9 November 2018

# Danske Daily

## Fed remains on track for December hike

### Market movers today

- In Norway, inflation data for October is due out. We estimate core inflation slowed to 1.8% y/y, from 1.9% y/y in September. For more see *Scandi markets* overleaf.
- In the UK, focus remains on Brexit, where we have seen mixed signals on whether the UK Cabinet is about to reach an agreement on the UK's backstop proposal (backstop is the solution to avoid a harder border if negotiations on the future relationship breaks down). Besides this, we are due to get the monthly GDP figure for September (and hence the first full estimate for growth in Q3), which we estimate rose 0.1% m/m. We believe it is likely GDP grew 0.6% q/q in Q3.
- In the US, preliminary consumer confidence from the University of Michigan is due out in the afternoon.

### Selected market news

The positive risk sentiment in financial markets seen earlier this week did not last long. Asian stock markets fell 1-2% overnight, while the USD stayed strong and the 10Y US yield continues to trade around this year's peak of 3.23%. The oil market sold off further yesterday, with the price of Brent crude falling below USD71/bbl.

Chinese inflation data for October was published overnight. It came in roughly as expected – PPI was 3.3% y/y, down from 3.6% y/y in September, and CPI was 2.5% y/y, unchanged from the previous month. Hence, inflationary pressures remain muted in the Chinese economy and do not constrain the People's Bank of China from keeping an easy stance on monetary policy.

Money-supply growth in Japan is also worth keeping an eye on. Both growth in M2 and M3 money supply slowed in October to 2.7% y/y and 2.3% y/y, respectively.

Finally, the Reserve Bank of Australia kept monetary policy unchanged but signalled that higher rates are to come amid a sound economy but downplayed the likelihood of a near-term move.

As expected, the Fed stayed on hold today and made no major change to the policy signals in the statement, which means the Fed is still on track to hike rates again in December. A few in the market had speculated that the Fed would cut interest on excess reserves (IOER) by 5bp at this meeting, as the effective Federal funds rate had crept higher leading up to the meeting. However, the Fed could instead make an adjustment hike of 15-20bp of IOER in December following a widely expected 25bp hike of its target rate (see *FOMC Review – No change to the Fed's hiking plans*, 8 November).

**Selected readings from Danske Bank**

- *FOMC Review – No change to the Fed's hiking plans*, 8 November
- *Strategy – Japanese investor flows into US, UK, EU and Scandinavia for September 2018*, 8 November
- *Reading the Markets Denmark - Focus on remortgaging in social housing, pressure on DKK subsides and DGB 0.25% 11/18 maturing*, 8 November

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## Scandi markets

In Norway, inflation has surprised on the upside over the past three months. The core rate was 1.9% y/y in September, once again well above the level projected by Norges Bank (1.6%). A glance at the underlying data reveals that the causes are not straightforward. First, prices of imported goods have been higher than expected, due partly to a departure from the normal seasonal pattern. This could be down to chance (e.g. the abnormal weather) but could also be due to the delayed effects of the krone's depreciation in H2 17. Second, prices for Norwegian agricultural produce also climbed more than expected over the summer, due partly to the settlement with farmers but also to the dry summer destroying parts of the harvest. We are not sure how much of the increase in import prices is only temporary but we do believe that much of the climb in prices for domestic agricultural produce is just that. Therefore, we estimate some of the rise in core inflation in recent months reversed in October, with the annual rate slowing to 1.8%.

In Sweden, we will keep our eyes on the consumption indicator for September, one of the final pieces of the GDP puzzle for Q3. Retail sales rose slightly year on year, while car sales fell sharply, down 40% y/y. The consumption indicator printed a meagre 0.4% y/y in August on the back of negative growth in July. Hence, it looks as though Q3 will be a really weak quarter for private consumption. The risk is that our Q3 GDP indicator, currently just above 2%, will fall after today's numbers. Meanwhile, Riksbank Board members seem to have no problem starting to hike rates even though growth loses momentum.

## Fixed income markets

No news from FOMC is not particularly good news for US treasuries, as the Fed remains on autopilot for 3%. Yesterday night, we did a small move higher in yields and the curve 2s10s flattened to 25bp but the moves were muted as risky assets came under pressure. Short-term risk appetite will continue to set the direction but the underlying trend is still towards higher US treasury yields. We continue to target 3.50% on a three- to six-month horizon – see *here*. For more on the FOMC meeting see *here*.

