US Market Wrap

5th June 2024: Strong US data and dovish BoC push stocks to record highs

- **SNAPSHOT**: Equities up, Treasuries up, Crude up, Dollar flat/up
- **REAR VIEW**: Hot ISM Services PMI; BoC cuts rates 25bps as expected; ADP misses expectations; ECB insiders suggest July rate cut probability is low; China Caixin Services PMI rise; DoE posts surprise build, but not as large as private inventory.
- **COMING UP**: **Data**: Australian Trade, EZ & UK Construction PMI, Italian Retail Sales, EZ Employment (F), US Challenger Layoffs, IJC **Events**: ECB Policy Announcement **Speakers**: ECB President Lagarde; BoJ's Nakamura Supply: Japan, Spain, France

MARKET WRAP

Stocks were bid on Wednesday as markets digested a soft ADP, a BoC rate cut and hot US ISM Services PMI. Stocks were trending higher as US players arrived and extended to record high territory throughout the rest of the session as it reacted to the mixed data. There was a brief knock in reaction to the Services PMI data, but ultimately it was deemed a positive for stocks on encouraging growth prospects (note the weakness seen after a soft Chicago PMI last Friday and Manufacturing PMI on Monday). At the same time, although the ADP data was soft, it is usually an unreliable indicator for the NFP on Friday, which participants are looking to for a more up-to-date assessment of the labour market. Aside from the data, there was also a dovish BoC rate decision, which saw a rate cut of 25bps as expected, while Governor Macklem signalled more cuts are coming. Despite the strong PMI data, T-notes were bid in reaction to the ADP data despite a brief knock on the PMI data with yields lower by c. 4-5bps across the curve. Attention now turns to the ECB rate decision on Thursday and the NFP on Friday previews for both are available below.

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US ISM SERVICES PMI: The Headline ISM Services PMI was hotter than all analyst forecasts at 53.8, above the consensus 50.8 and most optimistic forecast of 52.5. The hot print saw it return to expansionary territory after dipping beneath 50 in April, with the May print the highest since August 2023. The upside was led by the surge in business activity, which accelerated to 61.2, the highest level since November 2022 and more than paring the drop seen in April. Meanwhile, ahead of the NFP report on Friday, the employment component remained in contractionary territory, but not as low as the prior month, suggesting job growth is still slowing, but at a slower pace than the prior month. With a lot of attention on prices, the prices paid component eased to 58.1 from 59.2, indicative of rising prices, but at a slower rate than before. Meanwhile, New Orders rose to 54.1 from 52.2. It is worth noting that although this is a solid report on the headline and business activity, it does follow the steep drop in April. ING suggest to look at the two-month average, which "paints a picture of solid, but slowing service sector growth". On prices, ING "would expect that to ease further over the next couple of months as lower oil prices feed through into lower fuel costs".

US ADP: The ADP's gauge of private payrolls reported additions of 152k jobs in the month, missing expectations (exp. 175k), with the payrolls services provider stating that both jobs gains and pay growth are slowing going into the second half of the year. “The labour market is solid, but we're monitoring notable pockets of weakness tied to both producers and consumers,” its chief economist said. Within the ADP report, the median change in annual pay for job stayers was unchanged at +5.0% Y/Y, while the measure for job changers declined to 7.8% Y/Y from 9.3% in April; ADP said pay growth was also slowing into H2 of 2024. Pantheon Macroeconomics, while providing its usual caveats about the unreliability of ADP as a forecasting metric for the official NFP Data, said this month's reading is consistent with private payrolls rising by around 150K in May; "We're sticking with our Homebase model forecast for May and continue to brace for a run of sub-100K payroll prints over the summer months, given the ongoing decline in measures of vacancies and the steep drop in hiring intentions in business surveys, as well as the deterioration in leading indicators of layoffs, such as the Challenger and WARN data," the consultancy said. (NOTE: PM looks is a touch bearish than consensus for the NFP headline, forecasting gains of 180k in the month vs the consensus 185k).

NFP PREVIEW:** Analysts expect the rate of monthly payroll additions to tick up slightly in May, although still remain beneath recent trend rates. Wage growth is seen accelerating slightly on a monthly basis, but is likely to be unchanged on an annualised basis; analysts have noted that the Quits Rate in the recent JOLTs data (for April) is consistent with a moderation in wage pressures ahead. Labour market proxies have been mixed in the month, with jobless claims little changed in the survey windows that coincide with the jobs report. The ADP's gauge of payrolls disappointed to the downside, however. The ISM surveys both saw a tick up in the employment sub-index, with the manufacturing sector's gauge back into expansion territory. Meanwhile, the consumer view of the jobs market has improved in the month. The market reaction will be based on both the headline and the wage metrics in conjunction; if both came in hot, analysts think it would pressure risk assets, and Treasury yields could rise; conversely, a miss on both may support Treasuries, but equities could succumb to the growth concerns narrative. To download the report, please click here.

