US Market Wrap

15th May 2024: Stocks and bonds rally after soft CPI boosts Fed rate cut bets

- **SNAPSHOT**: Equities up, Treasuries up, Crude up, Dollar down
- **REAR VIEW**: Soft headline CPI, analysts see Core PCE between 0.2-0.26%; Soft US Retail Sales; NY Fed Manufacturing disappoints; Mester echoes Powell (pre-data), Schmid is prepared to be patient (pre-data), Kashkari happy to keep policy where it is for a while longer (post-data); Surprise crude stock draw; NFLX reaches 40mln global MAUs on ad supported plan;
- **COMING UP**: **Data**: Japanese GDP, Australian Employment, Italian CPI (F), US IJC, Philly Fed **Speakers**: BoE's Greene; Fed's Harker, Mester, Bostic, Barr **Supply**: Japan, Spain, France, US **Earnings**: Deutsche Telekom, Siemens, Sage, easyJet, Applied Materials, Bath & Body Works, Deere, Walmart.

MARKET WRAP

The highlight of the day was the softer than expected US CPI report which saw markets back to fully pricing in two rate cuts this year, with the first move now fully discounted by September. Stocks and bonds were instantly bid and despite some post data chop, both finished the day around highs, with the S&P 500 closing at a fresh ATH. The soft CPI was the key driver, although a weak Retail Sales report supported the moves. The Buck was the FX laggard, with the DXY falling from a peak of 105.06 to a trough of 104.300 while Treasuries were bid across the curve to see the 10yr yield fall from c. 4.45% to a low of 4.34%. The move lower in yields supported both Gold prices and the Yen while cyclical currencies also benefited from the rally in stocks. Bitcoin also rose to the highest level since April 24th, but meme stocks (AMC, GME) were hit after their rocket trip to the moon seen earlier in the week. Crude prices sold off throughout the US morning and saw a fleeting bid on the US data, but ultimately settled in the black after a surprise draw in the EIA inventory data. Note, that after the CPI data, many analysts started to release their forecasts for Core PCE, the Fed's Preferred gauge of inflation, which is expected now to come in between 0.20-0.26% but the import price data tomorrow could have some sway on these forecasts (via WSJ's Timiraos who compiled analyst forecasts). Fed's Kashkari spoke after the data, but he reiterated the Fed line that they need to keep rates on hold for a while longer to figure out where inflation is headed, a message likely to be echoed by the several Fed speakers due throughout the rest of the week, given the CPI data is just one data release.

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CPI: The CPI data was a touch cooler than expected with the headline M/M at 0.31% (exp. 0.4%, prev. 0.4%), while the Y/Y headline eased to 3.4%, in line with analyst expectations. The annualized numbers saw 3mth at 4.6% (prior 4.6%), 6mth at 3.7% (prior 3.2%). The core numbers came in at 0.292% M/M, in line with the 0.30% forecast, edging down from the prior 0.4%. The Y/Y was also in line at 3.6%, down from the prior 3.8%. Although a welcome report, particularly after the slew of hot reports in Q1, the Fed will likely stress that inflation is still too high and they still need more confidence that inflation is heading back to 2% in a sustainable manner, and given this is just one report, more data will be needed. The Fed will also likely continue to convey a higher for longer message to ensure inflation returns to target. Nonetheless, it does help support the argument that perhaps the Q1 data was just a "bump", but it would be wise not to draw conclusions just from one report. A cooler headline inflation number and cooler components of the PPI report on Tuesday do bode well for a cooling PCE number at the end of the month, the Fed's preferred gauge of inflation. Capital Economics writes that Core CPI was even better than it looked, and given the soft PPI PCE components released on Tuesday, the desk now estimates core PCE increased 0.2% M/M. Cap Eco adds that all things considered, it is consistent with a Fed rate cut in September.

