US Market Wrap

30th May 2024: Stock slide continues despite bond relief rally ahead of PCE

- **SNAPSHOT**: Equities down, Treasuries up, Crude down, Dollar down
- **REAR VIEW**: Q1 GDP and Core PCE revised lower; Fed's Williams sticks to script; US to restrain AI chips sales to the Middle East; Cooler Spanish Headline CPI Y/Y; Cautious BAC trading update; Woeful CRM guidance; OPEC+ sources suggest extension of voluntary cuts; Large crude stock draw, but gasoline and distillates see large build.
- **COMING UP**: **Data:** Japanese Tokyo CPI, Retail Sales, Chinese PMIs, German Import Prices, Retail Sales, French CPI, EZ CPI, US PCE (Apr), Canadian GDP **Events**: France Credit Rating Review ** Speakers:** Fed's Bostic **Supply**: Australia

MARKET WRAP

Risk off conditions continued on Thursday, though Treasury yields saw some reprieve, falling by 5-8bps. Equities were trading on the back foot from the get-go, and only briefly rallied following the second look at US GDP data in Q1 (headline cooled as expected, and many of the inflation gauges cooled, while consumer spending was revised lower). However, the upside proved fleeting. In terms of the micro, there was a mixed performance from the retailers in earnings reports (KSS was particularly disappointing, though DG fared better), while the tech and communications sectors were dragged lower after a dismal update from CRM afterhours on Wednesday; there were further reports in the session that hit tech (US reining in chip sales to the Middle East after fears they could make their way to China, while TikTok is reportedly preparing a US copy of its core algorithm in an effort to appease US lawmakers). The Dollar was under pressure for much of the session as Treasury yields declined; the ZAR was ultimately weaker amid election uncertainty, while havens like the JPY and CHF rallied against the greenback. Crude futures were lower, with some citing gasoline demand concerns after the EIA report, while others were taking a cautious attitude ahead of OPEC+'s weekend meeting (sources said OPEC+ was looking at extending some output cuts, but the news only briefly supported the complex). Fedspeak failed to add anything incremental to the narrative, with FOMC vice chair Williams largely reiterating recent remarks. Traders are also awaiting the April PCE data, due Friday for further steer on how the Fed will proceed with policy through the end of this year.

US

US GDP: The second look at US GDP in Q1 saw the headline revised down to 1.3% from the initially reported 1.6%; the GDP deflator was unrevised at 3.1%, but all other inflation focussed components saw downward revisions (PCE Prices Prelim revised down to 3.3% from an initial 3.4%, Core PCE Prices were revised down to 3.6% from 3.7%, PCE excluding-Food, Energy and Housing was revised down to 3.2% from 3.3%, while PCE services prices excluding Energy and Housing was revised down to 4.9% from 5.1%). Elsewhere, the Consumer Spending estimate eased to 2.0% from 2.5%. Oxford Economics said that the downward revision to the Q1 GDP headline will not rattle the Fed, as a chunk of the weakness early this year was attributed to inventories and net exports, which are volatile components of GDP. "Revisions to the headline and core PCE deflator were modest, at best," OxEco writes, "the new data does not alter our subjective odds that the first rate cut will occur in September, but this is contingent on inflation moderating over the next couple of months." (NOTE: money markets assign an approximate probability of 80% of a November rate cut, with the first fully-discounted rate reduction priced for December).

INITIAL JOBLESS CLAIMS: Weekly US initial jobless claims printed 219k in the May 25th week (exp. 218k, prev. 216k), while continuing claims came in at 1.791mln in the May 18th week (exp. 1.797mln, prev. 1.787mln). Pantheon Macroeconomics said "the trend in claims appears to be rising, albeit fitfully and from a very low level," with the four-week average now at its highest since late September, while leading indicators (like Challenger layoffs, WARN notices, and the Conference Board's gauge of fear of layoffs) pointing to further increases ahead. "To be clear, payroll growth can slow much further even if claims remain at their current level, if gross hiring slows far enough, as the NFIB and other business surveys suggest," Pantheon adds, "but if gross hiring is falling and gross firing is rising, the downturn in job growth would be quicker".

