

Sunrise



Friday, 26 May 2023

KBC Sunrise Market Commentary

Markets

- UK bonds crashed for a second day straight with yields adding 10.6-19.2 bps across the curve. **UK money markets discount an additional 100 bps tightening by December** following the big upside CPI surprise Wednesday morning. Sterling initially revisited YTD highs but unable to force a break higher, technical return action kicked in. EUR/GBP eventually closed narrowly above 0.87. Bonds in the US and Germany slid as well with huge underperformance of the former. US yields ripped between 0.9 (30-y) and 15.6 (2-y) bps higher. Second-tier but above-consensus data including weekly jobless claims spurred the move with **recessionary along with financial stability concerns easing**. Markets even fully priced in a July rate hike. **Optimism about US negotiators reaching a debt ceiling deal** also helped sentiment. A two-year suspension in return for spending cuts is on the table. German yields followed from a distance. Changes varied from +3.7 to 6.2 bps with the belly underperforming the wings and the 10-y yield testing the 2.53% resistance area. ECB's Nagel, Knot and Villeroy hit the wires on a hawkish note. The US dollar performed strongly, even as Wall Street posted gains up to 1.7% (Nasdaq, Nvidia-sparked rally). EUR/USD closed around important support of 1.0727. The trade-weighted index took a look beyond 104.089 resistance to close at 104.25 – the highest since mid-March. USD/JPY ventured north of 140 for the first time since November last year.
- The Asian session this morning is a quiet one. Aside from Tokyo CPI (see below) there's little news. Speaker of the House McCarthy vowed to continue working until a debt ceiling deal is reached. We wouldn't be surprised if they'd strike one during the weekend. In the run-up, we still have **US PCE deflators** and durable goods orders scheduled for release today. The former are the Fed's preferred inflation gauge and seen accelerating from 4.2% to 4.3% on a 0.3% m/m pace for the headline. Core PCE should come in at an unchanged 4.6% (0.3% m/m). An outcome in line with expectations probably is enough to sustain the current bond yield trend, be it on a less blistering pace. The technical charts offer help as well with the US 2-y and 10-y yield surpassing 4.50% and 3.80% levels respectively. A weekly close above that level would be a major plus. This also goes for the DXY dollar closing above 104.089 level and EUR/USD sub 1.0727. Both levels are being tested as we write. **UK April retail sales this morning surprised to the upside**, with the core gauge double the 0.4% that was expected. It comes with a downward revision of the March figure though. EUR/GBP in a first reaction barely budes. The 0.87 big figure for the time being survives.

News & Views

- The Reserve Bank of South Africa yesterday raised its policy rate by 50 bps to 8.25%**. This was expected by the majority of analysts. The Bank slightly upwardly revised its growth forecast for this year from 0.2% to 0.3%. Expected growth for 2024 and 2025 was left unchanged at 1.0% and 1.1% respectively. **Forecasts for 2023 and 2024 inflation were raised to 6.2% (from 6.0) and 5.1% (from 4.9%)**. The SARB targets an inflation between 3-6%. **Risks to the inflation outlook still are assessed as being to the upside**. At the current repurchase rate level, policy is labelled as being restrictive, consistent with elevated inflation and risks. The Bank also sees a growing external financing need with the current account deficit expected to rise from 2.5% this year to 3.6% in 2025. SARB Governor Kganyago mentioned the **risk that globally tighter financial conditions are raising the risk profiles of countries needing foreign capital**. In this respect, the rand weakened sharply further yesterday reaching a record low against the dollar near USD/ZAR 19.84.
- Inflation excluding fresh food in the Tokyo area in May slowed more than expected from 3.5% on April to 3.2%**. At the same time, **the core measure excluding food and energy unexpectedly rose from 3.8% to 3.9%**, the highest level in more than 40 years. The Tokyo data are seen as a good precursor for the national data. The data suggest that inflation still might hold above the BoJ 2.0% inflation target for quite some time, **fueling the debate whether the Bank should gradually tweak its ultra-easy policy**. The combination of higher US yields recently and the ongoing easy policy stance of the BoJ overnight temporarily propelled the USD/JPY cross rate north of the psychological barrier of 140 (currently 139.7).

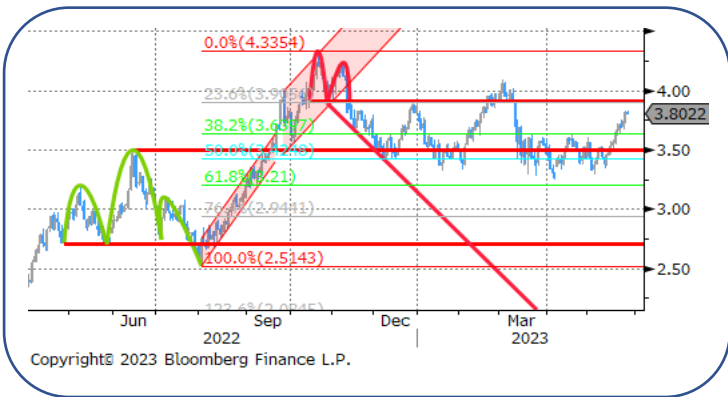
Graphs



GE 10y yield

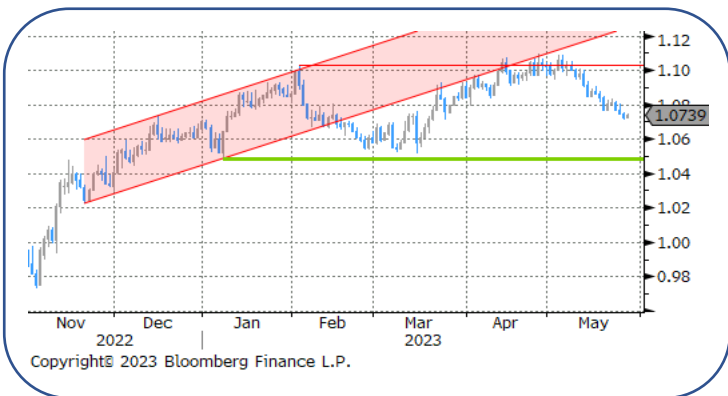
The ECB adopted a more gradual approach by slowing its tightening pace from 50 to 25 bps in May.

