4 November 2016

Danske Daily

Market movers today

- **Today, the US jobs report for October due out at 13:30 CET will be in focus**. We continue to receive mixed signals about the labour market. Claims figures continue to signal job growth well above 200,000, while the Markit PMI employment index for October points to growth just above 100,000. We estimate jobs growth was 170,000 in October. The unemployment rate rose to 5.0% in September due to an increasing participation rate. That the unemployment and underemployment rates have moved sideways in 2016 indicates that there is still slack left in the labour market. We estimate the unemployment rate was unchanged at 5.0% in October, with the probability skewed towards a fall back to 4.9%. We estimate that average hourly earnings increased 0.3% m/m in October, implying an unchanged annual growth rate of 2.6% y/y. Wage growth has moved sideways in 2016, indicating that the underlying inflation pressure is still subdued.
- **In Europe**, the October service and composite PMIs for Italy and Spain and final revisions of the PMIs in eurozone, France and Germany are due out.

Selected market news

Risk aversion continues to dominate financial markets as the US election approaches. Clintons lead in the polls has narrowed significantly in recent weeks and according to the poll aggregator FiveThirtyEight, the odds of a win for Clinton have fallen further to 66.2% from 67.7% yesterday. Around the third Presidential debate on 19 October the odds of a Clinton win was estimated to 87.3%.

The negative sentiment from the US session last night has been carried over to the Asian session where markets also trade lower this morning. The oil price declined further yesterday with the price on Brent crude seen trading as low as USD46.21/bbl. The Vix volatility index has also increased further and is trading close to the levels seen around the time of the UK's EU referendum in June.

In the UK, Brexit uncertainties got a new twist yesterday as the UK High Court ruled that it is parliament – not the government – that has the power to trigger Article 50. The UK government has said that it will appeal the verdict, which means that we should get a final ruling from the Supreme Court in December. We still think Article 50 will be triggered eventually (although the triggering may be delayed past March). However, if the Supreme Court also concludes that the government cannot trigger Article 50 and that parliament will be more involved in the negotiation process, it means that a 'softer' Brexit has become more likely, as a majority of the members of parliament have a pro-EU stance and voted for remain.

We have changed our call on the Bank of England. Before the Bank of England's (BoE) monetary policy meeting yesterday, we called for another 15bp rate cut in February. However, as the BoE changed its communication from an easing bias to a neutral bias, by saying it 'can respond in either direction', we no longer expect the bank to ease monetary policy further. We still think it is unlikely that the BoE will tighten monetary policy in a time of elevated political uncertainty, but we now think we need to see a substantial slower growth and/or higher unemployment before easing becomes likely again. UK money market is also pricing in an unchanged Bank Rate for the coming 12 months.

Selected readings from Danske Bank

- *Bank of England review: BoE shifts from easing to neutral bias - we no longer expect a further rate cut*

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Scandi markets

Sweden. On 2 November, we changed our call on the Riksbank and now expect it to deliver a 10bp repo rate cut at its monetary policy meeting on 20 December. In *Reading the Markets Sweden* (3 November), we analyse the implications for the Swedish fixed income market and the SEK.

Fixed income markets

Yesterday, the UK government lost the Brexit lawsuit regarding Article 50, meaning that parliament will have to vote to activate Article 50. This could potentially mean a softer Brexit, as parliament (comprising mostly 'remainers') will be more involved in the Article 50 process. This should not stop a Brexit but might cause a delay. The market reaction was somewhat muted with UK yields initially moving lower, but as the Bank of England kept rates and purchase targets unchanged while sounding hawkish the 10Y Gilt increased by 5bps although a mere 2bp relative to Bunds.

Keep an eye out for the US non-farm payroll figures this afternoon, as it could be last nail in the dovish Fed members' coffin and most certainly pave the way for a December rate hike.

Moody's is due to review the ratings of Belgium and Fitch has the Netherlands on the spot. Belgium is struggling, but Moody's is already lower than Fitch and S&P so no change is expected. With regard to the Netherlands, no change is expected as well.

