US Market Wrap

1st September 2023: Stocks and yields rise after NFP, hawkish Mester and hot ISM

- **SNAPSHOT**: Equities up, Treasuries down, Crude up, Dollar up
- **REAR VIEW**: NFP beats but unemployment rate jumps, wages cool; Manufacturing ISM hotter than forecast; Strong construction spending; Mester downplays dovish aspects of jobs report; AVGO earnings disappoint; TSLA cuts prices in the US and China.
- **WEEK AHEAD**: Highlights include RBA and BoC rate decisions, US ISM Services PMI and China Trade Data. To download the report, please click here.
- **CENTRAL BANK WEEKLY**: Previewing RBA and BoC rate decisions; Reviewing ECB Minutes. To download the report, please click here.

MARKET WRAP

Stocks were predominantly firmer on Friday, but the cyclical Russel 2000 outperformed its peers supported by upside in regional banks, while the Nasdaq was the laggard due to higher yields and as Tesla (TSLA) tumbled following US and China price cuts. The highlight of the day was the US NFP report which saw headline come in above expectations, but the unemployment rate shot up to 3.8% from 3.5%; wages cooled, confirming the signs recently of a slowing labour market. The knee jerk dovish reaction pared shortly after, however, as Fed hawk Mester (2024) downplayed some of the more dovish aspects of the report, noting how the unemployment rate is still low and stressed a data dependent stance for future decisions. A further unwind was seen after the US ISM Manufacturing PMI results, which came in above consensus expectations, particularly in prices paid component – albeit the sector still remains in contractionary territory with readings sub-50. FOMC pricing had moved dovishly, with markets almost fully pricing in its first cut in May 2024, while the odds of another hike in November had diminished. Elsewhere, crude prices continued their ascent with participants eyeing next week's OPEC+ production cut announcement from Russia, with eyes also on Nigeria production amid looming labour strikes. In FX, the Dollar outperformed while cyclical currencies, GBP and CAD, were the underperformers. The Treasury curve eventually bear-steepened in wake of the aforementioned data and Fedspeak, perhaps with position squaring also a factor after the T-note rally seen this week and as we enter the long weekend on account of the US Labor Day.

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NFP: The NFP headline printed 187k in August, above expectations of 170k, though the prior was revised down to 157k from 187k initially reported. Meanwhile, the two month net revisions were -110k, again showing how recent data has been prone to downward revisions, and may not have been as strong as initially implied. The key figure today was the unemployment rate, which jumped to the highest level since March 2022 to 3.8% from 3.5%, despite expectations for an unchanged print, which came alongside a jump in the participation rate too, which rose to 62.8% from 62.6%, edging closer to the Fed's year-end unemployment rate forecast of 4.1% (that was pencilled in June, with the Fed set to provide updated projections in September). The rise in unemployment was also coupled with softer wages, with monthly earnings rising by 0.2%, beneath the expected 0.3% and beneath the prior 0.4%, seeing the slowest gain since Feb 2022. The annual earnings figure was 4.3% Y/Y, beneath the expectation of an unchanged pace of 4.4%. Overall, the report was judged as dovish, and in an immediate reaction, resulted in a lower implied probability of another hike from the Fed, with just 10bps of hikes priced in for November, implying a 40% probability of a hike vs 50% pre-data, while September still leans heavily towards an unchanged decision. Looking ahead, rate cuts are almost fully priced by May 2024, with a slight probability of an earlier cut in March. Overall, the data supports the views that Fed rate hikes are behind us, and it is likely to be welcomed by the Fed given they want a slowing labour market to help with their fight against inflation. However, with September largely seen as a skip, there is a lot of focus on inflation, and there is still plenty of data between now and the November meeting for the Fed to make their mind up, but the upcoming CPI report on September 13th will help cement those expectations further. It is likely the Fed will keep optionality open however, retaining their data dependent stance, but it is clear both the labour market and inflation has been slowing and expectations for more hikes are dwindling.

ISM MANUFACTURING PMI: The ISM Manufacturing PMI data rose above expectations to 47.6 (exp. 47.0) from 46.4, remaining in contractionary territory, but not as deep as July. The prices paid component saw a notable increase, rising to 48.4 from 42.6, above the 43.9 expectation, which still implies prices are falling, just at a slower rate than previously, given that the reading is still sub-50. Employment was also "strong", rising to 48.5 from 44.4, despite expectations for a decline to 44.2. New orders however declined to 46.8 from 47.3. Overall, the report alluded to a slowing decline in manufacturing, but all components still remain in contractionary territory; ING notes that this report remains consistent with a GDP slowdown, pointing out that this was the tenth consecutive month of manufacturing in contraction.