Yesterday, Italy once again came under pressure and the spread against Germany widened 5Y to 293bp. The EU commission released new autumn forecasts and in respect of Italy growth was seen at 1.2% in 2019 and importantly the budget deficit in 2019 and 2020 was seen at 2.9% and 3.1%, respectively, which is above the 2.4% assumed by the Italian government. The next focal point is now the 13 November deadline, when Italy is supposed to answer the Commission on its request for a revised budget.

Yesterday, we published *Reading the Markets Denmark*. We put focus on the remortgaging in social housing, take a sneak-peak ahead of the upcoming mortgage bond auctions and discuss why the DGB-Bund spread can tighten further ahead of the 15 November redemption money in Denmark. See also *Japanese Investor Flow Data*, 8 November.

## FX markets

EUR/USD extended its decline last night despite the no-surprises Fed announcement. We still look for USD strength to remain towards year-end on the carry and cyclical support the greenback is set to enjoy for some time still (see also *FX Strategy - EUR/USD break of 1.13? Yes - and here's why*, 6 November). As risk assets have recovered markedly over the past week, so has USD/JPY, helped along by a renewed uptick in US Treasury yields. EUR/CHF continues to be little moved by risk sentiment and even if Italy revises down its budget deficit next week, CHF is unlikely to pay much attention as the franc (and SNB) remains more focused on the ECB than anything else. EUR/GBP is still trading heavy, as the markets generally sense the sky is clearing but do not forget the key hurdle that any deal will have to pass is the UK parliament.

We expect focus in Scandi markets to be on Norwegian inflation at 08:00 CET: our call on core inflation falls at the lower end of analyst estimates and hence could on balance be marginally negative for NOK. However, in light of recent price action, we would probably have to see more substantial disappointment for EUR/NOK to break substantially higher. Yesterday, EUR/SEK breached below the technically important 200-day moving average at 10.308, which opens the way for the next support level at 10.2275. We have previously alluded to a couple of potentially SEK-negative events that could materialise before the 20 December Riksbank decision, such as the risk of a new election and the seasonal pattern for EUR/SEK going into year-end. We maintain that the cross is a sell on rallies towards 10.40/50 with a 10.20 target as we approach the Riksbank rate hike that is due in December.

**Key figures and events**

| Friday, November 9, 2018 | | | | Period | Danske Bank | *Consensus* | Previous |
|---|---|---|---|---|---|---|---|
| 1:30 | AUD | RBA Statement of Monetary Policy | | | | | |
| 2:30 | CNY | PPI | y/y | Oct | | | 3.6% |
| 2:30 | CNY | CPI | y/y | Oct | | | 2.5% |
| 8:00 | NOK | Core inflation (CPI-ATE) | m/m\|y/y | Oct | **0.1%\|1.8%** | *......\|1.9%* | 0.5%\|1.9% |
| 8:00 | DKK | Trade balance ex ships | DKK bn | Sep | | | 5 |
| 8:00 | DKK | Exports | m/m | Sep | | | |
| 8:00 | NOK | CPI | m/m\|y/y | Oct | | *---\|3.4%* | 0.6%\|3.4% |
| 8:00 | NOK | PPI | m/m\|y/y | Oct | | | 1.5%\|21.1% |
| 8:00 | DKK | Current account (nsa\|sa) | DKK bn | Sep | | | ...\|8.7 |
| 8:45 | FRF | Industrial production | m/m\|y/y | Sep | | *-0.3%\|1.1%* | 0.3%\|1.6% |
| 9:30 | SEK | Household consumption | m/m\|y/y | Sep | | | 1.5%\|0.3% |
| 10:30 | GBP | GDP, first estimate | q/q\|y/y | 3rd quarter | **0.6%\|1.5%** | *0.6%\|1.5%* | 0.4%\|1.2% |
| 10:30 | GBP | Monthly GDP estimate | m/m\|q/q | Sep | **0.1%\|0.6%** | *0.1%\|...* | 0%\|... |
| 10:30 | GBP | Index of services | m/m\|3m/3m | Sep | | *0.001\|0.005* | 0\|0.005 |
| 10:30 | GBP | Trade balance | GBP mio. | Sep | | *-1484* | -1274 |
| 14:30 | USD | PPI | m/m\|y/y | Oct | | *0.2%\|2.7%* | 0.2%\|2.6% |
| 14:30 | USD | PPI core | m/m\|y/y | Oct | | *0.2%\|2.5%* | 0.2%\|2.5% |
| 16:00 | USD | University of Michigan Confidence, preliminary | Index | Nov | | *97.9* | 98.6 |

*Source: Bloomberg, Danske Bank*

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