US Market Wrap

August 3rd 2023: Bond rot continues as rates vol spikes and Dollar struggles into NFP

- **SNAPSHOT**: Equities down, Treasuries down, Crude up, Dollar flat.
- **REAR VIEW**: US ISM Services PMI disappoints; US Jobless Claims inline; US Unit Costs ease, Productivity rises; BoE hike 25bps; Saudi to extend voluntary 1mln BPD cut; Unscheduled BoJ bond buy; QCOM sales and guidance miss; Ackman short US 30yr.
- **COMING UP**: **Data**: EZ Retail Sales, US NFP, Canadian Unemployment **Speakers**: BoE's Pill **Earnings**: Credit Agricole, Commerzbank, Maersk & Berkshire Hathaway.

MARKET WRAP

Stocks were ultimately just slightly lower on Thursday where indices recovered into the NY afternoon as the acute Treasury bear-steepening lost momentum. On which, the spike in yields, particularly at the back-end, appears to be driven by continued concerns over the ramped Treasury supply calendar announced this week but also some force selling concerns given Fitch's downgrade earlier in the week - Bill Ackman announcing he was short in size late on Wednesday was the cherry on the cake. In FX, the DXY was ultimately flat with risk currencies paring losses as stocks recovered through the US session, while havens Yen and Swissy outperformed; note that Sterling was flat where the currency failed to extend a sell-off despite the BoE's downgrade to a slower 25bp hike. Maybe there is something to be said, from a stability perspective, for the lack of material Dollar appreciation despite the c. 15bp spike in bond yields, which has also coincided with a spike in implied Treasury vol. Meanwhile, oil prices surged back higher after Saudi announced it will be extending its 1mln BPD production cuts through September ahead of Friday's JMMC, with energy in general trading well after the heavy losses on Wednesday.

GLOBAL

BOE REVIEW: As expected, the MPC came to market with a 25bps rate hike, taking the Base Rate to 5.25% and disappointing some outside calls for a larger 50bps move. The decision to raise rates was subject to an 8-1 vote with Dhingra the lone dissenter whilst the magnitude of the rate hike was subject to hawkish dissent from Mann and Haskel who backed a 50bps increase. The decision to move on rates was backed by the consensus view that although recent data outturns had been mixed, some key indicators, notably wage growth, had surprised significantly on the upside. In the accompanying statement, the MPC reiterated that "if there were to be evidence of more persistent pressures, then further tightening ... will be required"; it is worth noting that the MPC judges current policy as restrictive. Moving forward, Bailey stated that the MPC needs to make absolutely sure that inflation falls all the way back to 2%. The forecasts embedded in the accompanying MPR saw the 2023 inflation projection held at 5% whilst the two-year forecast was revised higher to 1.5% from 1.0% but ultimately still seen below target and therefore indicative that the MPC judges the current rate path to be tighter than required to return inflation back to mandated levels. From a growth perspective, GDP is seen at 0.5% per annum from 2023-2025. In the follow-up press conference, Bailey cautioned that continued strength in services prices may suggest high inflation will persist, adding that upside surprises on wage inflation suggest that it will take longer for second-round effects to fade. Bailey refused to get drawn into hypothesizing what will happen next for the Bank Rate and stressed the Bank's data dependency, however, he did note that there is more than one path for rates that would deliver inflation back to target. On the balance sheet, Deputy Governor Ramsden said that the MPC will make a decision on QT in September, however, he personally can see the case for slightly increasing the pace. Overall, the choppy price action in the aftermath of the announcement suggested that there was "something for everyone" in the release, or at least, there is uncertainty over what is to come in the coming months. That said, markets have seen a mild dovish repricing with the terminal now seen at circa 5.7% vs. 5.57% pre-release, likely as a result of the MPC now judging policy to be restrictive. In terms of desk views, ING suggests a "hike in September seems likely, but by November we think the news on services inflation and wage growth should be looking a little better".

US ISM SERVICES: ISM Services in July remained in expansionary territory for the seventh straight month but fell to 52.7 from 53.9, short of the expected 53.0. The internals were also disappointing as business activity and new orders fell to 57.1 (prev. 59.2) and 55.0 (prev. 55.5), respectively, in addition to employment declining to 50.7 (prev. 53.1) ahead of the payrolls report on Friday. However, the inflationary gauge of prices paid eerily lifted to 56.8 from 54.1. Within the release it added that the majority of respondents are cautiously optimistic about business conditions and the overall economy. Overall, ING noted, the ISM activity indicators suggest that manufacturing is in recession and service sector output is becoming a little more sluggish. The publication added, “in the near term their employment components indicate the likelihood of slowing hiring while the tightening of lending conditions and higher market interest rates indicate the threat of a major slowdown can't be ignored”.

