Tuesday, 19 September 2023

KBC Sunrise Market Commentary

Markets

- In a session deprived of key eco data and with markets awaiting more concrete guidance from tomorrow's Fed decision/economic projections, **the by default trend in yields was still north.** Additional (Fed and even ECB) rate hikes beyond September remain an option and it will take a lot of progress on inflation for centrale bankers to ease the 'higher for longer' mantra. Aside from changes in interest rates, central bankers also have **other 'technical options' to drain excess liquidity/tighten monetary conditions** (cf Reuters article on ECB sources published yesterday afternoon infra). In this context, the ECB pause didn't prevent EMU/German yields to gain further traction. Bund yields added between 4.3 bps (5-y) and 2.7 bps (30-y). The German 30-y yield touched a new cycle top just below 2.86%. The 10-y (2.71%) is nearing cycle peak levels in 2.74%/2.77% area. US yields initially followed the uptrend, but momentum dwindled mid-morning, maybe due an unexpected sharp setback in the NAHB home builders confidence. NAHB analyzed that "*High mortgage rates are clearly taking a toll on builder confidence and consumer demand, as a growing number of buyers are electing to defer a home purchase until long-term rates move lower.*" Many builders indicated to have recurred to incentives, including price concessions. Whatever, the reason Treasuries found a bottom. The 2-y yield kept a gain of 2.1 bps. Longer maturities lost op to 3.3 bps (30-y). 'Improving' sentiment in in Treasuries also helped an intraday bottoming in equities. The three major US index finished the little changed. Rising oil prices remains a source of uncertainty both for bonds and equities, with Brent testing the $95 p/b barrier. **The mild setback in US (real) yields also took some shine of the dollar.** DXY eased from the 105.3 area to close near 105.1. USD/JPY is holding close to the 147.95 recent top, but no new attack occurred, for now. **EUR/USD initially didn't go anywhere, but captured a better bid after the Reuters article on potential further ECB steps (close 1.0692).** The latter move also propelled EUR/GBP back above the 0.86 level (close 0.863).
- **Today's eco** calendar is thin with only US housing starts and permits, the OECD economic outlook and final EMU CPI to guide intraday trading. **We expect the downside in yields to remain well protected going into tomorrow's Fed decision.** Fed governors might reinforce the higher for longer mantra by lowering expected rate cuts next year. A higher dot for the neutral rate, if it were to occur, also would be an important sign. Over the previous two sessions, the dollar took a breather, but we still expect the greenback to have the better cards in a context of global tightening of monetary conditions. Recent top levels (DXY 105.44, USD/JPY 147.95, EUR/USD 1.0635/32) stay within reach.

News & Views

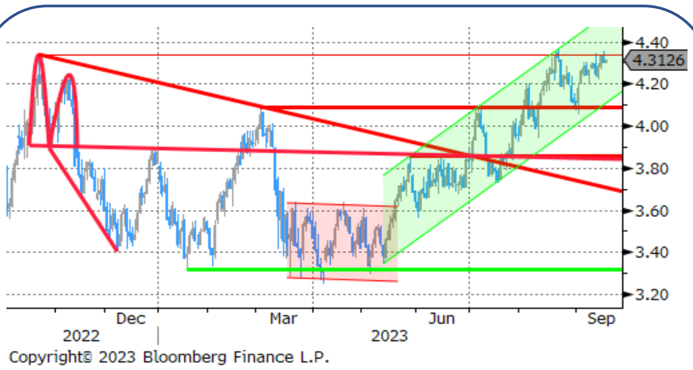
- News agency Reuters quoted sources in an article on the ECB's next steps. They indicated that tackling inflation is top of their mind right now, after raising the deposit rate a tenth consecutive time last week, to 4%. **Discussions center around three topics. First,** the amount of reserves banks must park unremunerated at the ECB. People close to the matter suggest several policy makers want to raise the minimum reserve ratio from 1% currently to 3% or 4%. That would take away €330bn-495bn from the current €3.7tn excess liquidity. **Second,** the ECB is looking into **a faster reduction of its €4.8tn bond portfolio (APP + PEPP).** Options include active sales from the APP or ending PEPP reinvestments before the current shelf date ("at least until end 2024"). **Finally**, the ECB is looking into switching back **from to a corridor-system from the current floor-based system.** That requires significantly shrinking excess liquidity and doesn't seem to be something which can be implemented in the near term. The Reuters article suggests that policy makers are split between bundling decisions altogether (takes time) or using a step-by-step approach In which raising the minimum reserve ratio could be enforced as soon as October, with a decision on APP/PEPP coming in December at the very earliest, but more likely only in March of next year.