CONSTRUTCTION SPENDING: US Construction Spending was hot in July, rising 0.7% M/M, above the 0.5% expectation, while the prior was revised up to 0.6% from 0.5%. Private construction rose by 1%, while residential construction +1.4%, and non-residential +0.5%. Public construction rose 0.4%, with educational construction +0.1% and highway construction +0.6%. Oxford Economics writes that construction spending continued at a solid pace, but the drivers have shifted: "with residential spending stabilising after a year of declines, and the prior boom in factory construction levelling off." The consultancy also notes that with "spending still rising at a decent clip, overall investment growth appears to have remained solid at the beginning of the third quarter." The desk goes on to warn residential spending could see renewed pressure as a result of higher mortgage rates over the coming months, which can have a chilling effect on new construction, while a weaker labour market will also undermine home demand.

FED: Fed's Mester (non-voter, hawk), in wake of the jobs report, said the jobs market was still strong amid signs of rebalancing, acknowledging that employment growth has slowed, but at 3.8% the jobless rate is still low. She repeated that inflation remains too high, but she does see progress on lowering price pressures. Mester reiterated the main Fed debate is how restrictive policy needs to become and for how long, repeating future Fed policy decisions will be based on incoming data and that the Fed must balance risks when setting interest rate policy.

FIXED INCOME

Treasuries bear steepened after a jump in the unemployment rate and hotter than expected ISM manufacturing survey while Mester downplays dovish jobs report. At settlement, 2s +0.7bps at 4.866%, 3s +2.6bps at 4.572%, 5s +4.7bps at 4.289%, 7s +6.6bps at 4.257%, 10s +8.0bps at 4.171%, 20s +8.6bps at 4.476%, 30s +8.3bps at 4.287%

INFLATION BREAKEVENS: 5yr BEI +3.6bps at 2.313%, 10yr BEI +2.9bps at 2.272%, 30yr BEI +2.8bps at 2.265%.

THE DAY: Treasuries traded sideways overnight and through the European morning in anticipation of the NFP report which saw choppy price action. The headline beat accompanied by a downward revision and a surprise jump in the unemployment rate overall confirmed the jobs market in the US is cooling, which saw T-Notes spike to session highs with the 10yr yield just dipping beneath 4.06%, the lowest since 10th August. The move was short-lived however and gradually pared into commentary from Fed hawk Mester and the ISM Manufacturing PMI survey, which came in above consensus expectations, albeit still in contractionary territory. T-notes took a hit in wake of Mester's commentary who took out some of the dovishness of the report, exclaiming the jobs market is still strong and that the 3.8% unemployment rate is still low, whilst maintaining a data dependent stance for future decisions. Further selling pressure was seen on the jump in the manufacturing prices paid component, adding to concerns about the progress on lower goods prices. However, it is worth stressing it still remained in contractionary territory, therefore it still slowed in August, just at a slower pace than July. T-notes continued lower throughout the session where the 10yr yields hit a high of 4.2%, before paring gradually into settlement in quiet trade ahead of the labour day holiday on Monday. The overall reaction to money market pricing was a dovish one, where the NFP report saw prospects of another Fed hike diminish somewhat while rate cuts were briefly fully priced in for May 2024. The manufacturing ISM however saw this marginally unwind, with now c. 23bps of cuts priced for May, almost fully priced for the first 25bp cut, with a risk of an earlier cut in March. Attention will lie heavily on the August CPI report due September 13th, during Fed blackout, to help sway expectations, but for now, the September meeting is sure to be a skip while the Fed assesses more data ahead of November.

STIRS:

- SR3U3 +1.0bps at 94.598, Z3 +0.5bps at 94.605, H4 +0.0bps at 94.800, M4 -1.0bps at 95.105, U4 -1.5bps at 95.470, Z4 -1.5bps at 95.815, H5 -2.0bps at 96.080, M5 -3.0bps at 96.245, U5 -3.5bps at 96.330, U6 -6.5bps at 96.395, U7 -8.0bps at 96.350
- NY Fed RRP Op demand at 1.574tln (prev. 1.652tln) across 94 bidders (prev. 105).
- SOFR flat at 5.30% as of Aug 31st, volumes rise to USD 1.549tln from 1.311tln.
- EFFR flat at 5.33% as of Aug 31st, volumes fall to USD 97bln from 100bln.