FX markets

Normally, the non-farm payroll number would be dearly anticipated and a critical market mover including for the USD. However, with five days to go to the US election and a neck-to-neck race between the two candidates, even the mother of all data releases is under threat to take a less prominent role. Nevertheless, following the FOMC statement on Wednesday highlighting the need to 'wait for some further evidence of continued progress toward its objectives', the jobs report will be important for the Fed before it makes it mind up about a rate hike in December. However, with the market more or less priced for a rate hike, we would probably need a very weak number to change the market's mind and send the US dollar lower. Hence, at the end of the day, focus will remain on next week's election with the USD being more sensitive to election polls – in that regard, we see highly different directions for the EUR/USD following Tuesday's outcome, with the cross likely to move to 1.13-1.14 in the case of a Trump win and 1.07-1.08 into the Fed's December meeting if Clinton wins.

EUR/GBP declined significantly yesterday due to the combination of the High Court's ruling and the BoE's shift to a neutral stance. In the short term, we expect GBP trading to be more volatile and further GBP appreciation should not be ruled out – ahead of the US election in particular on 8 November we could see a further reduction in short GBP/USD bets. Over the medium term, we do not see today's events as a major game changer for GBP. We still target EUR/GBP at 0.91 in 3M and 0.92 in 6M given that we still think that the combination of significant economic imbalances (large current account deficit and a negative net international investment position) and Brexit uncertainties justifies a significant undervaluation of the GBP.

Regarding the SEK, we think it is too early to expect a strengthening of the krona. We see three potential triggers for renewed strength of the currency: (1) the Riksbank, 2) stronger-than-expected macroeconomic data and (3) misalignment of the SEK getting more traction. The biggest obstacle to a stronger SEK is probably the Riksbank, while we think that increasingly subdued expectations on the Swedish economy make positive surprises more likely, which may offer some tailwind to the currency, which we think is clearly in undervalued territory.

In Egypt, the central bank took the first step towards letting the Egyptian pound float yesterday in a move to meet the conditions for USD12bn in assistance from the IMF. At the same time, the central bank hiked its benchmark deposit rate by 300bp and allowed the currency to trade at 13 per USD +/- 10% in the interbank market. The USD/EGP increased to 13.89 following an FX auction by the central bank. The pound will be allowed to freely move in accordance with supply and demand starting on Sunday. There is a high likelihood that it may weaken further given a sizeable current account deficit and the large unmet FX demand (with the black market rate trading at around 18 per USD). However, the combination of IMF support and fiscal consolidation (the Egyptian government announced a cut to energy subsidies yesterday) will take away some of the upward pressure to the USD/EGP cross. Our rough assessment suggests that the EGP was about 30-40% overvalued before the move yesterday.

Key figures and events

Friday, November 4, 2016				Period	Danske Bank	*Consensus*	Previous
-	EUR	Moody's may publish EU's debt rating					
-	EUR	Fitch may publish Netherlands's debt rating					
-	EUR	Moody's may publish Belgium's debt rating					
9:00	DKK	Forced sales (s.a.)	Number	Oct			
9:00	DKK	Bankruptcies (s.a.)	Number	Oct			
9:15	ESP	PMI services	Index	Oct	**55.4**	*55.0*	54.7
9:45	ITL	PMI services	Index	Oct	**51.5**	*51.5*	50.7
9:50	FRF	PMI services, final	Index	Oct	**52.1**	*52.1*	52.1
9:55	DEM	PMI services, final	Index	Oct	**54.1**	*54.1*	54.1
10:00	EUR	PMI composite, final	Index	Oct		*53.7*	53.7
10:00	EUR	PMI services, final	Index	Oct	**53.5**	*53.5*	53.5
11:00	EUR	PPI	m/m|y/y	Sep		*-1.8%|0.0%*	-2.1%|-0.2%
13:30	USD	Non farm payrolls	1000	Oct	**170**	*173*	156
13:30	USD	Unemployment	%	Oct	**5.0%**	*4.9%*	5.0%
13:30	USD	Average hourly earnings, non-farm	m/m|y/y	Oct	**0.3%|2.6%**	*0.3%|2.6%*	0.2%|2.6%
13:30	USD	Average weekly hours	Hours	Oct		*34.4*	34.4
13:30	USD	Trade balance	USD bn	Sep		*-41.0*	-40.7
13:30	CAD	Net change in full time employment	1000	Oct			23
13:45	USD	Fed's Lockhart (non-voter, neutral) speaks					
18:00	EUR	ECB's Constancio speaks in USA					
21:00	USD	Fed's S.Fischer (voter, neutral) speaks					

Source: Bloomberg, Danske Bank Markets

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