US Market Wrap

5th February 2024: Stocks and bonds fall on hot data and more hawkish Fed Speak

- **SNAPSHOT**: Equities down, Treasuries down, Crude up, Dollar up.
- **REAR VIEW**: ISM Services PMI beats while prices paid jump; Fed's Powell, Bowman, Goolsbee and Kashkari all on wires; MCD earnings disappoint; CAT earnings beat; CTLT to be bought by Novo Nordisk.
- **COMING UP**: **Data**: UK BRC Retail Sales, Australian Retail Sales, German Industrial Orders, Italian Consumer Confidence, EZ Retail Sales, Canadian Ivey PMI, NZ Jobs data, Australian Construction Index **Events**: RBA Policy Announcement; ECB Consumer Expectations Survey Speakers: RBA post-announcement press conference; Fed's Mester, Harker, Kashkari, Collins; BoC Macklem **Supply**: Netherlands, UK, US **Earnings**: BP, Infineon, UBS, BMPS, Eli Lily, Ford, GE Healthcare, Chipotle.
- **WEEK AHEAD**: Highlights include RBA, Chinese inflation, US ISM Services PMI and US annual CPI revisions. To download the report, please click here.
- **CENTRAL BANK WEEKLY**: Previewing RBA, Banxico, RBI; Reviewing FOMC, BoE, Riksbank and BCB. To download the report, please click here.
- **WEEKLY US EARNINGS ESTIMATES**: [TUES] TM, LIN, LLY, AMGN; [WED] CVS, BABA, UBER, DIS, PYPL; [THURS] AZN, PM, COP, SPGI; [FRI] PEP. To download the full estimates, please click here.

MARKET WRAP

Stocks were lower on Monday but recovered gradually, albeit significantly, from the lows earlier in the session that were seen as part of the broader hawkish reaction to the hot ISM Services. In stocks, Caterpillar (CAT) was firmer despite mixed results and guidance; McDonald's (MCD) fell on disappointing comp sales; Boeing (BA) fell on more 737 problems; Nvidia (NVDA) firmed on a Goldman PT rise. There was a slew of Fed Speak to digest including Chair Powell speaking on 60 Minutes, where he largely stuck to the FOMC script, while the broader tone of Fed Speak has been relatively hawkish, in fitting with Powell's pushback on a March cut. The climb in yields continued to fresh YTD highs amid the hawkish Fed Speak and the busy debt supply calendar, accentuated by the hot ISM Services print, which included an uncomfortable rise in the prices paid component. In FX, the Dollar was bid broadly alongside the rising US yields, with USD/JPY also stretching to new YTD peaks. Oil prices were firmer on Monday, recovering off earlier lows despite the stronger Dollar. However, metals succumbed to the firmer Buck.

US

ISM SERVICES:The US ISM Services PMI in January was hot. The headline rose to 53.4 from 50.5, above the expected 52.0, and above the upper end of the forecast range of 53.2, while prices paid surged to 64.0 (prev. 57.4), the highest since February 2023. Employment lifted back into expansionary territory printing 50.5 (prev. 43.8), while business activity was unchanged at 55.8. Backlog of new orders and supplier deliveries both rose back above 50.0 to 55.0 (prev. 52.8) and 52.4 (prev. 49.5), respectively. Overall, the report is hawkish, and after Friday's US jobs report it is the second figure which provides further tailwinds for those calling for the first cut to happen in May or later. Within the dataset, ISM's Nieves said, "The past relationship between the Services PMI and the overall economy indicates that the Services PMI for January (53.4 percent) corresponds to a 1.5% increase in real GDP on an annualized basis." On the release, Pantheon Macroeconomics adds, "The 2.9-point rise in the headline sounds impressive but a rebound always seemed likely after the sharp December drop". Moreover, PM states, "the data adds to the evidence that the Fed's rate hikes have not yet led to a marked slowdown in the services sector. But some tailwinds for the services sector, most notably, consumers' excess pandemic savings, are now fading", and Pantheon expect growth in services activity to moderate over the next few quarters. Although, the consultancy does conclude it sees little sign of this happening just yet.