CRUDE

WTI (V3) SETTLES USD 1.92 HIGHER AT 85.55/BBL; BRENT (X3) SETTLES USD 1.72 HIGHER AT 88.55/BBL

Oil prices were bid on Friday after the latest NFP report unwound some expectations for more rate hikes while there are more supply concerns after Nigeria's main labour union announced it intends to undertake strikes as eyes turn to Russia's OPEC+ cut deal announcement next week. The gains in oil came despite a stronger greenback which was seen after a hotter than expected ISM manufacturing PMI report, albeit the report still showed the manufacturing sector is slowing, just not as quickly as it was the prior month. Still, a huge jump in the prices paid was enough to keep the dollar bid, but the crude complex still trended higher. It is unclear how much impact the Nigerian strikes will have on the country's oil production, but the NNPC noted Nigeria is currently pumping 1.67mln BPD of oil and condensates, and we will look to updates to this figure as strikes take place. In Russia, the Kirshi oil refinery reportedly halted operations following an incident at a neighbouring power plant, according to Reuters sources, albeit details are light. A lot of the move is a continuation of the price action seen on Thursday after Russia announced it will unveil its new OPEC+ supply cut deal while Saudi Arabia are widely expected to extend the voluntary 1mln BPD oil production cuts into October. However, with Iran turning on the taps, the latest Bloomberg survey noted the OPEC August crude output rose 40k BPD to 27.82mln BPD, holding steady as Saudi curbs offset Iran gains. Note, the Weekly Baker Hughes Rig Count data saw drillers leave oil rigs unchanged at 512, while natgas rigs were down 1 to 114, with the total down 1 to 613.

In NatGas, Chevron (CVX) Australia and unions are meeting next week for talks in mediation in the LNG facilities dispute. However, overnight, Chevron's (CVX) Australia LNG workers rejected the Co's bargaining offer, according to unions; less than 1% of the Wheatstone and Gorgon downstream workforce voted in support of the offer, according to Reuters. Current industrial action plan could see tools downed for up to 11 hours and the halt for certain tasks from September 7th until at least the 14th.

EQUITIES

CLOSES: SPX +0.18% at 4,516, NDX -0.07% at 15,491, DJI +0.34% at 34,838, RUT +1.11% at 1,921.

SECTORS: Energy +2.06%, Materials +1.02%, Financials +0.80%, Industrials +0.51%, Health +0.23%, Technology +0.22%, Real Estate -0.07%, Utilities -0.52%, Communication Services -0.54%, Consumer Discretionary -0.54%, Consumer Staples -0.83%.

EUROPEAN CLOSES: DAX -0.67% at 15,840, FTSE 100 +0.34% at 7,464, CAC 40 -0.27% at 7,297, Euro Stoxx 50 -0.36% at 4,282, IBEX 35 -0.59% at 9,450, FTSE MIB -0.64% at 28,648, SMI -0.49% at 11,072, PSI +0.13% at 6,182.

STOCK SPECIFICS: **Dell (DELL)** beat on EPS and revenue, with breakdown revenue strong, alongside stellar guidance. Next quarter outlook topped expectations and it lifted the FY view. Following earnings, Morgan Stanley named Dell a top pick in IT hardware. **Walgreens (WBA)** CEO announced she is to step down and Ginger Graham has been appointed interim CEO, with search process to identify a permanent CEO underway. As a result, co. cuts FY23 adj. EPS view to the low end of 4-4.05 range. **Broadcom (AVGO)** posted a decent report, where profit and adj. EBITDA beat with revenue as expected while Q4 guidance more-or-less in line, disappointing some investors. **Lululemon Athletica (LULU)** beat on EPS, revenue, and comps. Q3 guidance was better-than-expected and it raised the FY revenue guide. **Elastic (ESTC)** smashed current quarter expectations in addition to providing stellar guidance. **MongoDB (MDB)** beat on EPS and revenue as management drives top-line growth; co. also posted impressive margin expansion and lifted the FY and next quarter outlook. **VMware (VMW)** beat on EPS but missed on revenue. **Chevron (CVX)** Australia and unions are to meet for mediation talks next week in LNG facilities dispute, according to Reuters citing sources. **Meta (META)** may allow Instagram and Facebook users in Europe to pay and avoid ads, according to NYT. **Humana (HUM)** sued the US government to block a policy that would allow Medicare to claw back billions of dollars in payments to insurance companies. **Amgen (AMGN)** settled with the FTC on the USD 27.8bln **Horizon (HZNP)** deal, according to Bloomberg. **Booking (BKNG)** intends to challenge the EU veto of the Etraveli deal, via Reuters citing sources. **Nio (NIO)** delivered 19,329 vehicles in August, +81% Y/Y. **Tesla (TSLA)** cut prices for the US and China Model S and X vehicles. US FTC won a key victory in its long running investigation and lawsuit over **Intuit's (INTU)** tax advertisements for its tax prep service, Turbotax, according to Politico; Intuit says it will appeal, still remains committed to free tax preparation.

