US Market Wrap

21st August 2023: Bonds tumble but tech stocks rally ahead of Jackson Hole

- **SNAPSHOT**: Equities mixed, Treasuries down, Crude down, Dollar flat.
- **REAR VIEW**: PBoC cut less than expected, China state banks active in FX; WSJ's Timiraos speaks on R* ahead of JH; Soft German PPI; UK clears AVGO/VMW deal; Iraq and Turkey to discuss resumption of oil exports through Ceyhan oil terminal.
- **COMING UP**: **Data**: Richmond Fed Index **Events**: Fed Discount Rate Minutes **Speakers**: Fed's Barkin, Bowman & Goolsbee **Earnings**: Royal Unibrew & Lowe's Companies Inc

MARKET WRAP

Stocks were predominantly firmer on Monday, extending Friday's post-opex recovery, with big tech leading the strength in US indices, while the small-cap Russell 2k underperformed. Nvidia (NVDA) led the charge higher (+8.5%), continuing to benefit from an endless supply of analyst PT hikes and broader momentum ahead of its earnings report on Wednesday. There was no major US data on Monday ahead of the Flash PMIs on Wednesday. Nonetheless, Treasuries resumed their downtrend amid the hawkish PBoC LPR cut and higher US neutral rate debate, ignited by a WSJ/Timiraos article on the matter over the weekend ahead of Jackson Hole, steepening the curve in the process as the cash 30yr yield approaches new peaks at 4.50%. In FX, the DXY was flat with Swissy and Euro outperforming, activity currencies flat, and the Yen seeing notable underperformance on yield differentials. Note the Yuan was in focus with the offshore trading firmer and onshore flat, where aside from the smaller than expected rate cut, traders cited by Reuters noted China's 1m offshore Yuan forward had spiked amid a liquidity squeeze. That follows separate Reuters reports during APAC that China's major state-owned banks were seen mopping up offshore Yuan liquidity on Monday. Oil prices were choppy amid US storm concerns in the Gulf of Mexico and broader risk appetite failing to prevent losses, perhaps a function of reports Iraq was in discussion with Turkey to try and resume 450k BPD exports via Ceyhan that have been halted for five months amid a legal disagreement.

FIXED INCOME

T-NOTE (U3) FUTURES SETTLE 18 TICKS LOWER AT 109-02+

Treasuries resumed their downtrend Monday with the hawkish PBoC cut and higher neutral rate debate ahead of Jackson Hole. 2s +5.4bps at 4.990%, 3s +6.0bps at 4.704%, 5s +7.3bps at 4.455%, 7s +8.2bps at 4.425%, 10s +8.5bps at 4.336%, 20s +8.8bps at 4.647%, 30s +7.2bps at 4.451%.

INFLATION BREAKEVENS: 5yr BEI +2.4bps at 2.367%, 10yr BEI +3.7bps at 2.355%, 30yr BEI +3.8bps at 2.347%.

THE DAY: T-Notes printed their session peaks of 109-22 at the globex open. Better selling developed later in the APAC morning after the PBoC cut its 1yr Loan Prime Rate less than expected and left the 5yr LPR unchanged, despite expectations for a 15bp cut. The selling extended into the European handover where contracts hit initial lows of 109-09, with the long end leading the weakness. The larger decline in German PPI than expected coincided with a partial recovery, with T-Notes running up into resistance at 109-16+ ahead of US trade.

The US' return from the weekend saw T-Notes extend to new lows, troughing at 108-31 going into the NY afternoon. Given the quiet calendar, there was a lot of attention on a weekend WSJ Timiraos article talking up the potential for higher US neutral rates, which some speculate could be a preface for Fed messaging at the Jackson Hole event (which starts Thursday), particularly given the event's title, “Structural Shifts in the Global Economy.” However, Timiraos wrote later on Monday in a tweet thread that it's unlikely that Powell believes neutral rates have moved higher. Coincidence or not, contracts did pare off lows from there into settlement.

STIRS:

- SR3U3 -1.5bps at 94.585, Z3 -3.5bps at 94.585, H4 -5bps at 94.765, M4 -6bps at 95.055, U4 -6bps at 95.405, Z4 -7bps at 95.695, H5 -7.5bps at 95.905, M5 -8bps at 96.03, U5 -8.5bps at 96.085, U6 -10bps at 96.145, U7 -10bps at 96.115.
- SOFR flat at 5.30% as of Aug 18th, volumes fall to USD 1.314tln from 1.343tln.
- NY Fed RRP op demand at USD 1.825tln (prev. 1.819tln) across 96 counterparties (prev. 98).
- EFFR flat at 5.33% as of Aug 18th, volumes rise to USD 100bln from 98bln.
- US sold USD 75bln of 3-month bills at 5.300%, covered 2.96x; sold USD 67bln of 6-month bills at 5.295%, covered 2.95x.

