newsquawk

US Market Wrap

29th June 2023: Cyclicals prosper and yields soar after solid US data

- **SNAPSHOT**: Equities mixed, Treasuries down, Crude up, Dollar up.
- **REAR VIEW**: Jobless claims reverse lower; Strong upward revisions to Q1 GDP; Spanish and German inflation contrasts softer Italian metrics; Bostic reiterates no need for further hikes; Deeper fall in nat gas inventories than expected; Banks fly through Fed stress tests; MU numbers impress but profit view weak with concerning China guidance.
- **COMING UP**: **Data**: Tokyo CPI, China NBS PMI, Germany Retail Sales, France CPI (Prelim), EU CPI (Flash), US PCE **Speakers**: Riksbank's Bremen & Thedeen **Supply**: Italy.

MARKET WRAP

Equity trade was mixed Thursday with a cyclical/value bias on chunky upward revisions to Q1 US GDP and the sudden move back lower in weekly initial jobless claims. The strong economic data saw the real-economy levered Russell 2k index outperform the benchmark SPX and NDX indices. Financials, Basic Materials, Industrials, and Energy were top-performing sectors, while Comms, Consumer Staples, and Tech all underperformed. The pullback in near-term recession risk saw massive front-end led Treasury selling (2yr yield up over 15bps) with Fed pricing edging further towards the Dot Plot-implied two more 25bp hikes, albeit still not quite there. The move higher in real yields - specifically the US 5yr TIP testing above 2% for the first time since October last year - saw Gold prices tumble beneath USD 1900 /oz for the first time since mid-March, although later reclaimed the round figure. In FX, The Dollar was firmer with particular strength vs funders (Euro, Swissy, and Yen) while G10 activity currencies faired relatively better - note sudden strength in Yen earlier on in the absence of fresh catalysts saw speculation of BoJ intervention ramp up. In commodities, oil was modestly firmer in choppy/tight ranges while nat gas saw more pronounced gains after the deeper fall in inventories than expected.

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JOBLESS CLAIMS: Initial jobless claims reversed lower to 239k (exp. 265k, prev. 264k), after three consecutive prints above 260k, as the metrics are a reminder that labour markets are still quite tight, keeping a hike next month at the FOMC on the table and with it the risks of another hike later in the year. In wake of the data, Fed pricing lifted to a circa 84% chance of a 25bps hike from ~78%. Looking at the largest state contributors to the fall, California and Texas saw the largest drop in non-seasonally-adjusted claims, with declines of 10k and 9k, respectively. Note that seasonal adjustment factors added c. 7k to the headline decline, with Oxford Economics noting that seasonal factors will exert a downward impact on claims for the next three weeks, as those factors anticipate a variety of seasonal layoffs. The consultancy says, "those layoffs could include some autoworkers on temporary layoff as plants close to retool for new models, although those layoffs are far less concentrated in the summer than they were many years ago." Meanwhile, continued claims dropped to 1.742mln from 1.759mln, and beneath the expected 1.765mln. Overall, Oxford Economics still expects jobless claims to rise later in the year as the economy weakens and falls into a recession. The consultancy concludes, “given our forecast for the recession to be mild, along with the difficulties employers have faced hiring workers following the pandemic, we expect job losses in this recession will be relatively small compared to prior recessions.”

GDP: The final Q1 GDP number was revised up to 2.0% from 1.3%, well above expectations for a rise to 1.4%. The report noted that the updated estimates primarily reflected upward revisions to exports and consumer spending that were partly offset by downward revisions to nonresidential fixed investment and federal government spending. Imports, which are a subtraction in the calculation of GDP, were revised down. The GDP sales metric was revised up to 4.2% from 3.4%, above expectations of 3.5% while the deflator was unchanged at 4.1%, shy of the 4.2% expected. Consumer spending was hiked up to 4.2% from 3.8%. The final PCE prices for Q1 cooled to 4.1% from 4.2%, despite expectations for it being unrevised. Looking ahead, analysts at Oxford Economics expect weaker performance in H2 23 as higher interest rates and tighter credit conditions weigh on consumers and businesses. OxEco adds, "Given the current state of the economy, a recession is unlikely to start in Q3. We still think that a recession is more likely than not, though a "soft landing" cannot be entirely ruled out."

