

07 September 2016

Danske Daily

Market movers today

- **Today, in the US**, the Fed's Beige book is due to be released.
- **In the euro area today**, the German industrial production figures for July are due to be released. German industrial production is especially important following the Brexit vote due to the size of the German manufacturing sector. The industrial production figures for June showed strength and we estimate July figures followed a similar trend and confirm the economic resilience.
- **In the UK, focus today will be on the first hard post-Brexit data as industrial production for July is due out.** We would also look out for the NIESR GDP estimate for August, as it is usually a good predictor of actual GDP growth. In addition, the Bank of England's Mark Carney, Jon Cunliffe, Kristin Forbes and Ian McCafferty are due to participate in a hearing of the Parliament's Treasury Committee.
- **Today, focus in Sweden will be on the Riksbank's monetary policy decision (09:30 CEST)**, where our point estimate is for no change. **In Norway**, we estimate that industrial production for July, which is also due to be released today, climbed 1.5% m/m.

Selected market news

Yesterday, we saw a big drop in the ISM non-manufacturing index from 55.5 in July to 51.4 in August. The drop in the ISM non-manufacturing index is the biggest since November 2008 and the ISM non-manufacturing index is at the weakest level since 2010. Both the ISM non-manufacturing index and the Markit PMI services index gave a weak signal yesterday. On the back of the very weak ISM non-manufacturing index, 2Y and 10Y government bond yields in the US initially declined by approximately 5bp and 4bp, respectively, and closed the day around 7bp and 6bp lower than the level before the data release.

In general, it was a rather mixed session in global financial markets yesterday, slightly skewed towards risk-off sentiment. Stock markets were fairly calm and moved mainly sideways, whereas we saw a rally in fixed income markets. The 10Y government bond yield not only fell in the US but also in Germany and Japan by approximately 4bp and 1bp, respectively. Moreover, Brent oil decreased, though modestly, to USD47.35/bbl, and in FX markets the US dollar (USD) weakened sharply on the back of the weak August ISM non-manufacturing index.

Today has been another quiet morning. So far, it has been a rather mixed session in the Asian stock markets and regarding risk sentiment, it has been quite mixed as well with the 10Y government bond yield in Japan down by approximately 2bp at the time of writing and Brent oil climbing back to USD47.6/bbl.

Selected readings from Danske Bank

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Scandi

We expect unchanged policy from the Riksbank today, i.e. no news either in terms of the repo rate or the repo rate forecast, nor in terms of the size or composition of the QE programme. The latter may become a prime consideration in October as a rising government budget surplus risks drying up government bond supply in 2017, forcing the Riksbank to reluctantly consider buying covered bonds later this year instead. A side story that has been discussed recently is whether and when the Riksbank will re-introduce the tolerance interval around 2%. This may happen at some of the next three meetings, perhaps even today. If it does, it should be noted that the Riksbank will continue to aim at 2%, where the ± 1 pp band around the target is for pedagogical purposes (i.e. 2 % on average but within a 1-3% range). Importantly, we are convinced that the Riksbank will not be introducing a 'target interval' (where 1.0% is as good as 2.0% or 3.0%). In that sense, we are sure the Riksbank does not want to be perceived as becoming less ambitious – it would be counter-productive. It may also announce a change of the target variable, probably from CPI to the current 'policy variable' CPIF but HICP is also an alternative. These changes should not have any implications for monetary policy.

The Swedish National Debt Office (DO) is due to release the August budget outcome. The DO's estimate is for a SEK20.6bn surplus. Clearly, a better outcome would be supportive of our view that the DO needs to cut bond supply significantly in October (new forecast). The backdrop is that new forecasts by the ESV and NIER both have the 2017 budget balance at more than SEK50bn better than the DO.

Norway. The surprise fall in manufacturing production in June fuelled some uncertainty about the outlook. Based on leading indicators such as business confidence, the PMI and Norges Bank's Regional survey, there is much to suggest that the sharp fall of 2.9% m/m was a temporary phenomenon. Therefore, we estimate something of a correction in July, with manufacturing production climbing 1.5% m/m.

