US Market Wrap

11th October 2023: Stocks and bonds rise despite hot PPI on eve of CPI

- **SNAPSHOT**: Equities up, Treasuries up, Crude down, Dollar flat.
- **REAR VIEW**: Hot PPI; Fed minutes reveal little new, many support proceeding carefully; Waller says tighter fin. conditions will do some of the work for the Fed; Putin says OPEC+ deal very likely to be extended; Weak 10yr auction; MSFT tweaks to ATVI deal are said to avoid EU probe; CMG to raise prices.
- **COMING UP**: **Data**: Japanese Corporate Goods Price, UK GDP Estimate, Services, Industrial Output, Trade Balance, US Core CPI, IJC, Cleveland Fed CPI **Events**: ECB & Banxico Minutes **Speakers**: ECB's Elderson, Panetta; Fed's Bostic, Logan & Collins **Supply**: US & Italy **Earnings**: Walgreens & Delta.

MARKET WRAP

Stocks were choppy but ultimately firmer Wednesday with weakness for both stocks and bonds in the NY morning pared into the close. The above forecast PPI numbers ignited some inflationary concerns although traders are very much waiting for the CPI figures on Thursday before reaching conclusions. The FOMC minutes also lacked any surprises. Treasuries saw pronounced flattening amid haven demand on widening Israel conflict (reports of missile exchanges between Lebanon and Israel in the London morning), but all yields closed off their lows after the hot PPI data and the weak 10yr auction. Meanwhile, Fed's Waller (voter, hawk) was the latest official to say the tightening of financial markets (higher bond yields) will do some of the work for the Fed. Elsewhere, oil futures continued to pare their Monday spike as supply risk concerns faded despite Putin touting extended OPEC action into next year; an NYT report noting Iranian leaders being surprised by the Hamas attacks added to the crude selling. The Dollar Index was flat with mild outperformance in Swissy and Sterling offset by selling of the Dollar bloc and the Yen, with the latter tracking the bounce off lows in yields. In equities, kidney dialysis and related names (DVA, BAX, FMS) were heavily sold after Novo Nordisk (NVO) announced it would end a diabetes drug trial early after interim analysis for the treatment Ozempic showed success in preventing kidney failure.

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PPI: Overall, PPI was hotter than expected. Headline PPI rose 0.5% M/M in September (prev. 0.7%), above the consensus 0.3%, with the Y/Y lifting 2.2% (prev. 2.0%, exp. 1.6%). Core metrics also surpassed expectations with M/M and Y/Y climbing 0.3% (exp. & prev. 0.2%) and 2.7% (exp. 2.3%, prev. 2.5%), respectively. Although, the supercore measure (ex-Food/Energy/Trade) Y/Y eased in September to a pace of 2.8% (prev. 2.9%). The headline was boosted by a 0.9% increase in food prices and a 3.3% jump in energy prices, where Pantheon Macroeconomics note that "neither of which is likely to be repeated this month, and the recent drop in gasoline prices alone will subtract about 0.4% from the October headline." Elsewhere, despite the persistent rise in core services, core goods prices continue to moderate and rose only 0.4% annualised throughout Q3, as goods demand continues to fall. As such, analysts add, this trend should continue over the course of the year as demand for goods falls amid slowing consumer appetites and the economy slows as tighter lending conditions dampen business activity. Overall, while Fed officials are committed to bringing down inflation and greater weight will be put on the CPI release on Thursday, elevated prices keep the risks of additional rate hikes in play but for now, markets are strongly suggesting that Fed rate hikes are over.

