US Market Wrap

13th December 2023: Stocks, Bonds & Gold rip while Dollar dips on dovish Fed

- **SNAPSHOT**: Equities up, Treasuries up, Crude up, Dollar down.
- **REAR VIEW**: Ubiquitously dovish FOMC; Softer-than-expected US PPI; Weak UK GDP data; Argentina devalued the Peso by more than 50%; Larger-than-expected EIA crude draw; PFE FY24 guidance disappoints; TSLA recalls 2mln vehicles amid autopilot issues.
- **COMING UP**: **Data**: UK RICS Housing Survey, Australian Employment, Spanish CPI (Final), US Export & Import Prices, IJCs, Retail Sales, Australian PMI (Flash) **Events**: BoE, ECB, SNB, Norges, Banxico Policy Announcement **Speakers**: ECB's Lagarde Press Conference **Supply**: Japan & US.

MARKET WRAP

Stocks, Bonds, and Gold all surged while the Dollar slumped in response to the ubiquitously dovish FOMC. The gains were led by the small-cap Russell 2k, with regional banks flying, while the equal-weighted S&P beat the market cap-weighted index - a move lower in rates is seen as most beneficial to those with weaker balance sheets, who need to refinance their debt. The 2yr yield plunged nearly 30bps to 4.45% at the time of writing, while the 10yr yield is down nearly 20bps, and is testing 4.00% to the downside. The Fed made dovish tweaks to the statement guidance and slashed its 2024 median dot by more than expected to imply three rate cuts in 2024 vs its prior median of one cut (street was looking for two cuts). In the press conference, Powell also gave the nod to upcoming rate cuts, noting they discussed the timing of rate cuts at the meeting and there was a general expectation that rate cuts will be a topic of discussion going forward. Money markets are now pricing in an 88% probability of the first 25bp rate cut in March vs 50% before the FOMC, with 140bps of easing seen throughout 2024 vs 115bps before. Crude prices saw relatively little reaction to the FOMC but had ground higher throughout the session with inventory data showing deeper than expected draws. Elsewhere, the PPI data was cooler than expected, and Fed Chair Powell acknowledged this, alongside CPI on Tuesday, led some policymakers to adjust their SEP forecasts. Attention now turns to the plethora of central bank releases on Thursday, including SNB, Norges Bank, BoE and ECB rate decisions.

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FOMC STATEMENT & SEP ANALYSIS: The Fed left rates unchanged at 5.25-5.5%, made dovish tweaks to its statement, whilst indicating a greater fall than many had expected to its Fed rate projections. The 2024 median rate dot was dropped to 4.6% from the prior 5.1%, beneath the analyst consensus 4.9%, indicating three cuts from current levels in 2024 - the uncertainty remains high, however, with eight out of 19 officials forecasting rates above the median and five beneath it with a forecast range of 3.9–5.4%. The 2025 median Dot was dropped to 3.6% from 3.9%, whilst the 2026 and long run dots were left unchanged at 2.9% and 2.5%, respectively, bucking some expectations for an upward drift in the longer run ('neutral') estimate. The lower rate projections were reflective of faster progress than previously anticipated for inflation, with the Core PCE projections falling to 3.2% from 3.7% for 2023, to 2.4% from 2.6% in 2024, and to 2.2% from 2.3% for 2025. The unemployment rate forecasts were unchanged through 2025 (4.1% in both 2024 and 2025), while the 2024 GDP forecast nudged lower to 1.4% from 1.5% in 2024. The statement saw its tightening guidance softened, "In determining the extent of ANY [new word] additional policy firming that may be appropriate...", whilst it also maintained its language added in November describing financial and credit conditions as tighter, despite some expectations that it would be removed after a rally in USTs and stocks since then. It noted growth had slowed from the strong pace in Q3 (prev. expanded at a strong pace in Q3), while it also added that inflation has eased over the past year, but maintained language it remains elevated.

