



28th May 2024: Soft auctions support yields, at the expense of stocks

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- **SNAPSHOT:** Equities mixed, Treasuries down, Crude up, Dollar flat.
- **REAR VIEW:** Hot Consumer Confidence with rising inflation expectations; Weak 2- and 5-yr auctions; Fed's Bowman would have supported waiting before slowing QT, or for a more tapered run off; Kashkari will no be pencilling more than two cuts this year; China takes property market measures; Israel strikes Rafah over the weekend.
- **COMING UP: Data:** NZ ANZ Business Outlook, Australian CPI, German GfK Consumer Sentiment, Spain Retail Sales, German CPI, US Richmond Fed Index **Speakers:** Fed's Williams, Bostic; BoJ's Adachi **Supply:** Australia, UK, Germany, US **Earnings:** Telecom Italia, HP, Salesforce.

MARKET WRAP

US equity indices were mixed on Tuesday, as traders returned from the long weekend; Nasdaq-100 was supported by continued upside in NVDA post-earnings, while the S&P and Russell 2000 lag, and the DJIA underperforms (-0.7%). Stocks fell out of their horizontal trading patterns in wake of an upside surprise in the US Consumer Confidence metrics, which saw inflation expectations tick up, while soft 2yr and 5yr note auctions resulted in higher yields, with the supply greeted by weak demand ahead of this week's PCE data (and Eurozone inflation metrics, and the forward-looking Tokyo CPI Data—all due for release at the end of the week). Fedspeak failed to add anything incremental to the narrative, although Fed's Kashkari once again warned that if inflation does not progress lower, then rate hikes could be on the agenda. Treasury yields rose in the wake of soft auctions, helping USD pare losses and inch into positive territory towards the end of the session, although the buck is now ultimately flat on the session. Crude futures rose in spite of the USD paring losses, with traders citing geopolitical events over the long weekend as a supporting factor for crude.

US

CONSUMER CONFIDENCE: The Conference Board's gauge of US consumer confidence surprisingly rose from 97.5 in April to 102.0 in May (the most optimistic forecast was for 101.0), with the headline likely also supported by easing gas prices and rising equities last month. Current conditions rose from 140.6 to 143.1, while expectations (which comprise around 60% of the headline) also picked up from 68.8 to 74.6. Pantheon Macroeconomics note "the rebound in expectations matters, as the index is a better guide to growth in consumer spending than the headline". Going forward, Pantheon expects confidence to take another knock over the next couple of quarters, given the raft of indicators pointing to a weaker labour market. On the inflation front, consumers' average 12-month inflation expectations ticked higher to 5.4% M/M (prev. 5.3%), which may have been the cause of the increase in the share of consumers expecting higher rates over the year (at 56.2% from a prior 55.2%). Fewer participants said jobs were "hard to get" compared to the prior month, and slightly fewer consumers said business conditions were "good", whereas the number of consumers that said "bad" remained unchanged from April.

FED GOVERNOR BOWMAN said that she would have supported either waiting to slow the QT pace, or for a more tapered slowing in the balance sheet runoff. In her view, bank reserves are not yet near 'ample' levels given the still-sizable take-up of ON-RRP. Bowman said it is important to keep reducing the balance sheet size to reach ample reserves as soon as possible and while the economy is strong. She also acknowledged it is important to communicate that any change to the run-off rate does not reflect a change in the Fed's monetary policy stance. Bowman 'strongly' supports the principle of balance sheet holdings primarily being composed of Treasuries, noting a longer-run balance sheet 'tilted slightly' toward shorter maturities would allow flexibility in approach. In the future, when the Fed conducts QE to restore market functioning or financial stability it should communicate that purchases will be temporary and unwound when market conditions have normalised. The FOMC would have benefited from an earlier decision to taper and end QE in 2021; it would have also allowed earlier rate hikes.

FED'S KASHKARI (non-voter) said that the central bank should wait for significant progress on inflation before cutting rates, and it could even potentially lift rates if inflation fails to come down further (he has made similar arguments recently), and went on to say that he does not think anyone has taken potential rate hikes off the table. The Minneapolis



Fed chief added that rates could stay on hold for an indefinite period of time, and later said he would not be pencilling in more than two rate reductions this year. Kashkari reiterated the risks he sees around CRE, and he remains confident on growth, stating that weakness in the economy is not needed to get inflation lower, despite the US labour market remaining tight. Elsewhere, he said that the short-run neutral rate may have gone up temporarily.

FIXED INCOME

T-NOTE (M4) FUTURES SETTLE 13 TICKS LOWER AT 108-09+

T-notes bear steepened with pressure observed in wake of hot consumer confidence, rising inflation expectations and weak 2- and 5-yr auctions. At settlement, 2s +1.9bps at 4.972%, 3s +2.8bps at 4.751%, 5s +5.0bps at 4.581%, 7s +5.9bps at 4.555%, 10s +6.5bps at 4.538%, 20s +7.4bps at 4.746%, 30s +7.5bps at 4.652%.

