expected; UK PPI beneath expected; Hawkish ECB Speak; Cushing crude inventories balloon.
- **COMING UP**: **Data**: US Durable Goods, GDP Advance/PCE Prices Advance (Q4), IJC, New Home Sales, Japanese CPI **Event**: SARB Policy Announcement **Earnings**: Diageo, STMicroelectronics, Nokia, SAP, LVMH; Comcast, Intel, Visa, Southwest **Supply**: Italy & US **Holiday**: China (Lunar New Year).
- **THIS WEEK'S EARNINGS**: CMCSA, MA, INTC, V, CVX, AXP. To download the report, please click here.

MARKET WRAP

Stocks were little changed after earlier losses pared gradually through the session. The losses initially stemmed from the tech sector, particularly after Microsoft's (MSFT) lacklustre cloud unit guidance which also initially weighed on Amazon (AMZN). But, the losses in indices were clawed back aided by the dovish BoC rate decision, as well as the reversal in both MSFT and AMZN, supporting the major US indices into the close ahead of a plethora of US data points throughout the rest of the week. Treasuries saw mild bull-steepening in choppy trade after the dovish BoC hike and the strong 5yr UST auction. The Dollar was sold as the dovish BoC reinforces dovish Fed expectations, although the Loonie recovered off lows. Global inflation data was in focus after both New Zealand and Australian CPI figures came in hotter-than-expected, although UK PPI data came in on the soft side. Oil prices were little changed in choppy trade, with EIA inventory data showing the largest build at the Cushing Oklahoma delivery hub since April 2020, although the nationwide inventory figures weren't as eye-catching.

CENTRAL BANKS

BOC: The Bank of Canada (BoC) hiked rates by 25bps as expected to 4.50%, however, it gave an explicit signal it expects rates to be held at this level providing the economy develops broadly in line with its forecasts. Although it did caveat it is prepared to hike rates even further if it is necessary to bring inflation back to target. The explicit pause signal was a dovish surprise with desks expecting the bank to maintain its prior guidance to consider further rate hikes, thus leaving open the optionality, especially after the latest hot jobs report. The MPR saw the bank lower its 2022 and 2023 inflation forecast but sees 2024 inflation at 2.3% (prev. 2.2%), the same year it expects it to reach its target. Growth forecasts were raised in 2022 and 2023, but lowered in 2024. Meanwhile, the neutral rate estimate of 2-3% was left unchanged and the output gap estimate was revised higher to 0.5-1.5% from 0.25-1.25%. The press conference saw Macklem really stress that the pause is a conditional pause on how the economy develops and they are pausing to assess whether they have reached a sufficiently restrictive level. Macklem repeated the statement that if they need to do more to get inflation to target, they will and they are prepared to hike rates further if upside risks materialise - but this would require an accumulation of evidence before later noting that the bar to hike rates is higher than it was before. Macklem also stressed that it is far too early to be talking about rate cuts, while when asked about a recession says there could be a mild recession but it would not be a major contraction, noting the BoC expects growth to stall over the next few quarters, but it is what is needed. In a later Reuters interview, Macklem added that if service price inflation is stickier than expected, the BoC would likely need to raise rates further and the biggest near-term economic risk would be if a rapid reopening of China's economy caused global commodity and oil prices to rise. Analysts at Oxford Economics agree with the pause taken as the Canadian economy is very sensitive to rate hikes due to elevated household debt and overvalued housing. The desk added Canada is likely already in the early stages of a recession that will last through 2023, while OxEco expects the BoC to keep rates on hold throughout 2023 before easing to neutral in 2024.

FIXED INCOME

T-NOTE (H3) FUTURES SETTLED 3+ TICKS HIGHER AT 115-04+

Treasuries saw mild bull-steepening in choppy trade after dovish BoC and a strong 5yr UST auction. 2s -2bps at 4.133%, 3s -2.2bps at 3.841%, 5s -2.5bps at 3.557%, 7s -2bps at 3.505%, 10s -1.1bps at 3.456%, 20s -0.7bps at 3.732%, 30s -0.6bps at 3.615%.

