Wednesday, 07 June 2023

KBC Sunrise Market Commentary

Markets

- German Bunds outperformed US Treasuries during European trading hours following **an unexpectedly strong decrease of inflation expectations in the ECB's April Consumer Expectations Survey.** The divergence between the two became even larger as US Treasuries started underperforming (especially at the front end the curve) during the US session. The move started after **the US Treasury announced plans to boost the size of its coming bills sales:** $60bn for the 4-week tenor (+$25bn), $50bn for the 8-week tenor (+$35bn) and $46bn for the 17-week auction (+$2bn). Since the debt ceiling has been raised, **the US Treasury is rapidly trying to replenish its depleted general account with the Fed which shrank to its lowest level since 2017.** In coming weeks/months, sizes at the longer tenors will be upped as well with **the bigger question being whether this will drain more liquidity in times of Fed rate hikes and QT or whether it will just trigger a shift in investor allocation from one cash instrument to the other.** Daily changes on the US curve ranged between +1.3 bps (2-yr) and -4.2 bps (30-yr). Minutes before the market close, US Treasuries managed to erase a large part of the intraday losses in a strange, inexplicable, short squeeze. German yields closed the session up to 4 bps lower at the front end and broadly stable at the very long end. Loss of interest rate support at the front end pulled EUR/USD back below 1.07 to close at 1.0693.

- Asian risk sentiment is mixed this morning as **weak Chinese trade data** (May exports -7.5% Y/Y) add to growth worries. The calendar is again razor thin. **The OECD updates its economic outlook.** Yesterday's, the World Bank did the same. It projects global growth to decelerate from 3.1% in 2022 to 2.1% in 2023. Risks of financial stress in emerging markets and developing economies is intensifying amid elevated global interest rates. **The Bank of Canada's policy rate decision is today's biggest wildcard.** Money markets are split 50/50 over whether the BoC will lift its policy rate again by 25 bps after pausing in March and April. **It would be an omen for global central banks** after the RBA earlier this week conducted a second 25 bps rate hike after a one-meeting pause in April.

News & Views

- **Global supply chain pressures eased further in May** according to the NY Fed's Global Supply Chain Pressure index (GSCPI) which eased from to -1.71 from -1.35 in April. The reading was **the lowest since the start of the series in 1997.** There were significant **downward contributions from Great Britain backlogs and Taiwan delivery times.** Euro Area delivery times and backlogs exhibited the largest sources of upward pressure in May. Looking at the underlying data, **readings for all regions tracked by the GSCPI are below their historical averages.** The GSCPI integrates a number of commonly used metrics with the aim of providing a comprehensive summary of potential supply chain disruptions. Global transportation costs are measured by employing data from the Baltic Dry Index and the Harpex index, as well as airfreight cost indices from the US BLS. The GSCPI also uses several supply chain-related components from PMI surveys, focusing on manufacturing firms across seven interconnected economies

- **Australian GDP rose 0.2% Q/Q and 2.3% Y/Y in the first quarter of 2023.** It was the sixth straight rise in quarterly GDP, but the slowest since the Covid-19 lockdowns in September 2021. **Private and public global fixed capital formation** (respectively +1.4% after -0.9% in Q4 and +3% from -1.2%) were the **main drivers of GDP growth. Household consumption continued to slow in Q1 rising 0.2% Q/Q** and resulting in a 0.1 ppt contribution to growth. **Net trade detracted 0.2 ppt from growth as exports increased 1.8% and imports rose 3.2.%.** Despite the deceleration in growth, **prices continued to grow strongly in Q1.** The GDP implicit price deflator rose 1.9% Q/Q and 6.8% Y/Y. **Compensation of employees also continued to rise (2.4%)** as did employment, hours worked, pay raises and bonuses in the public sector. **The household saving to income ratio fell to 3.7%, its lowest level since 2008,** driven by higher income tax payable, interest payable on dwellings, and increased spending due to the rising cost of living pressures.

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

Wednesday, 7 June		Consensus	Previous
US			
13:00	MBA Mortgage Applications	--	-3.70%
14:30	Trade Balance (Apr)	-$75.8b	-$64.2b
21:00	Consumer Credit (Apr)	$22.000b	$26.514b
Canada			
16:00	**Bank of Canada Rate Decision**	**4.50%**	**4.50%**
Germany			
08:00	Industrial Production SA MoM/WDA YoY (Apr)	0.60%/1.50%	-3.40%/1.80%
Italy			
10:00	Retail Sales MoM/YoY (Apr)	0.30%/--	0.00%/5.80%
China			
07JUN	Exports YoY CNY (May)	-0.80%A	16.80%
07JUN	Imports YoY CNY (May)	2.30%A	-0.80%
07JUN	Trade Balance CNY (May)	452.33bA	618.44b
Events			
01:20	**RBA's Lowe-Speech**		
01:50	RBA's Bullock-Panel Discussion		
09:00	**OECD Publishes Economic Outlook**		
09:50	**ECB's Guindos Speaks in Brussels**		
10:30	ECB's Knot Speaks		
11:10	ECB's Panetta Moderates Panel in Brussels		
14:00	ECB's Vujcic Speaks		

10-year	Close	-1d		2-year	Close	-1d	Stocks	Close	-1d
US	3.66	-0.02		US	4.48	0.01	DOW	33573.28	10.42
DE	2.37	-0.01		DE	2.85	-0.03	NASDAQ	13276.42	46.99
BE	3.04	-0.01		BE	2.92	-0.04	NIKKEI	32032.12	-474.66
UK	4.21	0.00		UK	4.48	0.03	DAX	15992.44	28.55
JP	0.42	-0.01		JP	-0.06	0.00	DJ euro-50	4295.22	1.98
IRS	EUR	USD	GBP	EUR	-1d	-2d	USD	-1d	-2d
3y	3.30	4.24	4.92	Ester	3.1450	-0.0030			
5y	3.07	3.87	4.55	Euribor-1	3.2540	0.0320	Libor-1	5.1906	0.0000
10y	2.99	3.69	4.13	Euribor-3	3.4760	-0.0170	Libor-3	5.5091	0.0000
				Euribor-6	3.7150	-0.0240	Libor-6	5.6633	0.0000
Currencies	Close	-1d		Currencies	Close	-1d	Commodities	Close	-1d
EUR/USD	1.0693	-0.0020		EUR/JPY	149.32	-0.24	CRB	260.68	0.24
USD/JPY	139.63	0.05		EUR/GBP	0.8607	-0.0008	Gold	1981.50	7.20
GBP/USD	1.2424	-0.0014		EUR/CHF	0.9705	-0.0004	Brent	76.29	-0.42
AUD/USD	0.6671	0.0054		EUR/SEK	11.6728	0.0465			
USD/CAD	1.3403	-0.0042		EUR/NOK	11.8631	0.0429			

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