28 October 2016

Danske Daily

Market movers today

- It's a busy day today on the data front with a focus on the US. Most important is **US GDP** data for Q3 as it's an important input to the Fed's rate hike decision. We have a below-consensus estimate of 2.0% q/q AR (consensus 2.6% q/q AR), which would be disappointing given the low growth in the previous three quarters (has averaged 1.0% AR). The US GDP report will also provide news on core inflation pressures with the Q3 core PCE print.
- The US **Employment Cost Index** (ECI) for Q3 – also released at 14.30 - will also be important for the Fed. ECI has hovered around 0.6% q/q over the past two years corresponding to around 2.5% on an annualised basis. Consensus is for an unchanged rate but any increase from this level could add to the Fed's inclination to hike rates in December. Some wage pressure measures (job openings, jobs hard to get versus jobs plentiful etc.) point to rising wage pressures.
- In Europe, eyes will be on **preliminary German inflation** data for October starting with the first regional länder data at 9.00CET and the release for all Germany at 14.00CET. Inflation is set to rise above 0.5% y/y for the first time in more than a year. We look for inflation to be on a rising trend globally over the coming quarters due to the rise in commodity prices this year, *see Global Inflation: Set to surprise on the upside lifting long-dated inflation pricing*, 27 October 2016.
- Other global events to follow will be EU data on economic sentiment for October and the rate decision from the Central Bank of Russia (expected unchanged at 10.0%).
- In **Scandinavia, Norway releases retail sales and unemployment and retail sales is also due in Sweden**, see next page.

Selected market news

The bond sell-off continued yesterday as markets started to expect gradual rates increases from the Fed starting in December while hawkish comments from some ECB members caused anxiety in euro bond markets (see below). The sell-off is having a negative effect on equities which closed slightly lower in US yesterday. Asian stock markets are mixed this morning with the Nikkei higher but Chinese stocks lower in the offshore market.

In commodity markets oil prices recovered a bit yesterday rising above USD50 per barrel again. But the big move has been in iron ore where prices have been spiking to the highest level since early 2015. Stronger steel demand from China this year due to the boost in infrastructure and residential construction is lifting prices. The rise in iron ore and metal prices is having a positive impact on emerging markets assets, not least Brazil which is a big producer of iron ore. Brazil's stock market is up 48% this year (85% in USD as the real has strengthened as well).

In Japan, deflation continued with the CPI at -0.5% y/y (CPI ex fresh food) in September. The strengthening of the JPY over the past year is making it hard for the Bank of Japan to get inflation up.

Selected readings from Danske Bank

- *Norges Bank Review: Unchanged rates and signals*
- *Sweden: Soft Riksbank suggests more QE in December*

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Scandi markets

The Riksbank surprised on the dovish side yesterday sending EUR/SEK sharply higher (see below). Focus today will be on retail sales in Sweden and Norwegian data on retail sales and unemployment.

Fixed income markets

The notion of a 'dovish hike' from the Fed has often been mentioned but it is now time to introduce the concept of a 'hawkish extension' from the ECB. Hawkish comments from ECB executive board member Mersch (hawk) hit the market yesterday evening. The comments confirm our view that the governing council is becoming more and more divided while they also suggest the ECB wants to normalise policy rates (at least to zero) earlier than the Fed did after tapering. We still believe the ECB will extend QE by six months to September 2017.

Key sentences from Mersch are "The longer we remain in this low interest rate environment, the stronger the side effects of our measures will be. So it has to be our shared goal to leave behind this special situation as soon as possible in order to minimise potential damage." The comments also included a reference to bank profitability: "The fact that additional lending in the euro area is losing momentum and that German banks are saying that the negative deposit facility rate is constraining lending volumes warrants attention. We must be vigilant that this development does not spread to other euro area countries." Relevant for extension in December he said "Despite all these side effects, I would like to emphasise that the benefits of our monetary policy so far are prevailing. But this situation could change the longer these special circumstances continue."

The violent global fixed income sell-off continued yesterday with Gilts up by 10bps and Bunds closing 9bps higher. 5Y Germany has moved back above -40bp and for the first time since June is again eligible to be included in QE purchases.