Inflation breakevens: 5yr BEI +0.9bps at 2.254%, 10yr BEI +0.7bps at 2.292%, 30yr BEI +1.1bps at 2.313%.

THE DAY: Mild selling in USTs was seen through the holiday-thinned APAC session on the back of hotter-than-expected Australian and New Zealand CPI reports. T-Notes eked out session lows of 114-29+ at the London handover, before the mild losses were recovered, with Gilts leading the charge higher across the pond after a softer-than-expected UK PPI release. The dovish BoC rate hike, in which it gave an implicit nod to a pause in the hiking cycle, saw T-Notes print session highs of 115-13, although the bank noted this would be conditional, which led to a swift pullback. T-Notes retested session lows before midday in NY, although the front end was better supported. The solid 5yr auction later on led to a fleeting rally in Treasuries, but earlier ranges were respected with the contracts contained into settlement. The 7yr auction on Thursday is next up alongside initial Q4 GDP data, durable goods, Chicago Fed survey, jobless claims, new home sales, and the Kansas City Fed survey.

5YR AUCTION: A solid USD 43bln, 5yr offering from the Treasury that echoes all the other January auctions (not one tail), but all the more impressive given the unattractive relative valuation of the tenor. The 3.530% high yield was the lowest since August 2022, yet the auction stopped through by a chunky 2.4bps, better than the prior month's 0.4bps tail and six-auction average 0.4bps tail. The 2.64x bid/cover ratio exceeded the average. Dealers (forced surplus buyers) were left with a minuscule 8.8% (avg. 17.9%), thanks to another strong step-up in Indirects participation to 75.7% from 64.5% in December (avg. 64.3%), indicative of solid end-user demand.

STIRS:

- SR3H3 +2bps at 95.91, M3 +4bps at 96.675, U3 +5.5bps at 96.83, Z3 +6bps at 96.905, H4 +3.5bps at 96.95, M4 +1bps at 96.975, U4 +0.5bps at 96.99, Z4 -0.5bps at 96.975, H5 -0.5bps at 96.96, H6 flat at 96.76, H7 flat at 95.54.
- Block activity saw 49k SR3Z3/Z4 calendar spreads bought at -146bps, touted profit-taking after a flattener entered last September.
- NY Fed RRP op demand at USD 2.032tln (prev. 2.048tln) across 99 bidders (prev. 100).
- US sold USD 36bln of 17-week bills at 4.620%, covered 2.90x; sold USD 24bln of 2yr FRNs at a high discount margin of 0.200%, covered 2.80x (six-auction avg. 2.76x), Dealers took 32.5% (avg. 31.8%).

CRUDE

WTI (H3) SETTLED USD 0.02 HIGHER AT 80.15/BBL; BRENT (H3) SETTLED USD 0.01 LOWER AT 86.12/BBL

Oil prices were modestly firmer in tight and choppy trade on Wednesday amid mixed inventory data. There was little major newsflow to provide impetus for the benchmarks, instead, prices meandered through the session, finding a fleeting bid after the US inventory data (details below). Meanwhile, Valero, Motiva, and Exxon all gave updates that their Texas refineries affected by the Tuesday night storm were up and running. Away from the US, eyes turn to the JMMC meeting next week, with recent sources pointing to a recommendation of unchanged policy. Elsewhere today, Reuters reported Kazakhstan's TCO plans to raise crude oil exports via Georgia's port of Batumi to 150k T in Jan.-Feb. in efforts to diversify export channels away from CPC pipeline through Russia, that's compared to the 21k T per month average last year. And in the Middle East, Libya's NOC is to sign offshore gas exploration and production deals with Italy's Eni (ENI IM) on Saturday, according to NOC chief Bengdara in local press.

