US Market Wrap

17th May 2023: Stocks surge on debt ceiling optimism, regional bank recovery, and retail earnings

- **SNAPSHOT**: Equities up, Treasuries down, Crude up, Dollar up.
- **REAR VIEW**: Debt ceiling optimism; Strong WAL deposit update; TGT and TJX not as bad as feared; Mixed housing data; Average 20yr auction.
- **COMING UP**: **Data**: Japanese Exports/Imports, Australian Unemployment Rate, US IJC, Philadelphia Fed, Existing Home Sales **Speakers**: Fed's Jefferson, Barr, Logan; ECB's Lagarde, de Guindos; BoE's Bailey, Pill, Broadbent, Ramsden, Tenreyro **Supply**: Spain **Earnings**: BT, IDS; Walmart Holiday: Ascension Day (Limited Closures).

MARKET WRAP

Stocks rallied through the session on Wednesday, with desks citing optimism around debt ceiling optimism, more promising consumer earnings reports, and an optimistic regional banks update. On the latter, Western Alliance (WAL) gave a reassuring deposit update, helping regional banks surge. Meanwhile, Target (TGT) and TJX (TJX) reports were not as bad as the Home Depot (HD) figures/guide from Tuesday. Sentiment around the debt ceiling has been spun positively after President Biden cut short his Asia trip to engage in negotiations, in addition to Biden and House Speaker McCarthy naming top emissaries to negotiate a deal. Cross asset, Treasuries bear-flattened (2s +8bps, 30s flat) with the fading banking and debt ceiling concerns putting the onus back on the Fed to fight inflation - the June implied hike pricing remains stubbornly low at 20% but further out the curve some of the dovish pricing is being unwound, eyes turn to the Philly Fed survey on Thursday and Powell on Friday. The Dollar faded some of its initial strength Wednesday as risk appetite improved, seeing risk currencies recover while havens remained offered - note the Yuan is in focus after USD/CNH weakened above 7.0000 for the first time since late 2022 on overarching growth woes. In commodities, oil prices tracked stocks higher (and as the Dollar pulled back), with a bigger-than-expected build in US crude stocks an afterthought, copper prices also rallied on the Dollar reversal, aiding commodity currencies. Precious metals were little changed.

US

DEBT CEILING: There was some optimism on the debt ceiling after President Biden said he was confident the US will not default and the meeting on Tuesday was productive, he noted talks will be continuing throughout the week whilst he is at the G7 and he will stay in close contact with negotiators during his time away. He did also suggest there is a possibility of some work requirements being added to the bill, but he will not accept requirements that will affect the medical needs of people. Republican House Speaker McCarthy repeated that a debt ceiling by Sunday is doable and that he is optimistic about their ability to work together. Meanwhile, House Democratic Leader Jeffries said the House Democrats will file a 'discharge petition' on raising the debt limit in case it is necessary to avoid default. There were also reports via NBC that some of the progressive Democrats are urging Biden to prepare to invoke the 14th amendment to lift the debt ceiling and avert a default on his own, without an act from Congress.

HOUSING STARTS/PERMITS: US housing starts rose to 1.401mln (exp. 1.4mln) in April from 1.371mln in March, which saw a big downward revision from the initial 1.42mln. Pantheon Macroeconomics highlights that the rise "is more or less evenly split between single- and multi-family units, broadly in line with the levels implied by previously-granted permits." Meanwhile, building permits fell to 1.416mln from the upwardly revised 1.437mln (initially 1.43mln), beneath the consensus estimate of 1.437mln. "The small decline in April building permits, meanwhile, is entirely due to a 7.7% slump in the multi-family component, which is prone to wild swings month-to-month but has been trending sideways for over a year", Pantheon writes. The consultancy says the bigger picture is that residential construction is now stabilising, something that was a huge drag on fixed investment in 2022, although it warns the expected plunge in business capital spending is likely to offset any recovery in residential fixed investment.

FIXED INCOME

T-NOTE (M3) FUTURES SETTLED 11 TICKS LOWER AT 114-18+

Treasuries bear-flattened as stocks surged on positive regional banking updates and debt ceiling optimism, putting the onus back on the Fed to fight inflation. 2s +8.0bps at 4.154%, 3s +8.2bps at 3.815%, 5s +6.8bps at 3.590%, 7s +4.9bps at 3.582%, 10s +3.0bps at 3.579%, 20s +1.1bps at 3.978%, 30s +0.4bps at 3.877%.