US RETAIL SALES: Retail sales M/M was much cooler than expected coming in at 0.0% (exp. 0.4%, prev. 0.6%), with ex-autos 0.2% (exp. 0.2%, prev. 0.9%) and ex gas/autos -0.1% (prev. 0.7%). Retail Control fell 0.3% against the expected 0.1% rise and the prior 1.0%. On the data set, Oxford Economics notes "the fact that retail sales growth stalled is not a major concern since it mostly reflects a drop back in nonstore sales following the end of a one-off Amazon sales event that boosted April sales." As a result, Oxford estimates real consumption growth edged back in May, which together with downward revisions to previous months pushed its tracking estimate of real consumption growth in Q2 down to 2% annualized, suggesting a small downside risk to its baseline forecast for growth of 2.4%. Moreover, consumer spending is slowing as elevated interest rates weigh on rate-sensitive spending and as the labour market cools. As such, OxEco adds, “With aggregate balance sheets solid and the labor market cooling rather than collapsing, we expect that slowdown will remain gradual.”

NY FED MANUFACTURING: NY Fed Manufacturing was worse than feared, printing -15.6 (exp. -10.0, prev. -14.3) with the internals mixed. New orders and employment declined deeper into negative territory to -16.5 (prev. -16.2) and -6.4 (prev. -5.1), respectively. The inflationary gauge of prices paid dipped to +28.3 (prev. +33.7), albeit still remaining elevated, with prices received +14.1 (prev. +16.9). Shipments dramatically improved to -1.2 (prev. -14.4), while Delivery Times worsened and Inventories held pretty steady. Forward-looking indicators saw the six-month business conditions dip to +14.5 from +16.7, however, the prices paid outlook marginally rose to 41.4 (prev. 40.4) and prices received dipped to 24.2 (prev. 29.2). Within the report, the Economic Research Advisor at the New York Fed said “Manufacturing conditions remained sluggish in New York State in May, with activity and orders continuing to decline. Labor market conditions were also weak, as employment and hours worked both fell.”

FED'S MESTER (2024 voter, retiring): The WSJ posted an interview with Mester (voter) after-hours on Tuesday and she largely conveyed Chair Powell's message earlier in the day. Mester said the Fed is in a good place to study the economy before charting a rate path and she continued to highlight the high bar for hikes as she noted she isn't eager to consider a rate hike. The Cleveland President added it was appropriate for the Fed to hold rates steady as it awaits evidence that price pressures are easing further, again very in fitting with the broad message. Mester said it’s too early to conclude that they stalled out or that inflation is going to reverse but noted there are definite signs that the real side of the economy is moderating which is helping to bring balance back to the economy.

FED'S SCHMID (2025 voter): Said policy is in the correct place and continued vigilance and flexibility are necessary, while he is prepared to be patient as inflation eases back towards 2%. Schmid added inflation is still too high and the Fed has more work to do. He further noted interest rates could remain high for some time and doesn't think they should have slowed the balance sheet runoff.

FED'S KASHKARI (2026 voter): Kashkari spoke after the US CPI data, maintaining language that the Fed probably needs to keep policy where it is for a while longer to figure out where inflation is headed, reiterating that the biggest question now is how restrictive policy levels are. Kashkari said the Fed us focussed on underlying demand in the economy to get inflation down and the Fed is committed to achieving its 2% inflation goal. However, he did state that with higher US government debt, it might take higher borrowing costs in the near-term to achieve the 2% inflation goal. On the economy, the Minneapolis Fed President said that consumers are spending more than he would have expected, while he is very focused on housing and that it has been more resilient than he expected.

FIXED INCOME

T-NOTE FUTURES (M4) SETTLE 20 TICKS HIGHER AT 109-23

T-Notes rallied across the curve after soft US CPI and Retail Sales. 2s -9.1bps at 4.728%, 3s -10.5bps at 4.511%, 5s -10.8bps at 4.350%, 7s -10.1bps at 4.346%, 10s -9.1bps at 4.354%, 20s -8.5bps at 4.610%, 30s -7.6bps at 4.517%.

INFLATION BREAKEVENS: 5yr BEI -2.1bps at 2.310%, 10yr BEI -1.9bps at 2.320%, 30yr BEI -1.4bps at 2.331%.