FED'S WILLIAMS: spoke but largely stuck to the script. He acknowledged the lack of progress on lowering inflation but did suggest it should moderate in the second half of the year. He believes the policy is well positioned to get inflation back to target and he expects to see inflation at 2.5% this year (vs Fed median SEP 2.6% on Core, 2.4% on headline), before being closer to 2% in 2025 (vs Fed median of 2.2%). He also sees 2024 growth between 2.0-2.5% (vs Fed Median of 2.1%). On wages, he said that wage gains are still too high relative to the Fed's 2% inflation goal, while the labour market is still strong and still showing signs of tightness. Williams also echoed Powell and the FOMC statement that risks to achieve the Fed's dual mandate are coming into better balance, while the Fed will watch data when making policy decisions. He does not know when the Fed will change monetary policy, but at some point, interest rates will need to come down and that rate hikes are not in his baseline forecast, but it is unclear how much easing will be needed. On R-star, he said that there are no signs yet that the neutral rate has risen. Williams is also not worried about the actions of other central banks.

FIXED INCOME

T-NOTE FUTURE (U4) SETTLE 15+ TICKS HIGHER 108-17+

Treasuries see a relief rally on Thursday, supported by revisions lower to the Q1 Core PCE estimate ahead of the April PCE on Friday. 2s -5.6bps at 4.929%, 3s -5.9bps at 4.744%, 5s -7.1bps at 4.571%, 7s -7.4bps at 4.567%, 10s -7.2bps at 4.552%, 20s -6.9bps at 4.765%, 30s -6.1bps at 4.683%

INFLATION BREAKEVENS: 5yr BEI -0.3bps at 2.376%, 10yr BEI -0.1bps at 2.373%, 30yr BEI -0.3bps at 2.370%.

THE DAY: Treasuries saw a relief rally on Thursday after the downside seen throughout the week on account of hot consumer confidence and woeful auctions. The Treasury gains started overnight and continued the bid through the European morning before later extending on the US data. The second estimate of US GDP was revised lower in line with forecasts to 1.3% while Core PCE was revised lower to 3.6% from 3.7% which accelerated the upside in T-notes. However, Fed pricing was ultimately little changed. Fed's Williams and Bostic also spoke, but both said little to shift the dial. Williams was acknowledging the lack of progress recently on inflation, and that he does not know when the Fed will change monetary policy. Attention turns to the Eurozone CPI data Friday morning after mixed German CPI earlier in the week and soft Spanish CPI this morning. Following that, the highlight is the April Core PCE numbers from the US, Chicago PMI and more commentary from Fed's Bostic will also be in focus.

STIRS:

- US sold USD 70bln in 4wk bills at a high rate of 5.270%, B/C 2.83x; Sold USD 70bln in 8wk bills at 5.275%, B/C 2.94x
- US to sell USD 70bln of 13-week bills and USD 70bln of 26-week bills on June 3rd; both to settle on June 6th. Sizes unchanged.
- NY Fed RRP op demand at USD 0.452tln (prev. 0.459tln) across 77 counterparties (prev. 75)
- SOFR at 5.33% (prev. 5.32%), volumes at USD 1.807tln (prev. 2.013tln).
- EFFR at 5.33% (prev. 5.33%), volumes at USD 88bln (prev. 88bln).

CRUDE

WTI (N4) SETTLES USD 1.32 LOWER AT 77.91/BBL; BRENT (Q4) SETLES USD 1.55 LOWER AT 81.88/BB

Both WTI and Brent crude prices sold off on Thursday despite some citing the weakness in gasoline prices as a driver in the wake of the DoE report. There were several notable updates on Thursday, namely the weekly DoE inventory report, which in fitting with last night's private inventory data, saw a larger crude draw than expected heading into the Memorial Day weekend. However, the surprise builds in Gasoline and Distillates offset the larger-than-expected draw in Crude stocks. WTI and Brent fell to lows of USD 77.63/bbl and 81.88/bbl ahead of the energy settlement with OPEC+ sources and a weaker buck doing little to support the benchmarks. Ahead of the OPEC+ meeting on Sunday, Reuters reported that OPEC+ is discussing extending some oil output cuts expiring in 2024 into 2025, noting some cuts into 2025 will likely come on top of voluntary cut extensions into Q3 to Q4 of 2024. Elsewhere, US data saw the second estimate of GDP unrevised but consumer spending eased to 2.0% from 2.5% from the initial estimate, albeit Fed pricing was little changed but the Dollar has been weakening throughout the session on account of the move lower in yields after upside seen earlier in the week.

