US Market Wrap

1st June 2023: Stocks higher on debt ceiling optimism and falling Labor Costs ahead of jobs report

- **SNAPSHOT**: Equities up, Treasuries up, Crude up, Dollar down.
- **REAR VIEW**: Debt ceiling bill passed onto the Senate; ISM Manufacturing headline short amid fall in prices paid and new orders, while employment rose; Hot US ADP report; ULC revised much lower, with productivity higher; Jobless claims more-or-less inline; Retailers M & DG cut guidance; OPEC unlikely to deepen output cuts at June 4th meeting; GS & BAC execs note challenging macro environment; Harker toes a dovish line; EZ inflation data on the soft side.
- **COMING UP**: **Data**: US Labour Market Report **Rating Reviews**: Germany, France & UK.

MARKET WRAP

Stocks rallied through the session on Thursday after the US House passed the debt ceiling bill, where it is now at the mercy of the Senate, where it is largely expected to pass. The Russell 2k and Nasdaq 100 outperformed the S&P 500, although all saw gains. That's despite some concerning consumer updates with awful guidance on worsening macro conditions from Macy's (M) and Dollar General (DG), while BofA warned that the consumer is softening. Bonds were bid on the session, particularly after the massive slash to Q1 Unit Labor Costs, but also the soft ISM Mfg. survey that was weighed on by the fall in both prices paid and new orders, although note the stronger employment gauge ahead of Friday's jobs report. Meanwhile, Fed's Harker (voter) spoke again, out-doving his Wednesday comments by saying that the Fed is "near" pause territory, saying the FOMC should "at least" skip the June meeting. Cross-asset, the Dollar was lower and printed a new weekly trough of 103.490 as the index continued to slip in the tail-end of the US session with broad weakness across pairs. Oil prices rallied, enjoying the reprieve in the softer Dollar.

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PRODUCTIVITY & LABOR COSTS: The BLS revised Q1 productivity up to -2.1% from the initial -2.7% reading, the combined effect of a 0.3ppt upward revision to output and a 0.4ppt downward revision to hours worked. Meanwhile, and the market's focus, was the Unit Labor Costs print being slashed to 4.2% from 6.3%, well beneath street estimates of 6.1%, reflecting a 1.3ppt downward revision to hourly compensation and a 0.6ppt upward revision to labor productivity. Given the sensitivity around any wage/price spiral right now, the data was well received, despite it being backward looking at this point. But, while better than the initial reading, 4.2% ULC is still uncomfortably high for a 2% inflation target. Oxford Economics warns, "our proprietary wage growth tracker shows that wage growth is still running above of 5%. The Fed needs wage growth to slow to around 3.5% before it can be confident inflation will return to 2% on a sustained basis." All eyes to the average hourly earnings figures in the May employment report on Friday.

ISM MANUFACTURING: ISM Manufacturing PMI marginally dipped to 46.9 in May from 47.1 and fell ever-so-short of the expected 47.0 to remain in contractionary territory for the seventh straight month. Prices paid plunged to 44.2 (exp. 52.6, prev. 53.2) while employment remained in expansionary territory at 51.4 (prev. 50.2) having been forecasted to dip beneath 50 to 49.8. On the former, Pantheon Macroeconomics notes, “the survey only asks firms about prices paid, not prices received. The price index just tracks the trend in commodity prices; it does not tell us anything much about the outlook for core CPI/PCE goods inflation.” New orders and inventories also declined to 42.6 (prev. 45.7) and 45.8 (prev. 46.3), respectively. Production climbed back into expansionary territory, but desks suggest a significant risk that it falls back into contraction next month given the prevailing economic environment. Lastly, supplier deliveries printed 43.5 (prev. 44.6) and backlog of orders 37.5 (prev. 43.1), with the consultancy noting “the falls [delivery times and order backlogs], by contrast, has been a decent guide to the improvement in supply conditions and the resulting downshift in core goods inflation.”