THE DAY: T-notes rallied on the soft headline CPI data which helped offset some fears after the hot Q1 inflation prints and thus saw markets start to price in more rate cuts from the Fed with two cuts now fully priced by the end of the year, with the first cut fully priced (just) for September. T-notes peaked at 109-26+ directly after the CPI data (as well as cool Retail Sales and a weak NY Fed Manufacturing survey) before paring somewhat after. Nonetheless, once analysts’ forecasts for PCE started arriving, the bid gradually resumed to near the post CPI peaks ahead of settlement with Core PCE, the Fed's preferred gauge of inflation, expected to come in between 0.20-0.26% M/M. There was also commentary from Fed's Kashkari (2026, hawk) post data, but he did little to shift the dial, noting that the Fed is still focused on underlying demand in the economy to get inflation down, warning it might take higher borrowing costs in the near-term to achieve the 2% inflation goal due to higher US government debt. He also repeated the Fed line that they probably need to sit here for a while longer, to figure out where inflation is headed.

AHEAD: With the major risks out the way for the week, attention now turns to Fed speakers on Thursday and Friday (primer & schedule here). On Thursday, highlights are the US Jobless Claims, which come after a surge last week, as well as Housing Starts and Import Price data, with the latter potentially having implications for PCE forecasts at the end of the month. We also see next week's 10yr TIPS and 20yr bond announcement, and Fed speak from Barr, Harker, Mester and Bostic.

STIRS

- SR3M4 +2.0bps at 94.770, U4 +0.0bps at 94.945, Z4 +7.5bps at 95.190, H5 +10.5bps at 95.470, M5 +12.5bps at 95.710, U5 +13.5bps at 95.895, Z5 +13.5bps at 96.025, H6 +14.0bps at 96.120, M6 +13.5bps at 96.175, M7 +11.0bps at 96.265, M8 +9.5bps at 96.225.
- US sells USD 60bln in 4-month bills at 5.235%, covered 2.98x
- NY Fed RRP op demand at USD 0.444tln (prev. 0.468tln) across 74 counterparties (prev. 76)
- SOFR at 5.31% (prev. 5.31%), volumes at USD 1.838tln (prev. 1.805tln).
- EFFR at 5.33% (prev. 5.33%), volumes at USD 76bln (prev. 76bln).

CRUDE

WTI (N4) SETTLES USD 0.51 HIGHER AT 78.16/BBL; BRENT (N4) SETTLES USD 0.37 HIGHER AT 82.75/BBL

Crude prices ultimately settled slightly green with morning weakness reversed after a larger-than-expected draw in EIA crude inventories and a weaker buck post soft CPI. WTI and Brent hit lows of USD 76.70/bbl and USD 81.05/bbl, respectively ahead of the data. The downside appeared with a lack of fundamental reasoning although some upside was observed after the soft-leaning US CPI report, weighing on the Dollar, supporting global growth prospects, thus boosting crude prices. Nonetheless, any CPI-related crude strength was shortlived before continuing its move lower into inventory data with the move in the dollar initially paring. The data saw crude stocks draw by 2.5mln bbls, much deeper than the expected 540k draw, while distillates and gasoline also posted surprise draws. The bullish inventory data saw crude stocks trend higher into settlement with renewed weakness in the Dollar also supporting once the dust settled from CPI and the typical dovish reaction ensued (stocks, bonds gold, higher, dollar lower). Elsewhere, the IEA OMR cut its 2024 oil demand growth forecast by 140k BPD to 1.1mln, while it raised its 2025 world oil demand growth forecast to 1.2mln BPD from a prior estimate of 1.1mln. On production, Colombia is closing in on average oil production of close to 800k BPD, according to the oil regulator President. The Congo Oil Minister, via Energy Intel, said his country is not “battling” for a higher baseline In the coming 2-3 years, and that Congo plans to increase production by 40-50%.

EQUITIES

CLOSES: SPX +1.17% at 5,308, NDX +1.49% at 18,597, DJI +0.88% at 39,908, RUT +1.14% at 2,109

SECTORS: Technology +2.29%, Real Estate +1.69%, Health +1.44%, Utilities +1.41%, Communication Services +0.91%, Financials +0.72%, Industrials +0.63%, Materials +0.16%, Energy +0.15%, Consumer Staples +0.02%, Consumer Discretionary -0.01%.

