



Monday, 03 June 2024

KBC Sunrise Market Commentary

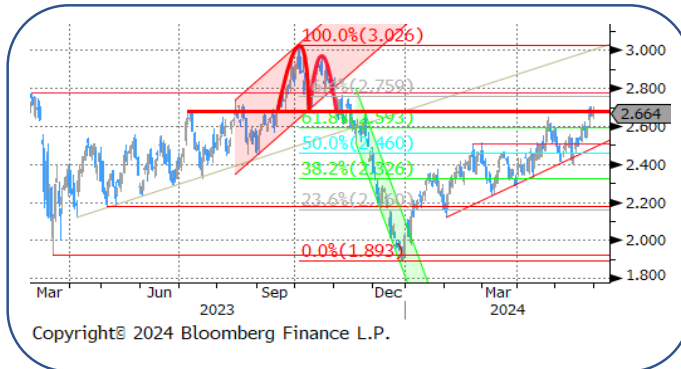
Markets

- US Treasuries closed near Friday's best levels on slightly softer April spending figures and a slower (but in line with forecasts) core PCE deflator pace.** Daily changes on the US yield curve ranged between -6 bps (5-yr) and -3 bps (30-yr). This contrasted with yield increases of up to 2.5 bps (3-yr) in Germany on the back of accelerating May EMU CPI data (core: 2.9% Y/Y from 2.7% Y/Y). **The combination pushed EUR/USD to the high 1.08 resistance area, but a real test didn't occur.** The pair closed the week where it started it, near 1.0840. US stock markets avoided losses thanks to a late-session sprint higher which resulted in gains of up to 1.5% for the Dow Jones. For once, the tech-heavy Nasdaq underperformed (flat).
- The **May US manufacturing ISM** kicks off a data-heavy US week today. Consensus expects a marginal improvement from 49.2 to 49.6. Apart from a one-off in March this year, the manufacturing ISM is in recessionary territory since November 2022. US Jolts Job openings are on tap tomorrow followed by ADP employment change and the services ISM on Wednesday. Payrolls finish it off on Friday. Don't look for Fed speeches as the black-out period in the run-up to the June 12 policy meeting kicked in. **From a market point of view, the flavour of the US data could switch the needle again between September and December for a first rate cut but this will likely keep US rates within recent trading ranges (eg US 10-yr yield 4.3%-4.73%).** Focus on the EMU side turns to **Thursday's ECB meeting which will bring a first 25 bps rate cut to the deposit rate (3.75% from 4%).** The bigger question remains whether the central bank commits to any guidance for the following meetings, something they refused to do so far. **Sticky Q1 wage growth, the bumpy inflation path ahead, recovering economic growth, and the Fed's reaction function all suggest limited scope to for follow-up cuts. We nevertheless think that the ECB will keep the option open.** Given current market pricing (2nd rate cut only discounted in December), this leaves scope for a more dovish market reaction at the front end of the curve (in the euro's disadvantage) in a steepening move. We see the longer end of the curve underperforming in such scenario on rising inflation expectations.

News & Views

- Rating agency S&P cut the French credit rating from AA to AA- with a stable outlook as public finances are a huge concern.** S&P expects the French debt-to-GDP ratio to increase to 112% of GDP in 2027, from about 109% in 2023, which would be the third highest in the euro area, after Greece and Italy. Last year's budget deficit came out at a higher than expected 5.5%. While the rating agency expects the deficit to shrink due to the economic recovery and recently implemented economic and budgetary measures, it will still average 4.6% over the 2024-2026 period before declining to 3.5% in 2027. In a broader perspective, S&P also assesses that **France's track record of fiscal consolidation has been weak over the past decades.** It has not reported a primary budget surplus since 2001. The agency expects interest rate payments to increase to 5% of general government revenues in 2027 from 3% in 2023. Even so, the pass-through is mitigated due to the long maturity of France's outstanding debt (> 8.5 years).
- OPEC+ decided to extend the level of agreed production cuts for an amount of 3.66mn b/d until the end of 2025.** Aside from these cuts in the general framework, eight members of the cartel, including Saudi Arabia and Russia also committed to 2.2mn of **voluntary cuts.** These cuts were due to expire at the end of June, but are **prolonged until the end of September 2024.** Afterwards, they will be **gradually reduced between October 2024 and September 2025.** The meeting this weekend also addressed the issue on the **capacity targets of individual members.** The group intends to decide on capacity levels on the basis of an external review as a reference for 2026. Even as production cuts have been prolonged, the oil price (Brent crude) dropped to currently \$81/b. That's probably as markets doubt whether demand will be strong enough to digest the gradual reduction of the voluntary production cuts.