Fed Chair Powell, speaking to CBS in an interview aired Sunday but filmed on Thursday, largely repeated what was said at the FOMC press conference last week, repeating March is likely too soon to have confidence to cut rates but the Fed could move sooner if they saw labour market weakness or inflation really persuasively coming down. He also warned that more persistent inflation could mean a later move. Powell also repeated the Fed feels they can approach the rate cut timing question carefully as the economy is strong, but they are making good progress on inflation and he sees inflation continuing to move down through the first six months of the year due to base effects.

Fed's Bowman (voter, hawk), on Friday night, said she expects inflation to decline further with the policy rate held steady, noting it will eventually become appropriate to gradually cut rates if inflation continues to decline but reducing the policy rate too soon could mean more rate hikes are needed in the future, she also remains willing to raise the policy rate at a future meeting if it is needed. Bowman said the slowdown in recent months' inflation data is encouraging, but the January jobs report suggests progress on labour market rebalancing has stalled and there is ongoing elevated wage growth. She warned that upside risks to inflation include labour market tightness, easing financial conditions, and geopolitics. Bowman stated she will remain cautious on policy and is watchful on data as well as revisions.

Goolsbee (2025 voter, dove) repeated he does not want to rule out a March rate cut and reiterated that the economy has been quite strong. When he was quizzed on New York Community Bancorp (NYCB), he said it does not seem to be indicative of a wider issue in the banking system.

Fed's Kashkari (2026 voter, hawkish) released an essay on Monday where he concluded that a possibly higher neutral rate, as suggested by resilient economic growth, particularly in interest rate-sensitive sectors, means the Fed can take more time to assess upcoming data before beginning rate cuts. He noted that a higher neutral rate would mean policy may not be as tight as thought. Going further, he said he believes that commentary that real FFR has tightened dramatically over the past several months as inflation has fallen rapidly with nominal FFR unchanged "overstates changes in the stance of monetary policy." Kashkari did caveat that not all data on the economy is “unambiguously positive,” with some signs of weakness including climbing consumer delinquencies and CRE.

FIXED INCOME

T-NOTE (H4) FUTURES SETTLE 28 TICKS LOWER AT 110-25 Treasury sell-off continues amid a busy supply calendar and a hot ISM Services print. 2s +10.2bps at 4.472%, 3s +11.8bps at 4.268%, 5s +13.1bps at 4.124%, 7s +13.8bps at 4.156%, 10s +13.5bps at 4.166%, 20s +12.3bps at 4.460%, 30s +12.3bps at 4.350%.

INFLATION BREAKEVENS: 5yr BEI +6.4bps at 2.292%, 10yr BEI +5.4bps at 2.265%, 30yr BEI +4.8bps at 2.283%.

THE DAY: Treasuries extended last week's sell-off into the APAC session on Monday with hawkish reaffirmations from Chair Powell on 60 Minutes adding to the expected US supply this week. Selling pressures in APAC were accentuated by an FT article, "BoJ grows more confident about imminent exit from negative rates". Later on, national-level services PMI came in on the hot side in Europe. T-Notes hit support at 111-06+ in the Tokyo morning, then at 111-04 in the London morning.

The gradual decline extended as US participants returned from the weekend and 111-00+ held as support in the NY morning after a fresh wave of corporate supply weighed on USTs ahead of this week's Treasury auctions. However, the bounce in ISM Services, particularly the Prices Paid component, saw another wave of selling to take T-Notes to session lows of 110-22+, falling through the prior YTD lows of 110-26 in Jan, later in the NY morning. Contracts made a feeble recovery attempt before hovering back down towards the lows ahead of the settlement.

THIS WEEK'S AUCTIONS: US to sell USD 54bln of 3yr notes on Tuesday, USD 42bln of new issue 10yr notes on Wednesday, and USD 25bln of new issue 30yr bonds on Thursday; all to settle on Feb 15th. In Europe, the EU is set to tap 10/26 and 4/44 bonds on Monday, the UK is selling 30yr green bonds on Tuesday and 4yr notes on Wednesday, and Germany is selling 7yr notes on Wednesday. In Japan, a 30yr bond on Wednesday and a 5yr note on Friday.

FED PRICING: The implied probability for a March cut has fallen to 15% from 20% on Friday after the jobs data, and the implied probability for a cut by the May meeting has fallen to 75% now vs 90% on Friday. Meanwhile, the amount of cuts priced across 2024 has been slashed to 115bps from 124bps.