MINUTES: The FOMC Minutes revealed little new and were largely in line with Fed Speak. It's also worth noting that given it is an account of the September 20th meeting, there has been a notable move higher in yields since then which has seen Fed officials guide away from another Fed hike on account of the tighter financial conditions. Nonetheless, the minutes noted many participants noted data volatility and potential data revisions support the case for proceeding carefully in determining the extent of additional tightening. Meanwhile, in fitting with recent remarks, "several" noted that with the policy rate at or near peak, decisions and communications should shift to how long rates stay restrictive, vs how high they will rise. Elsewhere, and in also largely familiar commentary, they noted risks have become more two-sided but there are still upside risks to inflation, while many saw downside risks to economic activity and upside risks to the unemployment rate. The vast majority continue to judge the future path of the economy as highly uncertain. The Fed Staff report noted their economic forecast was stronger than July's projection on resilient consumer and business spending, but they assumed GDP growth for the rest of 2023 would be hampered a bit by UAW strikes with effects unwinding in 2024. Meanwhile, the Fed Staff noted going into the September meeting that yields on medium- and longer-term nominal Treasury securities rose more substantially, mainly reflecting higher term premiums and higher real yields. Note, Logan (voter) made the argument earlier in the week that if the rise in yields is due to higher term premiums, there may be less need for the Fed to raise rates, with Jefferson, Kashkari, Waller and Daly all also acknowledging the move in bond yields might have done the work for them, but some had given caveats around it, like if the move was led by strong economic growth prospects, the Fed would likely have to act.

FED'S WALLER (voter, hawk) said that financial markets are tightening and will do some of the work for the Fed, adding that the Fed can watch and see what happens and he will see how the higher longer-term rates feed into Fed policy; said long-term rates are determined by the market but clearly issuance has to have an impact on yields. On the economy, Waller said a deficit at 6% with low unemployment is hard to sustain. Said it is astounding how resilient the jobs market is, despite tighter Fed policy; noted recent inflation data has been very good. Also said it is hard to see a direct link from the Middle East violence to Fed policy unless there is a broader conflict.

BOSTIC (2024 voter, dove) said the Fed needs to do all they can to get inflation down to 2%, but noted there are a lot of signs the economy is starting to slow and he repeated his view that he does not think the Fed needs to do anything more with rates. He added however that if inflation was stalling, it would be a sign that they need to do more but stressed that elevated wages are following inflation and not leading it.

FIXED INCOME

T-NOTE (Z3) FUTURES SETTLE 7 TICKS HIGHER AT 107-30

Treasuries saw pronounced flattening Wednesday amid haven demand on widening Israel conflict, but closed well off highs after hot PPI data and a weak 10yr auction. 2s +1.5bps at 4.999%, 3s +0.3bps at 4.764%, 5s -2.1bps at 4.598%, 7s -4.3bps at 4.619%, 10s -6.8bps at 4.587%, 20s -9.5bps at 4.934%, 30s -9.7bps at 4.731%.

INFLATION BREAKEVENS: 5yr BEI -0.1bps at 2.310%, 10yr BEI -0.3bps at 2.323%, 30yr BEI -2.2bps at 2.395%.

THE DAY: Treasuries were rangebound during APAC trade, with T-Notes rising gently to highs of 107-28 with lows of 107-21. There was a strong bid in govvies as European trade got underway, and particularly in the long end with strong curve flattening flows, with haven demand attributed to missile fire between Israel and Lebanon. T-Notes peaked at 108-11 before Fed hawk Bowman (voter) spoke, saying more hikes may be needed, not acknowledging her colleague's line of thinking that higher bond yields mean fewer Fed hikes needed.

The downside picked up on the back of the hot September PPI data, although appetite to pile on was somewhat limited ahead of Thursday's CPI data. Nonetheless, T-Notes hit interim lows of 107-27 later in the NY morning, hovering slightly above into the afternoon, with Fed hawk Waller (voter) providing some support saying financial markets are doing some of the Fed's job for it. But, the weak 10yr auction saw contracts stretch lower to 107-25. The FOMC minutes contained little surprises, expressing the well-documented cautiousness on further tightening, with no reaction in USTs or Fed pricing. Note that curve spreads remained near lows through the whole US session after the strong flattening seen in the London morning.

10YR AUCTION: The USD 35bln 10yr note reopening saw weak demand, adding to the poor 3yr auction on Tuesday. The 4.610% stop, despite a massive cheapening from September's 4.289%, marked a tail of 1.8bps, worse than the prior on the screws and the six-auction average 1.2bps. The bid/cover ratio of 2.50x was beneath the prior 2.52x and average 2.63x. Dealers (forced surplus buyers) were left with a chunky 18.8% (prev. 13.7%; avg. 15.6%), with Indirects seeing a notable fall in participation to 60.3% from 66.3%.

THIS WEEK'S AUCTIONS: US to sell 20bln of 30yr bonds on Oct 12th; to settle Oct 16th.