NEXT WEEK (US items bolded):

- TUE: **Richmond Fed Index (Aug), Existing Home Sales (Jul), Goolsbee (voter, dove)**, New Zealand Retail Sales (Q2).
- WED: **Flash PMI (Aug), New Home Sales (Jul), 2yr FRN and 20yr bond auctions**, EZ & UK Flash PMIs (Aug), Canadian Retail Sales (Jun).
- THU: **Fed's Jackson Hole Symposium (24-26th Aug), Durable Goods (Jul), Chicago Fed NAI (Jul), Jobless Claims, KC Fed index (Aug), 30yr TIPS auction**, CBRT Announcement, BoI Announcement, BoK Announcement.
- FRI: **Fed's Jackson Hole Symposium (24-26th Aug), Uni of Michigan Final (Aug**), Japan's Tokyo CPI (Aug), German Ifo Survey (Aug), German GDP Detailed (Q2).

CRUDE

WTI (V3) SETTLES USD 0.54 LOWER AT 80.12/BBL; BRENT (V3) SETTLES 0.34 LOWER AT 84.46/BBL

Oil prices were choppy on Monday amid US storm concerns, a flat Dollar, and recovering stock appetite. US production is in the limelight amid a slew of weather warnings, where the NHC announced today that potential tropical cyclone Nine is nearing Texas, which is expected to become a tropical storm before it hits the coast. Looking globally, Chinese government data on Sunday showed Russia remained China's largest crude supplier in July (+13% Y/Y) despite smaller discounts and stronger domestic Russian energy demand. Meanwhile, Reuters reported that the Iraqi oil minister has arrived in Turkey to discuss several issues, including the resumption of oil exports (450k BPD) through Ceyhan oil terminal, with flows now having been halted for five months since the arbitration ruling on March 23rd found that Ankara owes Baghdad compensation. Nat gas supply risk in Australia remains a key energy risk too, with unions at Woodside Energy's (WDS AT) North West Shelf offshore gas platforms announcing Monday plans to strike as early as September 2nd if bargaining claims are not met by Wednesday.

EQUITIES

CLOSES: SPX +0.69% at 4,400, NDX +1.65% at 14937, DJIA -0.11% at 34,464, RUT -0.18% at 1,856

SECTORS: Technology +2.26%, Consumer Discretionary +1.15%, Communication Services +0.8%, Health +0.09%, Materials +0.02%, Financials -0.09%, Industrials -0.14%, Utilities -0.6%, Energy -0.62%, Consumer Staples -0.64%, Real Estate -0.88%.

EUROPEAN CLOSES: DAX +0.19% at 15,603, FTSE 100 -0.06% at 7,258, CAC 40 +0.47% at 7,198, Euro Stoxx 50 +0.29% at 4,225, IBEX 35 -0.05% at 9,263, FTSE MIB +0.81% at 27,987, SMI +0.17% at 10,857.

STOCK SPECIFICS: **Palo Alto Networks (PANW)** beat on profit and raised FY24 EPS view. Post-earnings, PANW had its price target raised at a plethora of brokerages, such as Wells Fargo, UBS, Baird, JPM, and BofA amongst others. Note, revenue marginally missed alongside disappointing FY24 outlook. **Permian Resources (PR)** is to acquire **Earthstone Energy (ESTE)** in an all-stock transaction for USD 4.5bln, inclusive of debt. UK CMA cleared **Broadcom's (AVGO)** USD 69bln purchase of **VMWare (VMW)** following a Phase 2 investigation; added the deal does not substantially reduce competition. **Xpeng (XPEV)** was upgraded at BofA; cited an improved outlook due to its partnership with Volkswagen and improving cost structure. **Napco Security Technologies (NSSC)** disclosed that an audit found errors in financial statements from the prior three quarters. Gross profit, operating income and net income in each period were overstated. Following this, it had numerous broker downgrades. **Goldman Sachs (GS)** is reportedly exploring a sale of the investment advisory business it purchased four years ago, according to the FT. **Citigroup (C)** CEO Jane Fraser is reportedly considering a major restructuring plan to break up the bank's largest division, the Institutional Clients Group (ICG), into its primary business segments: investment and corporate banking, global markets, and transaction services, according to the FT. Alphabet's YouTube (GOOG) is working closely with music partners, including **Universal Music Group (UMG)**, to develop an AI framework. **Vaccine names (MRNA, NVAX, BNTX)** soared with new variants arising ahead of fresh vaccine roll outs during Autumn, CNBC reported. Sentinel One (S) surged on Reuters source reports that the co. is exploring a sale, however the sources add that initial expressions of interest have not met Co.'s valuation expectations.

