21 November 2017

Danske Daily

Market movers today

- It is a **very light day** in terms of data releases; hence market focus is likely to be on the evolving political standstill in forming a new government in Germany after SPD left the coalition talks over the weekend.
- In **Hungary, the central bank decision is due** and we expect unchanged rates along with concensus expecations. The central bank may continue its dovish signals despite fast wage growth and strong economic activity.
- Statistics **Denmark publishes employment** data for September. The number of people in work rose in August after a slight fall in July, and we expect a further improvement in September.

Selected market news

In Germany snap elections moved closer yesterday as Chancellor Angela Merkel stated that she favours a new poll over a minority government, see *Politico*. With SPD having ruled out a new 'grand coalition' and Merkel ruling out a minority government the only option left seems to be a new election, see also *Flash Comment: The Jamaica Party is over*, 20 November 2017. A new government is not likely to be formed until well into 2018 delaying any potential Eurozone reforms.

Fed Chairman Janet **Yellen yesterday announced she will not continue at the Fed** when Jerome Powell takes over as Chairman after Yellen's term ends in February, see *Bloomberg*. Her decision leaves Donald Trump with a fourth spot to fill on the Federal Reserve Board.

The US leading indicator from Conference Board jumped back in October rising 1.2% m/m (consensus 0.8% m/m). September was revised up to 0.1% m/m from -0.2% m/m. The data underlines the strong picture of the US economy currently. US 2-year yields rose to a new high yesterday flattening the US yield curve further. The flattening has received much attention lately in relation to Fed policy with some arguing it worries the Fed as it is a signal of an economic slowdown. However, a San Francisco Fed paper yesterday argues that the low long-term yield is justified by a lower 'normal rate', risk of persistently low inflation and fiscal and geopolitical uncertainty, see *paper*.

Asian stock markets were strong overnight with gains across the board defying signs of a Chinese slowdown. China's Tencent grabbed the *headlines* yesterday as they joined the ranks of Apple and Facebook breaking the USD500 bn mark in market value. Tencent is the maker of the Chinese social media WeChat with close to one billion users. Chinese company Alibaba might be next in line as they currently have a market value of USD 474 bn.

Yesterday we published an update on the latest Chinese measures to crack down on shadow banking announced Friday last week: See *Flash Comment: China takes more steps to fight financial risks*. We also released travel notes from US trip visiting political analysts, think tanks, economists and journalists, see *US travel note: Tax cuts are coming but will be watered down*.

Selected readings from Danske Bank

- *US travel note: Tax cuts are coming but will be watered down*
- *Strategy - Consolidation from stretched levels*
- *New yield forecasts*

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Arne Lohmann Rasmussen on the prospects for the global bond markets

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- *FX Forecast Update*
- *Weekly Focus*

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Scandi markets

There are no big market movers in Scandi today.

Fixed income markets

It was again a positive day for the peripheral markets with spreads to Germany grinding tighter. In the US the curve continued to flatten even though this was a bear-flattening as 5Y US Treasury yields rose some 3.5bp, while 30Y was up 2bp. The flattening of the US treasury curve seen during this hiking cycle are reminiscent of the move in 2004-2005, where the US Treasury curve also flattened very significantly. The Fed Chairman Greenspan dubbed this the “bond conundrum”. The conundrum today is driven by lower inflation expectations, the market’s perception of the future fed funds equilibrium rate as well as a lower term premium. We currently see more risk of a further flattening of the US yield curve rather than a steepening as the BoJ and ECB continues the QE. Hence, there continues to be demand for US Treasuries from abroad even though the FX hedge is very expensive.

The refinancing auctions in Denmark continue and all issuers are coming to the market in the 1Y segment. RD, Nordea, Nykredit, BRF and DLR are all selling 1Y bonds for a total of DKK 15.4bn. On top of this they are also selling across the curve in 2Y, 3Y and 5Y bonds. We expect strong demand for the longer maturities as seen yesterday, where there was a bid-to-cover of more than 8 for the 9Y BRF noncallable bond – even though BRF only sold DKK 70m. However, the spread to DGB 1.75% 11/25 was 60bp. We strongly recommend buying the 3Y and especially the 5Y segment at the auctions.

