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US Market Wrap

18th May 2023: Dollar and yields soar on strong data and more hawkish Fed Speak ahead of Powell

- **SNAPSHOT**: Equities up, Treasuries down, Crude down, Dollar up.
- **REAR VIEW**: Logan and Bullard leaning to June hike; Philly Fed better-than-feared; Jobless claims fall beneath expectations; WMT lifts FY outlook; Mixed debt ceiling commentary; Banxico leaves rates unchanged, as expected; NFLX ad-supported tier gains 5mln users.
- **COMING UP**: **Data**: UK GfK Consumer Confidence, Japanese CPI, German Producer Prices **Events**: ECB Economic Bulletin **Speakers**: Fed's Powell, Williams, Bowman; ECB's Schnabel, Lagarde; BoE's Haskel **Earning** : Deere.

MARKET WRAP

Stocks were firmer on Thursday with a Big Tech bias; NDX outperformed the SPX and RUT. The heavy lifting was being done by the likes of Nvidia (NVDA), Amazon (AMZN), and particularly Netflix (NFLX), which saw near double-digit strength after a positive ad tier subscriber update. Despite the surge in the Philly Fed mfg. survey and fall in initial jobless claims, value and cyclicals underperformed, and it wasn't anything stemming from regional banks, rather seemingly a reaction to the hawkishly ramped Fed pricing/expectations and resulting Dollar strength after Fed's Logan (v) and Bullard (nv) gave the nod for a June hike, raising expectations that the Fed may have to push the economy into a recession. The Treasury curve saw further bear-flattening (2s +10bps, 30s +3bps) on the slew of hawkish Fed speak, with money markets creeping up to a 40% implied June hike vs 20% on Wednesday, where there will be much attention on Chair Powell's comments Friday to see whether he has a whetted appetite for a June hike. Commodities were broadly offered with Dollar on the up.

DATA

PHILLY FED: The Philly Fed manufacturing index spiked to -10.4 in May from -31.3 in April, above the expected -19.8 and countering the plunge seen in the Empire State mfg. survey earlier in the week. Looking within, new orders (-8.9 from -22.7) and shipments (-4.7 from -7.3) both rose but remained negative, while prices paid remained near cycle lows (10.9 from 8.2) and prices received made new lows (-7 from -3.3). Employment fell to -8.6 from -0.2, echoing the Empire Fed. The future capex plans index rose to 2.5 from -5.4, the first positive reading since February, and a sign of confidence in the banking sector given fears the recent bank failure fallout may lead to a contraction in lending and business spending, although note the fall in this measure in the Empire survey. While one to watch for the future is the jump in delivery times and unfilled orders, although both are still much lower than where they were during the peak of the supply chain crisis. Lastly, on the outlook, the future general business activity index reversed the rise in April, reapproaching the cycle lows in October 2022. The next survey data of note are the S&P flash PMIs and Richmond Fed both on May 23rd - we don't get the ISM mfg. for May until June 1st.

JOBLESS CLAIMS: Initial claims data, for the week that coincides with the BLS survey period for nonfarms, came in beneath expectations falling to 242k from 262k previously. The cooling down to 242k completely pares the large rise to 262k in the prior month. The continued claims data also fell by more than expected to 1.799mln from a prior 1.807mln, although that data does not coincide with the BLS NFP. The reversal from the prior weeks advance shows perhaps the labour market is loosening as fast as initially thought. Recent strong economic data (retail sales, IP, NFP) shows the economy is not cooling as quickly as perhaps the Fed would like, and there has also been a notable hawkish shift recently in Fed speak, opening the door to a June rate hike. Analysts at OxEco note the data is a reminder that labour market conditions are still relatively tight and although they expect the Fed to leave rates unchanged in June, a resumption of rate hikes cannot be ruled out if conditions do not ease more significantly.

EXISTING HOME SALES: Existing home sales fell 3.4% in April to 4.28mln, beneath the prior, downwardly revised, 4.43 mln and the expected 4.3mln. Inventory of homes for sale was 1.04mln units, 2.9 months' worth, and the national median home price fell 1.7% Y/Y to USD 388,800. Overall, US home sales remain subdued due to elevated borrowing costs, high prices and a lack of supply. ING notes, "new home sales should continue to outperform existing ones in this environment, but price risks remain skewed to the downside." The desk concludes, "Commercial real estate woes are the bigger concern as office vacancies and higher refinancing risks point to rising loan losses."

FED

LOGAN (voter), who was more dovish at the start of the week, struck a hawkish tone as she opened up the door to more hikes, suggesting data so far does not support justifying a pause in June, but upcoming inflation and employment data could change that view. The Dallas Fed President added she is concerned about whether inflation is falling fast enough, and notes managing risks must not stop the Fed from returning inflation to target. Logan noted the effect of banking stress so far is comparable to a 25 or 50bp Fed policy hike.