INFLATION BREAKEVENS: 5yr BEI +4.5bps at 2.177%, 10yr BEI +2.6bps at 2.240%, 30yr BEI +1.6bps at 2.281%.

TOKYO/LONDON: Treasuries extended their recovery into the Tokyo morning on Wednesday, led by the long end, while the front end struggled post-strong retail sales, IP data, and hawkish Fed Speak on Tuesday. T-Notes hit interim highs at 115-02+ before Europeans arrived and hit the bid. However, losses were capped after solid auction results in France, Germany, and the UK. A bullish UST call from JPM was also getting a lot of attention.

LONDON/NY: As US trade got underway, T-Notes clipped their earlier 115-02+ peaks before dipping as the latest slew of corporate supply was announced, with 10+ issuers in the primary market. The mixed housing starts and permits data was accompanied by front-end selling, although that may be more a function of the latest Reuters poll right before that saw 75/116 economists surveyed forecasting the Fed rate to be at 5.00-5.25% (current level) at the end of the year vs current 4.25-4.50% priced. A massive 26k 5yr block buyer just after 09:00ET saw the curve spike, sending T-Notes to session highs of 115-03.

NY AFTERNOON: Better Tsy selling soon returned late in the NY morning, and the front end was again driving the selling pressure, with stocks grinding higher on improved debt ceiling sentiment, stronger consumer earnings, and positive regional bank updates. The selling extended into the afternoon, with T-Notes falling through Tuesday's 114-23 low, and ultimately hitting troughs of 114-17 (ahead of May 1st low at 114-10) after the 20yr auction passed, which saw average demand vs the sector's recent history. Note 2yr T-Notes printed fresh MTD lows at 102-261 ahead of the April low of 102-247, with rate expectations largely in the 1yr1yr doing the work amid June pricing resistant to bake in more hike premia beyond 20% implied - Powell on Friday could be pivotal.

20YR AUCTION: A fairly strong 20yr bond auction from the Treasury with USD 15bln of new issue bonds sold at 3.954%, slightly above April's 3.92% stop. The auction saw a 1bp stop-through the WI, which is customary for 20yr paper at this stage, evident in the six-auction avg. also being a 1bp stop-through and last month's 0.2bp tail an outlier. The consistent stop-throughs in the sector is consistent with the notion that participants use the primary offerings to attain a yield pick-up: 20yr trades c. 50bps cheap on the 10s20s30s fly and is the second highest yield tenor on the coupon curve after the 2yr. The details under the hood were less impressive, with the 2.56x bid/cover ratio beneath the prior 2.66x and avg. 2.65x. Dealers (forced surplus buyers) were left with 11.3%, which is lower than last month's 12% but still above the average 9.5% takedown, indicative of the cohort having to backstop the auction to a greater degree than normal with Indirects taking less than average.

THURSDAY & FRIDAY: (Thurs) Japanese trade balance, Australian labour report, Philly Fed mfg. survey, IJC, existing home sales, 10yr TIPS auction, Banxico, Fed's Jefferson, Barr, and Logan; (Fri) G7 Summit in Japan, SARB, Japanese CPI, Fed's Williams, Bowman, and Powell.

STIRS:

- SR3H3 flat at 95.0575, M3 -3bps at 94.865, U3 -3.5bps at 95.115, Z3 -6bps at 95.52, H4 -9.5bps at 96.02, M4 -11.5bps at 96.465, U4 -10.5bps at 96.79, Z4 -9bps at 96.99, H5 -8bps at 97.09, H6 -6bps at 97.10.
- SOFR falls back to 5.05% from 5.06%, volumes fall to USD 1.466tln from 1.497tln.
- NY Fed RRP op demand at USD 2.214tln (prev. 2.203tln) across 103 counterparties (prev. 101)
- EFFR flat at 5.08%, volumes fall to USD 124bln from 126bln.
- US sold USD 39bln of 17-week bills at 5.100%, covered 2.57x.

