US Market Wrap

7th February 2023: Markets dance to the sound of Powell

- **SNAPSHOT**: Equities up, Treasuries down, Crude up, Dollar down.
- **REAR VIEW**: Powell said if data continues to be hot, Fed would raise rates more; Powell says disinflationary process has begun; New ECB ceiling on government deposits; EIA STEO raises '23 & '24 world oil demand forecast; Weak 3yr US auction; Kashkari tows usual hawkish line; RBA hikes rates 25bps, as expected, & sees further rises; USD 11bln INTC 7-parter.
- **COMING UP**: **Events**: US President Biden's State of the Union, BoC Minutes **Speakers**: Fed's Williams, Cook, Barr, Bostic, Kashkari & Waller; ECB's Knot & Elderson **Supply**: UK, Germany & US **Earnings**; ABN AMRO, Credit Agricole, Equinor, Amundi, Pandora, Societe Generale, AP Moeller-Maersk; CVS Health, Disney, Bunge, Uber, Goodyear Tire.

MARKET WRAP

Markets whipsawed on Tuesday with all focus on Fed Chair Powell. The Fed Chair gave a message for both hawks and doves, noting that the disinflationary process has begun although warning it will be bumpy ride before then warning if jobs data continues to come in hot and we see higher inflation reports, then the Fed will have to do more than what is priced in. Two way price action was seen during the discussion with Powell, before stocks then returned to close at session highs. T-Notes, however, settled at session lows after Powell's warning of the need to do more if needed while a dismal 3yr auction added to the Treasury weakness, as well as a slew of corporate supply updates, particularly the USD 11bln Intel (INTC) 7-parter. Tech stocks surged on Tuesday, as did Communication names while Energy stocks were supported by the rally in crude. Microsoft (MSFT) surged over 4% supported by its search engine update for Bing with OpenAI. Elsewhere, overnight saw the RBA hikes rates by 25bps as expected to 3.35%, while it maintained guidance that it expects further increases in interest rates helping the Aussie surge although JPY was the outperformer with analysts citing haven flows, repatriation flows and speculation on BoJ policy normalisation ahead of the BoJ governor nominee announcement later this month.

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FED CHAIR POWELL: The Fed Chair had a message for both the hawks and the doves on the policy spectrum. In the initial remarks in the discussion, he noted the message from last week's FOMC was that the disinflationary process has begun, albeit it is at a very early stage. On the January jobs report, he noted the labour market was very strong and he did not expect it to be that strong, adding if data were to continue to come in stronger than expected, the Fed would certainly raise rates more. Powell also reiterated that the Fed probably needs to hike rates further and they have still not reached a sufficiently restrictive level. On inflation, he noted the jobs report shows why the Fed thinks returning inflation to target will be a process that will take a significant period of time. Powell expects 2023 to be a year of a significant decline in inflation, but it will certainly take into next year to get down close to 2% - in fitting with the December SEP's. The Fed Chair also stressed the disinflation process is going to be bumpy and he worries most about when disinflation will take hold in the larger services sector, plus they need good prices to continue to fall. Powell also noted that it is a good thing that disinflation has begun without damage to the jobs market, while wage increases have come down to a level that's closer to sustainable. As Powell was leaving the discussion he stressed the point that if strong labour market continues, or higher inflation reports are seen, they may need to hike more than what is priced in and that it is his base case that it will take some time to get inflation down, while we will need to do more rate hikes, then look around, and see if it is enough.

KASHKARI: Kashkari (voter) said he is not seeing much imprint on the labour market from Fed's action; if had to pick a rate forecast, would not lower it from his Dec SEP forecast of 5.4% but rates may have to be held at a higher level for longer. Kashkari was surprised by the January jobs report, noting we have to bring the labour market into balance and we haven't done enough yet. He wishes we saw more evidence underlying inflation was trending down more, stressing the services side of the economy is still very robust. On the hot jobs report, he suggests nobody should overreact to one report, but there is underlying strength in the services sector while noting it is hard to imagine that strong job growth can occur with wage growth moderating. He added that markets are more confident than he is about inflation falling. Kashkari added the housing market is starting to show signs of life again, making the Fed's jobs harder. If financial

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conditions are easier, the Fed would have to do more on rates. Adding the Fed also could use the balance sheet, but the bar to changing the rundown path is quite high. Kashkari concluded that they have to let inflation guide policy, rather than their models.