CENTRAL BANKS

BOC REVIEW: The Bank of Canada cut interest rates by 25bps, taking the key rate to 4.75%, in line with the majority of expectations; some however had been looking for the central bank to leave rates unchanged, while markets were assigning a mere 20% probability of an unchanged outcome. Within the statement, the BoC noted that recent data has increased its confidence that inflation will continue to move towards the 2% target. It also notes that the three-month measures suggest continued downward momentum, while indicators of the breadth of price increases across components of the CPI have moved down further, although shelter price inflation remains high and risks to the inflation outlook do remain. The BoC is closely watching the evolution of core inflation and remains particularly focused on the balance between demand and supply in the economy, inflation expectations, wage growth, and corporate pricing behaviour. Given there were some expectations for a hold, some had been looking for perhaps a "less dovish" rate path ahead, with concerns on how far the Fed and BoC can diverge from policy. Nonetheless, Governor Macklem's post-meeting remarks noted that the BoC will take each meeting one at a time, and it is reasonable to expect more rate cuts if inflation continues to ease, indicating more rate cuts are likely. It is worth adding that, although some economists are sceptical about the extent to which the Fed and BoC can diverge, Macklem repeated that there is a limit to this, but we were currently not near that limit – perhaps giving the BoC more leeway ahead, even in the event of a more hawkish Fed. Money markets currently assign a 40% probability of a BoC cut in July, but are fully priced for another cut by September, while for the Fed, markets assign a 80% probability of the first cut in September, but is not fully priced until November.

ECB PREVIEW: The ECB is expected to lower the deposit rate from 4.00% to 3.75% for the first time since September 2019, with markets assigning a 94% chance to this outcome. With a rate reduction so widely expected, focus will be on hints over future rate cuts, with markets not fully pricing in another move until December. Changes to staff projections are likely to be minimal. To download the report, please click here.

FIXED INCOME

T-NOTE FUTURES (U4) SETTLE 9 TICKS HIGHER AT 110-09+

T-notes were bid after a soft ADP report and BoC rate cut, but knocked on hot services PMI before grinding higher into settlement. 2s -3.7bps at 4.733%, 3s -4.3bps at 4.513%, 5s -4.2bps at 4.310%, 7s -4.0bps at 4.297%, 10s -4.5bps at 4.291%, 20s -4.3bps at 4.522%, 30s -4.0bps at 4.444%.

INFLATION BREAKEVENS: 5yr BEI -0.1bps at 2.299%, 10yr BEI -0.7bps at 2.309%, 30yr BEI -0.9bps at 2.315%.

THE DAY: T-notes meandered overnight and into the European morning before grinding higher in response to the soft US ADP report, and ahead of NFP data due on Friday (note, many are cautious of explicitly connecting the two given ADP's poor forecasting track record of the NFP data). There was a brief extension to the upside on the BoC rate cut (as expected) but there was little signal to suggest that the pace of rate cuts would slow, where Governor Macklem said further rate cuts are to be expected if inflation continues to return to target – the statement acknowledged three-month inflation measures suggest continued downward momentum. Gains were wiped out in response to the hotter-than-expected US ISM Services PMI data, which came in above all analyst forecasts led by a surge in business activity. The downside failed to sustain however with Treasuries grinding higher throughout the rest of the session into settlement with yield lower across the curve by c. 4-5bps. Note, that analysts at ING are somewhat sceptical of the large business activity volatility and are looking at a two-month average instead, which still shows solid service sector growth, but at a slower rate.

STIRS:

- Market Implied Fed Rate Cut Pricing: September 21bps (prev. 19bps D/D), November 30bps (prev. 28bps), December 49bps (prev. 44bps).
- NY Fed RRP op demand at USD 371.8bln (prev. 378bln) across 76 counterparties (prev. 77)
- SOFR at 5.33% (prev. 5.35%), volumes at USD 2.092tln (prev. 1.912tln).

- EFFR at 5.33% (prev. 5.33%), volumes at USD 100bln (prev. 93bln).