CRUDE

WTI (M3) SETTLED USD 1.97 HIGHER AT 72.83/BBL; BRENT (N3) SETTLED 2.05 HIGHER AT 76.96/BBL

The crude complex was firmer on Wednesday and seemingly appeared to be a function of risk-on sentiment as opposed to any crude-specific catalyst, although some desks cited potential optimism in debt ceiling talks. WTI and Brent saw gradual upside through the European morning, but that accentuated from the cash open throughout the US session to hit highs of 73.26/bbl and 77.31/bbl from lows of 70.04 and 74.10, respectively. On the day, EIA weekly data saw an unexpected build of 5.040mln in crude (exp. -0.92mln), larger than the surprise build seen in the private inventory metrics Tuesday night, while the EIA report also saw gasoline and distillates show a slightly larger draw and build, respectively. Refining utilisation rose to 1% (prev. 0.3%, exp. 0.5%), and crude production fell 100k to 12.2mln. Separately, according to Iranian press Tasnim, Iran's Oil Minister noted the market is on track following recent OPEC+ decisions. From a macro perspective, looking ahead, the fundamental themes such as recession fears, demand woes, and debt ceiling talks remain of importance, on top of a Fed speak (namely Powell on Friday), Philly Fed and Walmart earnings (Thurs), and finally Japanese CPI (Fri).

RUSSIA: Russia has reportedly agreed to invest in six Iranian oil fields, according to Iranian press Tasnim. Further on Russia/Iran, Deputy PM Novak said swap supplies of oil products between Iran and Russia may total 4-5mln tonne per year. On production, Novak noted Russia reached oil production cuts of 500k BPD in May and the global oil market is balanced. In March, they said they would be continuing their voluntary output cut of 500k BPD until end-2023, a cut which is taken from the average production level for February.

EQUITIES

CLOSES: SPX +1.19% at 4,159, NDX +1.22% at 13,589, DJI +1.24% at 33,420, RUT +2.21% at 1,774.

SECTORS: Financials +2.09%, Energy +2.07%, Consumer Discretionary +2.04%, Industrials +1.7%, Real Estate +1.29%, Technology +1.28%, Communication Svs. +1.18%, Materials +0.67%, Health Care +0.1%, Consumer Staples -0.1%, Utilities -0.36%

EUROPEAN CLOSES: Euro Stoxx 50 +0.18% at 4,323, FTSE 100 -0.36% at 7,723, DAX 40 +0.34% at 15,951, CAC 40 -0.09% at 7,399, FTSE MIB -0.01% at 27,196, IBEX 35 +0.22% at 9,211, SMI -0.67% at 11,442.

STOCK SPECIFICS: **Western Alliance (WAL)** surged, and supported other regional banks and the KRE ETF, after it reported QTD deposit growth over USD 2bln, as of May 12th. Added deposit balances stabilised by March 20th and resumed growth. It added that Insured Deposit Strength was greater than 79% as of May 12th, up from 68% as of March 31st. **Target (TGT)** beat on the top and bottom line, but cut its Q2 profit outlook alongside re-affirming FY guidance. In commentary, TGT sales slowed in March and are decelerating further in April. **TJX Companies (TJX)** beat on profit but missed on revenue. In guidance, Q2 view was light but it raised the FY outlook, albeit below expectations. Despite soft guidance from both TGT and TJX, the companies, and other retailers, closed in the green as they were not as bad as feared after Home Depot (HD) on Tuesday. **Keysight Technologies (KEYS)** surpassed Wall St. expectations on the top and bottom line alongside raising the Q3 profit outlook. **Doximity (DOCS)** surpassed analyst expectations on the top and bottom line, but the Q1 and FY24 revenue guidance disappointed. **Wynn (WYNN)** was upgraded at Barclays citing the continuing recovery in Wynn's Macao properties. CNBC's Faber said **Amgen (AMGN)** believes they have a winning case and can beat FTC in court regarding the acquisition of **Horizon Therapeutics (HZNP)**. **Meta (META)** is set to face a record EU privacy fine over transatlantic transfers, according to Bloomberg. **Disney (DIS)** CFO said the co. is well on way to meet or exceed USD 2.5bln SG&A saving, adding they have Disney+ breakeven firmly in our sights. **EVgo (EVGO)** announced USD 125mln offering of Class A common stock.

TESLA: Had its annual shareholder meeting on Tuesday evening; highlights include Musk noting macro conditions will remain difficult for at least a year, although he is confident Tesla can navigate through the uncertainties. Musk said he was not considering stepping down as Tesla CEO and aims to complete design of next-gen Roadster model this year. Moreover, he said the automaker could consider giving advertising a shot. Separately, Tesla proposes setting up EV manufacturing plant in India and is in talks with government officials. Lastly, Tesla has reportedly filed paperwork with the intent to expand its EV factory in China, coined Giga Shanghai, according to InsideEVs; public notice shares potential expansion could allow Tesla to produce 1.75mln powertrains a year, up from 1.25mln.