EQUITIES

CLOSES: SPX -0.60% at 5,235, NDX -1.06% at 18,539, DJI -0.86% at 38,111, RUT +1.00% at 2,056.

SECTORS: Utilities +1.41%, Real Estate +1.51%, Materials +0.83%, Industrials +0.7%, Financials +0.61%, Consumer Staples +0.26%, Energy +0.24%, Consumer Discretionary +0.18%, Health +0.07%, Communication Services -1.06%, Technology -2.45%.

EUROPEAN CLOSES: DAX: +0.22% at 18,514.08, FTSE 100: +0.59% at 8,231.05, CAC 40: + 0.55% at 7,978.51, Euro Stoxx 50: +0.42% at 4,984.25, IBEX 35: +1.73% at 11,338.20, FTSE MIB: +0.87% at 34,447.57, AEX: -0.03% at 905.58, SMI: +0.79% at 11,883.20.

EARNINGS

- **Salesforce Inc (CRM)**: Beat on EPS but missed on revenue while guidance heavily disappointed expectations
- **HP Inc (HPQ)**: Beat on EPS and revenue and raised FY adj. EPS guidance.
- **Agilent (A)**: Beat on EPS but cut FY guidance.
- **Foot Locker Inc (FL)**: Saw a strong profit beat while comp sales were not as bad as feared.
- **Dollar General Corp (DG)**: EPS beat, revenue was in line while SSS were strong, although Q2 EPS guidance was soft.
- **Kohl's Corp (KSS)**: Posted a surprise loss per share and missed on revenue with woeful guidance
- **Best Buy Co Inc (BBY)**: Revenue and comp sales disappointed despite margin and EPS beats; guidance was affirmed but it does see profitability at the high end of their adj. operating income guidance
- **Birkenstock Holdings (BIRK)**: Beat on the top and bottom lines and raised revenue guidance.

STOCK SPECIFICS

- **Tesla (TSLA)**: Preparing to register FSD autonomous driving in China, according to sources cited by Reuters. TSLA also mulls selling FSD software as a monthly subscription, sources said.
- **NVIDIA (NVDA)**: Says that while supply for H100 continued to improve, we are still constrained on H200.
- **Apple's (AAPL)**: Next-gen operating systems will feature Project Greymatter, bringing a multitude of AI-related enhancements, according to Apple Insider.
- **Palantir (PLTR)**: Awarded a USD 480mln contract from US DoD.
- **Disney (DIS)**: Nelson Peltz's Trian fund dissolved its stake in the co. at close to USD 120/shr, according to CNBC.
- **Centene (CNC)**: Expects to announce on Friday at the Bernstein conference some intra-quarter insight, including higher-than-expected claims receipts in the co.'s Medicaid segment and noted the trend of higher medical costs in Medicaid continued into May. Still expects adj. EPS above USD 6.80/shr.
- **Zimmer Biomet (ZBH)**: Announced USD 2bln buyback programme.
- **American Airlines (AAL)**: CEO announced he intends to revamp a new sales strategy that has seen less revenue than expected from corporate travellers and travel agencies, according to FT. Note, co. cut guidance on Wednesday.
- **Snap (SNAP) / Meta (META)**: TikTok is reportedly planning a US copy of the app's core algorithm; the version may operate independently of Bytedance and be more conducive to US lawmakers demands, according to Reuters citing sources. TikTok later said this is inaccurate, however.
- **Nvidia (NVDA) & AMD (AMD)**: US to restrain AI chip sales to the Middle East by NVIDIA and AMD over concerns of being diverted to China, according to Bloomberg reports.
- **Summit (SMMT)**: The Phase 3 trial of HARMONI-2 successfully met its primary endpoint, convincingly outperforming **Merck's (MRK)** Pembrolizumab therapy.
- **Paramount (PARA)**: Skydance reportedly sweetens the merger offer for Paramount (PARA), according to WSJ citing sources, who note Paramount directors are expected to review the offer shortly.

