US Market Wrap

26th October 2023: Stocks down on large cap earnings; bond shorts cover despite massive surge in US GDP

- **SNAPSHOT**: Equities down, Treasuries up, Crude down, Dollar flat.
- **REAR VIEW**: Hot US GDP and Durable Goods; Jobless Claims above expected; Pending Home sales post surprise gain; Solid 7yr UST auction provides relief; META tumbles post earnings; ECB in line with expected; Israel says it will start ground op. in due course.
- **COMING UP**: **Data**: US PCE Price Index, Personal Income/Consumption **Earnings**: Air France, Carlsberg, Eni, Equinor, Sanofi; NatWest; Exxon, Chevron, Abbvie, Aon, Charter, Colgate, Phillips 66.

MARKET WRAP

The S&P 500 and Nasdaq were lower on Thursday as losses in Meta (META) post-earnings, and some other large cap names, weighed. The relief of the strong 7yr Treasury auction provided some support but indices extended back lower in late trade. However, the equal-weighted S&P 500 (RSP) saw gains (but closed flat), as did the small-cap Russell 2k index, aided by Q3 Advance GDP surging 4.9% (exp. 4.3%), with September Durable Goods orders also surging 4.7% (exp. +1.7%). On the other hand, jobless claims came in above estimates, more so in the continuing claims, although initial claims still remain very low. Treasuries ripped despite the largely solid economic data as shorts rushed in to take profits ahead of Friday's PCE and next week's key events; the 7yr auction saw strong demand, providing relief after the awful 5yr offering on Wednesday. The Dollar Index was ultimately flat with gains in Europe pared after the fall in Treasury yields post-data. The Euro was also little changed with the ECB leaving rates unchanged, as expected, whilst it also refrained (for now) from a hawkish adjustment to its PEPP reinvestments programme. USD/JPY remains in focus with the cross seeing a near 100pip kneejerk lower during the European morning after it hit a new high just beneath 150.80. Oil prices were sold despite the solid US data, initially tracking the Dollar, but benchmarks held onto losses as the Dollar pared gains.

GLOBAL

ECB: As expected, the ECB opted to call a "pause" in its hike campaign by keeping all three of its key rates unchanged. The Governing Council judges that rates are sufficiently restrictive to return inflation to target and noted that past interest rate increases continue to be transmitted forcefully into financing conditions. In terms of the economic outlook, the statement reiterated that inflation is still expected to stay too high for too long, and domestic price pressures remain strong. On the balance sheet, despite some outside expectations for a potential bringing forward, the ECB reaffirmed that reinvestments under PEPP will run until "at least the end of 2024". At the follow-up press conference, Lagarde offered a downbeat assessment in which she believes the economy will remain weak in the coming months and tighter financial conditions are weighing on the Eurozone. In terms of the policy decision, Lagarde revealed that today's actions were unanimously approved, adding that there was no discussion of an early end to PEPP reinvestments or adjustments to minimum reserves. However, ECB sources via Reuters later noted that policymakers agreed to debate PEPP reinvestment end date in early 2024 and to debate minimum reserves as part of the framework review in the Spring. The sources added that the expectation was that reinvestments would not end abruptly and the ECB would follow the sort of gradual approach it did with the APP. In terms of what lies ahead for the Bank, the President noted that just because policymakers opted for a pause today, it does not mean they won't necessarily hike in the future, but did note that the transmission of previous hikes will be felt into Q1 2024 and possibly beyond. Overall, the ECB has put itself in a position to take stock of existing actions, whilst continuing to keep options open for further adjustments to the upside. At this stage, Lagarde stated that discussion of rate cuts is premature, however, from a markets perspective, the first full 25bps cut is seen in July 2024.

US GDP: Headline Q3 Advanced GDP print was hot, rising 4.9%, above the 4.3% forecast and accelerating from the 2.1% growth in Q2 with a large jump in consumer spending to 4.0% from 0.8% in Q2. The headline was within the wide range of forecasts with the most optimistic view forecasting 6% growth, and the most pessimistic seeing 2.5% growth, and it was beneath the Atlanta Fed GDPNow estimate of 5.4%. The PCE data for Q3 was slightly softer than expected at 2.4% (exp. 2.5%) and down from the prior 3.7%, while the PCE Price Index ex-Food/Energy/Housing rose 1.8%, easing from the 3.1% pace in Q2, while ex-Energy/Housing rose 3.6% (prev. +3.5% in Q2). It is worth noting that although the price metrics were softer than expected, Q3 covers from July-September, we have already seen the

September CPI data and the September PCE report is due on Friday for a more timely picture. Although Q3 was hot, ING (and many other analysts) expect this growth to slow for Q4, noting "the headwinds facing the economy and the household sector in particular are intensifying and we look for the pace of growth to slow to 1.5% in the final three months of the year".