JEFFERSON (voter) largely repeated what he said last Friday, noting inflation is too high and by some measures, progress is slowing, however, he was cognizant of the lagged effects of monetary policy, noting a year is not long enough to feel the full effect of rate hikes so far. Given Jefferson is up for the Vice-Chair role, it is likely he will not try to "rock the boat" too much in remarks.

BULLARD (non-voter), via an FT interview, noted higher rates are insurance against inflation and he will keep an open mind going into the June meeting but is currently leaning towards a hike. That view was much more forthright on his preference for a hike in June vs his prior comments on May 5th, a few days after the FOMC, where he said the Fed will "ultimately" have to grind higher on rates, which seemed a compromise to the doves at the time before assessing incoming data. In the FT today, Bullard said he still believes rates are at the low end of the 'sufficiently restrictive' zone, with the top end seen above 6%, saying it's "better and more prudent to be in the middle of the zone". Bullard also reiterated his view that the fall in Treasury yields has offset the banking sector tightening.

FIXED INCOME

T-NOTE (M3) FUTURES SETTLE 21 TICKS LOWER AT 113-29+

Treasuries bear-flattened further on Thursday after strong Philly fed data, a fall in jobless claims, and hawkish Fed's Logan and Bullard. 2s +11.9bps at 4.275%, 3s +12.4bps at 3.938%, 5s +11.0bps at 3.702%, 7s +9.9bps at 3.681%, 10s +7.4bps at 3.655%, 20s +5.3bps at 4.036%, 30s +3.0bps at 3.908%.

INFLATION BREAKEVENS: 5yr BEI +1.9bps at 2.181%, 10yr BEI +1.8bps at 2.248%, 30yr BEI +1.4bps at 2.283%.

TOKYO/LONDON: After Wednesday's sell-off, T-Notes recovered into the Thursday APAC session, with peaks of 114-24 made in wake of the disappointing Australian labour market report. Selling slowly crept in from there as European trade began, not to mention the strong bid in global stocks, with spillover from EGBs as the region played catch up to the exuberant risk conditions in US trade on Wednesday. Note that most of northern Europe was absent for the Ascension Day holiday, but volumes were still decent. T-Notes crossed through Wednesday's 114-15+ low during London trade and went on to trough at 114-11+ at the NY handover ahead of the US data, with the front end leading, aided by an early 7.5 k block seller in the 2yr fut.

NEW YORK: The spike in the May Philly Fed manufacturing survey offset the plunge in the Empire survey earlier in the week, while initial jobless claims fell back to 242k, which in aggregate saw more bear-flattening flows to take T-Notes clean through their MTD low of 114-10 from May 1st. That only gathered momentum as comments from Fed's Logan (v) soon after gave the nod to a June rate hike. Fed Vice Chair nominee Jefferson (v) soon followed but largely repeated his remarks from last Friday. Jefferson was more ambiguous over policy preferences than Logan, but given price action, many framed them as hawkish too, citing his concern over the lack of progress in inflation. The 2s10s curve bottomed at -63bps, nearing the May 1st low of -64bps, before a slew of chunky 2yt fut block buys provided some support to the front end while duration stayed offered, taking the curve off its most invested levels into the NY afternoon. However, some renewed bear-flattening was seen later on in the aftermath of Fed's Bullard (nv) telling the FT he is currently leaning towards a June hike (prev. said on May 1st Fed would "ultimately" have to hike rates further), seeing T-Notes go on to trough at 113-28+ ahead of settlement. Meanwhile, the selling at the front end coincided with the cash 2yr yield breaking above the key 4.25% figure. All eyes to Powell on Friday, with Japanese CPI first up.

FRIDAY: G7 Summit in Japan, SARB, **Japanese CPI**, Fed's Williams, Bowman, and **Powell**.

10YR TIPS AUCTION: US sold USD 15bln of 10yr TIPS at 1.395%, stopped-through by 1.5bps, covered 2.31x, Dealers took 7.7%, Directs 15.9%, and Indirects 76.4%.

REFUNDING: US to sell USD 42bln of 2yr notes on May 23rd, USD 43bln of 5yr notes on May 24th, and USD 35bln of 7yr notes on May 25th; all sizes unchanged, as expected, and all to settle on May 31st. US also to sell USD 22bln in 2yr

FRN reopening on May 24th; to settle on May 26th. In bills, US announces a cut to its 21-day CMBs (May 23rd) to USD 35bln from 40bln, whilst it raised its 26-week bill (May 22nd) to USD 54bln from 51bln, leaving its 13-week bill (May 22nd) auction unchanged at USD 57bln; all bills to settle on May 25th.