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. The German 10-y is extensively testing the 2.50%/2.57% resistance area.



US 10y yield

The Fed hinted at a pause after a 25 bps hike in May. The regional bank implosion is expected to weigh on activity but elevated inflation prevents the Fed from rapid rate cuts. Markets still expect them in 2023H2, but systematically push the start further in time amid easing banking and recession concerns. They even begin discounting another hike first. Yields staged an impressive comeback. The 10-y surpassed 3.60% resistance, eyeing 3.90% next.



EUR/USD

The US dollar struck back in May. Local financial stability concerns moved to the background and market focus returned to monetary policy. Rebounding US yields brought EUR/USD to the 1.0727/1.0735 support zone. A break lower paves the way towards 1.06 in first instance. 1.0484/1.0499 is the hard lower bound as the ECB still retains a hawkish upper hand vs. the Fed.



EUR/GBP

The BoE's conditional rate hike approach comes back to haunt them after May CPI delivered a nasty surprise. UK money markets expect several more rate hikes this year, keeping sterling near Ytd highs. We hold our MLT bearish sterling bias for now. Divergency within the BoE about the way forward contrasts with unisono hawkish ECB rhetoric. It adds to the weak structural GBP cards (weaker growth prospects, twin deficits, brexit consequences).

Calendar & Table

Friday, 26 May		Consensus	Previous
US			
14:30	Personal Income/Spending (Apr)	0.40%/0.50%	0.30%/0.00%
14:30	Real Personal Spending (Apr)	0.30%	0.00%
14:30	PCE Deflator MoM/YoY (Apr)	0.30%/4.30%	0.10%/4.20%
14:30	PCE Core Deflator MoM/YoY (Apr)	0.30%/4.60%	0.30%/4.60%
14:30	Advance Goods Trade Balance (Apr)	-\$85.9b	-\$84.6b
14:30	Wholesale Inventories MoM (Apr P)	0.00%	0.00%
14:30	Retail Inventories MoM (Apr)	0.20%	0.70%
14:30	Durable Goods Orders (Apr P)	-1.00%	3.20%
14:30	Durables Ex Transportation (Apr P)	-0.10%	0.20%
14:30	Cap Goods Orders Nondef Ex Air (Apr P)	-0.10%	-0.60%
14:30	Cap Goods Ship Nondef Ex Air (Apr P)	0.10%	-0.50%
16:00	U. of Mich. Sentiment (May F)	58.0%	57.7
17:00	Kansas City Fed Services Activity (May)	--	7
Japan			
01:30	Tokyo CPI YoY (May)	3.20%A	3.50%
01:30	Tokyo CPI Ex-Fresh Food YoY (May)	3.20%A	3.50%
01:30	Tokyo CPI Ex-Fresh Food, Energy YoY (May)	3.90%A	3.80%
01:50	PPI Services YoY (Apr)	1.60%A	1.70%R
UK			
08:00	Retail Sales Inc Auto Fuel MoM/YoY (Apr)	0.30%/-2.80%	-0.90%/-3.10%
08:00	Retail Sales Ex Auto Fuel MoM/YoY (Apr)	0.40%/-2.80%	-1.00%/-3.20%
France			
08:45	Consumer Confidence (May)	--	83
Events			
09:30	ECB's Vujcic Speaks in Dubrovnik		
09:40	ECB's Lane Speaks		
10:00	Riksbank's Breman on economic situation		

10-year	Close	-1d		2-year	Close	-1d	Stocks	Close	-1d
US	3.82	0.08		US	4.53	0.16	DOW	32764.65	-35.27
DE	2.52	0.05		DE	2.90	0.05	NASDAQ	12698.09	213.93
BE	3.23	0.05		BE	2.99	0.05	NIKKEI	30946.16	145.03
UK	4.37	0.16		UK	4.56	0.18	DAX	15793.8	-48.33
JP	0.42	0.00		JP	-0.06	0.00	DJ euro-50	4269.64	5.90
IRS	EUR	USD	GBP	EUR	-1d	-2d	USD	-1d	-2d
3y	3.48	4.34	5.05	Ester	3.1480	0.0000			
5y	3.25	4.01	4.68	Euribor-1	3.1980	0.0600	Libor-1	5.1409	0.0000
10y	3.17	3.85	4.30	Euribor-3	3.4570	0.0420	Libor-3	5.4244	0.0000
				Euribor-6	3.7690	0.0250	Libor-6	5.5321	0.0000
Currencies	Close	-1d		Currencies	Close	-1d	Commodities	Close	-1d
EUR/USD	1.0725	-0.0025		EUR/JPY	150.2	0.27	CRB	258.49	-4.21
USD/JPY	140.06	0.59		EUR/GBP	0.8704	0.0011	Gold	1962.30	-20.80
GBP/USD	1.2321	-0.0044		EUR/CHF	0.9714	-0.0016	Brent	76.26	-2.10
AUD/USD	0.6505	-0.0039		EUR/SEK	11.6082	0.0818			
USD/CAD	1.3642	0.0047		EUR/NOK	11.8508	0.0743			

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