IBD/TIPP: IBD/TIPP economic optimism index for February rose to a 10-month high of 45.1, from 42.3, but remains in pessimistic territory sub-50. The headline was aptly supported by the three sub-indices which all rose. On this, the six-month outlook lifted 9.7% to 39.7, while the personal financial outlook jumped back into optimistic territory to 52.6. Finally, respondents' views on federal prices rose to 43.1. Overall, the report notes, "53% of adults polled think the U.S. economy is in a recession, down from 55% last month. That figure reached 61% in October." Note, the survey period was conducted between February 1st and 3rd.

FIXED INCOME

T-NOTE (H3) FUTURES SETTLED 8+ TICKS LOWER AT 113-07+

Treasuries steepened with heavy supply from both corporates and the Treasury weighing, with two-way flows seen on Powell's comments. 2s +2.1bps at 4.477%, 3s +0.6bps at 4.131%, 5s +3.0bps at 3.844%, 7s +3.9bps at 3.775%, 10s +4.5bps at 3.677%, 20s +4.4bps at 3.869%, 30s +4.4bps at 3.716%

Inflation breakevens: 5yr BEI +8.0bps at 2.360%, 10yr BEI +5.6bps at 2.320%, 30yr BEI +5.0bps at 2.270%.

THE DAY: Quiet/tight Treasury trade through APAC and the London morning on Tuesday after the big front-end-led sell-off in recent sessions took a pause. Fed's Bostic (non-voter) and Kashkari (voter) both gave remarks with a hawkish spin, expressing their surprise over the January NFP and touting hawkish policy options, but market participants were cautious to front-run Chair Powell. Treasuries initially rallied in a bull-steepener as Powell began speaking at the Economic Club of Washington, with the Fed Chair's comments largely in line with his FOMC presser from last Wednesday and seemingly not taking the opportunity to shift hawkish. T-Notes hit session highs of 113-28 as Powell spoke. However, that bid unwound after an awful 3yr Treasury auction (details below), in addition to Powell concluding his interview stressing that if we continue to get strong labour market reports, or higher inflation reports, the Fed may need to hike rates more than is priced in. T-Notes settled at lows before trundling marginally lower post settlement to 113-06+.

3YR AUCTION: A dismal USD 40bln 3yr offering from the US Treasury and a sour note to open the February coupon auction cycle on after a solid January showing. However, this offering already had a big asterisk over it heading into it given the shock jobs report on Friday, and subsequent pick-up in rates vol as Fed terminal rate pricing shifts higher. The 4.073% marked a 4bps tail, the largest in records as far back as 2016, night and day vs January's 2.3bps stop-through and the six-auction average stop-through of 0.3bps. The 2.33x bid/cover ratio was the lowest since November 2021. The takedown was slightly more encouraging with Dealers (force surplus buyers) left with 19.9%, above the prior 17.3% but still beneath the average 21%, that was due to a big step down in Indirects and a big step up in Directs.

AHEAD: Traders now look to the 10s and 30s new issues on Weds and Thurs, with little major on the US data front. However, we will get a deluge of Fed Speak from Williams, Cook, Barr, Kashkari, and Waller all on Wednesday.

STIRS:

- SR3H3 -1.0bps at 95.080, M3 -3.5bps at 94.845, U3 -3.0bps at 94.930, Z3 -3.0bps at 95.240, H4 -4.0bps at 95.720, M4 -3.0bps at 96.195, U4 -2.0bps at 96.530, Z4 -2.0bps at 96.710, H5 -1.5bps at 96.830, H6 -2.0bps at 96.975, H7 -3.5bps at 96.910.
- NY Fed RRP op demand at USD 2.058tln (prev. 2.072tln) across 104 bidders (prev. 103).