JOBLESS CLAIMS: Initial jobless claims edged up to 232k (prev. 230k) and were more-or-less in line with the expected 235k, while continued claims slightly lifted to 1.795mln (prev. 1.789mln) but were underneath consensus of 1.800mln. Jobless claims climbed higher throughout the majority of Q1 but have recently topped out and have actually drifted lower in recent weeks, a reminder that labour market conditions are still tight. As such, Oxford Economics adds, “While we expect the Fed to leave rates steady at its upcoming meeting, a more sustained loosening of labour market conditions is needed to keep rate hikes permanently off the table.” Note that these jobless claims figures are not the survey period for Friday's May jobs report.

ADP: The latest ADP report was strong, coming in at 278k, above the 170k expectation, but down slightly from the prior 291k. It also showed further signs of wage growth cooling for both job stayers and job changers. The former cooled to 6.5% from 6.7% and the latter to 12.1% from 13.2%. The Chief Economist at ADP noted "This is the second month we've seen a full percentage point decline in pay growth for job changers", adding "Pay growth is slowing substantially, and wage-driven inflation may be less of a concern for the economy despite robust hiring." The hotter than expected print comes ahead of the NFP on Friday (Full Newsquawk preview here), albeit the correlation between ADP and NFP is not the greatest, but many analysts also have been looking at the homebase data, which ING says was ok, while the latest employment metric from the ISM Manufacturing PMI survey accelerated further into expansionary territory but we will not see the Services ISM until Monday. Nonetheless, the ADP report clearly signals a robust labour market but with slowing wages, and participants will be looking to see if that translates into the NFP report on Friday.

NFP PREVIEW:The headline NFP is expected to cool in May to 190k from 253k, although analyst forecasts range between 100-293k. The unemployment rate is seen rising to 3.5% from 3.4%, while the wage metrics are seen easing to 0.3% from 0.5% M/M but maintaining April's 4.4% Y/Y pace. Labour market proxies for May ahead of the NFP saw a hot ADP employment number, but the wage components in that survey showed further signs of cooling. The jobless claims data that coincides with the BLS survey week were lower than expected, for both initial and continued counts. Meanwhile, the S&P Global PMI report noted manufacturing growth remained solid in May, while services employment rose at a quicker pace. The Challenger Layoffs came in above expectations. Albeit for April, the latest JOLTS data came in well above expectations. The report will be used to gauge the Fed's reaction function, where data in the run-up to the release (hot PCE and hot JOLTS) saw money markets price in a near 70% probability of a 25bp hike in June, but since then Fed voters have been calling for a "skip", albeit with the caveat that this could change depending on the data. We are also due a CPI and PPI report on the 13th and 14th of June, respectively, which will also be key for the Fed. To download the full Newsquawk preview, please click here.

FIXED INCOME

T-NOTE (U3) FUTURES SETTLED 8+ TICKS HIGHER AT 114-23+

Treasuries bull-steepened again Thursday after a slash in Q1 Unit Labor Costs, mixed ISM Mfg. data, and even more dovish Harker comments. 2s -5.1bps at 4.339%, 3s -5.1bps at 3.987%, 5s -4.4bps at 3.699%, 7s -3.8bps at 3.656%, 10s -3.3bps at 3.605%, 20s -4.0bps at 3.978%, 30s -2.7bps at 3.830%.

INFLATION BREAKEVENS: 5yr BEI +1.5bps at 2.128%, 10yr BEI -0.4bps at 2.187%, 30yr BEI -0.8bps at 2.227%.

TOKYO/LONDON: T-Notes hit resistance at 114-16 in the Tokyo morning on Thursday in wake of the House passing the debt limit (now goes to Senate vote) before better selling developed, with Wednesday's month-end and dovish Fed bid unwinding somewhat. The rise into expansionary for the Caixin China PMI only aided the pullback. T-Notes hit session lows of 114-01 in the London morning, not long after ECB's de Guindos stressed the need to do more on rates /inflation. Losses were then pared after the Eurozone inflation data came in on the soft side - Y/Y headline HICP fell to 6.1% from 7.0%, against expected 6.3% - albeit not too surprising given the misses in the state figures earlier this week.