POWELL PRESSER: Chair Powell declared in his presser that the Fed believes policy is at or near its peak, caveating that the Fed has been surprised in the past and is prepared to tighten policy further if appropriate, said policy will be kept restrictive until the Fed is confident it's on the path to 2% inflation. He noted inflation has eased without a significant rise in unemployment, with the usual caveats that inflation is still too high with a long way to go to target. He echoed his Spelman College appearance by bringing in the line that policy has been moved "well into restrictive territory" into his prepared remarks. Powell still believes more tightening is in the pipeline via lags, saying the full effects of tightening "have yet to be felt". He reiterated prior commentary on the labour market, saying it remains tight but coming into better balance, which policymakers expect to continue, putting further downward pressure on prices. Ahead of Core PCE on

Dec 22nd, Powell said the Fed expects a print of 3.1% Y/Y, but added that the Fed thinks it will take some time to bring inflation down to the 2% target.

Q&A: Powell announced that policymakers think they have done enough on rates and he said it is not likely the Fed will hike further, but caveated the Fed is not fully confident in that view yet. Meanwhile, when asked about rate cuts, Powell said they are beginning to come into view and are now a topic of discussion, saying the timing of cuts were also discussed (he said they were not even being considered at the November FOMC). He added that there was a general expectation that cuts would be a topic of conversation going forward. After Waller made the case the other week for cuts in the coming months if real rates continued drifting higher amid the decline in inflation, Powell said that the Fed is very conscious of real rates and it is a part of how it thinks about things. The Fed Chair made the point that the reason you would not wait to achieve 2% inflation to cut rates is that it would be too late for the economy, saying the Fed needs to reduce the restriction on the economy well before 2%, or they would overshoot. On a soft landing, Powell said he has always felt there was a possibility the economy could avert a recession while inflation came down, and so far that is what they are seeing, saying there is little basis for thinking the economy is in a recession right now. He added that while stronger growth will be good, it will mean it takes longer to get inflation down, suggesting the Fed could have to keep rates higher for longer or hike again due to above-trend growth. Powell noted they had seen real progress on core inflation, whilst saying they had made reasonable progress in non-housing services inflation. On the neutral rate, Powell said the Fed does not know if it has risen. And on the balance sheet, he said the runoff has been working pretty much as expected with reserves not at levels where they would need to slow or stop the runoff, highlighting that the policy rate and balance sheet are on different tracks.

PPI: PPI for November was unchanged M/M, despite expectations for a 0.1% gain with the prior revised up to -0.4% from -0.5%. Y/Y PPI rose 0.9%, beneath the 1.0% forecast while the prior was revised down to 1.2% from 1.3%. Looking into the details, both the index for final demand goods and services were unchanged. The unchanged good prices followed the 1.4% drop in October while the services prices matched October's pace. In goods, price increases of 0.6% for final demand foods and 0.2% for final demand goods less foods and energy offset a 1.2% decrease in the index for final demand energy. Core PPI (ex food and energy) was cooler than expected with M/M unchanged (exp. +0.2%), matching the prior month pace. The core Y/Y eased to 2.0% from 2.3% (revised down from 2.4%) and beneath the 2.0% forecast. The Super Core (ex food, energy and trade) maintained a 0.1% gain in November while the Y/Y eased to 2.5% from 2.8%, which was revised down from 2.9%. Overall a dovish report with PPI beneath expectations and it was more dovish than the in-line CPI released on Tuesday. With PCE due 22nd December, and now with CPI and PPI behind us, Fed Chair Powell had stated that he believes some members did update their SEP forecasts in the wake of both CPI and PPI, and he even acknowledged the Fed expect the November PCE report to show Core PCE prices rose 3.1%. Meanwhile, Pantheon Macroeconomics "estimate that the core PCE deflator for November will rise by just 0.13%, pushing the Y/Y rate down to 3.3%."

CENTRAL BANKS

Plenty of Central Bank activity on Thursday, please follow the links to see the full previews

ECB PREVIEW: Expectations are for the ECB to stand pat on rates for a second consecutive meeting after halting its hiking campaign in October. In terms of recent economic developments, November’s flash CPI fell to 2.4% Y/Y from 2.9%, whilst the super-core metric declined to 3.6% Y/Y from 4.2%. Survey data saw a pick-up in the Eurozone composite PMI for November from 46.5 to 47.6, but ultimately is still suggestive of negative growth in Q4. In terms of communications from ECB officials, great attention has been placed on remarks from Germany’s Schnabel, who noted that further hikes were “rather unlikely” after November inflation data cooled, and declined to endorse guidance for steady rates for several quarters. These remarks have subsequently accelerated pricing for 2024 rate cuts with a March reduction priced with around 60% probability. Signalling for 2024 action may come via the accompanying macro projections, which ING suggests should see downward revisions for growth and inflation in 2024 and 2025. Finally, speculation continues to mount over the Bank’s balance sheet and a potential early conclusion to PEPP reinvestments after Lagarde stated on November 27th that PEPP will be discussed in the “not-so-distant future”. However, many desks are of the view that the December meeting would be too soon for such an adjustment. To download the full Newsquawk preview, please click here.

