US Market Wrap

24th February 2023: Stocks and Bonds lower as Hot PCE adds to hawkish pricing

- **SNAPSHOT**: Equities down, Treasuries down, Crude up, Dollar up.
- **REAR VIEW**: Hot PCE data; New home sales tops expected; Mester notes little more needed on rate hikes; Collins confirms recent data affirms case for further hikes; Jefferson adds wage growth still to high; BA temporarily halts 737 Dreamliners; GS approves $30bln share buyback programme; US announces new Russia sanctions; Poor ADSK guidance.
- **COMING UP**: **Data**: EZ M3, Consumer Confidence Final, US Durable Goods, Japanese Retail Sales **Speakers**: BoJ nominee Ueda; ECB's Lane, BoE's Broadbent, Pill **Supply**: EU **Earnings**: ABF, Occidental, Zoom.
- **CENTRAL BANK WEEKLY**: Previewing BoJ Governor, ECB minutes; reviewing FOMC minutes, PBoC, RBA, RBNZ, Riksbank, BoK, CBRT. To download the report, please click here.
- **WEEK AHEAD**: Highlights include US ISM, BoJ Governor nominee, China PMI, EZ flash inflation, ECB minutes. To download the report, please click here.
- **NEXT WEEK'S EARNINGS**: [MON] OXY; [TUES] TGT, MNST; [WED] LOW, CRM; [THURS] AVGO, COST. To download the report, please click here.

MARKET WRAP

Stocks and bonds took a hit to end the week after more hot inflation data saw a hawkish shift to Fed pricing. The Fed's preferred gauge of inflation topped expectations and accelerated from the prior, adding to the chorus of hot data we've seen in January. Once the data was digested, market pricing was choppy and saw three 25 bp hikes priced in for March, May and June while the probability for a 50bp hike hit as high as 35% before paring to c. 20%. The terminal rate moved up slightly to 5.4%. The data also led to more hawkish commentary from Mester who said it shows the Fed have to do "a little more", while Collins said the data affirms the case for more rate hikes and Jefferson warned high inflation may come down only slowly. Treasuries saw lows in the afternoon before paring slightly into settlement with the 10yr yield peaking at 3.978%, matching the Thursday high. Crude prices initially tumbled with risk before making a remarkable recovery despite the Dollars rally on the hawkish data.

US DATA

PCE: The PCE data was hot. Core PCE rose 4.7% Y/Y, accelerating from the upwardly revised 4.6% and above the expected 4.3%. The M/M rose 0.6%, hotter than the expected and upwardly revised prior of 0.4%. The hot prices echo what was seen in the CPI report and shows more evidence of prices not cooling as much as initially hoped. There has been a marked shift higher in Fed pricing in wake of the data given it is the Fed's preferred gauge of inflation and the probability of a 50bp hike is now at 35% from 24% before the data, and up from 20% on Thursday while markets are now fully pricing in 25bps moves in March, May and now June. Personal income rose less than expected at 0.6% (exp. 1.0%, prev. 0.3%) and was led by the 8.7% increase in the Cost-of-Living Adjustment (COLA) benefits but Capital Economics note the benefits were "slightly more than offset by the expiry of some one-off state tax credits and the extended child tax credit while the adjusted consumption was above expectations at 1.8% (exp. 1.3%)". Real consumption rose 1.1% in line with expectations while the adjusted consumption rose 1.8%, above the 1.3% expectation. Capital Economics note they "continue to expect first-quarter real consumption to be 3.5%, with overall GDP growth at 1.5%." Note, WSJ's Timiraos highlighted "Fed officials have focused attention on inflation in services that exclude housing, given the potential for it to be stickier (and because housing inflation is set to slow)". He points out the January core PCE services inflation ex-housing data saw the 3 month annualized rate at 5.2% and the 12-month change at 4.5%.

