

24 January 2017

Danske Daily

Market movers today

- In the **euro area**, the **PMI figures** are due to be released. The PMIs have improved significantly over the past few months in both manufacturing and services. However, the leading PMI indicators show more mixed signals. In line with other survey indicators, we still expect manufacturing PMIs to increase, but less than in previous months. Note also that the input/output prices increased significantly throughout 2016, and could start to flatten as commodity prices are stabilising. With regard to leading service PMIs, future business expectations increased significantly in December while the new business indicator remained stable. Thus, we expect service PMIs to see a further increase in January.
- Today, the **US PMI index** brings us the first indications on 2017 activity. The **manufacturing PMI index** rose again in December, reaching 54.3 up from 54.1 in November, the highest level in almost two years. It seems as if the manufacturing sector ended 2016 on a strong footing and we expect the current trend to have continued into 2017, although we are still waiting for 'hard data' to confirm this. We estimate the Markit manufacturing PMI index has stayed more or less unchanged at around 54.3 in January.
- In the **UK**, the main event is the **Supreme Court ruling**. According to a previous story in *The Guardian*, 11 January 2017, the UK government expects to lose the appeal. Based on Theresa May's speech, it seems as if she has accepted that parliament needs to be involved in the negotiation process, as she mentioned the final deal will be put to a vote in both Houses of Parliament. For more details on May's speech, see *Brexit Monitor #21*, 17 January.
- The **Italian constitutional court** will hold a hearing today regarding the **new electoral reform** for the lower house. The outcome could become a market mover as the expectations of a snap election may increase despite the outcome. Increased expectations for a new election would not be positive for Italian government bonds.

Selected market news

- While Trump's inauguration speech did not contain much further insight into his economic policy, the first business day in office did. As one of his first actions as the 45th president of the US, **Donald Trump signed an executive order to withdraw the US from the Trans Pacific Partnership (TPP)**. Trump is likely to keep his 'tough on trade' approach and squeeze Mexico (and Canada) further with NAFTA seemingly next on his 'renegotiation' agenda.
- The US's withdrawal from the TPP initially sparked negative risk sentiment, with leading US equity indices dropping and Treasury bonds rallying in the earlier parts of the US session (albeit reversing some later). The morning **activity in Asia has been much more muted**, with Hang Seng gaining slightly, Nikkei losing a bit, Japanese government bonds fairly unchanged and the dollar appreciating on the margin.

Selected readings from Danske Bank

- *ECB Review: Draghi remains dovish until core inflation rises*
- *Markedspladsen (only in Danish)*
- *Reading the markets Denmark*

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Fixed income markets

The ruling of the UK Supreme Court is due today. While the Court is expected to rule in favour of including Parliament, it will hardly come as a surprise given that Theresa May seems to have accepted that parliament needs to be involved in the negotiation process.

The first step in Trump's 'trade war' was taken yesterday, with him signing an executive order withdrawing the US from the Trans Pacific Partnership. The withdrawal from the TPP is likely to be just the first 'renegotiation' of trade deal that Trump has on his plate. Next up: NAFTA.

The Italian constitutional court will hold a hearing today regarding the new electoral reform for the lower house. The outcome could become a market mover as expectations of a snap election may increase despite the outcome. Increased expectations for a new election would not be positive for Italian government bonds.

Following the sell-off trend since Christmas, risk sentiment turned with both German cash and EUR swap curves flattening yesterday. The periphery in particular performed well relative to Germany with 10Y SPGBs outperforming the equal Bund despite the announcement of a new 10Y (Apr27) expected to be introduced today. Judging by the short squeeze three minutes after the new 10Y announcement the auction should be extremely well received.

In Scandi, we await the new 10Y in Denmark (Nov 27) and Sweden (May 28) scheduled for tomorrow. See *Government Bonds Weekly: New 10Y bonds in Denmark and Sweden*, 20 January 2017.

FX markets

EUR/USD traded just above the 1.0750 level most of the time overnight as comments from US Treasury Secretary nominee Steven Mnuchin about the strong dollar weakened the greenback further. As such, we still see EUR/USD in the range of 1.0350-1.0750 in coming months, targeting 1.04 in 1M and 1.05 in 3M. However, the lack of details in US president Trump's economic plans is clearly hurting the dollar, and as it remains uncertain when we will get more details, it could continue to grind lower in the near term. Tactically, we still favour selling EUR/USD on rallies, but note that technically, a clean break of the 5 December high at 1.0796 could open up for further EUR/USD upside and thus challenge our call for a lower EUR/USD near term.

GBP remains supported ahead of the Supreme Court announcement today (10:30 CET) on whether it is the government or parliament that can trigger Article 50. It is widely expected that the government will lose the appeal, meaning that parliament will have to vote in favour of triggering Article 50 before Brexit becomes a reality. If the ruling turns out as expected, it should have little market impact, as a decent size of short GBP bets are likely to have been cleared after May's speech. If the Supreme Court on the other hand rules that the government can trigger Article 50, it would be very negative for GBP. Hence, we believe the balance of risk is asymmetric as a government-loss is priced in, whereas a (surprise, but possible) government win would spark instant GBP weakness. On Friday, US President Trump and UK Prime Minister May are due to meet and discuss the US-UK special relationship. This might result in a positive statement from the two leaders and thus potentially support GBP short term. However, the reality might be less rosy and it is also worth noting that a US-UK free trade agreement cannot be created before details about the UK's future relationship with the EU in terms of an EU-UK free trade agreement and the customs union has been resolved. In any case, we still expect GBP to come under pressure as the triggering of Article 50 moves closer. We target EUR/GBP at 0.88 in 3M but see risks skewed to the upside.

In a very thin data calendar, EUR/NOK continues to trade 'heavy', shrugging off the oil price decline. The cross dropped below the 9.00 level yesterday and has been stable around 8.99 overnight. According to our short-term financial model, EUR/NOK is slightly undervalued suggesting a limited near-term downside potential. However, we expect the cross to continue to grind lower and we still like selling the cross on rallies and stick to our strategic short EUR/NOK positions in the FX Trading Portfolio (spot) and FX Top Trades (put spread), respectively.

Key figures and events

Tuesday, January 24, 2017

				Period	Danske Bank	Consensus	Previous
1:30	JPY	Nikkei Manufacturing PMI, preliminary	Index	Jan			52.4
9:00	FRF	PMI manufacturing, preliminary	Index	Jan	53.7	53.3	53.5
9:00	FRF	PMI services, preliminary	Index	Jan	53.3	53.1	52.9
9:30	DEM	PMI manufacturing, preliminary	Index	Jan	55.9	55.4	55.6
9:30	DEM	PMI services, preliminary	Index	Jan	54.5	54.5	54.3
10:00	EUR	PMI manufacturing, preliminary	Index	Jan	55.4	54.8	54.9
10:00	EUR	PMI services, preliminary	Index	Jan	54.0	53.9	53.7
10:00	EUR	PMI composite, preliminary	Index	Jan	54.6	54.5	54.4
10:30	GBP	Supreme Court ruling on Brexit					
12:00	TRY	Central Bank of Turkey rate decision	%		8.00%	8.50%	8.00%
14:00	HUF	Central Bank of Hungary rate decision	%		0.90%	0.90%	0.90%
15:45	USD	Markit PMI manufacturing, preliminary	Index	Jan	54.3	54.5	54.3
16:00	USD	Existing home sales	m (m/m)	Dec		5.53	5.61 0.7%
17:00	EUR	ECB's Praet speaks in Italy					
19:00	EUR	ECB's Lautenschlaeger speaks in Germany					

Source: Bloomberg, Danske Bank Markets

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