STIRS:

- SR3H3 -0.25bps at 95.0525, M3 -5.75bps at 94.8075, U3 -10.5bps at 95.01, Z3 -13.5bps at 95.385, H4 -16bps at 95.865, M4 -18bps at 96.29, U4 -18.5bps at 96.61, Z4 -17.5bps at 96.82, H5 -16bps at 96.935, H6 -11bps at 96.995.
- SOFR flat at 5.05%, volumes fall to USD 1.401tln from 1.466tln.
- NY Fed RRP op demand at USD 2.238tln (prev. 2.214tln) across 102 counterparties (prev. 103).
- EFFR flat at 5.08%, volumes rise to USD 130bln from 124bln.
- US sold USD 36bln of 4-week bills at 5.370%, covered 3.15x; sold USD 36bln of 8-week bills at 5.020%, covered 2.39x; sold USD 45bln in 56-day CMBs at 5.230%, covered 2.40x.

CRUDE

WTI (M3) SETTLED USD 0.97 LOWER AT 71.86/BBL; BRENT (N3) SETTLED USD 1.10 LOWER AT 75.86/BBL

The crude complex was lower as strong US economic data and hawkish Fed rhetoric saw the Dollar surge to a two-month high amid increasing expectations the Fed could hike in June. Oil-specific newsflow was on the light side on Thursday, with the complex continuing to be driven by macro sentiment. Prices trundled lower throughout the US session in the wake of the aforementioned data (lower-than-expected jobless claims and not as bad as feared Philly Fed) and Fed rhetoric to see them print lows of USD 71.42/bbl and 75.50/bbl, respectively, in pre-settlement trade. Meanwhile, according to Reuters citing traders, Russian Urals oil strengthened to minus USD 7.5-8/bbl against ICE Brent at delivery in Chinese ports, the highest since December.

NATGAS: In the wake of the weekly EIA data, which saw a smaller-than-expected storage build, nat gas futures saw a tear higher to settle up over 8% - eyes to the Baker Hughes US rig count on Friday which saw a notable surge in gas prices last week after the big fall in nat gas rigs. Meanwhile, in Europe, TTF prices fell back beneath EUR 30/MWH, the lowest level since June 2021 and back to its 'normal' trading range, with storage levels exiting the winter well above average.

EQUITIES

CLOSES: SPX +0.94% at 4,198, NDX +1.81% at 13,834, DJI +0.34% at 33,535, RUT +0.58% at 1,784.

SECTORS: Technology +2.06%, Communication Services +1.79%, Consumer Discretionary +1.54%, Financials +0.7%, Industrials +0.67%, Materials +0.55%, Energy +0.49%, Health -0.24%, Utilities -0.36%, Consumer Staples -0.44%, Real Estate -0.68%.

EUROPEAN CLOSES: Euro Stoxx 50 +1.20% at 4,367, FTSE 100 +0.25% at 7,742, DAX 40 +1.33% at 16,163, CAC 40 +0.64% at 7,446, FTSE MIB +0.14% at 27,235, IBEX 35 +0.02% at 9,213, SMI -0.71% at 11,437.

STOCK SPECIFICS: **Walmart (WMT)** beat on EPS, revenue, and total US comp. sales alongside raising FY profit view. In commentary, Co. said stubborn inflation in dry grocery and consumables is a key factor creating uncertainty for the back half of the year. **Micron (MU)** intends to make a multi-billion dollar investment in Japan, although a Japanese official said no decision had yet been made. Micron said it will bring EUV technology to Japan, advancing its next-generation memory manufacturing, and expects to invest up to JPY 500bln in 1-Gamma process technology over the next few years. **Cisco Systems (CSCO)** beat on top and bottom alongside raising FY EPS outlook. However, it reported a 23% decline in orders for Q3. **Take-Two Interactive Software (TTWO)** surpassed street expectations on bookings and signalled that a strong future gaming slate could fuel strong growth thereafter. Although, guidance for both the next quarter and FY was light. **Alibaba Group Holding (BABA)** posted a mixed report; beat on profit but missed on revenue and cloud revenue. Intends to offer its proprietary AI foundation model to the wider public and the intent is to integrate AI into all its services starting with DingTalk. **Synopsys (SNPS)** surpassed Wall St. expectations on top and bottom line, while guidance for both next quarter and FY was strong. **Amazon's (AMZN)** AWS plans to invest around USD 13bln in India by 2030, doubling down on its past investments to cater to an ever-growing demand. **Bath & Body Works (BBWI)** topped on profit alongside raising FY outlook. **Sony (SONY)** mulls partial spin-off and listing of its financial unit to help raise funds for investments in gaming and electronics. **Urstadt Biddle Properties (UBA)** is set to be acquired by **Regency Centers (REG)** for USD 20.40/shr in a USD 1.4bln all-stock deal. Note, UBA closed Wednesday at USD 16.95 /shr. **ESPN (DIS)** is reportedly laying the groundwork to sell its channel directly to cable cord-cutters as a subscription streaming service in coming years, according to WSJ citing sources; shift with implications for co. and broader TV business. **Netflix's (NFLX)** ad-supported tier, launched last November at USD 7/month, has gained almost 5mln active users per month.

