US Market Wrap

11th July 2024: Stocks rotate and bonds rally after soft CPI boosts Fed rate cut bets

- **SNAPSHOT**: Equities mixed, Treasuries up, Crude up, Dollar down
- **REAR VIEW**: US inflation cools more than expected; Fed's Cook attentive to unemployment rate; Daly and Musalem note the further inflation progress, but still want more data; Strong UK GDP; Japan reportedly intervened in FX; Gaza-cease fire framework agreed; Weak 30yr bond auction; AAPL settles EU antitrust probe; Weak DAL & PEP guidance.
- **COMING UP**: **Data**: Swedish CPIF, US PPI, Uni. of Michigan Prelim., Chinese Trade Balance **Earnings**: Bank of New York Melon, JPMorgan, Wells Fargo, Citi; Ericsson

MARKET WRAP

Stocks were mixed on Thursday as a cooler-than-expected CPI saw a rotation out of large-cap tech stocks into smaller-cap cyclicals with the Nasdaq plummeting but Russell surging. The SPX and NDX were consistently pushing record highs before today, and futures extended those levels after the cooler-than-expected CPI report. However, those gains were short-lived, perhaps with positioning over-extended after the recent rally. The Russell held onto its gains though given its recent underperformance and the index still has a few hundred points before testing the November 2021 record highs of 2,460. Looking at the spread between the R2K and NDX, it is currently just shy of 600bps, Goldman Sachs noted it is the largest 1-day spread since November 2020, and it's the second largest day of R2K>NDX performance in 20+ years. Meanwhile, the equal-weighted S&P also rallied while sectors were very mixed, with Tech, Communication, and Discretionary lagging, while Real Estate, Utilities, and Materials outperformed. The inflation data saw all headline and core M/M and Y/Y components beneath forecasts, which sparked a rally across Treasuries with the curve bull steepening as traders raised their Fed rate cut bets. Money markets are now fully pricing a 25bp rate cut in September, and 60bps of easing by year-end, which implies a 100% probability of two rate cuts this year, and a 40% probability of a third. The Dollar also took a nose dive to the dovish data with DXY testing 104.00 at the lows from a peak of 104.99. The Yen was the clear outperformer following the data, but a quick move 10 minutes after CPI sparked some fresh Yentervention speculation, with reports in TV Asahi and Mainichi later on suggesting Japan did intervene, but officials were reluctant to admit it. Elsewhere, DAL and PEP guidance disappointed with focus turning to the big banks on Friday as the Q2 earnings season gets underway.

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CPI: The US CPI data was cooler than expected across the board. Core CPI rose by 0.1% M/M in June, beneath the 0.2% forecast and prior, while the Y/Y pace eased to 3.3% from 3.4% in May, despite expectations for the pace to be maintained at 3.4%. The headline came in beneath all analyst forecasts at -0.1%, beneath the +0.1% consensus and down from the prior unchanged print. Headline Y/Y eased to 3.0% from 3.3%, beneath the 3.1% forecast. Looking at the breakdown, indexes that increased in June include shelter, motor vehicle insurance, household furnishings and operations, medical care, and personal care. The indexes for airline fares, used cars and trucks, and communication were among those that decreased over the month. Pantheon stated how the huge drop in airline fares and used autos offset the rebound in auto insurance, although they labeled the 5% drop in airline fares as unsustainable. From a Fed perspective, this report is very welcomed and will help support the argument that the disinflationary trend has resumed after the cool April and May reports. This has seen money markets now fully price in a rate cut by September, vs a c. 72% probability beforehand. Looking to year-end, 60bps of easing is priced, implying two 25bp rate cuts, with a 40% probability of a third rate cut. Fed speak since the data from Musalem and Daly has seen that the Fed would still like to see more data before acting, but they did acknowledge the inflation progress.

JOBLESS CLAIMS: Initial Jobless Claims fell to 222k in the week ending 6th July, down from the prior 239k and beneath the 236k forecast. The drop saw the 4-week average ease to 233.5k from 238.75k. Continued Claims meanwhile, for the week ending 29th June, fell to 1.852mln from 1.856mln, beneath the 1.860mln forecast. Note, the drop in jobless claims may just be noise, Pantheon Macroeconomic' Shepherdson writes. He suggests taking claims numbers less seriously than usual from now through mid-August, as seasonals cannot cope with auto shutdowns, 4th of July, hurricanes, and the end of the NY school year.