US DURABLE GOODS: Durable goods soared 4.7% in September (prev. -0.1%), way above the expected (1.7%) and just beneath the upper bound of the forecast range (4.8%), largely due to the 131% surge in civilian aircraft orders, in part reflecting a huge order for Boeing aircraft by Ryanair. Nondefense capital goods orders ex-air rose 0.6%, above the expected (0.1%) but short of the upwardly revised prior (1.1%). Pantheon Macroeconomics adds, “the bigger picture is that core capital goods orders continue to trend lower in real terms, in line with depressed capital spending intentions”. However, while this weakness has been partly offset by rising business purchases of autos in recent quarters, spending here also appears to be slowing. Elsewhere, ex-defense and ex-transport printed 5.8% (prev. -0.7%) and 0.5% (exp. 0.2%, prev. 0.5%), respectively.

US JOBLESS CLAIMS: Initial jobless claims continued to hover around the 200k mark, printing 210k, marginally above the expected 208k and rising from the prior 200k. Continued claims rose to 1.79mln (prev. 1.727mln), surpassing the consensus (1.74mln) and outside of the upper boundary of the forecast range. On the latter, Oxford Economics notes the upturn suggests that, while the labour market may be characterized by few job losses, unemployed individuals are finding it more difficult to find new jobs, which would be consistent with a slower pace of hiring. Nonetheless, Oxford’s forecast is for no further Fed hikes and expect slower job growth and some modest job losses early in 2024. The consultancy adds that given the strong performance of the economy in Q3 the risk may be those occur later in the year, pushing the first rate cuts back to H2 ’24.

US PENDING HOME SALES: Pending Home sales rose by 1.1% in September, well above the expected decline of 1.8% but only slightly paring August's 7.1% decline. Nonetheless, the NAR Chief Economist notes that despite the gain, "pending contracts remain at historically low levels due to the highest mortgage rates in 20 years". The Chief Economist also stated that inventory also remains tight which hinders sales and keeps prices elevated, adding that because of "homebuilders' ability to create more inventory, new-home sales could be higher this year despite increasing mortgage rates. This underscores the importance of increased inventory in helping to get the overall housing market moving".

FIXED INCOME

T-NOTE (Z3) FUTURES SETTLED 21+ TICKS HIGHER AT 106-11

Treasuries rip despite solid economic data as shorts take profit ahead PCE and next week's key events; 7yr auction saw strong demand. 2s -7.3bps at 5.048%, 3s -8.9bps at 4.888%, 5s -11.0bps at 4.806%, 7s -9.8bps at 4.880%, 10s -9.6bps at 4.857%, 20s -9.2bps at 5.204%, 30s -9.0bps at 5.002%.

INFLATION BREAKEVENS: 5yr BEI -2.0bps at 2.394%, 10yr BEI -1.5bps at 2.424%, 30yr BEI -1.9bps at 2.516%.

THE DAY: After Wednesday's awful 5yr auction, T-Notes hovered just above their Wednesday lows (105-18) heading into the Thursday APAC session. Contracts stretched lower to fresh troughs of 105-15+ at the London handover with EGBs and Gilts offered, part catch-up and also in anticipation of an expected surge in US Q3 GDP data, 7yr auction, and the ECB rate decision. The latter left rates unchanged as expected with a lack of movement on PEPP, proving some support out of EGBs.

Treasuries saw two-way flows as the 08:30ET data slate was released, with massive beats in GDP and Durable Goods orders somewhat offset by the above forecast jobless claims (albeit still low) and the beneath forecast Q3 PCE. T-Notes eked out a fresh session low of 105-15 in a kneejerk before swiftly reversing higher to c. 106-00, with shorts quick to take profit rather than chasing further upside in yields. Prices edged cautiously higher into the NY afternoon with some anxiety ahead of the 7yr auction, but once that passed with solid demand (details below), T-Notes surged higher again, printing peaks of 106-13 ahead of settlement. September PCE data and the final October Uni of Michigan survey serve as Friday's highlights, while otherwise, attention now starts drifting to next week's quarterly refunding announcement, FOMC, and NFP.