Fixed income markets

The strong rally in the EUR FI market yesterday was fuelled by the -4.1 decrease in US ISM non-manufacturing (the biggest since November 2008). Once again, a 5-7bp move lower across the US curve caused a sharp flattening driven by the long end of the German curve, which decreased 8bp. 2Y Germany also decreased further to -68bp, reflecting that the market is pricing in some probability of the ECB allowing purchases below the depo rate. Today's supply is in 10Y Germany, and Italy will do an exchange auction, where the Tesoro will sell Sep-28 and do buybacks in 17s and 18s.

Denmark is also in the market with a tap in the 2Y and the old 30Y benchmark (Nov-39). We expect the DMO will sell for around DKK2.5bn. The Danish funding requirement fell by DKK2bn with the publication of the budget last week. The high level on the government account gives potential for further buybacks. The DMO surprised somewhat by selling in the old 30Y benchmark. However, if investors wish to buy long DKK risk, then DGB 4.5% 11/39 is the only place to find duration. In contrast, there is a risk of further underperformance in the old 30Y German government bonds, regardless of whether or not the ECB adjusts its QE purchase pattern. We see value in buying DGB Nov-39 against equivalent German government bonds at the auction. See *Strategy: Danish government bond auction - focus on the tap in the 30Y*, 5 September 2016. Finally, note that Sweden is tapping SEK3.5bn in the 10Y today.

FX markets

The US dollar (USD) weakened sharply on Tuesday on the back of a very weak August US non-Manufacturing Composite Index, which fell to 51.4 from 55.5 previously. The data, together with the weaker-than-expected ISM manufacturing data last week and the soft August non-farm payroll, supports our view that the Federal Reserve will keep interest rates unchanged at its meeting on 21 September. The USD weakened particularly strongly versus emerging market and commodity currencies like ZAR, BRL and NZD. In our view, the prospects for emerging market currencies, e.g. BRL and RUB, remain solid, especially with the Fed likely to be on hold at least until end-2016. We continue to see EUR/USD in a 1.09-1.14 range with selling opportunities occurring in the 1.1350-1.1400 area.

In the Scandies, NOK strengthened during the day, supported by the recent uptick in the NIBOR fixing. Technically, EUR/NOK is looking bearish with the next key support level coming in at 9.1443, the 2016 low. Today, we expect the Riksbank to keep monetary policy unchanged, which should put slight further downward pressure on EUR/SEK. Technically, EUR/SEK is also looking bearish with a possible move down to the low 9.40s over the coming week.

Key figures and events

Wednesday, September 7, 2016

				Period	Danske Bank	Consensus	Previous
-	GBP	BoE's Carney in hearing in the Parliament's Treasury Committee					
-	CNY	Foreign exchange reserves	bn. USD	Aug		3191	3201.1
-	PLN	Polish central bank rate decision	%		1.50%	1.50%	1.50%
1:50	JPY	Official reserves assets	USD bn	Aug			1264.8
3:15	USD	Fed's Williams (non-voter, neutral) speaks					
3:30	AUD	GDP	q/q y/y	2nd quarter		0.4% 3.2%	1.1% 3.1%
7:00	JPY	Leading economic index, preliminary	Index	Jul		98.6	99.2
8:00	DEM	Industrial production	m/m y/y	Jul	-0.1% ...	0.1% 0.1%	0.8% 0.5%
9:30	SEK	Riksbank, rate decision	%		-0.50%	-0.50%	-0.50%
9:30	SEK	Budget balance	SEK bn	Aug			3.7
9:30	GBP	Halifax house prices	m/m 3Ms/YoY	Aug		-0.3% 7.0%	1.0% 8.4%
10:00	NOK	Manufacturing production	m/m y/y	Jul			-2.9% -6.5%
10:00	NOK	Industrial production	m/m y/y	Jul	1.5% ...		-5.1% -8.7%
10:30	GBP	Industrial production	m/m y/y	Jul		-0.3% 1.9%	0.1% 1.6%
10:30	GBP	Manufacturing production	m/m y/y	Jul		-0.4% 1.6%	-0.3% 0.9%
13:00	USD	MBA Mortgage Applications	%				2.8%
16:00	GBP	NIESR GDP estimate	q/q	Aug			0.3%
16:00	CAD	Bank of Canada rate decision	%		0.50%	0.50%	0.50%
20:00	USD	Fed releases their 'Beige Book'					

Source: Bloomberg, Danske Bank Markets

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