NEW YORK: Going into the NY morning, the recovery in USTs lost some momentum on the above forecast ADP employment print, although that downside spurt swiftly faded as T-Notes broke through Wednesday's 114-20 highs after the massive downward revisions to Q1 Unit Labor Costs (4.2% from 6.3%). Consumer concerns were also likely behind the govvie bid after massive guidance cuts from retail stalwarts Macy's (M) and Dollar General (DG), who both cited deteriorating macro conditions. T-Notes ultimately peaked at 115 on the nose in the wake of the ISM Mfg. data that saw a fall in both prices paid and new orders, although the employment subindex was strong ahead of Friday's NFP. Note that while T-Notes hovered sideways through the NY afternoon, the front end found some renewed strength after Fed's Harker (voter) gave fresh remarks where he indicated the Fed was nearing the point where it could hold rates for a while (a pause).

STIRS:

- SR3M3 +3.75bps at 94.7575, U3 +4.5bps at 94.875, Z3 +5.5bps at 95.21, H4 +7.5bps at 95.695, M4 +8bps at 96.175, M5 +4.5bps at 97.005, M6 +4bps at 97.00.
- SOFR jumps 2bps to 5.08% as of May 31st, volumes spike to USD 1.623tln from 1.53tln (month-end factors to consider).

- NY Fed RRP op demand tumbles to USD 2.160tln from 2.255tln, across 102 counterparties (prev. 107) amid the USD 64bln T-bill and CMB settlement cash drain Thursday.
- EFFR flat at 5.08%, volumes fall to USD 118bln from 127bln.
- US sold USD 25bln in 3-day CMBs at 6.150%, covered 2.38x; sold USD 36bln of 4-week bills at 5.130%, covered 2.85x; sold USD 36bln of 2-month bills at 5.220%, covered 2.83x.
- US announces new USD 15bln 1-day CMBs on June 2nd, to settle on June 5th.
- US "tentatively" announces plans to sell USD 65bln in 13-week bills and USD 58bln of 26-week bills both on June 5th, which will be dependent on Congress passing debt limit.

CRUDE

WTI (N3) SETTLED USD 2.01 HIGHER AT 70.10/BBL; BRENT (Q3) SETTLED USD 1.68 HIGHER AT 74.28/BBL

The crude complex was in the black on Thursday as the House passed the debt ceiling bill, with the Dollar falling, offsetting OPEC sources and the surprise crude build. Reuters sources noted, as expected, OPEC+ is unlikely to deepen output cuts at June 4th meeting, where the general consensus is OPEC will hold output steady (Newsquawk preview available here), some analysts refuse to rule out another production cut citing mixed demand indications from China and rising crude inventories in the US. On the latter, crude stocks surprisingly rose in the weekly EIA data (+4.5mln bbls), in fitting with the private data Wednesday night (+5.2mln bbls), while gasoline was a smaller draw than expected and distillates an unexpected build. Overall, crude production fell by 100k. Analysts note the build-in inventories in the week just prior to Memorial Day, which traditionally marks the start of peak driving season in the US, reflects poorly on the broader economy. Looking ahead, attention will be on the US jobs report on Friday as well as any Fed speak ahead of the blackout and the aforementioned OPEC+ meeting on Sunday.

PRODUCTION/EXPORTS: Iraq's oil exports averaged 3.3mln BPD in May, unchanged from April, while Russian oil product exports from the Black Sea port of Tuapse planned at 1.209mln tonnes in June vs. 1.446mln tonnes scheduled for May, according to traders. Lastly, Libyan oil production reached 1.208mln BPD (vs 1.223mln BPD reported on the 6th April), according to NOC.