CRUDE

WTI FUTURES (N4) SETTLE UP 0.82 AT USD 74.07/BBL; BRENT FUTURES (Q4) SETTLE USD 0.89 HIGHER AT USD 78.41/BBL

Crude prices were choppy throughout the session in response to US data, inventories and Fed rate cut bets. There was plenty of macro data to digest however, where in the US the ADP employment report was softer than expected, but the ISM Services PMI was much hotter than forecasts, sending mixed signals for crude demand, while the BoC enacted its first rate cut and suggested more are coming. The crude highlight was arguably the DoE inventory report, which ultimately aw a surprise build with larger stocks in the products, initially seeing both WTI and Brent test the early morning lows sub USD 73.00/bbl and USD 77.00/bbl respectively. However, once the data was digested, it was judged as not as bearish as the private inventory report had signalled on Tuesday evening, and crude prices began to reverse, likely also aided by the Dollar coming off highs, to see WTI reclaim USD 74.00/bbl and Brent reclaim USD 78.00 /bbl. It is worth noting that the latest Fed poll has the majority of analysts forecasting the first rate cut in September, with markets pricing this in with an 80% probability. Elsewhere, Saudi Arabia set the July Arab Light crude oil OSP to Asia at plus USD 2.40, a USD 0.50/bbl cut from the June OSP, the first cut in five months but broadly in line with market expectations. Note, Saudi also lifted Light OSPs to Northwest Europe by USD 1/bbl to USD 3.10 vs ICE Brent, while left the US Light OSP unchanged at plus USD 4.75 vs ASCI.

EQUITIES

CLOSES: SPX +1.18% at 5,354, NDX +2.04% at 19,035, DJI +0.25% AT 38,807, RUT +1.47% at 2,064.

SECTORS: Energy flat, Utilities -0.58, Industrials +1.0%, Materials +0.72%, Financials +0.22%, Real Estate -0.14%, Consumer Staples -0.22%, Consumer Discretionary +0.67%, Communication Services +1.51%, Health +0.43%, Technology +2.68%

EUROPEAN CLOSES: DAX: +0.89% at 18,570.27, FTSE 100: +0.18% at 8,246.95, CAC 40: + 0.87 at 8,006.57, Euro Stoxx 50: +1.65% at 5,035.05, IBEX 35: +0.59% at 11,353.10, FTSE MIB: +0.68% at 34,507.84, AEX: +1.88% at 918.67, SMI: +1.16% at 12,148.71

Earnings

- **CrowdStrike Holdings Inc (CRWD):** Beat on EPS, and revenue while guidance was also above expectations.
- **Hewlett Packard Enterprise Co (HPE):** Beat on top and bottom line, with guidance above expectations for the FY.
- **Dollar Tree Inc (DLTR):** Beat on EPS, missed on revenue and announced a review of strategic alternatives for Family Dollar. Comp sales missed while it cut FY EPS guidance.
- **Brown-Forman Corp (BF.B):** Beat on EPS, revenue missed, and gave a positive FY25 organic net sales growth.
- **Campbell Soup Co (CPB):** Beat on revenue and earnings as well as reporting strong guidance.

STOCK SPECIFICS

- **Intel (INTC) and Apollo (APO):** Announced an agreement where APO will lead an investment of USD 11bln to acquire from INTC a 49% equity interest in a JV entity related to Intel's Fab 34. Separately, the INTC CEO expects the co. to regain some market share, according to Bloomberg.
- **NXP (NXPI) and TSMC (TSM):** Plans to build a USD 7.8bln Singapore chip plant, according to Bloomberg. Plans to repurchase 3.2mln shares between 6th June and 5th August; approved capital boost for TSMC Global for up to USD 5bln.
- **Disney (DIS), Comcast (CMCSA), Amazon (AMZN):** NBA reportedly closing on a USD 76bln TV deal; is in advanced talks with NBC (CMCSA), Amazon (AMZN) and ESPN (DIS), according to WSJ.
- **PVH Corp (PVH):** Beat on EPS and revenue although guidance was soft. It also announced a leadership update where the CEO of Tommy Hilfiger and PVH Europe is set to leave the co.
- **UnitedHealth (UNH):** Board authorised a cash dividend of USD 2.10/shr (prev. 1.88).
- **Eli Lilly (LLY):** Announced the departure of its CFO, Anat Ashkenazi. Anat Ashkenazi to join as CFO of Google and Alphabet (GOOGL).
- **Campbell Soup Co (CPB):** Beat on revenue and earnings as well as reporting strong guidance.
- **American Express (AXP): eBay (EBAY)** will reportedly drop American Express Co. cards as a payment option on the online marketplace because of “unacceptably high fees,” according to an email reviewed by Bloomberg.