WEEKLY FX WRAP

Buck rattled by NFP, but bolstered by strong manufacturing ISM

USD/CAD: The Greenback remained on track (narrowly) to break a multi-week winning streak, but after retreating in wake of a weak US jobs report it rebounded firmly on the back of a strong manufacturing ISM, with the DXY posting a new 104.240 session high from deeper 103.260 post-NFP low. To recap, headline payrolls printed at 187k in August vs 170k expected, but came with a net -110k two month back revision, a surprise rise in the unemployment rate, to 3.8% from 3.5% and softer than forecast average earnings. Conversely, the manufacturing ISM beat consensus, at 47.6, prices paid jumped to 48.4 and the employment component to 48.5 vs 47.0, 43.9 and 44.2 expected respectively. However, market pricing barely budged on the latter having already tilted closer towards 100% for no change in rates at this month's FOMC policy meeting, and the index remained some distance from w-t-d peak set on Tuesday, at 104.360, when month end rebalancing was supportive along with other bullish factors. The Dollar subsequently waned after a bigger than expected decline in JOLTS job openings and hit a low ebb (102.920 in DXY terms) when ADP missed, Q2 GDP was downgraded in the second release along with quarterly PCE prices. Pending home sales were above forecast later on Wednesday and helped the Buck bounce, while the more timely July PCE inflation data was largely a non-event given that Fed Chair Powell already spilled the numbers, albeit alluding to a firmer than actual y/y core, but a blow-out Chicago manufacturing PMI was clearly predictive. From a psychological perspective, any close above 104.000 in the index would be constructive and 104.190+ could prove really bullish as that is where the DXY signed off last Friday. Aiding its US rival's cause, the Loonie collapsed from 1.3490 towards 1.3600 and not far from the current 1.3637 weekly low in response to a shock and relatively steep Q2 annualised Canadian GDP contraction, not to mention the manufacturing PMI slipping further sub-50 to cement expectations for the BoC to remain on hold. Indeed, the spike in Usd/Cad was hardly impeded by a strength in crude prices exacerbated by Nigeria's main labour union planning warning strikes on 5th and 6th September to protest against the increasing cost of living before a total and indefinite shutdown of the nation from September 21st.

GBP/AUD/EUR/JPY/NZD/CHF: All made way for their US peer's late revival and unable to avoid being caught in the scramble that may well have been compounded by the fact that Monday is Labour Day. The Pound could feasibly have gleaned more traction from another round of comments from BoE Chief Economist Pill who reiterated that the MPC needs to be particularly wary about letting an inflation persistence dynamic set in as it has not yet seen a downturn in core inflation that would reassure us. On the flip-side, he also one option for policy is to hold rates steady for longer and he tends to favour that approach. Regardless, Cable careered from 1.2712 to 1.2595 within wider w-t-d 1.2746-1.2564 extremes. Elsewhere, the Aussie retreated through 0.6500 for a third time and lost some cohesion with the Yuan after soft monthly CPI and significantly worse than feared building approvals outweighed an upward revision to final retail sales and back the consensus for no change from the RBA. On that note, there were enough references to a deteriorating Eurozone economy from even the most hawkish ECB members and a softer than expected core CPI print to scupper the Euro via dovish repricing for this month's meeting, irrespective of hotter than forecast German and French national inflation data. Hence, Eur/Usd recoiled from 1.0881 towards the 1.0783 weekly base having made false breaks of the 100 DMA earlier in the week and topping out at 1.0945 against the backdrop of big, expansive option expiry interest. Meanwhile, the Yen continued to track UST-JGB spreads following dovish guidance from BoJ Governor Ueda at the end of Jackson Hole and other Board members thereafter with the possible exception of Tamura who personally feels that the sustained and stable achievement of the Bank's 2% inflation target is in sight. However, Usd /Jpy reversed sharply from 147.38 on Tuesday to 144.45 post-US labour data before rebounding back over 146.00, and the correction looked partly technical, positional and month end-related given little change in Japanese fundamentals. Back down under, the Kiwi failed to derive much lasting impetus from encouraging improvements in ANZ business or consumer sentiment as Nzd/Usd faded between 0.6014-0.5888 parameters, and it was a similar story for the Franc within 0.8549-0.8860 bounds in context of slightly firmer than expected Swiss y/y CPI, albeit other macro indicators were downbeat.

SCANDI/EM: No less than three Riksbank officials, including Governor Thedeen attempted to talk up the Sek, but to little avail notwithstanding Floden asserting that it is 20% undervalued. In contrast, the Nok was cushioned by buoyant Brent after the Norges Bank nudged up its daily quota of foreign currency purchases for September compared to last month, and the Cny/Cnh were boosted by numerous Chinese stimulus measures, extremely weighted PBoC reference rates, major state banks cutting depo and mortgage rates and a hefty 200 bp RRR reduction to take effect from September 15th. Turkish banks came out in support of the Try yet again and the CBRT repeated guidance for more tightening as appropriate to ensure the disinflation process gets underway by the start of 2024, but Banxico called time on the Peso's appreciation via notification that it will let its hedge book that is short Usd/Mxn roll down.