STIRS:

- SR3Z3 -0.5bps at 94.575, H4 -2bps at 94.695, M4 -3bps at 94.91, U4 -3.5bps at 95.18, Z4 -4bps at 95.475, H5 -3.5bps at 95.735, M5 -1.5bps at 95.91, U5 -1bps at 95.99, Z5 +0.5bps at 96.025, Z6 +4bps at 96.02, Z7 +7bps at 95.90.
- SOFR flat at 5.31% as of Oct 10th, volumes rise to USD 1.522tln from 1.404tln.
- NY Fed RRP op demand at USD 1.239tln (prev. 1.222tln) across 100 counterparties (prev. 98).
- EFFR flat at 5.33% as of Oct 10th, volumes fall to USD 95bln from 100bln.
- US sold USD 56bln of 17-week bills at 5.355%, covered 3.37x.

CRUDE

WTI (X3) SETTLES USD 2.48 LOWER AT 83.49/BBL; BRENT (Z3) SETTLES USD 1.83 LOWER AT 85.82/BBL

Oil futures continued to pare their post-Israel spike on Wednesday as supply risk concerns faded despite Putin touting extended OPEC action. WTI and Brent futures fell gradually through the session, accelerating in the NY morning on reports in NYT that Iranian leaders were surprised by the Hamas attacks, troughing at USD 83.11/bbl and 85.21/bbl, respectively. There was an earlier fleeting bout of strength after Russian President Putin, after Saudi/Russia conversations earlier Wednesday, said the OPEC+ deal is very likely to be extended, with further steps to stabilise markets possible next year; Putin warned oil prices could have fallen below USD 50/bbl without oil supply cuts. Elsewhere, we got the latest EIA STEO, where both the 2023 and 2024 world oil demand growth forecasts were cut from last month. Traders are now looking to the weekly US energy inventory data with the private release due later Wednesday ahead of the official EIA figures on Thursday (both a day delayed due to Columbus Day). Current expectations (bbls): Crude +0.5mln, Gasoline -0.8mln, Distillates -0.8mln.

EQUITIES

CLOSES: SPX +0.43% at 4,377, NDX +0.72% at 15,241, DJI +0.19% at 33,805, RUT -0.15% at 1,773

SECTORS: Real Estate +2.01%, Utilities +1.63%, Technology +1.01%, Communication Services +1.07%, Industrials +0.62%, Consumer Discretionary +0.48%, Materials +0.23%, Financials +0.11%, Health -0.43%, Consumer Staples -0.64%, Energy -1.35%.

EUROPEAN CLOSES: DAX +0.24% at 15,460, FTSE 100 -0.11% at 7,620, CAC 40 -0.44% at 7,131, Euro Stoxx 50 -0.09% at 4,201, IBEX 35 +0.09% at 9,360, FTSE MIB +0.36% at 28,419, SMI +0.32% at 11,036.

STOCK SPECIFICS: **Exxon (XOM)** confirmed a merger with **Pioneer Natural Resources (PXD)** in an all-stock transaction for USD 253/shr with the deal valued at USD 59.5bln. **Humana (HUM)** CEO Bruce Broussard is to step down in H2 '24, with Jim Rechtin named his successor. **Novo Nordisk (NVO)** will end a diabetes drug trial early after interim analysis for the treatment Ozempic showed success in preventing kidney failure. Note, kidney dialysis and related services names such as **DaVita (DVA) and Baxter (BAX)** in the US and **Fresenius Medical (FMS)** in Europe saw notable weakness. **HP Inc. (HPQ)** FY24 profit view was in line with expectations but it raised its dividend 5%, noting it expects a rebound in PC demand after a two-year slump. **Walgreens Boots Alliance (WBA)** appointed Tim Wentworth as its new CEO, starting on October 23rd. **Disney (DIS)** confirmed it is raising prices for Disneyland Resort and Walt Disney World Theme Parks, effective immediately. **Plug Power (PLUG)** sees FY revenue at USD 1.2bln, but looking further ahead, projected a sharp rise in revenue as by 2027 looks for roughly USD 6bln and circa USD 20bln by 2030. **Take-Two (TTWO)** was upgraded at Raymond James who expressed optimism about its near- and medium-term future. In the chip space, Samsung Electronics gained in South Korea trade after prelim Q3 operating profit and sales topped expectations. Its quarterly profit decline was less severe than expected, mainly due to improved performance in its chip division. **Birkenstock (BIRK)** set its IPO price at USD 46/shr, valuing the company at around USD 8.6bln, slightly lower than its initial target of USD 9.2bln, while it opened even lower at USD 41/shr. **Microsoft's (MSFT)** tweaks to **Activision (ATVI)** deal are said to avoid EU probe; UK merger regulator's approval is expected in the coming days, according to Bloomberg. Ahead of earnings, Goldman Sachs (GS) announced the sale of Greensky to the Sixth Street-led consortium; noting the transaction is expected to result in a negative USD 0.19 EPS impact on its Q3 23 results. **Brinks Co (BCO)** denied earlier reports it was in talks about a strategic transaction with **NCR Corp (NCR)**. **Chipotle (CMG)** reportedly plans to hike prices after pausing price raises this year, according to CNBC. US Steel (X) saw gains on chatter that a Japanese co. is rumoured to be working with ArcelorMittal (MT NA) on its interest in the **X**.

