Monday, 05 June 2023

KBC Sunrise Market Commentary

Markets

- **US payrolls delivered once more in May.** The Bureau of Labour Statistics reported a 339k net job gain for May. Payrolls beat consensus by a wide margin (237k!!), also taking into account upward revisions to the March and April data (+93k). The employment increase was nevertheless **at odds with a significant increase in the unemployment rate** (5.7% from 5.4% despite stable participation rate) with the latter being derived from the separate Household Survey which pointed at a >300k net job… loss in May! Average hourly earnings came in as expected at 0.3% M/M (4.3% Y/Y). Markets had to digest the numbers coming from a week long dovish repositioning after future Fed vicechair Jefferson and voting Fed Harker pulled the plug on a June rate hike. **It's skip and go** when it comes to them and probably the majority within the Fed. **Markets now fully discount a 25 bps July rate hike** while the odds of the US central bank hiking already next week are further reduced. **US yields rose by 7.3 bps (30-yr) to 15.8 bps (2-yr) in a daily perspective.** US Treasuries underperformed German Bunds with German yields closing 3.3 bps (30-yr) to 9.5 bps (2-yr) higher. **The dollar profited from the rate support,** but as for US yields, last week's highs were untested. The trade-weighted dollar (DXY) closed at 104.02 from 103.56 and a May high at 104.70. EUR/USD closed at 1.0708 from 1.0762 and compared to the May low of 1.0635. **US stock markets didn't bother the higher US interest rates** as the ongoing labour market strength once again underpins the resilience of the economy. Key indices closed 1% (Nasdaq) to 2% (Dow) higher. Talk that China weighs new property spending to help the economy benefited risk sentiment as well. Asian risk sentiment remains bullish this morning with China underperforming despite a strong services PMI. **Higher oil prices** (see below) offer part of the explanation. They weigh on core bonds as well.

- Today's agenda contains **US non-manufacturing ISM.** We expect the **global divergence between weakness in manufacturing and strength in domestic services** to persist in the US as well. This should avoid a nasty, negative surprise. The eco calendar contains second tier eco data this week with US and European central bankers in their blackout period ahead of key policy meetings next week. **This sets the stage for more sideways action with May highs in US rates and the dollar being important resistance levels.** We keep a close eye at **US Treasury funding statements/action** as well. They ran down their general account at the Fed to a rock-bottom $23bn against the background of the debt ceiling debate and have to replenish in coming weeks/months.

News & Views

- At the **OPEC+ meeting** on Sunday in Vienna, **Saudi Arabia announced that it will cut its production by 1 mln barrels per day** as the country aims to stabilize the market, amid persistent downward pressure on the oil price. **Other members of the group didn't engage to a further reduction,** but agreed to **maintain current cuts till the end of 2024.** Russia also didn't commit to deeper cuts. The United Arab Emirates even are allowed a higher production quotum for 2024. The oil price this morning gains modestly with Brent trading close to $77/b.

- **Rating agency S&P kept the French AA credit rating unchanged on Friday. The outlook remains negative.** The agency expects tighter financial conditions and high core inflation to restrain the country's activity in 2023 and 2024. **It expects France's budget deficit to decline to 3.8% of GDP in 2026 from about 5% in 2023. Government debt is expected to stay above 110% of GDP,** with the forecasts still subject to risks related to growth and the implementation of the government's economic and fiscal policy. **Rating agency Fitch affirmed its AA- UK rating and also kept a negative outlook.** The agency expects the UK general government debt to GDP ratio to reach 104.8% of GDP by 2024 from 101% in 2022. The negative outlook signals macroeconomic challenges, including weak growth and suborn inflation, higher borrowing costs and expenditure pressures due to the cost of living crisis and the upcoming elections. **Fitch expects the UK to enter a mild recession in 2023 with a 0.1% contraction of GDP in 2023 and a weak recovery of 1.0% in 2024.** Finally, **Fitch kept the US AAA credit rating on watch negative,** even after the political agreement to raise to US debt ceiling, avoiding a default as the rating agency will 'consider the full implications of the most recent brinkmanship episode and the outlook for medium-term fiscal and debt trajectories'.

