

Danske Daily

Optimism regarding trade talks and Brexit sends yields higher

Market movers today

- US-China trade talks continue today and given the statements from President Trump, the trade talks have developed well so far. Hence, we still see a decent chance of an interim deal being struck.
- UK and Ireland held “constructive” talks on Brexit yesterday. EU and UK will meet today and continue negotiations – see more below. The optimism had a significant impact on Gilts as well as the GBP. GBP strengthened against the Euro and 10Y Gilts moved some 12bp yesterday.
- On the data front, the preliminary consumer confidence for October from University of Michigan will be interesting. The service PMI has declined lately and suggests the slowdown is spreading to this part of the economy too. Consumer confidence has still held up well, which has also been highlighted by some Fed members. Any sign of weakness here would add to the pressure for more rate cuts.
- Tonight, Fed members Rosengren (non-voter, hawk) and Kaplan (non-voter, neutral) will both speak.

Selected market news

Yesterday, the Brexit negotiations got back on track after Irish PM Varadkar and UK PM Johnson met. We have not received many details yet (probably because neither side wants to risk jeopardising the fragile negotiations) but the most difficult part of the negotiation is customs, so Varadkar and Johnson may have found a way forward here. The problem is that PM Johnson’s potential majority in the House of Commons is also very fragile and he cannot afford to lose support from DUP and the group of hard Brexiteers within his own party. This means that one should not get hopes too high yet, and our base case remains another extension followed by snap election but the coming days are going to be extremely important. Today, UK Brexit Secretary Barclay and EU Chief negotiator Barnier meet at 09.30 CET followed by a briefing to the EU ambassador. EU has set a deadline today to reach an agreement before the EU summit next week but this is probably a soft deadline so a deal can be reached at a later stage (also the EU still has an possibility to call an extraordinary EU summit to ratify an agreement).

The trade talks between the US and China went very well according to President Trump. The talks continue today. The combination of more optimism on Brexit as well as the US-China trade talks sent bond yields higher in both Europe and US yesterday as risk sentiment turned positive. Asian equity markets have followed the positive sentiment this morning, while the Asian bond markets have seen rising yields this morning.

Selected reading from Danske Bank

- *US-China Trade - 60% probability of an interim deal*
- *Euro Area. Manufacturing cycle Recovery or Recession*

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Scandi

There are no market movers in Norway and Sweden today. In Denmark, the recent rise in yields has brought back 1% 30Y callables as the main 30Y callable bond, while 0.5% 30Y bonds close for issuance. The rise in yields has slowed the daily tap issuance in Danish callables mortgage bonds, and currently we are in an environment where the interest for refinancing may falter. There is still plenty of cash that needs to be reinvested and we see good demand for callables.

Fixed income markets

Yesterday was characterised by the big sell-off in European and US government bond yields. This was in our view driven by expectations of a partial trade deal between the US and China as well as the Irish PM and the UK PM characterising their meeting as constructive.

A Brexit deal as well as a deal between the US and China will push yields higher short-term, but we are seeing a slowdown in macro data and very limited inflationary pressure. Furthermore, we are entering period where there is a significant amount of cash that need to be reinvested in the Eurozone. Hence, a rise in yields and a bearish steepening is likely to be short-lived in our view.

There are potential rating reviews from Belgium and Germany. We do not expect any changes to the rating or the outlooks.

FX markets

Today we expect FX markets to be driven by trade news and Brexit deadlines (see above). On the latter EUR/GBP went down by nearly 2 percent yesterday on news that Ireland PM Leo Varadkar might support a Brexit compromise, after talks with Boris Johnson. The move comes after weeks of increased pessimism on possible progress. Further, the UK monthly GDP tracker came out decently, alleviating the need to add near-term pressure on Sterling by moving forward pricing of a possible cut by Bank of England. Details on what such a compromise would entail remains sparse, as does the reality of such a compromise in getting through parliament. For now, we prefer to fade the move in Sterling as yet another sentiment-driven shift but without being rooted in a check of political reality.

In the Scandies, yesterday's inflation prints and positive trade news aided both SEK and NOK higher. EUR/SEK especially dropped sharply as the market re-priced the Riksbank after the inflation numbers being in line with its forecast. This is the first "positive" news for the Riksbank in a long time, which in themselves should give some relief going into the October meeting. EUR/SEK dropped eight figures over the day, a bigger selloff than normal given such a small deviation from consensus. We still think they will have to reconsider the plan to hike rates and that eventually they will cut rates. We think there are good arguments for revising the rate path already at the October meeting, but it is admittedly less of a clear case after the inflation data. Please see today's Reading the Markets Sweden (published later today), for a thorough discussion about the SEK outlook.

In the same Scandi ballpark neighbouring NOK also found support from the inflation release as the Norwegian core measure (marginally) beat Norges Bank's projection. Key to the inflation outlook in Norway going forward is the last months' weakening of the NOK which will contribute to higher inflation as domestic inflation also keeps rising. Whether it ultimately will be enough for another Norges Bank rate hike all boils down the global investment environment and the level of the NOK. Irrespectively we think rates markets are wrong in pricing in 15bp worth of cuts from Norges Bank next year. Near-term, however, it's all a question about global risk sentiment for where the NOK is heading. For now we stay sidelined.

Key figures and events

Friday, October 11, 2019			Period	Danske Bank	Consensus	Previous
-	EUR	S&P may publish Germany's debt rating				
-	EUR	Moody's may publish Belgium's debt rating				
-	GBP	EU ambassadors deadline for reaching Brexit deal				
8:00	DEM	HICP, final	m/m y/y	Sep	-0.1% 0.9%	-0.1% 0.9%
9:00	ESP	HICP, final	m/m y/y	Sep	0.4% 0.2%	0.4% 0.2%
14:00	USD	Fed's Kashkari (non-voter, dovish) speaks				
14:30	CAD	Net change in full time employment	1000	Sep		23.8
14:30	USD	Import prices	m/m y/y	Sep	0.0% ..	-0.5% -2.0%
16:00	USD	University of Michigan Confidence, preliminary	Index	Oct	92.0	93.2
19:15	USD	Fed's Rosengren (non-voter, hawk) speaks				
21:00	USD	Fed's Kaplan (non-voter, neutral) speaks				

Source: Bloomberg, Danske Bank

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