EQUITIES

CLOSES: SPX +0.99% at 4,221, NDX +1.31% at 14,441, DJIA +0.47% at 33,061, RUT +1.05% at 1,767.

SECTORS: Technology +1.33%, Industrials +1.26%, Materials +1.24%, Energy +1.23%, Consumer Discretionary +1.22%, Communication Services +1.15%, Financials +1.09%, Health +0.67%, Real Estate +0.03%, Consumer Staples -0.09%, Utilities -0.78%.

EUROPEAN CLOSES: Euro Stoxx 50 +0.94% at 4,257, FTSE 100 +0.59% at 7,490, DAX 40 +1.21% at 15,853, CAC 40 +0.55% at 7,137, FTSE MIB +2.01% at 26,575, IBEX 35 +1.30% at 9,167, SMI +0.71% at 11,297.

STOCK SPECIFICS: **C3.ai (AI)** guidance disappointed, although it did post a shallower loss per share than expected and beat on revenue. **Nordstrom (JWN)** posted a surprise profit per share and beat on revenue; Q1 gross profit margin +110bps Y/Y, which execs said reflected its focus on increasing inventory productivity. **Salesforce (CRM)** beat on EPS and revenue while guidance was also strong, but investors are focusing on higher-than-expected capital costs and lower demand for consulting deals in Q1. **Lucid (LCID)** is raising USD 3bln through a new stock offering. **Chewy (CHWY)** reported an unexpected profit per share and topped on revenue alongside lifting Q2 and FY revenue outlooks. Exec said 2023 was off to a strong start with net sales per active customer and Autoship customer sales both hit new record highs. **Okta (OKTA)** posted solid numbers for Q1 alongside lifting guidance for the next quarter and FY guidance. However, cPRO fell short as management spoke about rising macro pressures with next quarter guidance light with analysts noting investors will focus on the cRPO shortfall. **Victoria's Secret (VSCO)** notably missed on EPS and marginally fell short on revenue with total comp. sales declining 11% adding to poor Q2/FY guidance. **Amazon (AMZN)** faces EU review for its USD 1.65bln **iRobot (IRBT)** purchase, according to Bloomberg. **Microsoft (MSFT)** execs actively looking at ways to close the USD 69bln acquisition of **Activision Blizzard (ATVI)** despite a UK veto on the deal, according to MLex. Such a move would almost certainly trigger legal action from the UK's CMA. In other news, Microsoft inks a deal for AI computing power with **Nvidia (NVDA)**-backed CoreWeave that could be worth billions, according to CNBC.

RETAILERS: **Macy’s (M)** missed on revenue and cut FY guidance well beneath estimates. In commentary, it said starting in late March, demand trends weakened further in discretionary categories. The CEO later added cooler temperatures and headlines surrounding layoffs, as well as the banking crisis, were factors that impacted demand trends. **Dollar General (DG)** missed on EPS, SSS, and revenue alongside cutting EPS growth guidance amid the macroeconomic environment being more challenging than previously anticipated and having a significant impact on customers' spending levels and behaviours. On this, the CEO believes headwinds have had a disproportionate impact on its core customers and does continue to see signs of increasing financial strain. Also, DG no longer expects to repurchase 500mln of shares in 2023. **Target (TGT)** was downgraded at JPM citing several factors, including a weakening consumer spending environment, ongoing share losses from recent controversies, and grocery inflation headwinds. Meanwhile, Bank of America (BAC) CEO Moynihan said later on that US consumer spending is slowing, noting that and restaurant spending is now down to 3% Y/Y from 17%, with spending up only 3% this month, down from 9% growth.

FINANCIALS: **Goldman Sachs (GS)** President Waldron stated the macro backdrop is extraordinarily challenging and there's no real stress on consumers but are embarking upon further targeted actions with its headcount. On specifics, added M&A is definitely a more challenging environment and volumes are down accordingly. Waldron noted it will be a softer quarter for markets business and its tracking down a little over 25% Y/Y in FICC and equities. Regarding regionals, noted they will have a lower capacity to lend. **Bank of America (BAC)** CEO Moynihan said loan growth will be flattish this quarter, with non interest deposits around today less likely to move. BofA said Investment Banking fees are likely to be in the low USD 1bln range in Q2 and concluded by saying you're seeing signs of a slowdown coming.