US FX WRAP

The Dollar was bid on Wednesday despite the risk on trading conditions, although this did put a limit on the Dollar's gains while the upside in UST yields was capping a further pullback. The DXY rose to highs of 103.12 before paring beneath 103 and hovering around 103.50 throughout the latter part of the session. There was no Fed Speak, but on data, the housing backdrop was mixed with building permits falling 1.5% to 1.416mln from 1.437mln, despite expectations for an unchanged print. Housing starts moved up from the prior revised 1.371mln to 1.401mln, more or less in line with expectations.

The Euro fell victim to the Dollar strength with EUR/USD losing hold of 1.0850 from a high of 1.0873. The Final EZ HICP inflation data was largely unrevised and in line with expectations while ECB speak saw de Cos note the ECB is getting near the end of its cycle, while de Guindos said tightening is mostly done but they still have a way to go. EUR/GBP was lower on hopes the EU could spare the UK on car tariffs after reports noted productive talks were held and as automaker groups urged for this to be the case. Softening China data/growth expectations likely weighed on the single currency too.

The Yuan weakened above the pivotal 7.0000 figure vs the Dollar for the first time since Dec'22. The as-expected fixing only emboldened the sellers, while the PBoC's efforts to offset the weakness via rate differentials, issuing CNY 25bln worth of bills in Hong Kong, didn't stop the currency's selling momentum. The weak IP data from Tuesday was added to by slowing new home price gains on Wednesday, which has also been accompanied by some Sell Side strats cutting their 2023 GDP forecasts, including JPM (5.9% from 6.4%) and Barclays (5.3% from 5.6%), whilst some of those maintaining their forecasts cite low base comparisons from 2022 making it easier to achieve higher growth, in addition to expectations of stimulus measures such as infrastructure investment and targeted consumption support.

The Yen, and other traditional havens (XAU, CHF), were weaker vs the Dollar on the strong risk appetite with US equities surging on debt ceiling hopes while some of the retail earnings were not as bad as was portrayed by Home Depot on Tuesday. Regional banks also surged on the encouraging update from WAL, adding to hopes the fin stability woes have eased since the collapse of SVB, Signature and First Republic. Note, for the Yen specifically, GDP came in above analyst expectations at 0.4% Q/Q and also above expectations on an annualised basis at 1.6% but it had little impact on the pair which rose above the 200dma at 137.08 to highs of 137.63 in the US session. The move higher in US yields and rampant jump in equities was the primary driver of the moves in the Yen, which is also what drove gold prices lower while the CHF was weaker vs the Dollar but flat against the Euro.

Cyclical currencies were mixed, albeit all off worst levels as risk recovered. The NZD outperformed after ANZ hiked its terminal rate forecast for the RBNZ to 5.75% by July, while it also sees a 25bp hike in June but sees a 20% probability of a 50bp hike. AUD only saw marginal gains on the buck while GBP was flat despite the risk environment, although GBP firmed vs the Euro as mentioned above. The Aussie was also limited by a cooler-than-expected wage price index for Q1. CAD saw some gains vs the buck with USD/CAD dipping beneath 1.35 to c. 1.3450, supported by the jump in crude prices.

EMFX was mixed. In **LatAm**: BRL saw marginal gains despite slowing inflation data seemingly tracking the risk tone. The Brazilian IGP10 inflation index slowed to -1.53% from -0.58% in May, cooler than the expected -1.53% which will likely only emphasise calls from the government for the BCB to lower rates, something which Finance Minister Haddad called upon once again today. COP and CLP outperformed in LatAm FX due to gains in crude and copper while MXN was the laggard ahead of the Banxico rate decision on Thursday (primer here).

Elsewhere in EM, the ZAR was notably weaker after retail sales declined 1.6% in March from the prior and expected -0.7% - note the prior was revised down from -0.5%. The latest SARB rate decision poll by Reuters was revealed, which has analysts expecting a 25bp hike on May 25th before pausing, with rate cuts seen in Q1 and Q3 of 2024. The TRY was weaker following continued weakness in local bank stocks on election uncertainties ahead of the run off on May 28th.