US Market Wrap

8th August 2023: Stocks and yields slide while Dollar rises on a slew of global risk off catalysts

- **SNAPSHOT**: Equities down, Treasuries up, Crude up, Dollar up.
- **REAR VIEW**: Dismal Chinese trade data; Harker nods to no more hikes and 2024 cuts; Moody's downgrades US regional banks; Italy announces windfall tax on banks; Major Chinese developer missed payments on Dollar bonds; Strong US 3yr auction; US trade deficit narrows; UPS cuts revenue guidance; Strong LLY earnings & lifts outlook.
- **COMING UP**: **Data**: Chinese CPI & PPI **Supply**: UK, Germany & US **Earnings**: Continental, E.ON, Bellway, Flutter & Walt Disney.

MARKET WRAP

Stocks were lower with the risk-off out of Europe and APAC accelerating at the US open, although indices pared off lows gradually into the US close. Banks were hit on both sides of the pond with Moodys' downgrade of US regionals adding to the malaise in Italian banks after Rome approved a windfall profit tax. Sentiment was already weak coming out of APAC on Tuesday after dismal China trade balance data for July and after Country Garden Holdings, a major Chinese developer, announced it had missed payments on Dollar bonds - the Yuan suffered. Treasuries bull-flattened into the US session but failed to extend in it, with the initial risk aversion accompanied by solid auctions across Japan, Germany, UK, and later in the US, where a particularly strong US 3yr auction sets off the Q3 refunding supply ahead of the 10yr and 30yr offerings on Wednesday and Thursday. The DXY was firmer, albeit off best levels, with Yen the G10 underperformer after soft Japanese wage data, while high beta currencies also suffered with broader risk sentiment. Oil prices were ultimately firmer Tuesday after initial losses post-China trade data were unwound through the US session, coinciding with some fresh Saudi jawboning, and despite the stronger Dollar - eyes to the weekly US energy inventory data. Otherwise, Wednesday appears lined up to be a quiet one ahead of the pivotal US CPI report on Thursday.

US

FED: **Harker (voter)** took a different line to Governor Bowman, who supports additional rate increases, noting that barring any "alarming" new data by mid-September, he believes "we may be at the point where we can be patient and hold rates steady". He also added that should we be at that point we can hold steady, "we will need to be there for a while... do not foresee any likely circumstance for an immediate easing of the policy rate." The Philadelphia Fed President said the latest PCE inflation report showed continued disinflation Y/Y on the headline measure and there was also promise in the core measure. He sees core PCE declining to just below 4% by the end of 2023, below 3% in 2024, and at 2% target in 2025. As the economy continues to "move along", he expects unemployment "to tick up slightly" and better align with the natural unemployment rate. He expects only a "modest slowdown" to accompany a "slow but sure disinflation". Harker sees GDP growth "slightly lower" than seen so far this year. Also sees the "US on the flight path to the soft landing we all hope for". Harker also revealed he is focused on the October 1st resumption of federal student loan repayments. He added the Fed's forecast is not that inflation might spike back up and notes supply chain issues are starting to heal, though are not "perfect". Harker added that the fiscal stimulus is burning off, noting we're going back to a more normal circumstance. He is sceptical that AI will cause a significant productivity boost. Harker later noted in a local radio interview that sometime, probably next year, the Fed will start cutting rates, warning he does not want to overdo it with Fed tightening. **Barkin (2024 voter)** noted that GDP remains solid and the labour market is remarkably resilient, adding that inflation remains too high. Barkin also highlighted that in his view, the workforce remains the number one issue for US companies and the US is still structurally short of skilled workers.

INTERNATIONAL TRADE: The trade deficit narrowed to USD 65.5bln in June from 68.3bln, but not as much as the expected 65.0bln, with most of the improvement driven by a 1.0% decline in imports, which Oxford Economics notes was the fourth monthly decline in H1 2023. Exports only fell 0.1%, albeit for a third straight month, with the consultancy adding the real trade deficit remained larger in Q2 than in Q1, corroborating the initial Q2 GDP report that showed net trade detracted from growth in the quarter. Overall, OxEco notes “weakening consumer demand for goods and retreating inventory growth by businesses have softened imports this year, while exports continue to trend downward as the global economic backdrop softens.” As such, Oxford expects depressed trade flows through the rest of 2023, and a sustained recovery in 2024 after the US exits a mild recession and external demand improves.