CRUDE

WTI (H3) SETTLED USD 3.03 HIGHER AT 77.14/BBL; BRENT (J3) SETTLED 2.70 HIGHER AT 83.69/BBL

The crude complex closed at session highs, boosted further by commentary from Fed Chair Powell speaking with both a hawkish and dovish tone in addition to the ever-present recovering demand in China. On the latter, the IAEA's Birol expects half of 2023 global oil demand growth to come from China while the EIA also expressed that the increased global demand growth will primarily come from China. Full details of the EIA STEO are available below. Meanwhile, we saw further Turkey reopening updates following the quake. Looking ahead, there is private inventory data after-hours. This week's analyst expectations (bbls): Crude +2.5mln, Distillates +0.1mln, Gasoline +1.3mln.

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TURKEY: Turkey has reportedly ordered the resumption of oil flows to the Ceyhan export terminal, and as such pumping has reportedly begun on the Kirkuk-Ceyhan oil pipeline from Iraq with exports from Ceyhan expected to begin on Tuesday. In addition, the first crude oil tanker docks at Turkey's Ceyhan port since earthquake and tanker to load Iraqi crude, according to ship tracking and trade sources cited by Reuters.

FREEPORT: Freeport LNG is on track to stop receiving pipeline natural gas on Tuesday after receiving small amounts over the past 12 days at its Texas export plant, according to Refinitiv.

EIA STEO: 2023 world oil demand forecast was raised by 60k BPD to a 1.11mln BPD Y/Y increase, with 2024 forecast raised by 70k BPD to a 1.79mln BPD Y/Y increase. On crude oil production, 2023 is seen rising 590k BPD to 12.49mln BPD (prev. +550k); and 2024 seen rising 160k BPD to 12.65mln BPD (prev. 400k). For a full breakdown, please click here.

EQUITIES

CLOSES: SPX +1.29% at 4,164, NDX +2.12% at 12,728, DJIA +0.78% at 34,156, RUT +0.76% at 1,972.

SECTORS: Energy +3.07%, Communication Services +2.48%, Technology +2.47%, Materials +1.3%, Financials +1.16%, Health +0.64%, Industrials +0.25%, Consumer Discretionary +0.22%, Utilities -0.08%, Real Estate -0.31%, Consumer Staples -0.36%.

EUROPEAN CLOSES: EURO STOXX 50 +0.09% at 4,209, FTSE 100 +0.36% at 7,864, DAX 40 -0.16% at 15,320, CAC 40 -0.07% at 7,132, FTSE MIB +0.36% at 27,118, IBEX 35 +0.14% at 9,172, SMI -0.41% at 11,236.

STOCK SPECIFICS: **Lockheed Martin (LMT)** was double-upgraded to ‘Outperform’ from ‘Underperform’ at Credit Suisse. **Boeing (BA)** will cut about 2k white-collar jobs in finance and HR through a combination of attrition and layoffs. **Disney (DIS)** set its annual shareholder meeting for April 3rd; gives DIS two months to convince shareholders that Nelson Peltz is not needed on the board. **Progyny (PGNY)** received a strong sell opinion from Spruce Point. **CVS Health (CVS)** reportedly closing in on a deal to acquire **Oak Street Health (OSH)** for about USD 10.5bln including debt, WSJ reported; Cos. discussing a price of USD 39/shr, and a deal could be announced as soon as this week. Note, CVS is scheduled to report earnings on Wednesday. **Bed Bath & Beyond (BBBY)** announced a USD 1bln stock offering. **Criteo (CRTO)** taps **Evercore (EVN)** to explore a sale, according to Reuters sources. **Zoom (ZM)** is to reduce its workforce by 15% or 1.3k employees. **Baidu’s (BIDU)** ChatGPT-styled project is called Ernie Bot; is to complete internal testing in March before launching it publicly. **Microsoft (MSFT)** announced its Bing search engine with OpenAI.