FED

DALY said that it is likely some policy adjustments will be warranted, noting recent inflation prints are a relief, but progress is bumpy. She believes the economy looks to be on a path where one or two rate cuts this year would be "more or less" the appropriate path, but she still needs more information before the Fed can fully take the next step, although she did state every meeting is live. On the economy, Daly expects inflation will come down gradually and noted that the labour market is gradually slowing. She said shelter prices are coming down, but a lack of supply means the process is slower than in history, but there is still more room for policy to push down shelter inflation. She also said the decline in the super-core ex-housing inflation is welcome. On the labour market, Daly said the US is at the point where additional labour market slowing is more likely to result in a climb in unemployment, noting it has softened, but it is still solid. She also acknowledged it is a fairly big signal from the Fed that so many of them are talking about the labour market, a nod that the Fed are focused on both sides of their mandate now that risks are more balanced.

MUSALEM said that monetary policy is restrictive right now, Fed is making progress and the latest inflation data points to "encouraging further progress" (Note the FOMC statement acknowledged modest further progress). Musalem still wants more evidence that inflation is moving to 2% but he did agree the disinflation process is ongoing. He said the jobs market is strong, but it has cooled in recent months, noting it is moving back into better balance. He also stated the current unemployment rate is still low, despite the recent rise. Musalem sees the economy growing between 1.5-2.0% this year, beneath the Fed median view of 2.1%. He noted that he supports the FOMC's outlook for monetary policy, that current settings are appropriate, and that the economy may be shifting into a higher interest rate regime vs pre-pandemic.

FIXED INCOME

T-NOTE (M4) FUTURES SETTLE 21 TICKS HIGHER AT 111-05

T-notes bull steepen after soft CPI boosts Fed rate cut bets. At settlement, 2s -12.6bps at 4.507%, 3s -12.7bps at 4.269%, 5s -11.2bps at 4.127%, 7s -10.0bps at 4.142%, 10s -8.5bps at 4.195%, 20s -7.4bps at 4.502%, 30s -6.5bps at 4.405%.

INFLATION BREAKEVENS: 5yr BEI -5.1bps at 2.190%, 10yr BEI -3.2bps at 2.251%, 30yr BEI -1.9bps at 2.280%.

THE DAY: The Treasury curve bull steepened with T-notes rallying to the softer-than-expected US CPI. The data was cooler than forecasts on all fronts with the Core rising just 0.1% M/M with the headline declining by 0.1%. Alongside the soft CPI was a drop in jobless claims, albeit analysts are cognizant of noise given it covers the 4th of July week, particularly as we enter the summer months. The CPI was of course the highlight of the day and T-notes peaked at 111-10+ from a pre-data low of 110-13. The soft reading also saw traders ramp up their rate cut bets from the Fed, with a 25bp rate cut now fully priced for September, while money markets now imply a 40% probability of three 25bp cuts this year from the Fed. T-notes pared slightly from peaks heading into the 30yr bond auction, which saw a chunky tail (more below), putting some pressure on T-notes but it managed to hold above 111-00. Elsewhere, Fed speak saw Daly and Musalem acknowledge recent "encouraging" inflation progress, but they would still like to see more data, although Daly was cognizant of the slowing labour market and acknowledged it is likely some policy adjustments will be warranted, noting every meeting is live. However, it appears she is more referencing September, November and December, with July still largely expected to be a hold given there is not much data between now and then for the Fed to become convinced inflation is returning to 2%. By September, however, there will be plenty more including two more CPI reports and three more NFP releases.

30YR: The 30yr bond auction was soft, seeing the USD 22bln offering sold at a high yield of 4.405%, tailing the When Issued by 2.2bps, the largest tail since November. The Bid-to-Cover was also soft at 2.3x, beneath the 2.49x prior and 2.42x average. The breakdown also was not great, with a decline in indirect demand to 60.76% from 68.5%, falling beneath the 67.6% average. There was a slight uptake in direct demand however above averages, but it still left dealers with an above average 15.88%.

STIRS:

- Market Implied Fed Rate Cut Pricing: September 25bps (prev. 20bps D/D), November 39bps (prev. 31bps), December 61bps (prev. 51bps).
- NY Fed RRP op demand at USD 404bln (prev. 422bln) across counterparties 72 (prev. 76).
- US sold USD 85bln in 8wk bills at 5.260%, B/C 2.63x; sold USD 90bln in 4wk bills at a high rate of 5.270%, B/C 2.69x.
- SOFR at 5.34% (prev. 5.34%), volumes at USD 1.949tln (prev. 1.913tln).

- EFFR at 5.33% (prev. 5.33%), volumes at USD 88bln (prev. 84bln).