FIXED INCOME

T-NOTE (U3) FUTURES SETTLED 9 TICKS HIGHER AT 111-13

Treasuries bull-flattened after dismal China trade data and solid demand for global supply. 2s -0.2bps at 4.756%, 3s -2.5bps at 4.419%, 5s -4.0bps at 4.111%, 7s -4.4bps at 4.073%, 10s -5.6bps at 4.022%, 20s -5.9bps at 4.357%, 30s -5.3bps at 4.204%.

INFLATION BREAKEVENS: 5yr BEI -4.9bps at 2.373%, 10yr BEI -5.5bps at 2.362%, 30yr BEI -5.3bps at 2.326%.

THE DAY: It had been one way trade higher for duration entering the US session Tuesday with sustained bull-flattening that got going in the APAC session on the back of downbeat Chinese trade data, with exports tumbling 14.5% Y/Y in July, which was accentuated by Country Garden Holdings, a major property developer in China, missing Dollar bond payments. A solid JGB 30yr auction only supported the trend. While in Europe, the ECB's survey of consumer inflation expectations fell to their lowest since the pre-Ukraine invasion, with stock sentiment hampered, specifically in banks, after Italy's windfall tax. Supply in the region was also well received, with solid auctions for both German Bobl and UK inflation linkers.

T-Notes peaked at 111-22 at the NY handover, with the cash 10yr yield flirting beneath 4%. But a wave of corporate Dollar debt announcements coincided with some rate lock-related hedging flows (swap paying/Tsy selling) that capped further upward momentum. Meanwhile, Fed's Harker (voter) said in no uncertain terms that he expects no more Fed hikes, absent any "alarming" data, although that caused little reaction in markets with the viewpoint already implied in market pricing, and having been expressed by some other officials. There was no major US data, neither will there be on Wednesday, ahead of Thursday's CPI figures. Instead, T-Notes pared gradually from their peaks into the NY afternoon, albeit still bid on the session. The solid 3yr auction saw a fleeting bid for the front end.

3YR AUCTION: A solid USD 42bln 3yr note auction from the Treasury, where the 4.398% high yield marked a chunky 1.8bp stop-through the WI, better than the prior 0.2bp stop-through and six-auction average 0.1bp tail. The 2.90x bid /cover ratio exceeded the prior (2.88x) and average (2.69x) too. The breakdown was equally as impressive with Dealers (forced surplus buyers) left with just 10.3% (prev. 10.8%; avg. 15.8%), thanks to a big step-up in Indirects participation to 74% from 69.4%, reflective of solid end-user demand, whilst Directs took a step back in participation. Attention now focuses on the 10yr and 30yr offerings on Wednesday and Thursday, which are parts of the curve where supply indigestion concerns weigh larger.

STIRS:

- SR3U3 flat at 94.60, Z3 -0.5bps at 94.65, H4 -1bps at 94.93, M4 -0.5bps at 95.315, U4 +0.5bps at 95.735, Z4 +1.5bps at 96.075, H5 +2bps at 96.315, M5 +2.5bps at 96.465, U5 +3.5bps at 96.535, U6 +5.5bps at 96.62, U7 +6.5bps at 96.54.
- SOFR flat at 5.30% as of August 7th, volumes fall to USD 1.349tln from 1.369tln.
- NY Fed RRP op demand at USD 1.778tln (prev. 1.811tln) across 103 counterparties (prev. 102); coincides with USD 20bln T-Bill net settlement.
- EFFR flat at 5.33% as of August 4th, volumes decline to USD 106bln from 112bln.
- US sold USD 55bln of 42-day CMBs at 5.275%, covered 2.95x; sold USD 44bln of 1yr bills at 5.060%, covered 2.97x.
- US raises 4-, 8-, and 17-week bill auction sizes by USD 5bln, 5bln, and 2bln, respectively, to USD 75bln, 65bln, and 48bln; 4- and 8-week sold on Aug 10th, 17-week sold on Aug 9th; all to settle on Aug 15th.

THIS WEEK (US items bolded):

WED: **10yr auction**, Chinese Inflation (Jul). THU: **Fed's Bostic, CPI (Jul), Jobless Claims, US budget, 30yr auction**, RBI Announcement, Banxico Announcement, OPEC MOMR. FRI: **US PPI (Jul), US Uni of Michigan Prelim. Survey (Aug)**, IEA OMR, UK GDP (Jun), French/Spanish Final CPI (Jul).

REFUNDING: US to sell USD 42bln of 3yr notes (prev. 40bln) on Aug 8th, USD 38bln of 10yr notes (prev. 35bln) on Aug 9th, and USD 23bln of 30yr bonds (prev. 21bln) on Aug 10th; all to settle August 15th.

