Wednesday, 17 May 2023

Dear reader,

There will be no KBC Economics-Markets reports on Thursday May 17th and Friday May 18th.
We resume our publications on Monday May 21st.

KBC Sunrise Market Commentary

Markets

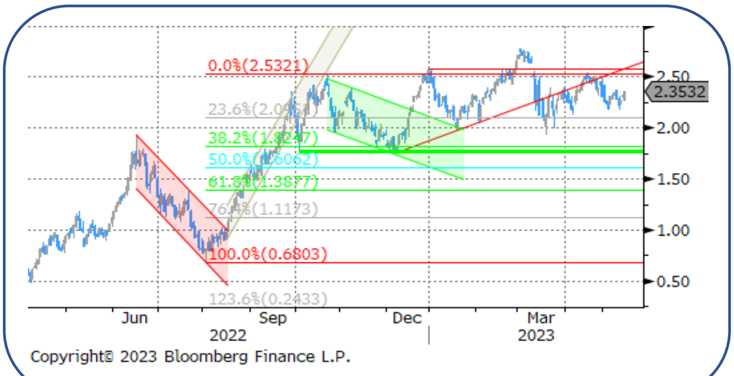
- **US treasuries extended their underperformance against German Bunds yesterday as some data beats strengthen the notion that the US customer isn't backing down yet, hinting at a more resilient economy.** Core US retail sales rose by 0.6% M/M with the control group even gaining 0.7% M/M and providing a solid start to Q2. The NAHB housing index increased a fifth consecutive time to the highest level since July (see News & Views). More Fed governors weighed in the debate, highlighting the toss-up that the June policy meeting will be. NY Fed Williams seems in favour of a wait-and-see approach like Chicago Fed Goolsbee and to a lesser extent Dallas Fed Logan. Atlanta Fed Bostic will let the data decide while Minneapolis Fed Kashkari and Richmond Fed Barkin believe there's no barrier to further rate increases. Cleveland Fed Mester joined that hawkish camp: "At this point, based on the data I have so far, given how stubborn inflation has been, I can't say I'm at a level of the Fed Funds rate where it's equally probably that the next move could be an increase or a decrease". US yields rose by 1.1 bp (30-yr) to 7.3 bps (2-yr). German yields added 3.9 bps (30-yr) to 6.1 bps (5-yr). Mixed German ZEW investor sentiment went unnoticed. Hawkish Austrian ECB member Holzmann said that he preferred a 50 bps rate hike earlier this month and that the ECB shouldn't pause hikes before they reach 4%. After last month's decision, he thinks that the bar to returning to 50 bps rate hikes is high. **The dollar overall profited from the yield advantage** with the trade-weighted greenback (DXY) testing the recent high at 102.75. EUR/USD approached the sell-off low at 1.0846, before closing at 1.0862. US stock markets yesterday underperformed (Dow -1%) with **risk aversion creating some additional USD-safe haven flows.** The US debt ceiling stalemate remains firmly in place with US Treasury Secretary Yellen's warnings proving futile for the moment. Apart from the US T-Bill and CDS market, the overall market impact remains low even as we're only a fortnight away from the assumed "X-date". Previous debt ceiling episodes learnt that a solution will eventually follow. Today's eco calendar is extremely thin with only US housing starts and building permits. It doesn't become much better on Thursday and on Friday, **making way for central bankers and especially risk sentiment to set the tone for trading. Current trends are sluggish stocks, weakness in US Treasuries and a better dollar.**

News & Views

- **Q1 Japanese growth rebounded more than expected.** Activity during the January-March quarter expanded at **an annualized rate of 1.6% (0.4% Q/Q),** beating expectations for a more modest growth of 0.8%. Activity was mainly supported by **a rebound in private consumption (0.6% Q/Q) and business spending (0.9% Q/Q)** as consumer spending regained traction post-Covid. Tourism was an important factor in the consumption revival. **Net exports subtracted 0.3 ppts from growth as exports (-4.2%) declined faster than imports (-2.3%).** The Q1 GDP price deflator printed exactly at 2%, close to expectations. The figure for the previous quarter was downwardly revised from 0.1% (QoQa) to -0.1%, which brought to economy in **a technical recession in the second half of last year.** A rebound in domestic demand as such is a positive development. However, the Q1 data probably needs confirmation for the BOJ to change its ultra-easy monetary policy. Markets this morning aren't preparing for such move as the 10-y yield dropped 3 bps to 0.367%. The yen also weakens with USD/JPY extending recent uptrend (136.65).

- **US NAHB Home Builders sentiment unexpectedly increased further from 45 in April to 50 in May.** According the NAHB statement *"Limited existing inventory, which has put a renewed emphasis on new construction, resulted in a solid gain for builder confidence in May even as the industry continues to face several challenges, including building material supply chain disruptions and tightening credit conditions for construction loans".* The May rise in the index was the fifth consecutive monthly rise. It was the first time for the index to reach the 50-level since July 2022.

Graphs



GE 10y yield

The ECB adopted a more gradual approach by slowing its tightening pace from 50 to 25 bps in May. It stated that in the base scenario rates will be brought to sufficiently restrictive levels (i.e. more hikes to follow) and will stay there for as long as necessary. **Combined with APP reinvestments fully stopping from 2023H2 on, we expect a solid bottom below European/German yields.**

US 10y yield

The Fed hinted at a pause after delivering a 25 bps hike in May. **The regional bank implosion is expected to additionally weigh on activity going forward.** But elevated inflation ties the central bank's hands in terms of rapid rate cuts. Markets disregard Fed guidance and expect the cutting cycle to start in 2023 H2 nonetheless. Short term yields remain near YtD lows. Longer tenors, including the 10-yr, suffer from recessionary fears. Support around 3.3% survived.