CRUDE

WTI (Q4) SETTLES USD 0.52 HIGHER AT USD 82.62/BBL; BRENT (U4) SETTLES USD 0.32 HIGHER AT 85.40/BBL

Oil prices were choppy on Thursday, with upside seen overnight extending on the prior days gains, peaking around USD 82.90/bbl and USD 85.89/bbl for WTI and Brent, respectively, before paring in European trade. Reports suggested the Gaza ceasefire agreement framework has been agreed but parties are now negotiating on how it will be implemented. Despite a cool US CPI, WTI and Brent initially hit a trough in wake of the data at USD 81.63/bbl and USD 84.64/bbl before paring to test the overnight peaks into settlement. The move off lows was perhaps driven by rising interest rate cut bets with the first-rate cut now fully priced by September, and the second fully priced by December, but money markets are implying around a 40% probability of a third 25bp rate cut by year-end. Elsewhere, the IEA Oil Market Report saw 2024 and 2025 oil demand growth forecast little changed from the prior month while China oil demand growth eased to 710k BPD in Q2 but Iran production rose to a six-year high. Meanwhile, in the US, Senior Energy Adviser Hochstein suggested on Bloomberg TV that the US can tap the strategic petroleum reserve if needed, providing conditions call for it.

EQUITIES

CLOSES: SPX -0.88% at 5,585, NDX -2.24% at 20,211, DJI flat at 39,754, RUT +3.57% at 2,125.

SECTORS: Technology -2.74%, Communication Services -2.56%, Consumer Discretionary -1.47%, Consumer Staples -0.35%, Health +0.72%, Financials +0.85%, Energy +1.05%, Industrials +1.26%, Materials +1.42%, Utilities +1.83%, Real Estate +2.66%.

EUROPEAN CLOSES: DAX: +0.72% at 18,540, FTSE 100: +0.36% at 8,223, CAC 40: +0.71% at 7,627, Euro Stoxx 50: +0.39% at 4,978, IBEX 35: +0.89% at 11,170, FTSE MIB: flat at 34,318, SMI: +0.92% at 12,263, PSI: +0.89% at 6,802.

STOCK SPECIFICS:

- **Delta Airlines (DAL) -** Missed on Q2 revenue and gave poor EPS guidance as well as a dim Q3 outlook.
- **Pepsico (PEP)** - Missed on Q2 top line and its FY Core EPS view came under expectations, though did beat on Q2 Core EPS.
- **Costco (COST)**- Will increase its annual membership fees by USD 5 and executive membership by USD 10. Co. also declared a quarterly cash dividend on its common stock of USD 1.16/shr.
- **Conagra Brands (CAG)** - Missed on Q4 revenue, and FY 25 EPS view.
- **GLP-1 Names (Eli-Lilly (LLY), Novo Nordisk (NVO), Viking Therapeutics (VKTX)) - Pfizer (PFE)** advances the development of a once-daily formulation of oral GLP-1 receptor against Danuglipron; ongoing study shows favourable pharmacokinetic profile for Danuglipron.
- **MicroStrategy (MSTR) -** Announced a 10-for-1 stock split.
- **Apple (AAPL)** - Settled EU antitrust probe over Tap-and-Pay tech, Co. avoided EU fine.
- **Envestnet (ENV)** - Confirmed that Bain Capital and Reverence offered USD 4.5bln to take the co. private, equating to USD 63.15/shr, in fitting with earlier Bloomberg sources.
- **Alcoa (AA) -** Reported a preliminary Q2 beat on revenue and adjusted income.
- **Chevron (CVX)** and **Hess (HES) -** Decision reportedly delayed by FTC to after **Exxon (XOM)** arbitration, according to Bloomberg. Expects the FTC's merger review process to be completed in Q3.
- **Tesla (TSLA) -** Plans to delay its robotaxi unveiling to October from August, according to Bloomberg, TSLA wants more prototypes before the event.
- **Boeing (BA)** - Nears deal to sell 20-30 777X jets to **Korean Air (003490 KS),** according to Reuters sources.
- **Nike (NKE) -** Moves senior executive to CEO advisor role; Thomas Clarke to advise CEO John Donahoe; John Joke to replace Tom Clarke as innovation head.
- **Bunge's (BG) -** USD 8bln deal for Viterra said to face risk of delays, according to Bloomberg. Bunge waits for approval from EU, China, and Canada and the acquisition is unlikely to be completed within Bunge's mid-2024 goal.