7YR AUCTION: A fairly strong USD 38bln 7yr auction from the Treasury, particularly when compared to some of the other offerings lately, like Wednesday's 5yr. The 4.908% stop marked the highest yield on offer for the 7yr since 2009, and stopped through the WI yield by 0.2bps, better than the prior month's tail of 0.3bps and better than the six-auction average 0.2bp stop-through. The bid/cover ratio of 2.70x was much better than last month's 2.47x, and similar to the average 2.73x. Dealers (forced surplus buyers) were left with 11%, well beneath the prior 14.6% and average 12.0%, with Indirects stepping up their participation to 70.6% from 65.5%, indicative of strong end-user demand.

STIRS:

- SR3Z3 +2bps at 94.575, H4 +4bps at 94.66, M4 +6bps at 94.875, U4 +7.5bps at 95.135, Z4 +9bps at 95.39, H5 +10bps at 95.605, M5 +11.5bps at 95.745, U5 +12bps at 95.810, Z5 +12.5bps at 95.825, Z6 +13bps at 95.76, Z7 +12bps at 95.61.
- SOFR flat at 5.30% as of Oct 25th, volumes rise to USD 1.439tln from 1.387tln.
- NY Fed RRP op demand at USD 1.09tln (prev. 1.101tln) across 98 counterparties (prev. 97).
- EFFR flat at 5.33% as of Oct 25th, volumes rise to USD 93bln from 83bln.
- US sold USD 96bln of 4-week bills at 5.295%, covered 2.94x; sold USD 86bln of 8-week bills at 5.330%, covered 2.52x.
- US leaves 13-, 26-, and 52-week bill auction sizes unchanged at USD 75bln, 68bln, and 44bln, respectively; 13- and 26-week sold on Oct 30th and 52-week sold on Oct 31st; all to settle on Nov 2nd.

CRUDE

WTI (Z3) SETTLED USD 2.18 LOWER AT 83.21/BBL; BRENT (Z3) SETTLED USD 2.20 LOWER AT 87.93/BBL

Oil benchmarks were sold on Thursday, unwinding their Wednesday recovery, weighed on by the initially firmer Dollar and despite solid US economic data. The losses were built during the European morning when the Dollar was rallying, with WTI and Brent futures hitting troughs of USD 82.56/bbl and 87.53/bbl, respectively, before paring losses somewhat as the hot US economic data was released, with the Dollar paring off best levels. Prices gravitated back towards the lows heading into settlement. In energy newsflow, preliminary programmes show output of the four main Nigerian crude oils is set to drop to 687k BPD in December (prev. 746k BPD in Nov programme) due in part to reduced loadings from the Qua Iboe stream. While in Venezuela, Repsol (REP SM) CEO said they are talking to PDVSA, saying there is room to begin reversing the production trend in the country.

EQUITIES

CLOSES: SPX -1.18% at 4,137, NDX -1.89% at 14,110, DJI -0.76% at 32,784, RUT +0.34% at 1,657.

SECTORS: Communication Services -2.58%, Technology -2.17%, Consumer Discretionary -1.56%, Health -0.98%, Energy -0.8%, Consumer Staples -0.63%, Industrials -0.44%, Financials -0.22%, Materials +0.72%, Utilities +0.86%, Real Estate +2.15%.

EUROPEAN CLOSES: DAX -1.08% at 14,731.05, FTSE 100 -0.81% at 7,354.57, CAC 40 -0.37% at 6,889.48, Euro Stoxx 50 -0.59% at 4,049.15, IBEX 35 -0.24% at 8,962.80, FTSE MIB +0.29% at 27,507.90, SMI -0.34% at 10,366.00.

STOCK SPECIFICS: **UPS (UPS)** revenue missed noting unfavourable macro-economic conditions negatively impacted global demand in the quarter; cut FY guidance. **Meta (META)** EPS and revenue surpassed expectations, but next quarter revenue guide was light. **Merck (MRK)** earnings beat with the drug breakdown also strong. FY sales view was raised but it cut its profit view. **International Business Machines (IBM)** beat on EPS and revenue alongside leaving FY revenue and cash flow guidance unchanged. **Align Technology (ALGN)** earnings missed and cut revenue guidance for both the next quarter and FY. **Hasbro (HAS)** fell short on the top and bottom line in addition to lowering FY23 revenue growth view. **O'Reilly Automotive (ORLY)** EPS, revenue, and comp. sales surpassed Wall St. expectations in addition to lifting FY outlook. **ServiceNow (NOW)** top and bottom line beat, with subscription guidance impressing for next quarter and FY. **Mattel (MAT)** warned of slowing demand for the toy industry heading into the crucial holiday season which took the shine off the co. beating on the top and bottom line and raising FY adj. EPS and EBITDA guidance. **Royal Caribbean Cruises (RCL)** EPS and revenue beat alongside raising next quarter and FY profit view driven by strong demand and continued strength in onboard revenue. Said results were better than expected due to stronger close-in demand and further strength in onboard revenue. **Bunge (BG)** Q3 results topped estimates alongside upping FY23 EPS outlook. **Southwest Airlines (LUV)** revenue missed and Q3 profit that fell about 30% on soaring labor and fuel costs. **Mastercard (MA)** had a mixed report; EPS beat but revenue beat. **Ford (F)** reached a tentative deal with UAW, while the UAW made a new proposal to GM, similar to the deal made with Ford but GM plan to prepare a counter offer on Thursday or Friday, according to Bloomberg. **Morgan Stanley (MS)** announced Ted Pick to become Chief Executive Officer on January 1, 2024; James Gorman to become Executive Chairman. The incoming CEO said this is a 'volatile environment' for investment banking.