BOE PREVIEW: Expectations are for the MPC to stand pat, maintain its Base Rate at 5.25% for a third consecutive meeting. Recent data saw headline CPI decline to 4.6% Y/Y in October from 6.7%, core fall to 5.7% Y/Y from 6.1% and all services slip to 6.6% Y/Y from 6.9% (vs MPC forecasts for 6.9%). On the growth front, October GDP contracted by 0.3% M/M whilst more timely PMI metrics saw the composite PMI rise to 50.7 in November from 48.7. In the labour market, the unemployment rate in the 3-month period to October held steady at 4.2%, whilst wage growth continued to ease. Governor Bailey has remarked that the full effect of higher rates is yet to hit the UK, adding that the MPC is not in a place to discuss rate cuts. Ultimately, with economic developments not shifting enough to warrant a change in stance from the Bank, consensus expects the MPC to continue to vote 6-3 in favour of standing pat on rates (hawkish dissent from Greene, Haskel and Mann). In terms of the policy statement, the MPC will likely reiterate that “policy will need to be sufficiently restrictive for sufficiently long to return inflation to the 2% target.” In terms of an outlook beyond the upcoming meeting, markets currently price the first 25bps reduction by June with a total of 92bps of cuts priced by year-end. To download the full Newsquawk preview, please click here.

SNB PREVIEW: Expected to leave rates unchanged at 1.75% given the cooler than expected November inflation print which was the first to account for the rental increase. However, this release means that a cut cannot be entirely dismissed given the SNB’s willingness to surprise and markets pricing around a 25% chance of a reduction. In the scenario of a hold, the statements language may feature a reference on further tightening given uncertainty around the evolution of the rental price index but is, on balance, unlikely to flag a cut. Rates aside, the SNB could tweak its FX language to de-emphasise the selling foreign currency element. To download the full Newsquawk preview, please click here.

NORGES BANK PREVIEW: Expected to leave rates at 4.25%, as recent developments should satisfy the condition that “… underlying inflation is on the decline”. However, a hike cannot be entirely dismissed given ongoing NOK weakness. Thereafter, attention turns to whether the path implies another hike (in the scenario of a hold) and then on where the first cut is projected as markets price two 2024 cuts. To download the full Newsquawk preview, please click here.

FIXED INCOME

T-NOTE (H4) FUTURES SETTLED 1 POINT & 11 TICKS HIGHER AT 111-28+

Treasuries saw massive bull-steepening after a ubiquitously dovish FOMC brings a rate-cutting cycle into view. At settlement, 2s -26.9bps at 4.462%, 3s -25.5bps at 4.176%, 5s -23.2bps at 3.995%, 7s -20.8bps at 4.037%, 10s -16.9 bps at 4.037%, 20s -12.8bps at 4.350%, 30s -11.1bps at 4.193%.

INFLATION BREAKEVENS: 5yr BEI +1.9bps at 2.110%, 10yr BEI +0.1bps at 2.169%, 30yr BEI -0.6bps at 2.227%.

THE DAY: Treasuries saw modest bull-flattening in the APAC session and London morning on Wednesday. There was some spillover from JGBs, with the long end in Japan trading particularly strong amid a BoJ buyback op and ahead of an auction on Thursday, with some block 2s/10s UST flatteners supportive of the flow too. The duration bid in Europe was aided a strong Gilt auction in addition to the surprise fall in UK Q3 GDP. The US short end was reluctant to advance ahead of the FOMC.

However, the bull-flattener turned into a bull-steepener in the NY morning on the back of the softer-than-expected PPI data, with softening core metrics observed. T-Notes advanced to interim highs of 110-31 in the immediate aftermath, just off the CPI peak of 110-31+, but failed to sustain any higher, although yields at the front and long end of the curve stretched out new lows for the day later in the afternoon ahead of the FOMC.