- **Psychedelics (MNMD, CMPS, ATAI):** The US FDA advisers did not approve the use of the drug MDMA to treat a form of mental illness, according to Bloomberg. The advisers voted 9-2 that Lykos Therapeutics data failed to show the drug is effective in patients with PTSD.
- **SAP (SAP GY):** Agreed to acquire **Walkme (WKME)** driving business transformation by enhancing the customer experience and enriching SAP business AI offerings; offer price represents a 45% premium to last close (USD 9.64/shr).
- **Amazon (AMZN):** Labour union has formally affiliated with the Brotherhood of Teamsters; members will vote to consent to the affiliation in the coming weeks.
- **Boeing (BA):** A further two whistleblowers go public over plane safety, reigniting safety and quality concerns. In addition, Starliner spacecraft launched successfully; BA and NASA will continue to work together to certify the Starliner for long-duration operational missions to the ISS. CEO to testify before US Senate committee on June 18th.
- **Toyota (TM):** Says it is to nearly double its output capacity of the Sorocaba plant in Brazil by 2026, according to the local head.
- **Walmart (WMT):** CEO said there is no impact from the war in Gaza, just a minor supply chain issue.
- **Mercadolibre (MELI):** Executive says the company is open to extra distribution centres in Brazil this year and investments in Brazil in 2024 are to surpass the initial plan of BRL 23bln.

US FX WRAP

The dollar climbed higher ahead of the ISM Services PMI release, although gains had pared slightly before with the weak ADP unemployment release supporting the downside move; ADP came in at 152k (exp. 175k), with manufacturing having the largest downside (-20K). That said, the strong ISM Services PMI saw Dollar gains resume. The DXY inched above its 200 DMA (104.43), peaking at 104.46 in response to the above all forecast report. It was the highest it had been for nine months, well above forecasts at 53.8 (exp. 50.8), driven by large upswings in business activity and new export orders. As the session progressed, the Dollar's strength had pared, dipping back below its 200DMA.

The Euro was ultimately flat ahead of the ECB rate decision on Thursday reaching lows of 1.0855. Money markets are pricing in approx. 95% of the ECB cutting rates by 25bps on Thursday and two full 25bps cuts by October later this year. Participants are mainly fixing their attention on commentary regarding the outlook surrounding future rate cuts. The Euro showed no reaction towards the EZ countries (Germany, Italy, France, and Spain) releasing mixed final revisions to May Service PMI's; the EZ services PMI saw a slightly revision lower, as did the composite.

Cyclical currencies (ex-CAD) outperform their G10 FX peers, but moves remain muted. The Aussie showed no initial reaction to real GDP coming in at 0.1%, beneath the 0.2% consensus although the prior was revised up to 0.3% from 0.2%, helping offset the headline miss. The muted reaction is perhaps explained by earlier comments from RBA's Bullock saying she expected the result to be quite low, although the Aussie showed strength after a strong China Caixin Services PMI. Note, the CAD was weaker vs the buck after the BoC cut interest rates by 25ps in line with expectations, although weakness has mostly pared, with rising crude prices offering some support, as did the dollar moving off its highs.

Haven currencies (Franc and Yen) gave back some of its recent outperformance with both currencies lagging their G10 FX peers on Wednesday with the downside move supported by strong ISM data, despite the weakness in UST yields.

It is worth noting that a lot of the carry trade unwind seen earlier in the week in wake of the Mexican election also paused on Wednesday. ING highlights that MXN/JPY was one of the most widely held carry trade strategies, and the Mexican election results coupled with reports suggesting the BoJ may cut its JGB buying plan next week, has seen this cross bear the brunt of the carry trade unwind. The bank also highlights that the cross fell 8% this week, but trade on Wednesday had pared some of those extreme moves, with the MXN peso surging an JPY tumbling.

In EMFX, the TRY saw gains after the Finance Minister in Turkey said they do not plan to tax profits on crypto or stocks. The Rand continued to see weakness post Tuesday's poor GDP result, despite stronger South African PMI and Business Confidence reported on Wednesday while election risk remains. MXN rebounded strongly as post-election nerves settle, or perhaps some think the sell off was overdone. PLN saw gains in wake of the NBP rate decision which saw interest rates remained unchanged for eight consecutive meetings at 5.75%.

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