INFLATION BREAKEVENS: 5yr BEI +2.2bps at 2.359%, 10yr BEI +1.5bps at 2.345%, 30yr BEI +1.3bps at 2.337%.

THE DAY: T-Notes meandered overnight before hitting highs in the US, morning tracking EGBs higher after dovish consumer inflation expectations from the Eurozone, while ECB speak saw Holzmänn repeat he would support a 25bp cut in June, and Knot said policy rates will slowly but gradually move to less restrictive levels; ECB are expected to cut rates by 25bps next week. T-Notes peaked at 108-29 before the selling ensued across the curve hot consumer confidence data in the US, which was accompanied by rising inflation expectations. Selling pressure accelerated after a weak 2yr auction before lows of 108-08 were seen pre settlement in the aftermath of the also weak 5yr supply; 5yr yields hit the highest levels since early May. Attention turns to 7yr supply on Wednesday, ahead of the 2nd estimate of US GDP on Thursday, and of course Friday's Core PCE data, not to mention several Fed speakers jotted throughout the week.

2YR AUCTION: Overall a relatively weak auction, the high yield saw a chunky 1bp tail, a sign of much lower demand vs last months auction which saw a stop through of 0.6bps, with a six auction average of a stop through of 0.2bps. The Bid-to-cover was also soft at 2.41x (prev. 2.66x, six auction average 2.59x). The soft demand was led by a large step back from indirect bidders, which took just 57.91% of the auction, beneath the 66.2% prior and average of 63.5%. Nonetheless, direct bidders saw a decent uptake, taking 25.52%, above the 19.7% prior and 20.5% average. Despite the increase of direct demand, it was not enough to completely offset the drop in indirect bidders, leaving dealers with a slightly above prior and average of 16.57%.

5YR AUCTION: After the relatively weak 2yr auction, the 5yr auction was also soft with bidders perhaps sat on the sidelines ahead of US Core PCE due on Friday. The 4.553% high yield tailed the when issued by 1.3bps, a chunkier tail than the prior 0.4bps and vs the six auction average stop through of 0.1bps. The bid cover of 2.3x was beneath the prior and averages. Unlike the 2yr auction, direct demand saw a step back to just 15.44% from 19.2%, while indirect demand was relatively unchanged at 65.04%, only a touch beneath the six auction average of 66.1%. Still, the drop in direct demand saw dealers, the forced surplus buyers, take home 19.5%, above the average 16.0% and prior of 15%.

STIRS:

- SR3M4 -0.5bps at 94.700, U4 +0.5bps at 94.865, Z4 -2.5bps at 94.970, H5 -2.5bps at 95.175, M5 -3.5bps at 95.365, U5 -3.0bps at 95.555, Z5 -3.5bps at 95.705, H6 -4.0bps at 95.820, M6 -5.0bps at 95.895, M7 -7.5bps at 96.045, M8 -7.5bps at 96.065.
- US to sell USD 60bln 17-week bills on May 29th; to sell USD 70bln 4-week bills (prev. USD 80bln) and USD 70bln 8-week bills (prev. USD 80bln) on May 30th, all to settle on June 4th.
- US sold USD 75bln 6-month bills at a high rate 5.170%, B/C 3.06x; sold USD 75bln 3-month bills at high rate 5.255%, B/C 2.87x.
- US sold USD 65bln 42-day CMBs at a high rate of 5.275%, B/C 3.07x.
- NY Fed RRP op demand at USD 0.418tln (prev. 0.431tln) across 71 counterparties (prev. 79)
- SOFR at 5.32% (prev. 5.31%), volumes at USD 1.909tln (prev. 1.916tln).
- EFR at 5.33% (prev. 5.33%), volumes at USD 90bln (prev. 82bln).

CRUDE

WTI (N4) SETTLED USD 2.11 HIGHER AT 79.83/BBL; BRENT (Q4) SETTLED USD 1.06 HIGHER AT 83.94/BBL

Crude futures were bid on Monday amid heightened geopolitical escalations following Israel's recent strikes on Rafah but ultimately settled off highs as the USD pared losses as yields rose. Traders will be eying inflation data out of the Eurozone and the US later in the week, and navigating some Fed speak, but energy focussed traders are also



beginning to focus on the OPEC+ meeting (Sunday, 2/Jun), where the cartel and its partners are expected to hold policy at their virtual confab. In deal news, Hess (HES) shareholders approved the USD 53bln merger with Chevron (CVX), though analysts note that there is still uncertainty with Exxon (XOM) over Guyana assets creates uncertainty given Exxon's alleged right of first refusal over Hess' assets in Guyana, which are currently operating under a joint agreement. Elsewhere, Energy Transfer (ET) has agreed to purchase WTG Midstream for USD 3.25bln, with the deal involving eight gas plants, two of which are under construction. NOTE: the discrepancy between Brent and WTI settlements today is likely due to the lack of WTI settlement on Monday on account of the public holiday.