UOM: The Final University of Michigan survey for February saw headline sentiment revised higher to 67.0 from 66.4 with the headline lead by a rise in expectations to 64.7 from 62.3, while current conditions was revised lower to 70.7 from 72.6. The revision higher follows the strong start to 2023 after a slew of hot economic data points (NFP, CPI, PPP, Retail Sales), while the hot inflation is behind the decline in the current conditions component with consumers digesting hot inflation reports and reports of layoffs. Inflation expectations were encouraging, the 1yr consumer inflation expectations were revised lower to 4.1% from 4.2%, while the 5-10yr gauge was left unchanged at 2.9%. Nonetheless, the report will likely do little to change the Fed's views on policy with the hot inflation reports seeing a lot of chatter from the FOMC for the need to do more; i.e. a higher for longer terminal rate.

NEW HOME SALES: New home sales for January rose 7.2% to 670k from 625k, and above the expected 620k. Looking at the internals, new home supply was 7.9 months' worth at current pace (prev. 8.7 months in Dec), while median sale price stood at USD 427,500 (prev. USD 430,500), -0.7% M/M. On the inventory, Oxford Economics note that home builders are likely to continue to offer incentives with that amount of inventory. Oxford adds, "new homes sales found support from a brief decline in mortgage rates and a large drop in median house prices in January." Nonetheless, the consultancy adds, "with financial markets pricing in a more hawkish Fed, mortgage rates have since rebounded, rising to levels from last November." As a result, higher rates will put renewed pressure on homebuying affordability and home sales in the first half of the year, though lower prices and incentives offered by homebuilders should prevent too steep of a drop.

FED

JEFFERSON (VOTER): Wage growth is still running too high to be consistent with timely and sustainably return to 2% inflation goal. The outlook for non-housing core services inflation depends on whether labour demand moves into better balance with labour supply. Jefferson noted the ongoing imbalance between supply/demand for labour suggests high inflation may come down only slowly and said the argument that policymakers should accept that disinflation will be costly is well-reasoned. Jefferson also noted the current situation is different from past inflation fights.

MESTER (NON-VOTER): We are going to have to do "a little more" on rate hikes saying the new inflation data affirms the case for more rate hikes to get inflation back to target. She did however state her view on inflation and the economy has not been changed by the latest data. Mester noted how the financial markets are now much more aligned with the Fed than before and her dot from December (a little above the Median of 5.1%) has not changed. She also repeated that the Fed will need to go above 5% funds rate and stay there for a while, until the inflation trend breaks lower. She also noted she has a little more impetus in inflation than some other Fed members, and that there has been some good movement on inflation measures but it is still too high. On the March meeting, she is not prejudging the size, saying it will depend on the data and the focus on 25bps or 50bps misses the bigger picture. On the PCE report, she said it shows the Fed needs to do "a little more"; gratifying that inflation declined from peak but more is needed, adding the rate peak matters more than meeting to meeting moves. She added the inflation risk is tilted to the upside and with the labour market so strong, the costs of undershooting or prematurely easing outweigh the costs of overshooting and that scenario analysis should play a larger role in policymaking.

COLLINS (NON-VOTER): Further interest rate rises needed to deal with too high inflation and recent US data affirms the case for more rate hikes. The Fed will need to get rates up and potentially hold them there for a long period. She is optimistic the Fed can get inflation down and achieve a soft landing. She is aware there are many risks, including negative economic outcomes.

BULLARD (NON-VOTER): Said it appears that the Fed may be able to disinflate in an orderly manner and achieve a relatively soft landing; adding the current situation for the US seems to fall more closely under the rubric of a "credible disinflation". He noted markets expect inflation to come under control in quarters and years ahead and inflation expectations are now near levels prevailing before the 2021 inflation shock. The St Louis Fed President repeated the Fed need to move quickly to shield credibility.

FIXED INCOME

T-NOTE (M3) FUTURES SETTLED 17+ TICKS LOWER AT 111-13

Treasuries saw pronounced bear-flattening after hot January PCE data gave credence to hawkish voices. 2s +11.0bps at 4.803%, 3s +11.9bps at 4.526%, 5s +10.0bps at 4.205%, 7s +7.8bps at 4.106%, 10s +6.6bps at 3.947%, 20s +7.5bps at 4.119%, 30s +5.5bps at 3.933%.

Inflation breakevens: 5yr BEI -3.0bps at 2.470%, 10yr BEI -2.4bps at 2.397%, 30yr BEI -0.6bps at 2.328%.