PENDING HOME SALES: US pending home sales in May fell 2.7%, deeper than the expected fall of 0.5% and marking the third consecutive decline for the index. There's nothing all that surprising in the decline given the known difficulties in the existing homes market with homeowners reluctant to sell their houses given mortgage rates at elevated levels. The index is now near its October 2022 lows with mortgage rates approaching the peaks (c. 7%) they were at back then.

FIXED INCOME

T-NOTE (U3) FUTURES SETTLED 1 POINT & 4 TICKS LOWER AT 112-04

Treasuries saw massive bear-flattening after a jerk lower in initial jobless claims and strong upward revisions to Q1 GDP. 2s +15.4bps at 4.876%, 3s +16.4bps at 4.501%, 5s +17.1bps at 4.143%, 7s +16.5bps at 3.997%, 10s +14.0bps at 3.852%, 20s +12.1bps at 4.118%, 30s +10.8bps at 3.912% .

INFLATION BREAKEVENS: 5yr BEI +3.9bps at 2.188%, 10yr BEI +3.1bps at 2.234%, 30yr BEI +3.0bps at 2.236%.

THE DAY: Treasuries drifted gradually lower through the APAC session on Thursday and T-Notes ultimately hit interim support at 112-27 later in the European morning. There were little fresh catalysts in APAC but do note the latest Japanese MoF data saw buying of foreign bonds dry up in the latest week, which if sustained could serve as an omen for the early July Treasury auctions. While in Europe, all the focus was on the inflation data with Spanish CPI coming in soft but the more widely followed German data saw an unwelcome rise in the regional figures. That only managed to sustained the trundle lower in USTs, rather than sharply accelerate it. There was muted reaction to the nationwide German inflation figures coming in on the upside, as the regionals suggested, with contracts hovering near lows into the US data on minimal activity - typically dovish remarks from Fed's Bostic had little sway either.

The whole Treasury curve knee-jerked lower after the consumer- and export-led upward revisions to the final Q1 US GDP data but perhaps more crucially, the surprise drop lower in weekly initial jobless claims to 239k from 264k massively undermined the narrative through June that we had entered a new regime of higher claims. T-Notes fell from 112-28+ to 112-15 in five minutes, with 130k TY traded in that 5m post payrolls window, that's vs comparable prior 3 weeks' post-IJC 5m volumes of 44k, 53k, and 85k. Contracts troughed at 112-01 an hour and a half later. As one would expect, flattener flows dominated in wake of the data, highlighted by a block 67.2k Dec'23 SOFR sold vs 36.7k 5yr futs bought (DV01 $1.6mln). Contracts across the whole curve hovered near lows right through the rest of the session in the absence of anything new to dig into.

FED PRICING currently sees an 84% implied probability of a 25bp hike at the July 26th FOMC from 78% before, with the terminal rate implied at 5.43% for the November meeting vs 5.36% beforehand, still not fully pricing in two more hikes as the Dots suggest.

FRIDAY: *Japanese Tokyo CPI (Jun),* ***Chinese NBS PMIs (Jun)****, German Unemployment (Jun),* ***EZ Flash CPI (Jun), US PCE (May)****, US Chicago PMI (Jun), and Uni. of Michigan Final (Jun)*.

STIRS:

- SR3U3 -5bps at 94.585, Z3 -12bps at 94.605, H4 -16.5bps at 94.865, M4 -19bps at 95.25, U4 -20.5bps at 95.665, Z4 -20.5bps at 96.015, H5 -20.5bps at 96.25, M5 -20.5bps at 96.39, U5 -19.5bps at 96.48, U6 -16.5bps at 96.67.
- SOFR fixing rises to 5.06% as of June 28th from 5.05%, volumes rise to USD 1.499tln from 1.481tln. NY Fed RRP Op demand at USD 1.935tln (prev. 1.945tln) across 102 counterparties (prev. 101)
- The USD 10bln fall in RRP usage is dwarfed by the USD 71bln T-bill settlement Thursday, which raises the possibility that this latest round of T-bill purchases has come mainly from bank reserves rather than the RRP.
- EFFR flat at 5.07% as of June 28th, volumes rise to USD 140bln from 132bln.
- US sold USD 71bln of 4-week bills at 5.085%, covered 2.53x; sold USD 61bln of 8-week bills at 5.190%, covered 2.61x.
- US left next Monday's 6-week, 13-week, and 26-week bill sizes all unchanged - USD 50bln, 65bln, and 58bln, respectively - with all three to settle next Thursday.