EARNINGS: **Activision (ATVI)** missed on EPS and revenue but beat on net bookings; MAUs were in line and said it is working towards closing the deal with **Microsoft (MSFT)** by June 30th. **Take-Two (TTWO)** EPS and revenue missed alongside woeful guidance; announced cost cutting measures. **DuPont (DD)** beat on EPS and revenue although guidance was weak; launched a USD 3.25bln buyback programme and raised its dividend 9%. **Royal Caribbean (RCL)** posted a narrower loss per share than expected while revenue was in line; guidance topped Wall St. expectations. **Centene (CNC)** surpassed consensus on EPS and revenue. **Pinterest (PINS)** beat on EPS but missed on revenue while MAUs were in line; announced a USD 500mln share buyback programme. **Chegg (CHGG)** beat on top and bottom but Q1 and FY23 revenue guide was poor; it said it’s facing subscriber growth challenges. **Skyworks Solutions (SWKS)** missed on EPS alongside next quarter guidance falling short but it is to purchase up to USD 2bln of common stock. **Fiserv (FISV)** topped consensus on profit and revenue; FY EPS guide also strong.

US FX WRAP

The Dollar was choppy on Tuesday with DXY trading between 102.99 and 103.96 before ultimately finishing the session in the red as Powell's commentary, US data and London fix selling pressures were digested. The highs were seen pre-Powell and post a strong improvement in the IBD/TIPP Economic Optimism index before initially stumbling to the lows on Powell's opening remarks at the discussion which focused on how the disinflationary process had begun. However, the move completely pared (as did the dovish reaction in stocks and bonds) with DXY back to unchanged levels as Powell stressed towards the end of the discussion they may have to do more than what is priced in if they continue to see strong job reports or higher inflation reports, adding it is his base case it will take some time to get inflation down. DXY nonetheless drifted back lower towards the close of the US session once the dust had settled.

The Euro was marginally weaker trading between 1.0699 and 1.0766 with the pair hovering around 1.0720, at pixel time, with 1.07 seen as support. There were several ECB updates on Tuesday, Villeroy spoke where he noted the better economic environment makes the monetary task easier (ie. is easier for the ECB to keep hiking rates), while he also noted they are not very far from the peak in inflation. Meanwhile, Nagel said it would be dangerous to think the inflation

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problem is solved and said that more significant rate hikes are needed. Schnabel said inflation momentum is still quite elevated and they cannot yet give the all clear.

The Yen saw notable gains vs the Dollar with USD/JPY falling from highs of 132.71 to lows of 130.49 in wake of Powell before moving off extremes into the close as UST yields moved higher. The dollar weakness into the London fix was also supporting the Yen demand while a lot of focus turned to next week's US CPI as well as the picks for new BoJ leadership. Note, some analysts were suggesting that BoJ YCC speculation also helped support the Yen.

The Franc also saw notable gains vs both the Dollar and the Euro, clawing back recent losses against the buck defending 0.9300 to the upside despite unemployment rates in Switzerland coming in in line with expectations.

Cyclical currencies saw the Aussie notably outperform in wake of the RBA overnight, who hiked rates by 25bps, as expected. Although, RBA maintained guidance that more rate hikes are to be expected helping AUD/USD rise above 0.6900 and eventually 0.6950 before paring back beneath the latter. NZD was flat vs the Dollar with Aussie tailwinds weighing on the Kiwi in wake of the RBA while AUD/NZD rose above 1.0950 and tested 1.10. GBP was flat but cable managed to hold above 1.20 in the US session while CAD saw marginal gains vs the buck but USD/CAD failed to hold beneath 1.3400. Macklem repeated familiar commentary that it is too early to think about rate cuts but if the economy develops as expected and inflation falls as predicted, more rate hikes will not be needed.

EMFX was mixed, CNH saw gains as the Dollar weakened while MXN was the outperformer and BRL was the laggard. MXN was supported by an unexpected rise in gross fixed investment data while BRL was hit on speculation President Lula may fire BCB Chief Neto. Elsewhere in Brazil, the latest BCB minutes were hawkish which saw the BCB remaining vigilant if maintaining the Selic rate will be enough to ensure the convergence of inflation, noting inflation expectations have deteriorated since the prior meeting.

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