EQUITIES

CLOSES: S&P 500 +0.0%, Dow Jones Industrial Average -0.6%, Nasdaq-100 +0.3%, Russell 2000 -0.2%.

SECTORS: Consumer Cyclical -0.1%, Consumer Staples -0.8%, Energy +1.1%, Financials -1.1%, Healthcare -1.3%, Industrials -1.3%, Materials -0.4%, Real Estate -0.6%, Technology +1.4%, Communications +0.5%, Utilities -0.1%.

EUROPEAN CLOSES: DAX: -0.48% at 18,684.66, FTSE 100: -0.76% at 8,254.18, CAC 40: -0.92% at 8,057.80, Euro Stoxx 50: -0.61% at 5,028.15, IBEX 35: -0.44% at 11,276.00, FTSE MIB: -0.29% at 34,659.55, AEX: -0.42% at 912.23

STOCK SPECIFICS:

- **Apple (AAPL):** iPhone sales in China surged in April, according to Reuters citing a data firm. Note, the WWDC will start on June 10th.
- **Micron (MU):** Reportedly plans to produce advanced DRAM in Japan by the end of 2027, according to DigiTimes.
- **Texas Instruments (TXN):** Elliott takes a USD 2.5bln stake in co, according to CNBC.
- **T-Mobile (TMUS):** TMUS is to acquire UScellular's (USM) wireless operations for USD 4.4bln.
- **DraftKings (DKNG):** Illinois senators approve budget that includes raising sports betting tax.
- **Vista Outdoor (VSTO):** CSG raised its offer to buy VSTO to USD 1.96bln, according to NYT.
- **Merck (MRK):** Announced P3 Keynote-522 trial met its overall survival endpoint.
- **AstraZeneca (AZN):** The TROPION-Lung01 P3 trial did not reach statistical significance in the overall trial population.
- **PayPal (PYPL):** Co. is planning an ad business, using the data of its customers, according to the WSJ.
- **Boeing (BA):** Awarded a USD 7.58bln Air Force contract.
- **Starbucks (SBUX)** set to resume union negotiations as it tackles issues at its stores, according to CNBC.
- **Hess (HES)** shareholders approve USD 53bln merger with **Chevron (CVX)**.

US FX WRAP

The Dollar was relatively flat on Tuesday, with the DXY trading in a tight parameter of 104.33 and 104.64. The lows were seen as US players arrived before paring any early session losses after a much stronger than expected Consumer Confidence report which also saw the 12mth inflation expectations move higher to 5.4% from 5.3%. The buck then pared losses slightly before a move higher in yields in the aftermath of two soft US 2yr and 5yr note auctions helped support the buck, albeit unchanged on the session.

The Euro was also flat vs the Dollar in tight trading ranges ahead of key risk events later in the week, namely the Eurozone HICP, US Core PCE and Tokyo CPI data on Friday. Nonetheless, in the Eurozone, the April consumer inflation expectations eased to 2.9% from 3.0% in the 1yr and to 2.4% from 2.5% in the 3yr, while the growth outlook was seen as less negative and the labour market was seen stable.

The Yen was marginally weaker on Tuesday with USD/JPY reclaiming 157.00 to the upside in wake of the move higher in UST yields post auctions, with the yield differentials weighing on the Yen, and boosting the Dollar.

Cyclical currencies were generally flat vs the buck, with Aussie, Kiwi and the Pound flat. Antipodes pared early strength as the dollar made a comeback while stocks sold off post open. For the Pound, with the election on July 4th, polls have Labour well in the lead, but some suggest a poll released later tonight will show an easing of the Conservative-Labour gap. The CAD sold off vs the buck with little reaction to hotter than expected PPI data.

CHF was the relative outperformer for the majority of the session but as UST yields ascended post hot consumer confidence and weak US auctions, it gave back its gains vs the Dollar and was ultimately flat.

The Yuan was flat vs the buck on both onshore and offshore. Note that China's Shanghai, Shenzhen and Guangzhou all released new measures targeting the Chinese property market.



EMFX was mixed: BRL saw mild gains while MXN saw notable weakness. ZAR remains in focus ahead of elections with the Rand strengthening into election day. Note, support for South Africa's governing African National Congress (ANC) has settled around 42% in the days leading up to Wednesday's election, according to a Social Research Foundation poll cited by Reuters.

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