US FX WRAP

Dollar flat after PPI ahead of CPI with yields predominantly lower

The Dollar was choppy on Wednesday with DXY testing 106 to the upside in wake of the hotter-than-expected US PPI data albeit as it failed to rise above the level the DXY pared to lows of 105.55 shortly after. Nonetheless, DXY later on rose to briefly breach 106.00 as UST yields moved off lows, albeit yields were still broadly lower on the session aside from the front-end amid the curve flattening. The FOMC minutes revealed little new information and are deemed rather stale given the move in yields since the latest FOMC meeting which has tightened financial conditions, reducing the need for Fed action, in the words of many officials, including Waller (voter, hawk) today.

The Euro was flat vs the buck and traded on either side of 1.06 in a 1.0581-1.0634 range. In the Eurozone, final German September inflation data was in line with expectations and unrevised but the consumer inflation expectations survey for August from the ECB saw the year-ahead gauge rise to 3.5% from 3.4% and the 3-year ahead rise to 2.5% from 2.4%. ECB Speak saw Knot note that the effects of inflation shocks are waning, but restrictive policies will be needed for some time and policy is in a good place now. De Cos is more confident that the trajectory of inflation might take the Eurozone back to target. Nagel noted pausing rates could be an option. Kazaks said the current interest rate is appropriate, but we cannot close the door on hikes and an early end to PEPP reinvestments should be discussed. Vujcic said if the outlook holds, no more rate hikes are needed. Holzmann however warned inflation could turn out stronger than thought, whilst suggesting a 90% cap on reserve remuneration.

The Yen was weaker vs the Dollar with USD/JPY rising back above 149.00 with some haven appetite being unwound since the Hamas attack on Israel, in addition to tracking the move off lows in yields through the US session. The Swiss Franc was the outperformer with USD/CHF testing 0.9000 and EUR/CHF maintaining sub 0.9600 throughout the session.

Cyclical currencies were lower, particularly AUD and NZD while the Looney was more flat, however, GBP was the outperformer and saw a mild bid vs the Dollar and the Euro. RBA Assistant Governor Kent stated monetary policy is slowing growth of demand and inflation but policy lags mean some further effects of past rate hikes are still to be felt through the economy, but repeated guidance that some further policy tightening may be required. Kent noted they have the opportunity to see how the economy reacts to past hikes and there are no current plans to accelerate the run-off of its bond holdings, but if the RBA were to sell bonds, it would do so in a way that does not disturb markets.

Scandis were weaker vs the Euro to a similar magnitude. For the SEK, Riksbank's Bunge said she is still worried about service prices and the SEK. She also noted the economy has been stronger than the bank had expected and she is concerned that inflation will prove higher rather than lower. She also noted that the Riksbank wants to be sure that inflation is low and stable around the target before we start cutting rates.

EMFX was mixed. BRL was flat after softer-than-expected inflation data, while MXN, COP and CLP saw gains despite weakness in both crude and copper prices. ZAR saw solid gains, tracking gold prices higher but also on remarks from the SARB Governor that interest rates are to stay higher for longer, but they do not know if hikes are on the horizon, noting they expect inflation to be sustainably on target in 2025.