The fall in the Fed's median rate dots (to imply three cuts vs prior one cut in 2024, four cuts in 2025, and three cuts in 2026), with dovish tweaks to the statement's guidance, saw a massive bull-steepener. Powell's dovish presser and Q&A, where he said rates are at or near the peak and the Fed is thinking about rate cuts, only cemented the moves, seeing T-Notes print session peaks of 112-03+ just before settlement, with the cash 10yr yield testing 4% to the downside. 2s10s spread closes c. 10bps steeper at -43bps. Attention now on Europe for Thursday with the SNB, BoE, and ECB all due.

FED PRICING had a major dovish repricing post-Fed, with 143bps of cuts now priced across 2024 vs 115bps just before the FOMC. The implied probability of a March cut has risen to 90% from 50%, while the Jan meeting has crept up slightly to 16% from no cuts priced beforehand.

STIRS:

- SR3Z3 +1.75bps at 94.6275, H4 +16.5bps at 94.96, M4 +27bps at 95.375, U4 +31.5bps at 95.75, Z4 +32bps at 96.085, H5 +30bps at 96.36, M5 +26.5bps at 96.545, U5 +24bps at 96.655, Z5 +21bps at 96.685, Z6 +16bps at 96.63, Z7 +14bps at 96.53.
- SOFR falls to 5.31% as of Dec 12th from 5.32%, volumes at USD 1.713tln (prev. 1.577tln).
- NY Fed RRP op demand at USD 0.823tln (prev. 0.838tln) across 95 counterparties (prev. 97).
- EFFR flat at 5.33% as of Dec 12th, volumes USD 106bln (prev. 102bln).
- US sold USD 56bln of 17-week bills at 5.250%, covered 2.84x.

CRUDE

WTI (F4) SETTLED USD 0.86 HIGHER AT 69.47/BBL; BRENT (G4) SETTLED USD 1.02 HIGHER AT 74.26/BBL

The crude complex saw gradual strength throughout the US session, albeit on a lack of oil-specific newsflow. Nonetheless, WTI and Brent saw fleeting upside to print highs of USD 69.71/bbl and 74.42/bbl, respectively, in wake of the weekly EIA data. In terms of figures, Crude stocks saw a greater draw than expected, in line with the private inventory on Tuesday night, while Distillates and Gasoline saw a larger and smaller build than forecasted, respectively. Overall, production was unchanged at 13.1mln BPD with refining utilisation falling 0.3%, against the expectations of a 0.5%. Elsewhere, the FOMC rate decision saw a broad dovish market reaction, although oil was little moved. Lastly, December OPEC MOMR saw 2023 world oil demand unchanged from the prior 2.5mln BPD, with 2024 world oil demand also unchanged with M/M expected to rise by 2.2mln BPD. Looking ahead, all participants await Super Thursday with rate decisions from ECB, SNB, BoE, Norges Bank, and Banxico, in addition to some US data.

EQUITIES

CLOSES: SPX +1.37% at 4,707, NDX +1.27% at 16,562, DJIA +1.40% at 37,090, RUT +3.52% at 1,947.

SECTORS: Utilities +3.72%, Real Estate +3.58%, Health +1.83%, Consumer Staples +1.82%, Financials +1.61%, Consumer Discretionary +1.35%, Energy +1.27%, Materials +1.2%, Industrials +1.14%, Technology +0.89%, Communication Services +0.65%.

EUROPEAN CLOSES: DAX -0.15% at 16,766.05, FTSE 100 +0.08% at 7,548.44, CAC 40 -0.16% at 7,531.22, Euro Stoxx 50 -0.14% at 4,530.35, IBEX 35 -0.22% at 10,096.10, FTSE MIB -0.15% at 30,295.69, SMI +0.38% at 11,193.80.