INVENTORIES: EIA reported a 0.5mln bbl build for US crude stocks in the latest week, marking the fifth straight build, albeit considerably less after the 8.4mln bbl build for the prior week, and on the lighter side of analyst expectations for a 1mln bbl build. However, Cushing stock saw a massive 4.3mln bbl build, the largest since April 2020 and the fourth build in a row. Some desks are pointing to the WTI futures curve's contango over the near-term horizon as a key driver in the chunky builds given it is cheaper to keep oil in storage for a future delivery date rather than export it, seen via the fall in US crude exports in January. Meanwhile, distillates drew 0.5mln bbls, the fourth draw in a row, while gasoline stocks built 1.8mln bbls, the third build in a row. Refinery utilisation rose 0.8%. Crude production remained unchanged at its peak of 12.2mln BPD.

EQUITIES

CLOSES: SPX -0.02% at 4,016, NDX -0.27% at 11,815, DJI +0.03% at 33,744, RUT +0.25% at 1,890.

SECTORS: Financials +0.74%, Consumer Discretionary +0.54%, Consumer Staples +0.28%, Materials +0.2%, Real Estate +0.11%, Health Care +0.01%, Energy -0.09%, Technology -0.26%, Communication Services -0.36%, Industrials -0.53%, Utilities -1.36%.

EUROPEAN CLOSES: EURO STOXX 50 -0.12% at 4,148, FTSE 100 -0.18% at 7,743, DAX 40 -0.08% at 15,0811, CAC 40 -0.09% at 7,043, FTSE MIB -0.03% at 25,875, IBEX 35 -0.11% at 8,957, SMI -0.07% at 11,398.

STOCK SPECIFICS: **News Corp (NWSA)** received a letter from Rupert Murdoch withdrawing the proposal to explore a potential merger with **Fox (FOX)**. Solar names, **Sunrun (RUN) and SunPower (SPWR)** were downgraded at Barclays; citing a potential slowdown in solar demand. Several Chinese suppliers to **Apple (AAPL)** are to soon seek govt approval to form joint ventures in India, according to Economic Times citing sources. **Tesla (TSLA)** is continuing investment in Nevada and will build two new factories, investing more than USD 3.6bln, adding 3,000 new team members. **Jacob's (J)** approved a USD 1bln share buyback programme and raised dividend to USD 0.26/shr from 0.23/shr. **BlackRock (BLK)** authorised share buybacks of up to 7mln additional shares and raises quarterly dividend to USD 5.00 from 4.88. **Nordstrom (JWN)** was downgraded to junk by Fitch at 'bb+'; outlook stable.

EARNINGS: **Microsoft (MSFT)** beat on profit and intelligent cloud revenue; missed on revenue and forecasts next quarter intelligent cloud revenue beneath expectations. Quarterly devices revenue fell 39%, driven by continued PC market weakness, and execution challenges on new product launches. Sees a decrease in next quarter total revenue growth by about 3 points due to FX impact. **Boeing (BA)** posted a surprise loss per share and missed on revenue despite a demand recovery; cited labour and supply shortages for disappointing numbers. **Intuitive Surgical (ISRG)** marginally missed on top and bottom line; cited a COVID resurgence in China negatively impacted procedure volumes in the area. **AT&T (T)** topped Wall St. consensus on EPS, revenue and postpaid phone subscribers; FY EPS view light. **F5 Networks (FFIV)** fell short of expectations on revenue alongside next quarter profit view coming in light. **General Dynamics (GD)** reported solid numbers, as it beat on top and bottom line alongside a record backlog of 91.14bln. FY23 guidance was light. **Kimberly-Clark (KMB)** marginally beat on EPS and marginally missed on revenue. Sees FX cutting 2023 operating profit by ~USD 300-400mln; inflation will continue to have an impact as certain commodity prices remain near peak levels and certain contracts. **Textron (TXT)** topped on revenue and raised FY23 guidance. **Amphenol (APH)** surpassed consensus on EPS and revenue, but next Q guide was short of expectations. **Freeport McMoRan (FCX)** posted solid numbers; CEO said it is very unlikely it would pursue M&A given its internal growth options and worker shortage in US is a strategic challenge.