Graphs



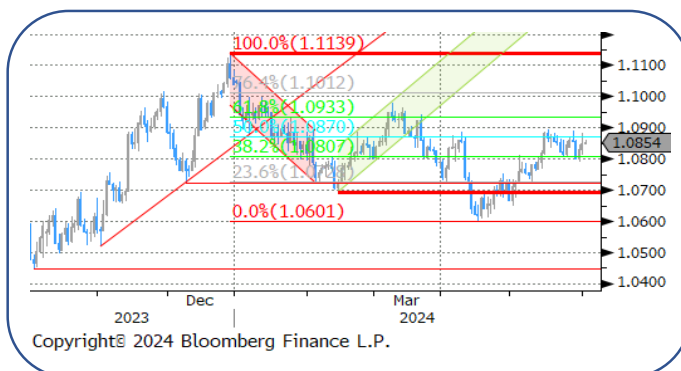
GE 10y yield

ECB President Lagarde clearly hinted at a June rate cut which has broad backing. A more bumpy inflation path in H2 2024, the EMU economy gradually regaining traction and the Fed's higher for longer US strategy make follow-up moves difficult. Markets are coming to terms with that. **The German 10y yield is setting a new YtD top.**



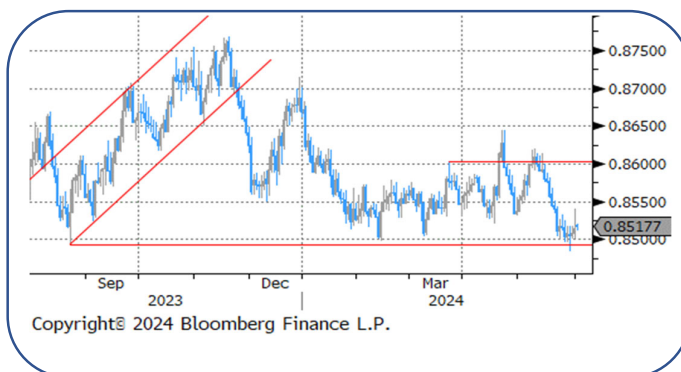
US 10y yield

The Fed in May **acknowledged the lack of progress** towards the 2% inflation objective, but Fed Chair Powell indicated that further tightening was unlikely. However, the FOMC Minutes still showed internal debate on whether policy is restrictive enough. **Sticky inflation suggests any rate cut will be a tough balancing act while several policy makers hint at a higher neutral rate.** The US 10-y yield is rebounding in the 4.3/4.7% trading range.



EUR/USD

Economic divergence, a likely desynchronized rate cut cycle with the ECB exceptionally taking the lead and **higher than expected US CPI data** pushed EUR/USD to the 1.06 area. From there, better EMU data gave the euro some breathing space. **The dollar lost further momentum on softer than expected early May US data.** Some further consolidation in the 1.06/1.09 area might be on the cards short-term.



EUR/GBP

Debate at the Bank of England **is focused at the timing of rate cuts.** Slower than expected April disinflation and a surprise general election on July 4 suggest that a June cut in line with the ECB looks improbable. Sterling gained momentum with money markets now discounting a Fed-like scenario. EUR/GBP tested the 2023 & 2024 lows near 0.85. We expect this important support level to hold.

Calendar & Table

Monday, 3 June		Consensus	Previous
US			
16:00	Construction Spending MoM (Apr)	0.20%	-0.20%
16:00	ISM Manufacturing (May)	49.6	49.2
16:00	ISM Prices Paid (May)	59.5	60.9
16:00	ISM New Orders (May)	--	49.1
16:00	ISM Employment (May)	--	48.6
Japan			
02:30	Jibun Bank Japan PMI Mfg (May F)	50.4A	50.5
UK			
10:30	S&P Global UK Manufacturing PMI (May F)	51.3	51.3
EMU			
10:00	HCOB Eurozone Manufacturing PMI (May F)	47.4	47.4
China			
03:45	Caixin China PMI Mfg (May)	51.7	51.4
Sweden			
08:30	Swedbank/Silf PMI Manufacturing (May)	--	51.4

10-year	Close	-1d		2-year	Close	-1d	Stocks	Close	-1d
US	4.50	-0.05		US	4.87	-0.05	DOW	38686.32	574.84
DE	2.66	0.01		DE	3.10	0.02	NASDAQ	16735.02	-2.06
BE	3.21	0.01		BE	3.17	0.02	NIKKEI	38942.44	454.54
UK	4.32	-0.03		UK	4.41	-0.06	DAX	18497.94	1.15
JP	1.07	0.00		JP	0.41	0.00	DJ euro-50	4983.67	1.49
IRS	EUR	USD	GBP	EUR	-1d	-2d	USD	-1d	-2d
3y	3.22	4.52	4.49	€STR	3.8920	-0.0180			
5y	3.01	4.27	4.19	Euribor-1	3.7170	-0.0330	SOFR-1	5.3279	-0.0002
10y	2.89	4.13	4.03	Euribor-3	3.7850	-0.0030	SOFR-3	5.3400	-0.0016
				Euribor-6	3.7450	-0.0140	SOFR-6	5.3082	-0.0052
Currencies	Close	-1d		Currencies	Close	-1d	Commodities	Close	-1d
EUR/USD	1.0848	0.0016		EUR/JPY	170.62	0.76	CRB	290.16	-2.84
USD/JPY	157.31	0.49		EUR/GBP	0.8515	0.0007	Gold	2345.80	-20.70
GBP/USD	1.2742	0.0010		EUR/CHF	0.9789	0.0004	Brent	81.11	-0.77
AUD/USD	0.6653	0.0020		EUR/SEK	11.4235	-0.0503			
USD/CAD	1.3628	-0.0053		EUR/NOK	11.3845	-0.0438			

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