In the European government bond market Finland will do a EUR 1bn tap in the new 10Y benchmark bond. Looking at the PSPP detail from August and September as well as the total purchase on Finnish government bonds and agencies, we expect that ECB has been active in the new 10Y benchmark or in some of other long-dated Finnish government bonds. This is due to the increase in duration on the Finnish PSPP portfolio from August to September, the weekly redemption data as well as ECB must be close to holding 33% of the Finnish PSPP-eligible bonds given the size of the portfolio relative to the outstanding stock of eligible PSPP bonds. Hence, we expect that the ECB will also be active after the auction. This will be the last auction from Finland in 2017 and thus we expect to see further performance in the 10Y RFGB versus peers.

FX markets

EUR/USD was somewhat volatile yesterday as Merkel refused to resign after the break-down in coalition talks, and as Yellen said she would step down from the board once Powell takes over at the Fed. In yesterday’s *FX essentials*, 20 November 2017, we stressed that the cross should stay range bound ahead of year end (1.1479-1.1880) but that we would tactically consider selling on spikes above 1.18 for a move lower short term. Today watch out for ECB’s Coeure speaking; he has previously delivered very insightful speeches on notably euro-zone portfolio flows which we deem could become key next year when markets gear up for the next ‘wave’ of ECB ‘normalisation’.

USD/JPY climbed higher yesterday supported by improved risk appetite. While we maintain a constructive view on USD/JPY over the medium term horizon, a stretched short JPY positioning (the latest IMM data showed that speculative accounts added further JPY shorts in the week ending 14 November) combined with stretched positioning/pricing of risk premiums across asset classes, still represent a downside risk short term. Tactically, we would consider buying USD/JPY on dips towards 111.65 (if the cross fails to break below this key technical support level) for a move towards 114.

GBP gained yesterday on reports that the UK government is preparing to increase its offer for the EU divorce bill from EUR 20bn to EUR 40bn. Meanwhile, political uncertainty in Germany continues weigh on the EUR and to some extend offsetting the negative impact on GBP stemming from political uncertainty in the UK leaving EUR/GBP risks a bit more balanced. As such, we still see EUR/GBP within the 0.8650-0.90 range near term, and tactically we maintain a buy on dips bias.

The SEK remains under pressure from the housing market with focus this week on the RB's Financial Stability report (due on Wednesday). As such, we expect EUR/SEK to remain bid as a 'housing risk premium' has entered SEK crosses and we prefer to buy EUR/SEK on dips and look for break of 10.00.

While we emphasize the vulnerability of the NOK in the month to come (seasonality), we underline that the case for a 2018 Norges Bank hike – unlike the Riksbank case – has actually improved in recent weeks amid better data (across the board, incl. housing) and a much weaker currency (3.7% weaker than Norges Bank forecast). Our fundamental predisposition therefore remains to sell EUR/NOK via options, but admittedly technicals and foreign investor focus on the Swedish housing market makes the timing tricky. Key resistance levels are 9.8004 (last week's high), 9.8906 (Dec 14 high) and 10.00 (figure). Key support levels are 9.70 (figure) 9.6435 (16 Nov low).

Key figures and events

Tuesday, November 21, 2017				Period	Danske Bank	*Consensus*	Previous
1:30	AUD	RBA November Meeting Minutes					
9:00	DKK	Employment (monthly)	1.000|m/m	Sep			2.700|0.2
14:00	HUF	Central Bank of Hungary rate decision	%		**0.9%**	*0.9%*	0.9%
16:00	USD	Existing home sales	m (m/m)	Oct		*5.4*	5.39|0.7%
16:00	EUR	ECB's Coeure speaks in Frankfurt					

Source: Bloomberg, Danske Bank

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Expected updates

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