THE DAY: After rallying into Thursday's close, Treasuries initially held onto their gains as the APAC Friday session got underway. As Europeans arrived T-Notes (M3) hit highs of 112-03 before unwinding and dipping into the red all before the US session got underway. The hot January PCE data saw T-Notes kneejerk lower from 111-20+ to 111-12+, and as the dust settled, extended on losses as front-end led selling pressure persisted in wake of hawkish Fed repricing. The downside was accentuated by a 6k T-Note block seller. The contracts found support at 111-05+ later in the morning, with some mild paring into the European close and mixed 10:00ET US data: the upward revision to the headline Uni of Michigan survey was accompanied by downward revisions to the near-term inflation expectations, while January new home sales came in on the hot side. However, Treasuries managed to stretch out new lows in the NY afternoon, ultimately troughing at 111-04+, with the cash 10yr yield peaking at 3.978%, matching the Thursday high.

AHEAD: With no coupon supply from the Treasury, next week's highlights include US ISM, another BoJ Governor nominee speech, China PMI, EZ flash inflation, and ECB minutes. Preview here. Month-end flows are also on the radar with Bloomberg's duration index extension estimate at a chunky +0.12yr for February on account of quarterly refunding.

STIRS:

- SR3H3 +0.8bps at 94.998, M3 -4.0bps at 94.625, U3 -7.0bps at 94.595, Z3 -11.5bps at 94.750, H4 -17.5bps at 95.080, M4 -21.5bps at 95.505, U4 -21.5bps at 95.900, Z4 -21.0bps at 96.165, H5 -18.5bps at 96.320, H6 -10.5 bps at 96.565, H7 -6.5bps at 96.635.
- Big option volumes in SOFR post-PCE, with block highlights including 42k S0M3 94.75/94.50 put spreads, 45k SR3Z3 94.25/94.75/95.875 call flys, 25k SR3U3 94.50/94 put spreads, amongst more.
- Fed pricing for March was choppy, with 50bps hike implied probability reaching as high as 35% at the extremes before settling back at 25%.
- Terminal rate pricing tested above 5.40%, initially come July, although interestingly the implied terminal rate has now shifted out to September.
- NY Fed RRP op demand at USD 2.142tln (prev. 2.147tln) across 104 bidders (prev. 102).

CRUDE

WTI (J3) SETTLED USD 0.93 HIGHER AT USD 76.32/BBL; BRENT (J3) SETTLED USD 0.95 HIGHER AT 83.16/BBL

The crude complex was very choppy to end the week, but ultimately firmer, absent of any oil-specific catalyst. The crude complex moved as a function of broader risk sentiment highlighted by WTI and Brent hitting lows of USD 74.09/bbl and 81.07/bbl, respectively, in wake of another hot US inflation data print, this time via core PCE for January. Although, the initial losses were reversed and oil saw notable strength to end the week and settled in the black. The upside started as European players left for the day despite the still risk-off conditions. On the week, WTI and Brent saw marginal losses in volatile trade as it was boosted by prospects of lower Russian exports but weighed on by global economic activity concerns and rising US inventories. Back to Friday, according to Reuters sources, Motiva is to shut its large coker at Port Arthur Texas refinery (636k BPD) next week for repairs, as well as its hydrocracker and small coker in mid-March for maintenance. Note, the upside in oil had already occurred well before this sources article. Next week, there is a lack of tier 1 US data, but the focus may continue to reside on global economic woes amid the tense geopolitical rhetoric.

RUSSIA: Russian President Putin spoke to Turkish President Erdogan and discussed practical aspects of increased supplies of Russian energy, according to TASS. The two also discussed agreements on exporting Ukrainian grain through the Black Sea and the export of Russian fertilisers and agricultural products.

BAKER HUGHES (w/e Feb 24th): Oil -7 at 600, Nat Gas unch. at 151, Total -7 at 753.

EQUITIES

CLOSES: SPX -1.05% at 3,970, NDX -1.73% at 11,969, DJI -1.02% at 32,817, RUT -0.92% at 1,890.