US JOBLESS CLAIMS: The jobless claims data was in line with estimates at 227k, with forecasts ranging between 210-240k, and rising from the prior 221k. Note, the seasonal factors had expected a decrease of 13,895 from the prior week, with the unadjusted claims at 205, -8.5k from the prior week. Looking at each state, the greatest fall in claims were in Ohio (-2,958), California (-2,386), and Georgia (-1,593), while the largest increases were seen in Missouri (+2,458), Illinois (+657) and New Jersey (+598). The 4wk average of initial claims fell to 228k from 234k. Initial Jobless Claims were also in line with analyst expectations at 1.7mln, with analyst forecasts ranging between 1.68 and 1.725mln. It is worth noting neither of these metrics coincide with the usual survey period of Friday's NFP report and this release will do little to alter Fed thinking. With claims around this level, it is not one to suggest an imminent recession, however analysts at Oxford Economics suggest the data is consistent with labour market conditions that are probably too tight for the Fed. The consultancy also expects claims will rise later in the year as the economy falls into a mild recession, but they expect the rise in claims to be modest compared to prior downturns.

FED: **Fed's Barkin (2024 voter)** noted inflation remains too high but last month's inflation reading was a good one and hopes it is a sign. He stressed the Fed's objective is not to cause a recession but to reduce inflation. He also suggested that if a recession were to occur, it might be less severe and cause less labour market dislocation, but warned a further economic slowdown is almost surely on the horizon. Barkin added that consumer spending, while weaker, is far from weak. Barkin, on a soft landing, said there is still a plausible story that inflation normalizes in short order and the economy dodges additional trauma. On lags, he noted that rate increases work with a lag and that many models estimate their impact should start to really hit around now. He also warned that what we learned in the ’70s, is that if you don’t get inflation under control, it comes back even stronger.

NFP PREVIEW: The rate of payroll growth is expected to slow in July, while measures of wage growth are seen cooling further. Analyst whisper numbers and gauges of the US labour market strength are supportive of a decent reading: ADP’s gauge of payrolls surprised to the upside once again, though many analysts dismiss the data series as a reliable forecaster for the NFP data; weekly claims data has trended lower relative to the June survey week; PMI surveys allude to healthy labour market conditions, and consumers have confidence in the outlook for the labour market. And tracking estimates are also above what the consensus predicts. Ahead, payroll additions are expected to ease further, but Fedwatchers still suggest that a print in July that is in line with the consensus would still likely keep the prospect of another FOMC rate rise in play. To download the full Newsquawk preview, please click here.

FIXED INCOME

T-NOTE (U3) FUTURES SETTLED 18 TICKS LOWER AT 110-07+

Treasuries saw further bear-steepening on overhanging Fitch and supply fears with vol buying accelerating. 2s +0.5bps at 4.896%, 3s +3.2bps at 4.591%, 5s +6.1bps at 4.302%, 7s +8.9bps at 4.261%, 10s +11.5bps at 4.194%, 20s +13.5bps at 4.494%, 30s +14.3bps at 4.308%.

INFLATION BREAKEVENS: 5yr BEI -0.4bps at 2.369%, 10yr BEI +0.6bps at 2.369%, 30yr BEI +1.3bps at 2.332%.

THE DAY: After recovering somewhat during the NY afternoon on Wednesday to resistance at 110-28+, T-Notes began drifting lower again during the APAC session on Thursday with continued supply pressures. Some of the weakness was JGB-led as yields in Japan continue to edge higher, which ignited another unscheduled BoJ buying operation. There also remain some concerns over UST demand from those mandated with AAA after Fitch's downgrade. The bearishness was accentuated by Hedge Fund manager Bill Ackman announcing Wednesday that he is short the US 30yr "in size". China's Caixin Services PMI coming in hot could only have helped the govvie selling.

The continuous, gradual selling saw T-Notes find initial troughs at 110-09+ in the London morning, with contracts hovering near lows into the NY handover. Data in Europe saw mixed Services PMI in Europe with no massive shocks in either way. While the BoE's 25bp hike saw two-way action but nothing much for Treasuries in the context of their large ranges.