US FX WRAP

The Dollar index tumbled on a cooler-than-expected US CPI report, with all components printing beneath forecasts. DXY fell from a peak of 104.990 in the European morning to a low of 104.17 in the wake of the data. Headline Inflation M

/M surprisingly indicated a deflationary figure for June, at -0.1% (exp. 0.1%, prev. 0.1%); its first drop since May 2020, driven by a fall in gasoline prices which offset an increase in shelter prices. Note, Initial Jobless Claims fell 17k W/W to 22k, much more than the expected 3k drop, while Continuing Jobless Claims also fell; but analysts warn of seasonal noise in the data, and in the summer months ahead. In terms of Fedspeak, Daly (2024 Voter, Dovish) said the economy looks to be on a path where 1 or 2 rate cuts this year would be 'more or less' the appropriate part (Fed Median dot plot points to 1 rate cut); furthermore she said that we are at the point where additionally labor market slowly is more likely to result in a climb in unemployment, further indicating attention on the cooling labour market. It is worth noting that money markets now price a full 25bps cut for September (prev. 72% before the CPI release), and 60bps of cuts are priced by year-end (prev. 49bps). Musalem also spoke, but his remarks were in fitting with the Feds' narrative, but he did state today's data showed "encouraging inflation progress". Potential buck movers that lie ahead include US PPI and UoM Consumer Sentiment on Friday.

The Euro firmed vs the Dollar but was sold vs the Pound with the Dollar weakness driving the majority of price action after CPI. As French Politics fades from the limelight, OAT/BUND spreads remain well off recent highs at 64.90. Meanwhile, on data, the Final German CPI and HICP for June was in line with expectations, ahead of the final Spain and French inflation data on Friday, as well as German PPI. As a reminder, the ECB blackout began today ahead of the ECB Interest Rate decision next Thursday, where the Central Bank is expected to hold the deposit rate at 3.75%. With regards to ECB pricing, money markets fully price another 25bps rate cut in October, but with an 81% chance of a 25bps rate cut in September, and a total of 46bps of rate cuts by year-end.

The Yen and Franc were among the best performers in the G10 space against the dollar. Yen took the spotlight in the space, with the cross dumping beneath 159.00 from a peak of 161.75. The initial move occurred in the wake of the soft US inflation, but another leg lower in the pair sparked fresh Japanese intervention speculation. On that, Japan's outgoing top currency diplomat Kanda said he is not in a position to note if it was intervention or not, and "If we intervened in FX, we will disclose at the end the month". Nonetheless, sources via TV Asahi stated the government and BoJ intervened in the FX market today.

Goldrallied throughout the session with gains arising from the lower inflation figure and bond yields sliding hard, in particular, the US 10-year yields fell by 10bps at one point in the session, though losses have pared slightly since. XAU/USD finishes the session near highs of 2,425/oz, its monthly high thus far, surpassing the highs seen in June. Gold posts its third consecutive day of gains.

Activity Currenciesmostly strengthened against the greenback, except for the CAD which saw modest weakness. The Pound outperformed in the space amid a myriad of data in the region. The release of most attention was the GDP M/M for May which doubled expectations of 0.2%, at 0.4% (prev. 0%), albeit, Cable initially reacted to the upside, but swiftly trimmed gains. Meanwhile, Manufacturing Output M/M for May was as expected at 0.4%, while Y/Y rose less than expected by 0.6% (exp. 1.2%); moreover, GDP Estimates M/M and Y/Y for May beat expectations. Cable rose above the 1.29 handle, reinforcing its title as the best-performing G10FX YTD with the post-US CPI dollar weakness supporting the move. The Aussie extended its three-day rally, while the Kiwi also gained on the day, reducing some of the heavy losses that ensued on Wednesday after the RBNZ dovish tilt after it held rates at 5.5%.

The Yuan saw gains thanks to the falling buck. USDCNH fell over 0.3%, with session lows of 7.258 in response to the soft US CPI print. Looking ahead, attention will be on Chinese Imports and exports for June; imports are expected to rise 2.8%, and exports are expected to rise 8%. The cross is set to endure its second consecutive week of gains, an event that hasn't occurred since March 2024.

EUR/SEK is flat ahead of Sweden's Inflation for June, which is expected to see the M/M at 0.1% and Y/Y at 2.8%. The Viking Cross extended its slump on Wednesday, driven by lower Norwegian inflation, falling to lows of 0.9738, yet reduced losses notably as the session progressed.

EMFX: MXN continues into its 8th day of consecutive gains, amid Banxico minutes which noted that slightly higher rates are expected for 2025 compared to prior projections and that most board members underlined that although the depreciation of the Mexican peso impacts inflation forecasts upwards, its effects are partly offset by those associated with the greater weakness exhibited by economic activity. MXN watchers await Industrial Production numbers on Friday for May. Elsewhere, BRL weakened despite Strong Retail Sales, Y/Y came in at 8.1% (exp. 4.1%), and M/M surprised to the upside at 1.2% (exp. -0.9%). USD/ZAR fell, brushing aside the misses on its Manufacturing Production for May, being supported by the upside in gold prices.

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