SECTORS: Real Estate -1.82%, Technology -1.77%, Consumer Discretionary -1.56%, Communication Services -1.43%, Health -1.27%, Consumer Staples -0.59%, Industrials -0.58%, Utilities -0.02%, Energy unch., Financials +0.1%, Materials +0.65%.

EUROPEAN CLOSES: EURO STOXX 50 -1.86% at 4,178, FTSE 100 -0.37% at 7,878, DAX 40 -1.72% at 15,209, CAC 40 -1.78% at 7,187, FTSE MIB -1.07% at 26,986, IBEX 35 -0.33% at 9,201, SMI -0.74% at 11,164.

STOCK SPECIFICS: **Boeing (BA)** has temporarily halted deliveries of its 787 Dreamliner jets as it conducts additional analysis on a fuselage component **(SPR)**. Deliveries will not resume until FAA is satisfied that the issue has been addressed. 787 production is continuing, and Boeing has not tweaked guidance. **Goldman Sachs (GS)** approved a new share buyback of up to USD 30bln. In other news, GS estimates possible further loss of USD 2.3bln from legal disputes. DoJ is preparing a suit to block **Adobe's (ADBE)** USD 20bln deal for Figma, according to Bloomberg. Case is expected to be filed next month, although the timing could slip. **Ford (F)** extended the shutdown of an electric F-150 plant by a week. **Cvent Holding (CVT)** reportedly rejected USD 8/shr acquisition offer from **Blackstone (BX)**, according to Reuters sources. Starboard Value wants **Salesforce (CRM)** to hit over 30% profit margins, closer to Oracle and Microsoft, and CRM is working on it, according to Business Insider citing a leaked documents. **Apple (AAPL)** hires ad executive for Apple TV+, in a sign of the cos. video ad ambitions, according to The Information citing sources. **Pioneer (PXD)** is reportedly considering an offer for **Range Resources (RRC)**, according to Bloomberg sources.

EARNINGS: **Autodesk (ADSK)** beat on EPS and revenue, but Q1 and FY23 profit guidance was light. **Booking Holdings (BKNG)** surpassed expectations on top and bottom line alongside announcing a USD 20bln share repurchase authorisation. Exec said it was encouraged by the continued strength and resiliency of demand from travellers last year and into the new year. **Warner Bros Discovery (WBD)** reported a deeper loss per share than expected alongside a miss on revenue and streaming subscriptions. **Beyond Meat (BYND)** reported a shallower loss per share than forecasted alongside topping on revenue. FY23 revenue view surpassed consensus. Sees positive cash flow in H2 and sees FY23 gross margin in the low double-digits, increasing sequentially throughout the year. **Block (SQ)** missed on profit but beat on revenue and saw strong growth in gross profit. **Carvana (CVNA)** provided a grim report, as it posted a deeper loss per share than expected and missed on revenue and used vehicle sales. Looking ahead, it guides to sequential reduction in retail units sold in Q1.

WEEKLY FX WRAP

Hot PCE inflation pushes DXY up to fresh m-t-d peak

USD - There are plenty more pieces of the macro puzzle to slot in before March’s FOMC policy meeting, but the recent run of largely stronger than forecast US data extended to the Fed’s preferred Personal Consumption Expenditures price measure and raised rate hike expectations in the interim. This also gave the Greenback further impetus and the Dollar index enough momentum to clear 105.000 plus all previous February highs on the way to 105.320 from a 103.750 weekly low. Next upside target for Buck bulls is the current 2023 pinnacle set on January 6, at 105.631, and could be achieved if the 10 year Treasury yield reaches the psychological 4% level that capped the benchmark cash rate on several occasions within a 3.98-84% range. To recap, the Greenback was already building a head of steam on return from the long Presidents' Day holiday weekend before prelim PMIs topped consensus and hawkish FOMC minutes arrived to set the stage for monthly PCE release, along with surprise upward revisions to Q4’s core inflation prints and GDP deflator. Note also, weekly jobless claims for this month’s NFP report remained below 200k to indicate ongoing tightness in the labour market, and at least one bank model signalled Usd buying for month end rebalancing vs all other G10 currencies. Returning to February’s Fed minutes, the accounts revealed that a few participants favoured a 50 bp hike in rates rather than the 25 bp delivered, while a number observed that a policy stance that proved to be insufficiently restrictive could halt recent progress in moderating inflationary pressures, and others acknowledgment that financial conditions had eased in recent months, which some noted could necessitate a tighter stance of monetary policy. Subsequent comments from various officials broadly chimed with the minutes, and there is more to come via Waller and Collins.