Fed's Barkin (nv) spoke ahead of the 08:30ET data, but added nothing incremental to the Fed debate. Initial jobless claims rose to 227 from 221k as expected, while Q2 productivity rose more than expected and unit labour costs slowed more than expected, with USTs seeing two-way action in the immediate aftermath, before further downside was seen, led by the long-end again and coinciding with a slew of put activity ahead of the ISM Services data, seeing T-Notes hit session lows of 110-05+, just off the early July lows of 110-05.

The miss on ISM Services didn't garner much immediate reaction but was soon followed by some chunky block steepeners, including 27.5k ZF/5.4k UB (5s30s), with the belly recovering into the NY afternoon and the long-end continuing to trade weakest. There was notable vol buying too, with implied vol having surged higher amid the latest bear-steepening, unsettling markets. Attention now hones in on Friday's payrolls report.

STIRS:

- SR3U3 -0.5bps at 94.59, Z3 -2bps at 94.62, H4 -2bps at 94.855, M4 -1.5bps at 95.19, U4 -1.5bps at 95.555, Z4 -2.5bps at 95.865, H5 -4bps at 96.095, M5 -6bps at 96.24, U5 -8bps at 96.30, U6 -10.5bps at 96.38, U7 -12bps at 96.32.
- SOFR falls to at 5.30% from 5.31% as of August 2nd, volumes fall to USD 1.416tln from 1.495tln.
- NY Fed RRP op demand rises to USD 1.777tln from 1.770tln, across 105 counterparties (prev. 101).
- EFFR flat at 5.33% as of August 2nd, volumes fall to USD 105bln from 108bln.
- US sold USD 71bln of 1-month bills at 5.275%, covered 2.80x; sold USD 61bln of 2-month bills at 5.285%, covered 2.77x.
- US raised its 16-, 13-, 26-, and 52-week bills by USD 5bln, 2bln, 2bln, and 2bln, respectively, to USD 67bln, 60bln, 40bln, and 55bln; 13- and 26-week auctioned on Aug 7th, 6-week and 52-week on Aug 8th; all to settle on Aug 10th.

FRIDAY: US Jobs Report (Jul), RBA SoMP, EZ Retail Sales (Jun), Canadian Jobs Report (Jul).

CRUDE

WTI (U3) SETTLED USD 2.06 HIGHER AT 81.55/BBL; BRENT (V3) SETTLED USD 1.94 HIGHER AT 85.14/BBL

Oil prices bounced back on Thursday as Saudi announced extended production cuts and the Dollar pared some strength. Sentiment in oil - and broader commodities - had hit a real snag after Wednesday's chunky selling with the refusal to sustain a bid on the massive 17mln bbl crude draw emboldening bears to see crude futures post their largest D/D loss since June, breaking the one-way traffic higher seen through July. Prices even began to extend lower on Thursday with WTI (U3) and Brent (V3) futures hitting lows of USD 78.69/bbl and 82.36/bbl, respectively. But the facts changed after Saudi came out and affirmed an extension of its production cuts with the potential to deepen them (more below), seeing prices rebound higher in the NY morning. There was some consolidation as the dust settled, but heading into the NY afternoon, combined with the Dollar paring some strength as the UST sell-off lost momentum, crude prices extended to highs ahead of their settlement, bringing prices back into their upward channel seen through July.

OPEC+: Saudi Arabia announced it would extend its voluntary oil production cut of 1mln BPD for another month to include September, which could be extended or, crucially, "extended and deepened", suggesting the Kingdom could go even further beyond what was largely considered the floor. The extension means Saudi will be producing 9mln BPD until at least the end of September, far beneath its maximum capacity of 12mln BPD. Meanwhile, Russian Deputy PM Novak announced Russia would continue to voluntarily reduce its oil supply in September, but at a smaller export reduction of 300k BPD vs the 500k BPD cut in August. The announcements preface the JMMC meeting on Friday, which kicks off at 13:00BST/08:00EDT, click here for a full Newsquawk primer.

EQUITIES

CLOSES: SPX -0.26% at 4,502, NDX -0.11% at 13,353, DJIA -0.19% at 35,216, RUT -0.28% at 1,961.