CRUDE

WTI (Q3) SETTLED USD 0.30 HIGHER AT 69.86/BBL; BRENT (U3) SETTLED USD 0.27 HIGHER AT 74.51/BBL

The crude complex settled marginally firmer in a choppy session, albeit in thin ranges, as markets continue to consider fears of rising interest rates in the wake of strong US data. US GDP final was revised much higher to 2.0% (exp. 1.4%, prev. 1.3%) while initial jobless claims reversed lower to 239k (exp. 265k, prev. 264k), after three consecutive prints above 260k, as the metrics are a reminder that labour markets are still quite tight, keeping further Fed hikes on the table. The strong data saw strength build for oil prices despite the firmer Dollar, with WTI and Brent going on to peak at USD 70.60/bbl and 74.98/bbl, respectively, before reversing to session lows of USD 68.93/bbl and 73.39 /bbl as Europe closed up shop. Prices recover into the black in the NY afternoon. Prior to the US data, WTI and Brent were modestly firmer in the European morning after a horizontal APAC session. Complex specific newsflow was sparse otherwise with the highlight being oil loading from Russia's Western Ports set to fall 18% in July M/M, according to Reuters calculations citing sources. Looking ahead, market participants await May Core PCE and Baker Hughes data on Friday.

NAT GAS: US nat gas futures rallied in wake of a smaller-than-expected weekly storage build accompanied by forecasts for increased demand over the coming two weeks than previously expected.

EQUITIES

CLOSES: SPX +0.45% at 4,396, NDX -0.16% at 14,939, DJIA +0.80% at 34,122, RUT +1.23% at 1,881.

SECTORS: Financials +1.67%, Materials +1.27%, Energy +1.11%, Industrials +0.94%, Real Estate +0.87%, Health +0.65%, Technology +0.13%, Consumer Discretionary +0.06%, Utilities -0.05%, Consumer Staples -0.15%, Communication Services -0.63%.

EUROPEAN CLOSES: Euro Stoxx 50 +0.23% at 4,354, FTSE 100 -0.38% at 7,471, DAX 40 -0.01% at 15,946, CAC 40 +0.36% at 7,312, FTSE MIB +1.05% at 27,928, IBEX 35 +0.31% at 9,510, SMI -0.11% at 11,171.

STOCK SPECIFICS: **Micron (MU)** Q3 numbers topped expectations, driven by AI sector demand and improved supply conditions in PC and smartphone markets. However, Q4 profit view disappointed and said recent Cyberspace Administration of China decisions is a significant headwind that is impacting the outlook and slowing recovery adding the ruling could affect half of the China-based customer revenue. Banks (**WFC, JPM, BAC, CFG, MS** etc) moved higher, higher after passing the Fed’s stress test. Tests revealed that large banks were resilient and capable of lending during severe recessions, with all 23 banks tested exceeding their minimum capital requirements. Separately in the banking sector, **Morgan Stanley (MS)** board is to discuss the CEO succession at the board meetings in July, September, and October, according to Reuters sources. Berkshire Hathaway purchased another 2.14mln more shares of **Occidental Petroleum (OXY)** bringing its total ownership to ~25%. Citi raised **Netflix (NFLX)** PT to USD 500 (prev. 400) and keeps a Buy rating on the shares; firm is more bullish on the likely success of its ad-tier. **Salesforce (CRM)** will invest USD 4bln in its UK business in the next five years. CRM said it was experiencing rapid growth in Britain as companies invest in their digital transformations and AI. **Disney (DIS)** downgraded at KeyBanc; said expectations "appear high" and its direct-to consumer subscriber growth has stalled. **BioXcel Therapeutics (BTAI)** said its experimental drug to treat agitation related to Alzheimer's disease met the main goal in a late-stage study, but the results were marred by concerns over data integrity at one of the trial sites. **FREYR Battery (FREY)** upgraded at MS; believes the co. can show meaningful progress on commercial milestones. **Joby Aviation (JOBY)** announced a USD 100mln equity investment from SK Telecom, expanding an existing partnership. Note, on Wednesday JOBY surged 40% it received a permit to begin flight testing its first electric vehicle takeoff and landing vehicle. **Eli Lilly (LLY)** is to acquire **Sigilon Therapeutics (SGTX)** for USD 14.92/shr in cash. Note, SGTX closed Wednesday at USD 3.93/shr.