AUD/JPY/NZD - Don’t fight the Fed is a well known adage and aptly framed by the fact that the Aussie and Kiwi lost out to their US rival even though RBA minutes were hawkish-leaning and the RBNZ maintained its elevated OCR flight path to supplement a half point hike. In short, the RBA did not mull a pause as it did in December as the Board considered 25 bp and 50 bp rate increases and opted for the former, while continuing to guide that further tightening is required to get inflation back to target, but Aud/Usd reversed sharply from 0.6900+ at best towards 0.6700 with added pressure coming from a marked deterioration in the Yuan. Across the Tasman, the RBNZ reaffirmed its intent to keep lifting rates and get to 5.5% on the grounds that the best way monetary policy can aid the recovery effort from Cyclone Gabrielle is to free up resources in the areas needed by slowing demand elsewhere in the NZ economy, but Nzd/Usd topped out around 0.6262 and only found its feet on approach to 0.6150, albeit held its advantage over the Aussie as the Aud/Nzd cross retreated to the low 1.0900 zone from circa 1.1085. Conversely, the Yen was victim of wider UST-JGB differentials on prospects of further Fed-BoJ divergence given no sign of change to the ultra-easy stance from Governor Kuroda’s replacement or the new Deputy nominees, irrespective of Japanese headline inflation accelerating to a four decade plus one year apex. Indeed, Usd/Jpy soared from just under 134.00 to almost 136.50 at one stage, with eyes on a key Fib retracement mark, at 136.66 and then 100 and 200 DMAs not far over the big figure above.

EUR/GBP/CAD/CHF - All unable to evade their US counterpart’s clutches, as the Euro fought in vain to breach 1.0700 convincingly when the Buck was at its lowest ebb and most vulnerable on Monday (with most US participants absent incidentally) before striving to stay afloat of the round number below and subsequently failing. In fact, Eur/Usd ducked under 1.0550 with little assistance from relatively mixed Eurozone PMIs, German ZEW and Ifo findings or mostly hawkish ECB rhetoric for that matter. Similar story for Sterling in the end, if not intermittently as Cable faded very close to 1.2150, let go of 1.2100, 1.2050, 1.2000 and 1.1950 to probe 100 and 200 DMAs regardless of flash UK PMIs that were more worthy of the name and comments from BoE hawk Mann that made up for, or arguably outweighed dovish remarks by her MPC adversary Tenreyro. In contrast, the Loonie had soft Canadian CPI to deal with and offset a recovery in WTI as Usd/Cad spiked from 1.3442 to new 1.3665 seven week high on the basis that the data justifies the BoC's decision to switch from tightening mode to a conditional pause, while the Franc felt the cost of carry between 0.9221-09403 parameters awaiting independent direction via the SNB next month.

SCANDI/EM - The Sek made several sorties beyond 11.0000 vs the Eur, but failed to sustain gains for tech rather than fundamental reasons given another stronger than expected core Swedish inflation update and hawkish Riksbank minutes backed up by commentary from Board members Floden, Ohlsson and Governor Thedeen himself. However, the Nok held mostly above with some fuel from Brent and CEE peers extended their winning streaks against the Eur. Meanwhile, the Mxn outperformed following its breach of major chart barriers vs the Usd, but the Zar only saw fleeting relief in wake of the SA budget, as assistance to ailing power provider Eskom was at the top end of expectations and staggered to ease the financial burden, and the Try derived little traction from the CBRT reverting to easing, albeit for one time only and by 50 bp in consideration of Turkey's unfortunate earthquake travails. In China, further depreciation for the Cny and Cnh after the PBoC left LPRs unchanged again, drained liquidity and Chinese-US relations continued to deteriorate. In India and SK, more intervention to prop the Inr and Krw, while the Ils suffered more investor angst over geopolitics and Israel's moves to reform the judicial system that a larger than anticipated BoI hike failed to stop the Shekel's slide.