STIRS:

- SR3H4 -3bps at 94.77, M4 -6.5bps at 95.12, U4 -8.5bps at 95.51, Z4 -10.5bps at 95.85, H5 -11.5bps at 96.145, M5 -12.5bps at 96.355, U5 -13bps at 96.48, Z5 -13.5bps at 96.53, H6 -13bps at 96.535, H7 -13.5bps at 96.455, H8 -13bps at 96.355.
- SOFR flat at 5.32% as of Feb 2nd, volumes fall to USD 1.849tln from 1.897tln.
- NY Fed RRP op demand at USD 0.552tln (prev. 0.513tln) across 80 counterparties (prev. 80).
- EFFR flat at 5.33% as of Feb 2nd, volumes rise to USD 91bln from 81bln.
- US sold USD 85bln of 3-month bills at 5.235%, covered 2.91x; sold USD 76bln of 6-month bills at 5.045%, covered 2.91x.

CRUDE

WTI (H4) SETTLED USD 1.54 LOWER AT 72.28/BBL; BRENT (J4) SETTLED USD 1.37 LOWER AT 77.33/BBL

Oil prices were lower on Friday despite geopolitical angst and the solid US jobs data, with the strong Dollar weighing. WTI and Brent futures began selling off at the NY handover and extended after the Dollar ripped higher post-NFP, with contracts troughing at USD 71.79/bbl and 76.85/bbl, respectively, later in the NY morning, hovering near lows into the afternoon and settlement. The benchmarks have seen their largest W/W losses since early October as prices retreat back into their multi-month ranges post-last week's breakout. Reports in Sky News Arabia Friday that the US strikes against pro-Iranian militias may begin within hours failed to ignite any meaningful recovery but perhaps limited further downside; NBC, citing officials, reported that Biden has settled on a counterattack plan that is expected to unfold over multiple days, and possibly weeks. There was also further reporting Friday of Hamas and Israel moving further away from a truce offer, but that again failed to lead to any noticeable price recovery after futures sold off on Thursday's fake news of a ceasefire. In the US, the weekly Baker Hughes rig count saw oil rigs unchanged at 499 while nat gas rigs fell two to 117, leaving the total declining by two to 619. Meanwhile, BP's (BP/ LN) Whiting, Indiana, refinery (435k BPD), following Thursday's blackout, has restored power but currently has no date set for its restart, Reuters reported.

EQUITIES

CLOSES: SPX -0.32% at 4,943, NDX -0.17% at 17,613, DJI -0.71% at 38,380, RUT -1.3% at 1,937

SECTORS: Materials -2.52%, Utilities -2.03%, Real Estate -2%, Consumer Discretionary -1.32%, Communication Services -0.82%, Financials -0.61%, Consumer Staples -0.6%, Industrials -0.54%, Energy -0.23%, Health +0.31%, Technology +0.58%.

EUROPEAN CLOSES: DAX: -0.08% at 16,904.06, FTSE 100: -0.04% at 7,612.86, CAC 40: -0.03% at 7,589.96, Euro Stoxx 50: -0.02% at 4,653.85, IBEX 35: -1.20% at 9,941.30, FTSE MIB: +0.76% at 30,952.79, SMI: +0.31% at 11,274.20.

EARNINGS:

- **Air Products and Chemicals (APD)** -16%: Missed on profit and revenue, with next quarter and FY EPS guidance light.
- **Caterpillar (CAT)** +2%: EPS beat driven by higher operating margins with revenue in line. FY24 top line seen "broadly similar" to FY23 (exp. +0.5%) and Q1 also "broadly similar" Y/Y (exp. +1.5%).
- **Estee Lauder (EL)** +12%: EPS and revenue surpassed Wall St. expectations but did cut FY profit view. Moreover, it is to lay off 3-5% of its global workforce.
- **McDonald's (MCD)** -4%: Revenue and global comp. sales fell short but profit beat.
- **Tyson Foods (TSN)** +2%: Topped Wall St. expectations on EPS and revenue.
- **ON Semiconductor (ON)** +10%: Q4 headline metrics beat, as did gross margin, but next quarter guidance was slightly disappointing.