Graphs

GE 10y yield

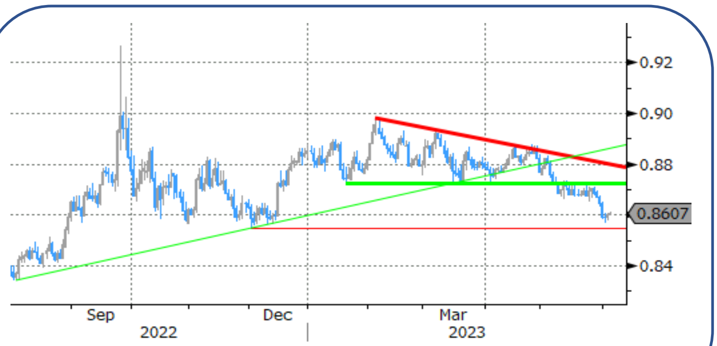
The ECB adopted a more gradual approach by slowing its tightening pace from 50 to 25 bps in May. It stated that in the base scenario rates will be brought to sufficiently restrictive levels (i.e. more hikes to follow) and will stay there for as long as necessary. **Combined with APP reinvestments fully 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. They want more evidence on the pass-through of the previous 500 bps of tightening. **The regional bank implosion is expected to additionally weigh on activity going forward.** But elevated inflation and a strong labour market mean that the Fed will likely have to hike its policy rate again by July. It triggered underperformance of US Treasuries during the month of May.

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 caused EUR/USD to fall below the 1.0727/1.0735 support zone, paving the way towards 1.06 in first instance. 1.0484/1.0516 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, pushing sterling to a now YtD high below EUR/GBP 0.865. The short-term momentum in sterling improved, but we stay cautious MLT. Divergency within the BoE about the way forward still might change sentiment on sterling further down the road.

Calendar & Table

Monday, 5 June		Consensus	Previous
US			
16:00	Factory Orders (Apr)	0.80%	0.90%
16:00	Durable Goods Orders (Apr F)	1.10%	1.10%
16:00	Cap Goods Ship Nondef Ex Air (Apr F)	--	0.50%
16:00	**ISM Services Index (May)**	**52.4**	**51.9**
16:00	ISM Services Prices Paid (May)	--	59.6
16:00	ISM Services Employment (May)	--	50.8
16:00	ISM Services New Orders (May)	--	56.1
UK			
10:00	New Car Registrations YoY (May)	--	11.60%
10:30	S&P Global/CIPS UK Services PMI (May F)	55.1	55.1
10:30	S&P Global/CIPS UK Composite PMI (May F)	53.9	53.9
EMU			
10:00	HCOB Eurozone Composite PMI (May F)	53.3	53.3
10:00	HCOB Eurozone Services PMI (May F)	55.9	55.9
10:30	Sentix Investor Confidence (Jun)	-15.1	-13.1
11:00	PPI MoM/YoY (Apr)	-3.10%/1.50%	-1.60%/5.90%
Germany			
08:00	Trade Balance SA (Apr)	16.0b	14.9bR
08:00	Exports/Imports SA MoM (Apr)	-2.50%/-1.00%	-5.90%R/-5.30%R
China			
03:45	Caixin China PMI Composite (May)	55.6A	53.6
03:45	**Caixin China PMI Services (May)**	**57.1A**	**56.4**
Czech Republic			
09:00	Average Real Monthly Wage YoY (1Q)	-6.40%	-6.70%
09:00	Average Nominal Monthly Wage YoY (1Q)	--	7.90%
Events			
15:00	**ECB's Lagarde appears before European Parliament's**		
16:00	**ECB's Nagel Speaks**		

10-year	Close	-1d		2-year	Close	-1d	Stocks	Close	-1d
US	3.69	0.10		US	4.50	0.16	DOW	33762.76	701.19
DE	2.31	0.06		DE	2.80	0.08	NASDAQ	13240.77	139.79
BE	2.99	0.05		BE	2.86	0.08	NIKKEI	32117.27	593.05
UK	4.16	0.04		UK	4.36	0.07	DAX	16051.23	197.57
JP	0.43	0.02		JP	-0.07	0.00	DJ euro-50	4323.52	65.91
IRS	EUR	USD	GBP	EUR	-1d	-2d	USD	-1d	-2d
3y	3.30	4.27	4.85	Ester	3.1480	0.0010			
5y	3.06	3.93	4.48	Euribor-1	3.2180	0.0080	Libor-1	5.1886	0.0256
10y	2.95	3.75	4.08	Euribor-3	3.4900	0.0280	Libor-3	5.4963	-0.0023
				Euribor-6	3.7280	0.0070	Libor-6	5.6234	-0.0240
Currencies	Close	-1d		Currencies	Close	-1d	Commodities	Close	-1d
EUR/USD	1.0708	-0.0054		EUR/JPY	149.76	0.39	CRB	259.69	2.32
USD/JPY	139.92	1.12		EUR/GBP	0.8600	0.0008	Gold	1969.60	-25.90
GBP/USD	1.2453	-0.0073		EUR/CHF	0.9732	-0.0014	Brent	76.13	1.85
AUD/USD	0.661	0.0039		EUR/SEK	11.5647	-0.0745			
USD/CAD	1.3425	-0.0024		EUR/NOK	11.7996	-0.0987			

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