US FX WRAP

Dollar pares gains as yields decline despite solid economic data, aided by a strong 7yr auction

The Dollar was flat on Thursday where the strong economic data and equity weakness was not enough to support the buck against a backdrop of lower yields. US GDP rose 4.9% in Q3, well above the consensus 4.3% although the Q3 PCE price data was cooler than expected, but not my much. Nonetheless, eyes turn to US PCE due Friday for a more timely picture of the inflation picture within the US. Aside from GDP, Durable Goods smashed expectations while jobless claims remain hot at 210k, but was marginally above the 208k forecast. The buck had started off with gains but heading into the end of the US session it was flat with yields moving further lower after a strong 7yr auction, paring the earlier Dollar strength.

The Euro was flat vs the Dollar with very little action seen throughout the ECB which was very much in line with expectations and Lagarde even noted in the press conference that PEPP or Minimum Reserve Requirement were not discussed at the meeting, although Reuters sources later stated policymakers agreed to debate PEPP reinvestment end date in early 2024 and to debate minimum reserves as part of the framework review in the Spring.

The Yen hit fresh cycle lows vs the buck with USD/JPY hitting a peak of 150.77 which saw a very brief, but sharp move lower to 149.88 which of course sparked fresh intervention speculation but with no official confirmation. The kneejerk lower swiftly pared back higher, with USD/JPY remaining above 150 heading into APAC trade Friday with Tokyo inflation data on watch.

The antipodean currencies were firmer vs the Dollar despite the risk off tone in markets. The Aussie was buoyed by commentary from RBA Governor Bullock that CPI was a little higher than expected but was about where they thought it would come. Bullock added the RBA is wary of inflation, and has made it clear they might have to hike again, but have not yet decided. Following the data and response from the RBA Governor, Westpac economists have changed their call for the RBA and now see a rate hike in November. NZD saw similar gains to the Aussie with NZD/USD rising above 0.5800 while AUD/NZD was relatively unchanged, trading between 1.0850-75.

GBP saw mild gains, primarily supported by the pullback in the Dollar while it found little help from a dire CBI distributive trade data but GBPUSD did manage to rise above 1.2100 as the dollar pared from highs.

CAD was marginally softer as the weakness in crude prices and dovish commentary from BoC Governor Macklem offset any support from the Dollar paring its initial highs. Macklem, just a day after the BoC, stated they may not have to raise further. He also acknowledged that the economy is not overheated anymore and if inflation cools as projected, it will not have to raise rates further.

Scandis were flat vs the Euro, with little independent impetus from mixed Swedish data and surveys, the Riksbank's credit line for Crown clearing institutions or the SNDO upgrading its 2023 budget balance estimate from deficit to surplus, while a dip in the Norwegian LFS jobless rate was offset by a fall in Brent.

EMFX was mixed. BRL was flat vs the Dollar but MXN and COP saw strong gains while CLP sold off. In Brazil, the IPCA-15 min-month inflation data was in line with expectations at 5.05% Y/Y and 0.21% M/M, while in Mexico the jobless rate was in line at 2.9%, falling from the prior 3.0%. The CLP sold off ahead of the rate decision due later Thursday where analysts expect a 75bp cut again. Elsewhere, TRY was little changed after the CBRT hiked by 500bps, in line with expectations, noting monetary tightening will be further strengthened as much as needed in a timely and gradual manner until a significant improvement in the inflation outlook is achieved. Meanwhile, INR was still marginally softer vs the Dollar despite reports that the RBI is likely selling USD to stem the INR's decline, according to traders cited by Reuters.