- **Chinese holdings of US Treasuries fell by $13.6bn in July to $776bn, the lowest level since mid-2009.** Treasury holdings ranged between roughly $1tn and $1.3tn between mid-2010 and early 2022. This year, China did rotate into higher yielding US agency debt. **Holdings of Japan, the biggest foreign owner of US Treasuries, increased by $6.9bn to $1.1tn** (down from $1.325tn record end 2021). **The UK's holdings, number 3, fell by $9.9bn to $662.4bn.** That remains near the highest level on record for the country.

Graphs

GE 10y yield

The ECB **raised its policy rate to 4%.** It strongly indicated that **the current level, if maintained for long enough, might bring inflation back to target.** Such scenario might **bring the 10-y Bund yield in a holding pattern.** Potential further steps in QT and rising oil prices protect the downside. Resistance stands at 2.67%/2.77%.



US 10y yield

After a pause in June the Fed again raised its policy rate in July. Further tightening is dependent on eco data. But (core) inflation above target, economic resilience and a tight labour market **makes a November/December hike still a real possibility.** The US 10-y yield, driven by the real yield component (highest since 2009), is testing the cycle high at 4.36%.

EUR/USD

A test of EUR/USD 1.1274 (76% retracement since early 2021 top to 0.9536 cycle low) was rejected, triggering return action lower. Two poor EMU PMI's and **UST underperformance allowed a strong dollar to take over** again. The expected end of the ECB rate hike cycle additional weighs on the euro. EUR/USD tested 1.0635 support. Next references are 1.0516/1.0484.

EUR/GBP

The BoE was unable to break the EUR/GBP stalemate. It downscaled the tightening pace to 25 bps in August and made additional tightening conditional on further evidence of persistent inflationary pressures. **ST consolidation between EUR/GBP 0.85/0.87 is at hand.**

Calendar & Table

Tuesday, 19 September		Consensus	Previous
US			
14:30	Building Permits Total/MoM (Aug)	1440k/-0.20%	1443k/0.10%
14:30	Housing Starts Total/MoM (Aug)	1439k/-0.90%	1452/3.90%
Canada			
14:30	**CPI NSA MoM/YoY (Aug)**	**0.20%/3.80%**	**0.60%/3.30%**
14:30	Trim YoY% (Aug)	3.70%	3.60%
14:30	Median YoY% (Aug)	3.70%	3.70%
EMU			
11:00	CPI MoM/YoY (Aug F)	0.60%/5.30%	0.60%/5.30%
11:00	CPI Core YoY (Aug F)	5.30%	5.30%
Events			
03:30	RBA Minutes of Sept. Policy Meeting		
11:00	**OECD Publishes Economic Outlook**		
14:30	ECB's Elderson Speaks		

10-year	Close	-1d		2-year	Close	-1d	Stocks	Close	-1d
US	4,30	-0,03		US	5,05	0,02	DOW	34624,3	6,06
DE	2,71	0,03		DE	3,26	0,04	NASDAQ	13710,24	1,91
BE	3,34	0,03		BE	3,45	0,04	NIKKEI	33166,6	-366,49
UK	4,39	0,03		UK	5,03	0,01	DAX	15727,12	-166,41
JP	0,72	0,00		JP	0,03	0,01	DJ euro-50	4245,88	-49,17
IRS	**EUR**	**USD**	**GBP**	**EUR**	**-1d**	**-2d**	**USD**	**-1d**	**-2d**
3y	3,58	4,58	5,04	Ester	3,6480	-0,0020			
5y	3,34	4,23	4,67	Euribor-1	3,7620	0,0000	SOFR-1	5,3235	0,0004
10y	3,24	4,01	4,30	Euribor-3	3,9030	0,0250	SOFR-3	5,3934	0,0024
				Euribor-6	4,0660	0,0110	SOFR-6	5,4650	0,0079
Currencies	**Close**	**-1d**		**Currencies**	**Close**	**-1d**	**Commodities**	**Close**	**-1d**
EUR/USD	1,0692	0,0035		EUR/JPY	157,82	0,24	CRB	289,38	-0,23
USD/JPY	147,61	-0,24		EUR/GBP	0,8634	0,0027	Gold	1953,40	7,20
GBP/USD	1,2383	0,0000		EUR/CHF	0,9592	0,0023	Brent	94,43	0,50
AUD/USD	0,6437	0,0005		EUR/SEK	11,9188	-0,0036			
USD/CAD	1,3486	-0,0039		EUR/NOK	11,5557	0,0581			

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