SECTORS: Utilities -2.29%, Real Estate -1.35%, Industrials -0.61%, Materials -0.6%, Health -0.5%, Technology -0.32%, Consumer Staples -0.17%, Communication Services -0.17%, Financials +0.07%, Consumer Discretionary +0.34%, Energy +0.95%

EUROPEAN CLOSES: DAX -0.79% at 15,893, FTSE 100 -0.43% at 7,529, CAC 40 -0.72% at 7,261, Euro Stoxx 50 -0.75% at 4,304, IBEX 35 -0.23% at 9,307, FTSE MIB -0.94% at 28,703, SMI -1.08% at 11,091.

EARNINGS: **QUALCOMM (QCOM)** missed on revenue and said 2023 handset units will be down at least a high single-digit percentage due to weak macro and slower China recovery. In addition, next quarter guidance was also short at the midpoint. EPS beat. **PayPal (PYPL)** missed on margins and active customer accounts; aside from that, it beat on revenue, profit was in line with next quarter guidance pretty good. **Moderna (MRNA)** posted a shallower loss per share than expected and beat on revenue. For the FY, sees COVID-19 vaccine revenue of USD 6-8bln (exp. 6.88bln). **Albemarle (ALB)** beat on profit and raised FY guidance citing rising lithium prices and vol. Although, revenue missed.

DXC Technology (DXC) missed on the top and bottom line alongside a disappointing outlook for both next quarter and FY. **DoorDash (DASH)** posted a deeper loss per share than expected but beat on revenue. Lifted FY23 adj. EBITDA and marketplace GOV outlook. **Etsy (ETSY)** earnings beat, but next quarter guidance was light. **Qorvo (QRVO)** surpassed St. consensus on profit, revenue, gross and operating margins. Next quarter outlook was strong as the management said it expects September quarterly revenue to increase sequentially by more than 50%, “driven primarily by content gains” from Apple. **McKesson (MCK)** exceeded expectations on EPS and revenue, approved USD 6bln increase to share buyback programme and lifted quarterly dividend. Finally, it raised FY24 adj. EPS view. **Goodyear Tire (GT)** posted a surprise loss per share and missed on revenue. Exec said results were impacted by softer industry volume, ongoing effects of inflation, and storm-related interruption of operations at Tupelo. **Nutrien (NTR)** announced strategic actions expected to reduce controllable costs and enhance FCF; decided to indefinitely pause its ramp-up plans for potash production and halt work on its clean ammonia project at Geismar, Louisiana, as it grapples with falling prices. **Robinhood (HOOD)** MAUs missed but posted a surprise profit per share and beat on revenue.

STOCK SPECIFICS: Jefferies downgraded **Southwest Airlines (LUV)**; said low-cost airlines appear to be struggling relative to premium peers, citing a key revenue margin for Southwest that shrunk during Q2. **Tesla (TSLA)** US executives and India's Commerce Minister held closed-door talks on carmaker's market entry plans, according to Reuters sources. **Chenier Energy (LNG)** CFO said it plans to step up its share repurchase programme and expects cost inflation of 10% for its expansion projects. **Kroger (KR) and Albertsons (ACI)** dodged a bid from consumers for a prelim injunction to halt the USD 24.6bln merger after a judge ruled the plaintiffs lacked standing and failed to explain how the deal would affect them personally. **Roku (ROKU)** downgraded at Citi. Avid Tech (AVID) soared on Reuters source reported PE firms Symphony Technology and Francisco Partners are among bidders for the co. Teamsters are demanding **Kinder Morgan (KMI)** negotiate a fair contract with better pay. **Disney’s (DIS)** ESPN is reportedly plotting its streaming future and is seeking tie-ups with leagues and rivals, according to WSJ citing sources.

US FX WRAP

The DXY was marginally lower on Thursday with a turn around in sentiment into the NY afternoon seeing DXY fall from highs of 102.84 to lows of 102.36, with the index hovering around 102.50 heading into APAC trade. Data saw jobless claims in line with expectations on both continuing and initial claims. Meanwhile, the ISM Services PMI missed expectations for July, falling to 52.7 from 53.9 (exp. 53.0). Overall business activity also declined, while the employment component fell to 50.7, just above contractionary territory of sub-50. Alongside this, the prices paid saw an increase, a worrying sign on the margin given the indicated growth slow down. Elsewhere, US unit labour costs growth for Q2 was much cooler than expected, while productivity beat. Challenger layoffs were lower than expected. Long-end Treasury yields continued to climb with alarming velocity ahead of NFP on Friday.

The Euro was relatively flat and traded either side of 1.0950 (currently sitting just below). EUR/USD hit a low of 1.0913 twice, more or less matching the 55dma at 1.0914 before moving higher. In Europe, the PMIs pointed to further inflation pressures while trade data in Germany disappointed, a full Newsquawk EU Data Wrap is available here.