Italy will be conducting its usual end of month taps in the 5Y and 10Y today. Following last week's crucial rating reviews, we expect this 'Rating Friday' to be a lot less eventful. Moody's will be reviewing the ratings of both {FI} Finland and {NE} Netherlands and we do not expect any changes to ratings or outlooks.

FX markets

EUR/SEK rose about 15 figures on the back of the Riksbank decision and naturally so. The Riksbank now expects the repo rate to be -0.56 by Q4 17 from -0.32 previously. This is important as it is unlikely that the ECB will cut rates deeper into negative territory. Clearly, Scandinavian banks are dealing better with negative rates than several euro area ones and there are a host of reasons for that, including a much larger fixed deposit base in the euro area countries. How banking systems are dealing with negative rates may affect relative monetary policy.

EUR/SEK is trading in uncharted territory and it is difficult to call the peak just yet. Short-term, expect EUR/SEK to trade in a volatile and choppy fashion. Over the medium-term, the upside in EUR/SEK should be limited given that the pair is already trading at overvalued levels in our view and also given that the ECB is expected to extend QE in December when we expect a Riksbank taper relative to the ECB. Note that the Riksbank still expects more than 5% SEK appreciation over the forecast horizon, albeit from a higher KIX level.

Following the Norges Bank meeting yesterday, global developments will be an important driver for NOK in the near-term; not least the development in the oil price as NB yesterday re-stated that the stronger NOK 'partly' reflects higher oil prices. As we expect the oil price to fall in the coming months and given an unfavourable year-end liquidity environment for the NOK, we think the NOK will weaken in the coming months, forecasting EUR/NOK at 9.10 in 1M and 9.20 in 3M. This view supports NB keeping rates unchanged in December also. In 2017, we expect a gradual appreciation of the NOK on a higher oil price, fundamental valuation and real rate differentials.

Key figures and events

Friday, October 28, 2016				Period	Danske Bank	*Consensus*	Previous
-	EUR	Moody's may publish Netherlands's debt rating					
-	EUR	Moody's may publish Finland's debt rating					
-	GBP	Nationwide house prices	m/m|y/y	Oct		*0.2%|4.9%*	0.3%|5.3%
-	GBP	S&P publishes UK's debt rating					
8:00	NOK	Retail sales, s.a.	m/m	Sep	**0.4%**		0.4%
8:45	FRF	Household consumption	m/m|y/y	Sep			0.7%|1.0%
8:45	FRF	HICP, preliminary	m/m|y/y	Oct	**...|0.6%**		-0.2%|0.5%
9:00	DKK	Confidence indicator, industry, s.a.	Net balance	Oct			-8
9:00	ESP	HICP, preliminary	m/m|y/y	Oct	**...|0.2%**	*---|0.1%*	0.7%|0.0%
9:00	ESP	GDP, preliminary	q/q|y/y	3rd quarter	**0.7%|...**	*0.7%|3.1%*	0.8%|3.2%
9:00	DKK	CB's securities statistics		Aug			
9:00	DKK	Foriegn portfolio investments		Sep			
9:30	SEK	Retail sales s.a.	m/m|y/y	Sep	**0.5%|3.0%**		0.6%|2.8%
9:30	EUR	ECB's Coeure speaks in Frankfurt					
10:00	NOK	Unemployment	%	Oct	**2.8%**		2.8%
11:00	EUR	Business climate indicator	Net bal.	Oct		*0.5*	0.5
11:00	EUR	Consumer confidence, final	Net bal.	Oct			
12:30	RUB	Central Bank of Russia rate decision	%		**10.0%**	*10.0%*	10.0%
14:00	DEM	HICP, preliminary	m/m|y/y	Oct	**...|0.6%**	*0.1%|0.6%*	0.0%|0.5%
14:30	USD	GDP, first release, preliminary	q/q ann.	3rd quarter	**2.0%**	*2.5%*	1.4%
14:30	USD	Employment cost index	m/m	3rd quarter		*0.6%*	0.6%
14:30	USD	Personal consumption, preliminary	q/q	3rd quarter		*2.6%*	4.3%
14:30	USD	PCE core, preliminary	q/q	3rd quarter		*1.6%*	1.8%
16:00	USD	University of Michigan Confidence, final	Index	Oct		*88.1*	87.9

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Expected updates

None.

Date of first publication

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