US FX WRAP

The Dollar sold off on Wednesday with lows seen in wake of the Bank of Canada rate decision which gave an explicit signal to a pause in its tightening cycle with participants expecting the Fed to follow suit given the BoC were the first to tighten policy, and now the first to pause. Nonetheless, money market pricing for the Fed was little changed with markets still pricing in a more dovish outcome than the Fed's guidance. Fed terminal rate is priced at 4.9%, which would imply two more 25bp hikes, vs the Fed's SEP guide of three more 25bp hikes.

The Euro saw gains vs the Dollar taking EUR/USD above 1.09, primarily led by weakness in the greenback in wake of the BoC rate decision and the equity market turnaround. With the Fed seen stepping down the pace of rate hikes next week, and the BoC initiating their pause, it has helped the Euro's upside with the ECB signalling more rate hikes are to come. ECB's Makhlouf today repeated Lagarde's guidance in December noting that a similar step to December's meeting should be taken at next week's meeting, implying a 50bp hike is appropriate, before raising rates again in March. The magnitude of the rate hike in March is currently pricing in between a 25 and 50bp hike, but leaning towards a 50bp move. Vasle meanwhile suggested 50bp hikes at the next two meetings are appropriate.

The Yen also benefited from the weaker greenback in a similar vein to the Euro with the BoJ largely expected to make a U-turn later in the year from its ultra-easy monetary policy settings. Japan PM Kishida today announced the new BoJ governor will be appointed once BoJ Governor Kuroda's term ends in April.

The Loonie saw weakness in wake of the BoC rate decision taking USD/CAD to highs of 1.3428 as although it hiked by 25bps as expected, it gave an explicit signal they are to pause rate hikes at this level providing the economy evolves broadly in line with its forecasts, although noted it is prepared to increase rates further if needed to return inflation to target. The explicit signal to cause is what sparked the dovish market reaction with expectations leaning towards the CB maintaining guidance for optionality. However, USD/CAD was off highs as the Dollar weakness fought back against the CAD weakness, particularly as Macklem stressed the pause is conditional on the economy performing as expected, and that they are prepared to hike rates if necessary while adding it is far too early to be talking about interest rate cuts.

Cyclical currencies were mixed. The AUD saw notable gains after the hotter-than-expected CPI data Wednesday ahead of the RBA rate decision on February 7th with markets pricing in a c. 20bp move. The NZD saw a different story however and weakened vs the Dollar with the currency hit by AUD/NZD headwinds in wake of hot Aussie inflation, and although New Zealand CPI came in above expectations, at 7.2% Y/Y in Q4, some draw attention to the figure coming in beneath the RBNZ's 7.5% forecast. GBP saw gains vs the Buck and the Euro although lows were seen in GBP in wake of the softer than expected PPI data although GBP then rallied throughout the afternoon after the US equity open as the Dollar sold off and equities staged a turnaround. It is also worth noting the large declines in nat gas prices which may help with growth concerns for gas importers.

EMFX was mixed. MXN may have been hampered by weaker-than-expected Mexican IGAE economic activity, but the BRL brushed aside a fall in Brazilian FGV consumer confidence and the ZAR was not that rattled or surprised by yet more Eskom load-shedding and the TRY derived some traction from an upturn in Turkish manufacturing sentiment while Bloomberg reported that Turkey is weighing Lira hedging restrictions to curb Dollar demand. THB was little changed after the Bank of Thailand hiked as expected by 25bps to 1.5%, with the end of the hiking cycle in sight as its current account outlook turns positive.