EUROPEAN CLOSES: DAX: +0.85% at 18,875.35, FTSE 100: +0.21% at 8,445.80, CAC 40: +0.17% at 8,239.99, Euro Stoxx 50: +0.41% at 5,101.15, IBEX 35: +1.10% at 11,362.80, FTSE MIB: +0.61% at 35,366.20, SMI: +1.02% at 11,904.06

STOCK SPECIFICS:

- **Boeing (BA) -**2%: DoJ says the Co. violated 737 MAX settlement.
- **Nextracker (NXT)** +7%: EPS and revenue beat, with FY EBITDA guidance better than expected.
- **Infinera (INFN)** -8%: Deeper loss per share, revenue missed with light next quarter outlook.
- **Monday.com (MNDY)** +21%: Top and bottom-line surpassed consensus, with strong Q2 and FY revenue guide.
- **New York Community Bancorp (NYCB) -**5.5%: Agrees to sell approx. USD 5bln in mortgage warehouse loans to JPMorgan Chase Bank (JPM).
- **DLocal (DLO)** -26%: All major metrics missed in its Q1 report.
- **Petrobras (PBR) -**7%: Brazil President Lula dismisses Petrobras CEO Jean Paul Prates; board asked to negotiate over the ending of his term.
- **Netflix (NFLX)** flat: Reaches 40mln global MAUS on its ad-supported plan; is to launch an in house advertising technology platform by the end of 2025, via Presentation. Also, reportedly nears deal for NFL games, and is continuing push into sports, according to Bloomberg.
- **Apple (AAPL)** +1.2%: New accessibility features are coming later this year; eye tracking comes to iPad and iPhone.

US FX WRAP

The Dollar sold off on Wednesday after the headline CPI came in beneath expectations, boosting Federal Reserve rate cut bets slightly. Although this is just one data release, it is an encouraging sign after the string of hot Q1 inflation reports, and thus will be a welcome sign to the Fed, but they will likely need to see more evidence of inflation narrowing.

Many economists, who use CPI and PPI to calculate PCE, have released their Core PCE forecasts and the current range is between 02-0.26% (via WSJ's Timiraos). DXY hit a low of 104.300, taking out the May low of 104.52 with technicians eyeing 104.00 to the downside. Note, Retail Sales data was also softer than expected while the NY Fed Manufacturing was worse than expected.

The Euro was bid thanks to the softer buck helping EUR/USD rise back above 1.0850 with Fed rate cut pricing leaning towards a September rate cut, narrowing the policy differentials between the ECB and Fed with the ECB looking set to cut in June. EUR/USD peaked at 1.0880, just shy of the April high at 1.0885. Note, EU Flash GDP for Q1 was in line with forecasts at 0.3%, with employment data also in line with expectations.

The Yen was among outperformers on Wednesday as the lower Dollar and lower UST yields post CPI gave the Japanese currency a helping hand, a move Japanese officials will be pleased to see after the pronounced weakening seen this year, prompting FX intervention from around the 160.00 mark in USD/JPY. USD/JPY fell from a peak of 156.56 to a low of 154.70 at pixel time. The Franc and Gold also saw decent strength on account of the lower UST yields post CPI.

Antipodes also outperformed with the Yen, but the Kiwi took the top spot in terms of performance, with both Aussie and Kiwi benefitting from the risk on trade while both were supported pre-data anyway on reports regarding China support. Bloomberg reported that China is considering government purchases of millions of unsold homes to ease the glut, while Beijing is seeking feedback on the preliminary proposal. Note, both offshore (CNH) and onshore Yuan (CNY) were firmer vs the Dollar on Thursday. Meanwhile, for the Aussie, wage data came in slightly softer than expected in Q1, hence the downside in AUD/NZD to sub 1.0950.

GBP saw notable gains vs the Dollar and slight gains vs the Euro with Cable rising above 1.2600 and 1.2650 with the Pound doing well in quiet trade post CPI, as well as the risk on environment.

Scandis both saw gains vs the Euro in the risk on trade while Swedish CPI was actually cooler than expected, resulting in choppy price action for the SEK vs the Euro, but the Viking cross, NOK/SEK, was bid.

EMFX was mixed, MXN saw notable gains vs the Dollar in quiet trade post soft US CPI while BRL was weaker vs the buck, but CLP and COP saw gains on account of gains in the copper and oil space, respectively. For the BRL, it is worth noting local markets were hit on account of the Petrobras (PBR) CEO being fired by President Lula. For the COP, worth noting that Colombia's economy grew 1.1% Q/Q in Q1, short of the 1.2% forecast, and 0.7% Y/Y, in line with forecasts.