Monday, 04 March 2024

KBC Sunrise Market Commentary

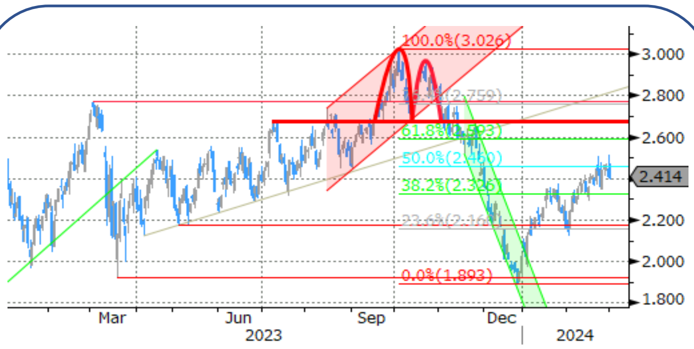
Markets

- EMU and US data on Friday provided conflicting evidence for global interest rate markets. As hinted by the national data on Thursday, the **Flash February EMU CPI doesn't allow the ECB to feel comfortable that price growth is on track to sustainably return to the 2.0% target anytime soon.** Due to favourable base effects, headline Y/Y inflation eased from 2.8 % to 2.6 %, but prices still rose 0.6% M/M, the fastest pace since April last year. **Core inflation** also slowed less than hoped for (3.1% from 3.3% vs 2.9% expected). The slowdown in services inflation still goes at a snail's pace (3.9% Y/Y from 4.0%). Stubbornly high inflation kept European/German yields in a tight range near the YTD peak levels, but it was not enough to force a break higher. **US yields** earlier last week already looked like running into resistance even as PCE defators published on Thursday (0.3% M/M headline, 0.4% M/M core) confirmed that there was no reason at all for the Fed to rush to rate cuts in the near future. Still, **a poor US Manufacturing ISM was enough for yields to leave the YTD peak levels.** The headline index unexpectedly eased from 49.1 to 47.8 (49.5 expected). Most details were weak (production 48.4 from 50.4; employment 45.9 from 47.1, new orders 49.2 from 50.4), with exports orders (51.6 from 45.2) an exception to the rule. Prices continue to rise (52.5). There is no causal link between a softer ISM and Fed being able to cut rates soon(er), **but US yields eased between 8.8 bps (5-y) and 5.1 bps (30-y).** The US 10-y real yield also drifted further south off the 2.0% mark (1.86%). Moves in EMU yields remained limited post the CPI data. German yields varied between 1.1 bp (2-y) and +1.1 bp (30-y). The decline in real yields was enough to propel the S&P 500 (+0.8%) and the Nasdaq (+1.14%) to new record levels. The dollar traded on the backfoot. EUR/USD rebounded from to 1.08 area to close at 1.0837.
- **This morning,** Asian equities mostly show modest gains with China underperforming as markets are looking out for the National People's Congress. The Nikkei tops the symbolic barrier of 40 000. **Later today, the calendar is almost empty, but some key topics are scheduled later this week.** On Wednesday, **Fed Chair Powel will testify before Congress.** On Thursday, the **ECB holds a regular policy meeting and will publish new Staff Economic Projections.** Given recent inflation data, there is little reason for Powell and/or Lagarde to leave their cautious wait-and-see stance. Regarding the data, we keep **a close eye at the US services ISM** (Tuesday) **and the payrolls** (Friday). Softer data might extend Friday's correction in yields. Still, we assume any setback to stay limited as long as Fed doesn't become more specific in its guidance on a first rate cut. The dollar is trading with a tentatively soft bias but for now easily holds above first key support levels (DXY 103 area, EUR/USD 1.09 area).