US FX WRAP

The Dollar was firmer on Thursday and the DXY printed a high of 103.440, as the upward revision to final Q1 US GDP and jobless claims falling well beneath the recent 260k area gave the Buck a big boost. The sharp rebound in the Greenback retraced any of the downside that might have been attributed to Fed’s Bostic who repeated his preference for a pause rather than skip or every other meeting pace of tightening. On that note, the line from Chair Powell (strong majority of policymakers see two ‘or more’ rate rises by the end of 2023) could have carried more weight even before the latest macro releases that nudged market pricing closer to done and dusted in terms of a 25bps hike at the July FOMC. Looking ahead, there is the pivotal core PCE on Friday, accompanied by June final UoM for the last trading session of the month and with trade thinning into the holiday-thinned start to next week.

Euro was the G10 underperformer as EUR/USD hit a trough of 1.0861 after the aforementioned US data favoured further rate hikes, reversing from the cross’ earlier peak of 1.0941. On the European data footing, Spanish and German inflation contrasted with Wednesday’s softer than Italian metrics, but there were base effects in Germany that are seen as a one-off. There is a slew of European data on Friday, with flash EZ HICP (Jun), EU Unemployment rate (May), and German Unemployment rate (Jun) all due.

Antipodeans were mixed, as NZD was lower, but AUD saw notable gains and henceforth was the clear outperformer. For the Aussie watchers, it seems somewhat odd and perhaps too simplistic to suggest that a significant upgrade to final retail sales was sufficient to keep the Aussie afloat on the 0.6600 handle against its US peer, but AUD/USD was also underpinned by AUD/NZD tailwinds and a couple of banks maintaining views that the RBA will still tighten rates again next week, and possibly in August as well. Meanwhile, NZD/AUD reversed from 0.6102 to worst levels of 0.6051 as the Dollar saw an influx of buying.

Loonie, which was flat, saw slight tailwinds from the crude complex with little CAD-specific newsflow, highlighted by USD /CAD hitting a low and high of 1.340 and 1.3285, respectively, on the eve of Canadian GDP and the Q2 business outlook for future sales.

Cable, which closes modestly softer, dipped to a trough of 1.2592, albeit only briefly residing beneath the key 1.2600 level as the Dollar bid as opposed to anything Pound related. Despite saying this, outgoing BoE dove Tenreyro said her vote to leave the bank rate unchanged at the meeting rested on what the latest data implied about the medium term - she gave a string of typically dovish, and overlooked, remarks through the session.

Yen was eventually weaker but that tells half of the story. In the European morning sudden strength was seen in JPY with no notable headlines to drive price action but with participants cognizant of Japanese MoF presence. USD/JPY fell from c. 144.50 to 144.15, however, the hot US economic data (revision up to GDP, fall in jobless claims) which saw a move higher in UST yields saw USD/JPY hit a fresh high of 144.72. There was no official confirmation of Japanese intervention, officials said they have no comment on the matter, but they are mindful of the one-sided moves. Post-this, BoJ Deputy Governor Himino noted recent rises in Japan's consumer inflation are much more modest than in the US and Europe, but stronger than previously expected. He added the BoJ must guide policy flexibly, but the best approach is to maintain ultra-easy monpol.

Scandis were weaker, with the SEK underperforming its counterpart as the NOK may have been slightly aided by crude prices. Riksbank hiked by 25bps, in line with expectations, but disappointing those who had looked for a 50bp move. This saw EUR/SEK rise higher, but the overall reaction was a choppy one. EUR/SEK had then reversed somewhat on the central bank providing a higher rate path, while it also noted a weak SEK is contributing to keeping inflation high and they are considering hedging part of the foreign exchange reserves.

EMFX was almost exclusively in the red vs the Dollar with the flat TRY the outperformer. CLP was hindered by falling copper prices, while others were just weighed on by the broader market sentiment. The Yuan was weaker. Overnight the PBoC set the USD/CNY midpoint at 7.2208 (exp. 7.2540, prev. 7.2101), and with the firmer than-expected fixing and reports via Reuters sources that Chinese state banks have been spotted selling USD in onshore currency markets at around the 7.25 mark, saw USD/CNY close lower, but once US trading got underway USD/CNH rose after a Dollar rally following more hot economic data.