US FX WRAP

The Dollar was lower on Thursday and printed a new weekly trough of 103.490 as the index continued to slip in the tail-end of the US session as sentiment improved. Nonetheless, the Dollar began to slide after a sharp downgrade to Q1 Unit Labor Costs that boosted USTs, though DXY was already fading following reports via Punchbowl that Senate Minority Whip Thune heard at least a dozen GOP offices are seeking amendment votes to the debt ceiling bill passed by the House, and some Democrats also indicating an interest in changes. Further on the data front, manufacturing ISM missed consensus marginally, but came with a bigger than forecast downturn in prices paid and weaker new orders, while employment stayed firm. On the labour front, jobless claims were more-or-less inline but ADP was strong ahead of NFP on Friday. Lastly, Harker (voter) noted the Fed is close to the point where it can hold interest rates in place (a pause?) and is closely monitoring data to assess whether additional policy tightening will be needed. Later he added he believes the Fed should "at least" skip rates in June.

Activity currencies (AUD, CAD, NZD, GBP) were all firmer to varying degrees on account of risk-on sentiment and broad Dollar weakness amid heightened expectations of a Fed pause at the June meeting. The Pound saw strength to see Cable top 1.2500 to highs of 1.2539, while USD/CAD hit a low of 1.3437 with the gains in the crude complex also supporting the Loonie. Note, this came even as Canadian S&P Global Manufacturing for May dipped back beneath 50. Aussie was the G10 outperformer to see the cross top out at 0.6581, which saw tailwinds from firmer commodities, an improved Australian CapEx metric, and follow-through from a decent Chinese Caixin PMI metric. Lastly, the Kiwi passed through 0.6000 and 0.6050 to a peak of 0.6077 awaiting independent direction from NZ terms of trade, import and export prices for Q1.

EUR, CHF, and JPY all saw gains against the Greenback, in that order of strength, with the Yen breaching 138.50 vs. lows of 139.94 amid little currency-related but on general sentiment and the aforementioned Dollar pullback. Euro breached psychological resistance and a big option expiry at the 1.0700 strike in wake of mixed Eurozone data and manufacturing PMIs. EUR/USD may have garnered some impetus from ECB President Lagarde repeating that inflation is too high and is set to remain so for too long, adding we will keep moving forward – determined and undeterred – until we see it returning to our 2% medium-term target in a timely manner, rather than Kazaks effectively agreeing with peak market pricing or minutes that were stale by nature. Elsewhere, the Franc traded between a 0.9054-0.9115 range as the Swiss trade surplus shrank and manufacturing PMI contracted more than feared.

Scandis gained with the SEK slightly outperforming its NOK counterpart as they saw a recovery due to the upside seen in the crude complex compensating for Norway's manufacturing PMI losing 50.0+ status, and the faster contraction in the Swedish equivalent.

EMFX predominantly saw gains against the Buck with the TRY, flat, residing as the underperformer. CLP was aided by the strength in copper, although IMACEC economic activity for April, a proxy used for GDP, fell 1.1% Y/Y beneath the expected -0.5%. As such, Pantheon Macroeconomics note the Chilean economy remains under severe pressure, but still believes that growth will gather strength gradually in the coming quarters, thanks to falling inflation, lower interest rates, and improving conditions for key exports. CNH eventually rallied on the wavering Buck after floundering in the European morning after little support for the Caixin PMI. CZK firmed up as the CNB lowered its countercyclical buffer for banks by 25bps to 2.25%, citing the economy in a downward phase of the financial cycle and the MXN took on board Banxico minutes confirming guidance that it is considered necessary to maintain the reference rate at its current level for an extended period of time.

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