News & Views

- **Rating bureau S&P raised Portugal's creditworthiness to A- from BBB+ with a positive outlook potentially paving the way for further upgrades within the next 24 months.** The agency lauded the country's steep deleveraging and ongoing strong budgetary performances, which is fueling a "significant and continued improvement in the external financial position and alleviating external liquidity risks." Last year's surplus, estimated at 1% of GDP, will ease but remain positive at 0.2% this year. S&P expects economic growth to decelerate to 1.4% this year and to pick up slightly but remain below 2% beyond 2024, underpinned by a robust labour market and rising real incomes, easing monetary conditions and an obstacle-free disbursement of the remaining €13.7bn EUNextGen resources. Inflation should return to the 2% target by 2026. **The credit watcher sees no major risks coming from the upcoming elections in March 2024 to the fiscal discipline currently in place.**
- **OPEC over the weekend confirmed a widely expected extension of current output curbs through June.** With current demand lackluster and the future uncertain amid (delayed) central bank easing and China's economic struggle, **the oil production group stuck to a 2.2 million-barrel-a-day reduction.** That's the amount on paper though and several OPEC members have consistently exceeded their quota's. **The OPEC statement noted that these voluntary cuts "will be returned gradually subject to market conditions" after the second quarter.** Limiting supply at a time of weak demand has helped the likes of Brent to recover from the December lows around $74/b to a s**hort-term equilibrium trading zone between $80-85.**

Graphs



10y yield

Huge December bond rally on goldilocks scenario: avoiding a recession while the disinflationary process allows central bankers to pivot to rate cuts. However, a strong February CPI validated recent ECB guidance that more confirmation is needed to decide on the timing of the first ECB rate cut, probably in summer. The 10-y German yield is nearing the 2.50% barrier, **but the move lacks conviction due to the poor EMU economic performance.**

US 10y yield

Fed chair Powell at the January press conference stressed that March wasn't the base case for a rate cut (but perhaps for a tweak to QT). Stellar payrolls and a big beat in the January US CPI, forced investors to abandon hopes an early/aggressive Fed rate cut. US yields jumped to new YTD highs. **A sustained move above 4.20/4.25% resistance suggests more upside.**

EUR/USD

The dollar lost out during the end of 2023 bond rally, but the 2023 high (1.1276) stayed out of reach. **The change of dynamics on bond markets improved the dollar's prospects.** The greenback is currently losing some momentum with the EUR/USD pair trying to escape the YTD downward channel. Low volatility dominates trading.

EUR/GBP

Going nowhere. Extremely narrow trading range defined by EUR/GBP 0.8493 and 0.8768 in place since May. The **Bank of England in January opened the door for rate cuts**, putting itself on par with the Fed and ECB despite higher inflation. For now, euro weakness prevails though.

Calendar & Table

Monday, 4 March		Consensus	Previous
Japan			
00:50	Monetary Base YoY (Feb)	2.40%A	4.80%
EMU			
10:30	Sentix Investor Confidence (Mar)	-10.6	-12.9
Events			
11:30	EU to Sell Up to EU2 Billion of 3.375% 2038 Bonds		
12:30	ECB's Holzmann Speaks		
17:00	Fed's Harker Remarks on Economic Impact of Higher Education		

10-year	Close	-1d		2-year	Close	-1d	Stocks	Close	-1d
US	4.25	-0.01		US	4.62	-0.02	DOW	38996.39	47.37
DE	2.41	-0.05		DE	2.90	-0.01	NASDAQ	16091.92	144.18
BE	2.98	-0.05		BE	2.99	-0.03	NIKKEI	39910.82	744.63
UK	4.12	-0.06		UK	4.30	-0.04	DAX	17678.19	76.97
JP	0.72	0.01		JP	0.19	0.01	DJ euro-50	4877.77	-6.00
IRS	EUR	USD	GBP	EUR	-1d	-2d	USD	-1d	-2d
3y	3.00	4.24	4.33	Ester	3.8870	-0.0190			
5y	2.80	4.00	4.03	Euribor-1	3.8650	0.0090	SOFR-1	5.3237	-0.0004
10y	2.73	3.87	3.84	Euribor-3	3.9370	-0.0050	SOFR-3	5.3307	-0.0050
				Euribor-6	3.9080	-0.0070	SOFR-6	5.2623	-0.0113
Currencies	Close	-1d		Currencies	Close	-1d	Commodities	Close	-1d
EUR/USD	1.0805	-0.0033		EUR/JPY	162.06	-1.27	CRB	275.08	-0.19
USD/JPY	149.98	-0.71		EUR/GBP	0.8559	-0.0001	Gold	2054.70	12.00
GBP/USD	1.2625	-0.0037		EUR/CHF	0.9557	0.0032	Brent	81.91	-0.24
AUD/USD	0.6497	0.0001		EUR/SEK	11.2087	0.0091			
USD/CAD	1.3579	0.0002		EUR/NOK	11.4771	-0.0024			

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