US FX WRAP

The Dollar was flat on Monday trading within a contained range where DXY saw a low of 103.13 and a high of 103.50. The gains in the Euro offset any support from the move higher in UST yields where the 10yr took out the 2022 highs to see levels not seen since 2007. Focus on Tuesday sees commentary from Fed's Bowman, Goolsbee, and Barkin, with the Richmond Fed Mfg survey and existing home sales the data highlights. Wednesday sees Flash PMIs. Attention then looks to Jackson Hole at the tail end of this week with Fed Chair Powell due on Friday. Attention on Monday was on WSJ's Timiraos latest article from the weekend who warned the era of historically low interest rates could be over, noting higher productivity and increased deficits could raise the ‘neutral’ rate of interest, limiting Fed cuts. Some had inferred this could be a topic for Powell on Friday, albeit, Timiraos tweeted on Monday recent remarks from several Fed officials, pushing back on expectations we could get such an announcement from the Fed Chair this week.

The Euro was an outperforming currency and attempted to reclaim 1.09 but failed to hold convincingly above the level but focus will be strongly on the EZ flash PMIs on Wednesday. Note, HSBC announced they opened a buy EUR/GBP trade idea this morning, "in part built on the idea of upside for the EUR from overly dovish rate expectations for the ECB". The desk notes the headline numbers of inflation are dropping, but core inflation is stickier and higher oil prices in EUR terms could hamper the headline downswing. The German PPI data did little to budge the Euro but the figures were cooler than expected, falling 6% Y/Y and -1.1% M/M.

The Yen was the lagging currency on Monday with the advance higher in US yields weighing which took USD/JPY back above 146.00 from lows of 145.15. Note, Japanese press Kyodo reported that due to rising yields after the BoJ policy tweak, Japan's MOF has raised the assumed long-term interest rate to 1.5% in FY24/25 (prev. record low 1.1% in FY23/24), albeit this did little to stop USD/JPY grinding higher throughout the session. Meanwhile, JPM's strats said in their latest note that they believe the MoF will not intervene in the FX market at around 145 level, with the threshold level for JPY buying intervention being around 150.

Yuan (offshore) was ultimately firmer vs the Dollar. The PBoC cut its 1yr LPR rate 10bps to 3.45%, albeit this was not as much as the 15bps many were expecting, meanwhile, the 5yr LPR was left unchanged, also despite expectations for a 15bp cut. There was some choppiness in USD/CNH following the announcement but ultimately the cross was lower on the day, pressured by reports China's major state-owned banks were reportedly seen mopping up offshore Yuan liquidity on Monday, via Reuters citing sources. Reuters reported later that China's 1m offshore Yuan forward had spiked amid a liquidity squeeze.

Antipodes saw marginal gains vs the flat dollar with the Kiwi the laggard vs the Aussie after New Zealand trade figures showed a deficit of 1.1bln in July, vs the prior surplus of 9mln. New Zealand saw 5.45bln of exports, down from the 6.31bln previously, while imports rose to 6.56bln from 6.3bln, with the decline in exports and increased imports resulting in the large deficit. AUD/USD reclaimed 0.6400 while AUD/NZD still managed to keep its head above 1.08 even with the NZ trade results.

Pound saw marginal gains vs the Dollar, but was was flat vs the Euro. The August House Price data in the UK saw prices dip 1.9% in August, accelerating from the prior drop of 0.2%. The Rightmove House Price Index report noted this was the largest monthly fall for August since 2018, and was twice as steep as the typical decline during summer. Home sales were down 15% vs pre-COVID levels and the number of homes on the market are down 10% from pre-COVID levels. Recent data from the UK has been mixed, last week saw a hotter-than-expected Core CPI release, while retail sales saw a chunky miss. The unemployment rate rose, but earnings were much hotter than expected, albeit it was buoyed by the one-off NHS bonus payments. Looking ahead, analysts at Rabobank write that "If UK recession risks are judged by the market to rise, additional BoE rate rises are far less likely to be able to lend GBP support. On the assumption that the USD will be well supported in the coming months, we see risk of GBP/USD slipping to 1.26 on a 3-month view and falling to 1.20 by the middle of next year. We continue to see risks between GBP and the EUR as well balanced and expect more range trading around the EUR/GBP 0.86 area on a 1-to-3-month view." Elsewhere, HSBC notes that consumer resilience in the UK is waning which may put the extra 75bp of hikes priced in from the BoE into question, suggesting EUR/GBP could push higher on narrowing rate differentials.

EMFX was mixed. BRL saw weakness alongside TRY while ZAR, RUB, MXN and COP strengthened, but CLP was flat. On the Real, analysts at Rabo see USD/BRL at 5.05 by year-end (currently 4.97) noting they expect to see the Real and other EM currencies enjoy less gains from carry trade strategies amid global risk off. MXN was only marginally firmer but attention will turn to the Banxico minutes on Thursday for any clues about rate cuts, but current guidance is for rates to stay at current levels for some time.

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