The Pound was flat vs the Dollar and weaker vs the Euro in the aftermath of the BoE which hiked by 25bps as expected where Haskell and Mann opted for a 50bp hike, but Dhingra voted to leave rates unchanged again, with the remaining in favour of the 25bp hike. It also maintained forward guidance, leaving the door open for rate hikes in the future if necessary. A full Newsquawk review is available here. On the decision itself, GBP/USD fell from 1.2660 to lows of 1.2625 as the lower 25bp hike was confirmed (there was some pricing for a larger 50bp move), although the move was swiftly pared. Market pricing currently sees a 62% probability of another 25bp hike in September taking the rate to 5.5%, a level NatWest believes to be the peak. Markets however price at a peak rate of 5.71% in March 2025, implying an 84% probability of another hike by then. The lack of downside in GBP likely reflects positioning given the strong repricing lower of UK rates, and sell-off in Sterling, heading into the meeting.

The Yen saw gains vs the Dollar with USD/JPY falling from highs of 143.89 to lows of 142.07 on the initial risk off throughout the European morning but saw a turnaround once sentiment improved as Europe left with the Yen trading off risk sentiment on Thursday. The gains in the Yen come despite another unscheduled bond buy operation from the BoJ during APAC trade, although Rabo highlights the recent actions from the BoJ are helping to clarify how far policymakers are likely to allow 10yr JGB yields to move with yields hitting 0.65% before they acted. Rabobank also note that "on the assumption that hopes remain that the BoJ can creep towards a gradual move away from extremely accommodative policy, we see the potential for USD/JPY to move back towards 138 on a 3-to-6-month view".

The Franc was initially on a softer footing following the region's CPI print which cooled from the prior reading to be in line with the market's forecast at 1.6% and below the SNB's Q3 CPI YY forecast of 1.7%. CHF later reversed course amid the risk tone and USD/CHF looks to end the US session lower in its 0.8734-98 intraday band.

Antipodeans were mixed but relatively flat with the Aussie seeing marginal gains vs the Dollar and Kiwi seeing marginal losses although downside for the high-beta currencies was cushioned by the Chinese Caixin Services PMI which topped forecasts, whilst Australia's Trade Balance printed at a slightly wider surplus than expected, although Imports and Exports both contracted. AUD/USD hit a high in the US session on the risk turnaround with the pair hitting a high of 0.6568 with technicians looking towards the 0.66 level on the upside, and the Wednesday peak of 0.6629. NZD/USD fell under 0.6100 but losses stopped short of 0.6050 at 0.6061, with levels under the half-round figure seen at 0.6048 (29th June low) and thereafter at 0.6028 (lows on both the 7th and 8th of June).

The Yuan firmed on both offshore and onshore currencies vs the Dollar following a better than expected Caixin Services PMI survey, which rose to 54.1 from 53.9, above the 52.5 forecast, albeit the composite fell to 51.9 from 52.5. Note, the PBoC also posted a firmer Yuan fixing than expected at 7.1495 (exp. 7.1933), but above the prior 7.1368. Note, the PBoC also held meetings Thursday to support the development of private firms in the country's latest stimulative-natured efforts.

EMFX was generally weaker with COP, BRL, and MXN underperforming following the BCB 50bp rate cut (more below), weighing on broader LatAm FX currencies with CLP also softer vs the buck albeit not to the same extent as its peers given a rally in copper prices. Elsewhere, in CEE the CNB maintained rates at 7.0% in a unanimous decision, noting rates will be higher than the baseline forecast scenario in the coming quarters, and noted risks to the baseline are significant and tilted to the upside. The CNB also formally ended its exchange rate intervention policy to see CZK weaker vs the Euro.

BCB: The Brazilian Central Bank opted to cut rates by 50bps, on the larger side of expectations with market pricing going into the event more or less a coin toss between a 25 or 50bp reduction. The decision was not unanimous, however, in a 5-4 vote split with Governor Neto opting for the 50bp cut. The Copom also provided guidance, noting "Committee members unanimously anticipate further reductions of the same magnitude in the next meetings, and it judges that this pace is appropriate to keep the necessary contractionary monetary policy for the disinflationary process." It is worth noting that Finance Minister Haddad had alluded to such a move ahead of the decision, noting there is room for a 50bp cut and he was certain rates would be lowered.