US FX WRAP

The Dollar was firmer Thursday and a hit two-month high of on account of strong US data, hawkish Fed speak, easing regional bank woes, and potential optimism around the debt ceiling. In wake of the former two, Fed pricing has picked up for a June rate hike with eyes on Chair Powell on Friday in a panel discussion to see if he adds further strengthening to a potential June hike. On the data, in the week that coincides with NFP survey period, jobless claims were lower than expected, while the Philly Fed Business Index was not as bad as feared, albeit still in negative territory. Additionally, prices paid saw a slight rise (off recent lows) while new orders saw the highest print since June 2022 and is at odds with the dismal NY Fed survey seen earlier in the week. The Fed highlight came via Logan (voter), who was initially on the dovish at the start of the week, opened up the door to more hikes, suggesting data so far does not support justifying a pause in June, but upcoming inflation and employment data could change that view. Bullard (non-voter) later on told the FT he is currently leaning to a hike in June.

Cable hit a low of 1.2392, with the weakness beginning in wake of US data which supports the view of the Fed being higher for longer. Additionally, there was a slew of BoE speak, albeit not much new. Governor Bailey said he does not envisage BoE balance sheet returning to where it was before the financial crisis, and Deputy Governor Ramsden noted QT has some effect on the economy, but a fairly small effect, and while there is potential for QT sales number to go up, does not see it going down. On Sterling, JPM's FX desk notes positioning risk saying "investor base across all parts of the franchise has been a buyer so far this year and the data and move appear to be running out of a little steam, flows appear to be showing the first sign of a turn in the last session on two."

Antipodeans saw similar losses, with the Aussie labouring after a weaker-than-expected employment change and rise in unemployment, to see AUD/USD hit a low of 0.6606, just managing to prevent dipping beneath the round 0.6600. NZD /USD hit a trough of 0.6205 ahead of trade data on Friday.

The Loonie was the G10 ‘outperformer', albeit still lower vs the Dollar, as BoC Governor Macklem reaffirmed commitment to get Canadian inflation back down to 2%, and he acknowledged that April CPI came in stronger, but core measures eased and the June rate call will be guided by economic data. Worth noting, the latest Financial System Review revealed more concern than in 2022 about the ability of households to service debt, given higher borrowing costs, but didn't impact price action of the currency.

Safe havens, CHF and JPY, were G10 underperformers with USD/JPY and USD/CHF hitting highs of 138.74 and 0.9062, respectively. The Yen cross hit new YTD peaks amid rising Treasury-JGB yield spreads, with Fed rate cut pricing retreating. Nonetheless, desks are citing some of the Yen weakness to market participants awaiting the risk-event of Japanese CPI on Friday which could potentially lift BoJ policy shift hopes, but probably not much.

Scandis saw pronounced weakness on Thursday as the Buck's surge accompanied with falling oil prices weighed. For the SEK, the currency is approaching its April and March highs of 11.4510 and 11.4815, respectively, vs the Euro, which if breached, would open up a run on the cross' all time highs from the GFC at 11.7860. ING, to wit, "The emergence of dissent within the Riksbank and lower-than-expected inflation figures are leaving the krona without a solid floor. Near-term vulnerabilities remain elevated, and our baseline scenario for a recovery in the second half of the year faces rising risks".

EMFX was lower across the board and fell victim to two-month highs in the Dollar. The Chilean Peso saw headwinds from lower copper prices while the RBI curbed INR declines to an extent via intervention. The Yuan saw downside and remains above the key 7.00 handle, but the currency will be hoping for a supportive PBoC midpoint fix after losing Fib retracement levels beneath 7.0000. For the Brazilian Real, according to Reuters sources, Brazil's government is to raise its 2023 GDP growth projection to 1.9% from 1.6% in March, whilst maintaining its 2024 forecast at 2.3%. In addition, Finance Minister Haddad said the economy had a good quarter and the country is on track to grow 1.8-2%.

MXN was lower on Thursday and extended those losses in wake of the Banxico rate decision, albeit soon pared the rate decision weakness, where it held rates at 11.25%, as expected, in a unanimous decision. For 2023 it decreased its inflation expectations while those for the longer term remained relatively stable at levels above target, but inflation is still projected to converge to the 3% target in Q4 2024. Additionally, Banxico considered the economy has begun to undergo a disinflationary process given that many pressures have eased, but deemed these pressures continue having an incidence on inflation, as it remains high and the inflationary outlook is still very complex. Overall, the balance of risks for the trajectory of inflation within the forecast horizon remains biased to the upside.

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