CRUDE

WTI (U3) SETTLED USD 0.98 HIGHER AT 82.92/BBL; BRENT (V3) SETTLED USD 0.83 HIGHER AT 86.17/BBL

Oil prices were ultimately firmer Tuesday after initial losses post-dismal China trade data were unwound later on amid some Saudi jawboning, that's despite the stronger Dollar. WTI and Brent futures tumbled out of APAC and through into the NY handover, catalysed by the double-digit declines in both Chinese imports and exports for July, where the futures hit lows of USD 79.90/bbl and 83.32/bbl, respectively. The recovery began around the time Saudi Arabia publicly reaffirmed its commitment to OPEC+ precautionary measures to support the stability of oil markets, albeit price action was far from spikey to the Saudi headlines. Prices recovered, and in a steady, gradual fashion, all the way into the black before settlement. Elsewhere, the August EIA STEO was released, which saw the 2023 world oil demand growth forecast left unchanged at 1.76mln BPD increase, while the 2024 forecast was cut by 30k BPD to a 1.61mln BPD increase. Otherwise, traders are now looking to the weekly US energy inventory data with the private data feed due later on Tuesday ahead of the official EIA figures on Wednesday. Current expectations (bbls): Crude +0.6mln, Gasoline flat, Distillates flat.

EQUITIES

CLOSES: SPX -0.42% at 4,499, NDX -0.87% at 15,273, DJIA -0.45% at 35,314, RUT -0.59% at 1,947.

SECTORS: Materials -1.06%, Consumer Discretionary -0.87%, Financials -0.87%, Technology -0.78%, Consumer Staples -0.66%, Industrials -0.46%, Real Estate -0.46%, Communication Services -0.24%, Energy +0.49%, Utilities +0.49%, Health +0.78%.

EUROPEAN CLOSES: DAX -1.10% at 15,775, FTSE 100 -0.36% at 7,527, CAC 40 -0.69% at 7,269, Euro Stoxx 50 -1.11% at 4,289, IBEX 35 -0.61% at 9,302, FTSE MIB -2.12% at 27,942, SMI -0.50% at 11,051.

STOCK SPECIFICS: **UPS (UPS)** missed on the top line and cut FY revenue guide, with figures impacted by labour agreements that diverted business away from the company. Note, profit beat. **Eli Lilly (LLY)** surpassed expectations on the top and bottom line alongside raising FY outlook; LLY also saw tailwinds from Novo Nordisk's obesity drug update. **Lucid (LCID)** posted a deeper loss per share than expected, missed on revenue and adj. EBITDA. Although, it is on track to achieve annual production guidance of more than 10k vehicles. **Datadog (DDOG)** revenue guidance for the next quarter and FY came in light. Note, EPS and revenue beat with profit outlook better-than-anticipated. **GlobalFoundries (GFS)** next quarter revenue guide light, but EPS and revenue beat. **International Flavors & Fragrances (IFF)** missed on the top and bottom line alongside lowering FY revenue guide with concerning macro commentary. **TransDigm (TDG)** EPS and revenue topped Wall St. expectations alongside lifting FY guidance. **Beyond Meat (BYND)** missed on revenue, lowered FY revenue guide and no longer sees positive FCF in H2. Exec noted ongoing category headwinds compressed net revenues, which impacted product sales mix and gross margins. **Chegg (CHGG)*** revenue beat while EPS marginally missed with Q3 revenue view in line. Exec noted Y/Y customer acquisition and retention rates improved and said feedback has been positive since the launch of its beta generative AI experience in May. **AMC Entertainment (AMC)** posted a surprise profit per share and surpassed expectations on revenue. Said the current quarter was off to a strong start driven by box-office hits such as "Barbie" and "Oppenheimer". **Sealed (SEE)** missed on revenue and lowered FY outlook. **Dish Network (DISH)** proposed to buy **EchoStar (SATS)** in stock-for-stock merger. **Fox (FOX)** beat on profit, with revenue inline, and authorised a USD 7bln share buyback programme.

BANKS: Ratings agency Moody's downgraded some US banks, and warned of possible cuts to others. Downgraded **M&T's (MTB), Old National (ONB), Associated Banc-Corp (ASB), BOK Financial (BOKF), Webster (WCFB), Fulton (FULT), and Pinnacle Financial Partners (PNFP)**. Also placed **Bank of New York Mellon (BK), US Bancorp (USB), Truist (TFC), State Street (STT), and Northern Trust (NTRS)** on review for downgrade. The CRA said that "many banks' Q2 results showed growing profitability pressures that will reduce their ability to generate internal capital," adding that this came "as a mild US recession is on the horizon for early 2024 and asset quality looks set to decline, with particular risks in some banks' commercial real estate portfolios." Affirmed ratings for **Ally Financial (ALLY), Fifth Third Bancorp (FITB), and Regions Financial (RF)**.