STOCK SPECIFICS: In wake of the **Seagen (SGEN)** acquisition **Pfizer (PFE)** updated its FY24 guidance, but both EPS and revenue fell well beneath expectations. **Tesla (TSLA)** recalled 2mln units amid autopilot issues; Tesla will release an over-the-air update (OTA) to fix autopilot control issues. **Southwest Airlines (LUV)** raised its forecast for Q4 fuel costs but expects unit revenue to improve to the higher end of its previous guidance range on the back of strong leisure demand. **ABM (ABM)** beat on EPS and revenue alongside raising dividend ~2% to USD 0.22/shr. **Coherent (COHR)** was downgraded at Morgan Stanley; said the recent share rally captures cos. near-term upside opportunity from AI and machine learning. **Cognyte Software (CGNT)** beat on the top and bottom line alongside FY24 guidance coming in above expectations. After trial results **Vertex Pharmaceuticals (VRTX)** said its drug, VX-548, was successful in reducing nerve pain in patients in a mid-stage trial. Wells Fargo initiated coverage of **Roblox (RBLX)** with an ‘Overweight’ rating; said the potential revenue from advertising on RBLX is underappreciated by the market. CNBC's Faber said that **US Steel's (X)** board is to meet on Wednesday to field bids that are in excess of USD 40/shr. **Etsy (ETSY)** is laying off roughly 11% of its workforce and estimates it will incur roughly USD 25-30mln in charges primarily in Q4 '23. **Apple (AAPL)** is reportedly set to be hit by an EU antitrust order in a fight with **Spotify (SPOT)**, according to Bloomberg; antitrust decision is due in early 2024 and could come with fines. Lending companies **Upstart (UPST)** and **Affirm (AFRM)** saw strong gains as they benefited from lower rates outlook from the Fed.

US FX WRAP

The Dollar was largely flat heading into the FOMC, but that swiftly changed in wake of the dovish FOMC and following Chair Powell’s presser. Recapping, the initial announcement saw the Fed leave rates unchanged, as expected, at 5.25-5.50%, but softened guidance to determining the extent of "ANY" additional policy firming that may be appropriate and moved the 2024 median dot to 4.6% (exp. 4.9%, prev. 5.1%). As such, this saw a broad dovish reaction (stocks, bonds, gold upside & Dollar weakness) with DXY selling off to print an initial low of 103.31 with Fed market pricing implying 127bps of easing through ‘24 (vs. 115bp pre-release). However, as Powell’s presser got underway and he continued the dovish tone by talking down the chances of another rate hike said the timing of rate cuts was discussed at the meeting. The dovish move accentuated to see the Greenback print a low of 102.770 and 141bps of cuts priced in by end ’24. As a result, and as you can guess, all G10 currencies gained off the weaker Buck to rise to strongest levels on the day ahead of Super-Thursday. For the record, November US PPI was unchanged M/M (exp. +0.1%) with the prior revised up to -0.4% from -0.5%, while Y/Y +0.9% (exp. 1.0%, prev. 1.2%). Looking into the details, both the index for final demand goods and services were unchanged.

Sterling was a relative G10 laggard (ex Dollar) following the dismal GDP data on the eve of the BoE, although the data will likely not have any influence on Thursday’s decision, where expectations are for the MPC to stand pat, but it could have some sway on the vote split. In terms of the metrics, Y/Y was worse than expected while M/M surprisingly declined with falls in every sector (services, construction & production). Cable printed a low of 1.2501, before surging to highs of 1.2634 post-Fed. As such, the Pound initially saw losses on Wednesday pre-Fed on account of the aforementioned data, but reversed the move, and some, after the surprise dovish meeting and Powell comments. Ahead of the Fed, the Yen was seeing slight gains amid the broader Dollar softer and pullback in US yields. But of course, as mentioned above after the dovish FOMC rate decision the Yen extended on gains to see USD/JPY print fresh session lows of 142.65. Overnight, the quarterly BoJ Tankan survey was largely better-than-expected, although the outlook for large manufacturers and large non-manufacturers disappointed. Looking to super Thursday, there are rate decisions from ECB, SNB, BoE, Norges Bank, and Banxico.

The ARS got whacked on Wednesday (in excess of 118% vs. the Buck) after Argentina's Economy Minister Caputo said on Tuesday they will move forward with eliminating taxation on exports and will reduce energy and transport subsidies, while FX rate will weaken to 800 pesos per dollar, devaluing the Peso by more than 50%.

The HUF saw some strength against the EUR after EU restored Hungary's access to EUR 10bln of cohesion funds, although three Hungary cohesion policy programmes which have a budget of EUR 6.3bln remain suspended, with overall funding that remains locked amounting to EUR 21bln. More broadly, EMs saw broad strength against the falling Greenback as Brazilian Real and Mexican Peso watchers will be awaiting the respective bank meetings on Wednesday and Thursday.