STOCK SPECIFICS:

- **Apple (AAPL)** +1%: iPhone assembler Foxconn expects its business this year to be "slightly better" than last year but is facing a shortage of chips for AI servers.
- **Boeing (BA)** -1.3%: Delays around 50 undelivered 737 Max after new quality defect due to mis-drilled holes discovered by supplier Spirit AeroSystems (SPR).
- **Catalent (CTLT)** +10%: To be acquired by Novo Nordisk parent co. for USD 63.50/shr. Note, CTLT closed on Friday at USD 54.51/shr.
- **Elanco (ELAN)** +8%: Merck (MRK) to acquire Elanco's Aqua business for USD 1.3bln.
- **GlobalFoundries (GFS)** -7%: Downgraded at JPM
- **Nvidia (NVDA)** +5%: GS raised the firm's PT to USD 800 (prev. USD 625) and keeps a Conviction Buy rating. Heading into Cos. Q4 results, sees constructive data points on gen AI infrastructure spending, material upside to 2024 and 2025 St. expectations and compelling risk/reward profile for the shares.
- **DocuSign (DOCU)** -8.5%: Potential PE suitors, Bain Capital and Hellman & Friedman, "have cooled" their pursuit of the Co., according to Reuters sources.
- **MorphoSys (MOR)** +56%: Novartis (NOVN SW) is reportedly in advanced discussions to acquire MorphoSys, according to Reuters citing sources.
- **Paramount (PARA)** -2.8%: Byron Allen says he’s begun talks with Paramount on buyout bid, according to Bloomberg.

US FX WRAP

The Dollar was bid on Monday with upside in UST yields supporting. Over the weekend, Powell on CBS repeated that a March cut is seen as too early while Bowman also said she is prepared to hike further if needed, while also cautioned against early rate cuts. Meanwhile, Fed's Goolsbee put emphasis on the need to see more data and Kashkari touted a potentially higher neutral rate as giving the Fed leeway to be patient on when it begins cutting. Data was also strong with the US Services PMI topping expectations with a large increase in the prices paid component.

The Euro was softer vs the buck with EUR/USD falling sub 1.0750 after failing to convincingly rise above the 100dma at 1.0782 while support was seen around the December low at 1.0723 before paring somewhat into the US close. There was little reaction on the final EZ PMI data but Tuesday's ECB consumer inflation expectation survey will be in focus.

The Yen continued its decline to see USD/JPY hit a fresh high of 2024 at 148.89 with moves continuing from Friday's hot US NFP while the upside in Treasury yields only supported the decline with yield/policy differentials narrowing between the US and Japan. There was attention on an FT article from the weekend too, "BoJ grows more confident about imminent exit from negative rates". CHF and XAU also saw weakness on the Dollar strength and upside in yields while EUR/CHF was flat.

Aussie and Kiwi were sold vs the Dollar, with weakness more observed in the Aussie on China woes after a miss in the Chinese Caixin Services PMI. CNH was flat however but there were more actions of support out of China where Chinese brokerages, including CICC, restrict cross-border swaps to control short-selling of stocks, according to Reuters sources. For the Aussie, attention turns to the RBA overnight, please click here for the Newsquawk Preview.

Sterling was the relative laggard with the Pound hit vs both the Dollar and the Euro. Cable fell beneath the 200dma at 1.2564 to lows of 1.2519 in the US session. There was little reaction to the ONS re-weightings which put the unemployment rate at 3.9% (prev. 4.2%), which enhances the case for the BoE to hold rates at current levels, albeit, concerns over data quality remain. There was also commentary from BoE's Pill who repeated that it is too early to say inflation has been suppressed, noting that he is not yet confident in inflation to reduce rates.

LatAm FX was impacted by a rising Dollar and commodity pressures. BRL was softer as iron ore prices fell while CLP and PEN saw notable downside on weak copper prices. COP was weaker however despite upside in oil, MXN was flat.

In CEE, both HUF and PLN were sold vs the Euro while there was only marginal weakness in CZK.

The Lira weakness continued on Monday after CBRT Governor Erkan resigned on Friday. Turkish President Erdogan has since appointed Fatih Karahan to head the Central Bank and in her first speech on Sunday evening pledged to maintain a tight monetary stance to get inflation under control; Cap Eco writes that as things stand, continuity in monetary policy looks set to continue. Meanwhile, the latest inflation data came in hotter than expected at 6.7% M/M in January with the Y/Y print a touch above forecast at 64.7%.