NVDA: CEO, speaking at a Keynote event, announced the new GH200 Grace Hopper super chip, with it to be in production in Q2 2024. GH200 Grace Hopper platform is "based on a new Grace Hopper Superchip with the world's first HBM3e processor - built for the era of accelerated computing and generative AI." The dual configuration delivers up to 3.5x more memory capacity and 3x more bandwidth than the current generation offering. In addition, CEO announced NVIDIA AI Workbench, a toolkit that allows developers to create, test and customise pretrained generative AI models on a PC or workstation, then scale them to virtually any data centre, public cloud or NVIDIA DGX(TM) Cloud. Finally, Nvidia and Hugging announced a partnership that will give developers of LLMs and other AI applications access to AI supercomputing.

US FX WRAP

The Dollar was firmer Tuesday in a session catalysed by risk-off trade following a couple of global updates. Firstly, ratings agency Moody's downgraded some US banks, and warned of possible cuts to others which saw the banking ETF's KRE and XLF fall 2% and 1.5%, respectively. In China, the deeper-than-expected contractions in exports and imports underscored dire demand – both domestic and foreign, whilst Country Garden Holdings, a major Chinese developer, missed Dollar bond payments. Europe added to the woes with Italian banks sold hard after the new windfall tax in the sector. Later in the US, Fed's Harker (voter) said barring any "alarming" new data by mid-September, believes "we may be at the point where we can be patient and hold rates steady", and he later added sometime, probably next year, Fed will start cutting rates. DXY printed a high of 102.800 with eyes on the July 3rd high of 102.84 ahead of the round 103.00, albeit the index pared somewhat into the US close. Looking ahead, the next clear catalyst isn't until US CPI on Thursday.

Antipodeans were the G10 underperformers with the Kiwi faring mildly worse than its counterpart. The Aussie was weighed on by the aforementioned risk-off tone and concerning Chinese data, in addition to a decline of Australian consumer sentiment and conditions overnight. AUD/USD hit a low of 0.6497, with technicians flagging June 1st low at 0.6483, then the YTD trough at 0.6456. Meanwhile, NZD/USD bottomed out at 0.6035 ahead of New Zealand inflationary forecasts and monetary conditions on Wednesday.

EUR, CAD, and GBP were all lower to varying degrees, albeit with not a great deal between them, against the Greenback due to the risk-averse trading conditions and the general Dollar bid as opposed to anything currency specific. USD/CAD traded between 1.3366-3501 but is off highs, at pixel time, as oil pared all losses and moved into firmer territory throughout the US afternoon as the Loonie followed suit. The Euro saw little reaction to the ECB June Consumer Inflation Expectations survey which downgraded the 12-month and 3-year inflation forecasts, although the data is relatively dated and the focus is very much on the next HICP print before the September policy announcement and projections. EUR/USD hit a low and high of 1.0930 and 1.1011, respectively.

CHF and **JPY** weakened with the Yen's own haven demand on China/global growth concerns offset by BoJ doubts, particularly after Japanese wage data suggested the BoJ has less scope to reduce its easy policies. USD/JPY traded between 142.41-143.49, while USD/CHF was more contained through 0.8720-82. Initially, into the US morning, the safe-haven properties helped the two haven currencies hold up better, albeit still lower vs the Buck, but as risk sentiment recovered it saw the pair retreat to worst levels.

EMFX was almost exclusively lower against the Buck with the BRL, flat, the outperformer. CLP saw weakness amid copper prices declining, while the ZAR was weighed on by spot gold dipping. The Mexican Peso watchers await Thursday's rate decision, where Banxico is seen holding rates at 11.25%.

The Yuan saw weakness following the aforementioned weak Chinese trade data, threatening China's recovery prospects and adding pressure on authorities to deploy more stimulus. To recap the latter, China's trade surplus widened to USD 80.6bln in July (exp. 70.6bln, prev. 70.6bln), with imports dropping to a rate of -12.4% Y/Y (exp. -5.0%, prev. -6.8%), reflecting weaker domestic demand, while exports fell by the largest margin since the pandemic's start, falling further to -14.5% Y/Y (exp. -12.5%, prev. -12.4%); the decline was due to lower prices rather than lower quantities. CapEco added exports could decline more before stabilising toward the end of the year, while imports might improve due to increased infrastructure spending and recovering international travel.