US FX WRAP

The Dollar sold off on Thursday with a paring of UST yields supporting the move, particularly in the wake of the second estimate of GDP which saw revisions lower to the GDP estimate, in line with forecasts, while Core PCE eased beneath the consensus to 3.6% from 3.7%, despite expectations for an unchanged print. Attention turns to the April Core PCE data on Friday for a more timely update on the Fed's preferred gauge of inflation. Fed's Williams and Bostic spoke too, albeit neither added anything fresh.

The Euro was stronger on Thursday, initially weakening early in the session but bounced off its 200DMA, showing no sustained reaction to Spain's CPI Y/Y flash NSA (MAY) report and a stickier Core print. The Euro showed little reaction initially to the release of the EZ's easing unemployment rate (record low print), economic sentiment miss, and the rise in consumer inflation expectations and selling price expectations. That said, the Euro strength has continued to strengthen throughout the day as the dollar took a hit. Markets await the EZ's Inflation Rate Y/Y flash and US Core PCE on Friday.

The Yen and Franc outperformed in FX on Thursday due to the move lower in UST yields although the CHF was the clear outperformer after stronger-than-expected GDP data. Also supporting the move were remarks from SNB's Jordan overnight, stating there is a small upward risk to the SNB's inflation forecast, adding he has reasons to believe the natural rate of interest has increased or might rise.

Cyclical currencies saw mild gains, but the Aussie was a cyclical outperformer after stronger-than-expected CapEx data overnight. Note, commentary from Rabobank suggests to "delay building long AUD positions until after the flurry of June central banks meetings" as there will then be more clarity on the rate paths from global central banks (Fed, ECB, BOE). The desk fears sticky US inflation could weigh on AUD/USD in the near term, but nonetheless see the pair at 0.68 on a six-month view before moving to 0.70 early next year. The cyclical upside came despite downbeat equity price action with the weaker buck supporting the move. For the CAD, attention turns to the BOC rate decision next week where the majority of analysts look for a 25bp rate cut, but some expect the BoC to hold; USD/CAD traded on either side of 1.3700 today. GBP also saw mild gains with Cable trading either side of 1.2700.

The Yuan was modestly stronger in Thursday’s session with the Yuan strengthening on reports that China state-backed property developer Vanke in advanced talks with banks for a USD 6.9bln loan, according to Bloomberg. It also reported that the developer may pledge nearly CNY 90bln of assets for the loan. The loan, if signed, would be the largest in Asia ex-Japan since 2022, and is another sign of China being willing to step in and support the market at a time of need.

EMFX was mixed but there was a lot of attention on the ZAR, which finished the session significantly weaker with polling stations still counting votes for the South African election. As a reminder, the ANC is expected to lose its majority (50% or more of the votes), as it is currently reported to have 43.51% of the vote after 20.22% of polling stations have been counted. The election uncertainty is what is weighing on the Rand today as the ANC looks like they will have to form an alliance with another party, where an alliance with Democratic Alliance is seen as a market positive, but an alliance with the MK or EFF party is seen as a negative. Elsewhere, the SARB Repo Rate was left unchanged at 8.25% as expected, while it primarily left forecasts unchanged, but it did note it sees CPI stabilising at the 4.5% goal in Q2-25, a slight improvement from March's meeting. It also eased the 2025 GDP forecast to 4.5% from 4.6%. Nonetheless, little reaction was seen and focus largely remains on the South African Election. Elsewhere, MXN and BRL were flat while CLP underperformed in LatAm FX on account of weaker copper prices while COP managed to find gains vs the Dollar despite the soft crude prices