EUR/USD

The euro profited from subsiding energy concerns and the ECB's policy stance. Even as the latter downshifted the tightening pace, it retains a hawkish upper hand vs. the Fed. Combined with local financial stability concerns, a sustained dollar comeback is unlikely. Failure to break the EUR/USD 1.1095 YtD high triggered rebound action lower.

EUR/GBP

The usually risk-sensitive **pound proved surprisingly resilient during the banking turmoil.** The BoE raised rates by 25 bps. A next move higher is still conditional but in any case priced in already. Divergency within the BoE about the way forward contrasts **with ongoing hawkish ECB rhetoric.** It adds to the already weak structural GBP cards (weaker growth prospects, twin deficits, long term brexit consequences…), but sterling tries to fight back.

Calendar & Table

Wednesday, 17 May		Consensus	Previous
US			
13:00	MBA Mortgage Applications	--	6.30%
14:30	Housing Starts Total/MoM (Apr)	1400k/-1.40%	1420k/-0.80%
14:30	Building Permits Total/MoM (Apr)	1430k/0.00%	1430kR/-7.70%R
Japan			
01:50	**GDP SA QoQ/QoQ Annualized (1Q P)**	**0.40%A/1.60%A**	**0.00%/-0.10%R**
01:50	GDP Deflator YoY (1Q P)	2.00%A	1.20%
01:50	GDP Private Consumption QoQ (1Q P)	0.60%A	0.20%R
01:50	GDP Business Spending QoQ (1Q P)	0.90%A	-0.70%R
01:50	Inventory Contribution % GDP (1Q P)	0.10%A	-0.50%
01:50	Net Exports Contribution % GDP (1Q P)	-0.30%A	0.40%
EMU			
08:00	EU27 New Car Registrations (Apr)	--	28.80%
11:00	CPI MoM/YoY (Apr F)	0.70%/7.00%	0.70%/6.90%
11:00	CPI Core YoY (Apr F)	5.60%	5.60%
Events			
01:00	**Fed’s Bostic and Goolsbee Discuss the Economic Outlook**		
09:15	ECB's De Cos Speaks		
11:00	ECB's Elderson Speaks		
12:00	ECB's Centeno Speaks at Bank of Portugal Press Conference		
17:15	**ECB's Guindos Speaks**		

10-year	Close	-1d		2-year	Close	-1d	Stocks	Close	-1d
US	3.53	0.03		US	4.08	0.07	DOW	33012.14	-336.46
DE	2.35	0.04		DE	2.66	0.05	NASDAQ	12343.05	-22.16
BE	3.07	0.05		BE	2.74	0.06	NIKKEI	30080.09	237.10
UK	3.82	0.00		UK	3.81	-0.01	DAX	15897.93	-19.31
JP	0.36	-0.04		JP	-0.06	-0.01	DJ euro-50	4315.51	-0.90
IRS	EUR	USD	GBP	EUR	-1d	-2d	USD	-1d	-2d
3y	3.20	3.89	4.26	Ester	3.1470	0.0020			
5y	3.03	3.60	3.98	Euribor-1	3.1580	0.0080	Libor-1	5.1077	0.0000
10y	3.00	3.53	3.74	Euribor-3	3.3820	0.0240	Libor-3	5.3304	0.0000
				Euribor-6	3.6580	-0.0050	Libor-6	5.3831	0.0000
Currencies	Close	-1d		Currencies	Close	-1d	Commodities	Close	-1d
EUR/USD	1.0862	-0.0012		EUR/JPY	148.16	0.15	CRB	259.89	-1.76
USD/JPY	136.39	0.27		EUR/GBP	0.8700	0.0021	Gold	1993.00	-29.70
GBP/USD	1.2488	-0.0041		EUR/CHF	0.9738	-0.0001	Brent	74.91	-0.32
AUD/USD	0.6656	-0.0044		EUR/SEK	11.2896	0.0339			
USD/CAD	1.3482	0.0015		EUR/NOK	11.6462	0.1177			

Contacts

KBC Economics – Markets Brussels		Global Sales Force	
Mathias Van der Jeugt	+32 2 417 51 94	Corporate Desk(Brussels)	+32 2 417 45 82
Peter Wuyts	+32 2 417 32 35	Institutional Desk(Brussels)	+32 2 417 46 25
Mathias Janssens	+32 2 417 51 95	CBC Desk (Brussels)	+32 2 547 19 19
		France	+32 2 417 32 65
		London	+44 207 256 4848
		Singapore	+65 533 34 10
CSOB Economics – Markets Prague		**Prague**	+420 2 6135 3535
Jan Cermak	+420 2 6135 3578		
Jan Bures	+420 2 6135 3574		
Petr Baca	+420 2 6135 3570		
CSOB Economics – Markets Bratislava		**Bratislava**	+421 2 5966 8820
Marek Gabris	+421 2 5966 8809		
K&H Economics – Markets Budapest		**Budapest**	+36 1 328 99 85
David Nemeth	+36 1 328 9989		

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