



Tuesday, 22 October 2024

## KBC Sunrise Market Commentary

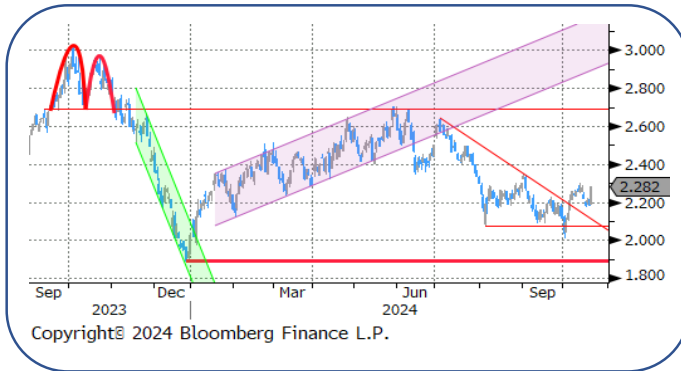
### Markets

- US yields closed this week's opening session 8.3 bps (2-yr) to 11.3 bps (10-yr) higher.** For the US 2-yr yield, it was the highest close since mid-August and above the strong 4%-resistance area. The US 10-yr yield finished above 4.2%, **completely erasing the August market-meltdown setback to 3.6% mid-September.** Don't go searching for any eco data to explain yesterday's dynamics. Once September US eco data (payrolls, CPI inflation, retail sales) ruled out the need for the Fed to stick to its bold opening move, **focus gradually turned from the November 7 Fed meeting to** that other key event the same week, **November 5 US presidential elections.** Both candidates continue to be neck and neck in the polls. As we near ballot date, **markets especially prepare for the potentially most eruptive outcome which would be a Trump win.** Recall that a Trump presidency would add \$7.5tn to an already yawning \$22tn cumulative deficits over the next decade (Harris: +\$3.5tn). These **bloated public finances** in an interest rate environment which can no longer be labelled by acronyms like ZIRP or NIRP cry for a return of credit risk premia. We see the **same thing happening in Europe**, with underperformance of bonds from countries like France and Belgium compared to countries who have finances better in check (eg Portugal, but also Italy for the moment). In theory, such worries should trigger more **bear steepening** of yield curves. The relatively strong increase at the front end of the US curve might be linked to comments from **Minneapolis Fed Kashkari** who wondered whether **the neutral rate is higher still** (economic resilience) than policy makers currently take into account (already a reset compared to pre-pandemic levels) and who stressed that **rates will be higher if deficits go to the moon.** The latest upleg in US yields has been primarily driven **higher real rates** instead of inflation expectations. German yields shadowed the US move yesterday, with yields ending the session 7.2 bps (2-yr) to 9.9 bps (10-yr) higher. On FX markets, the dollar closed at its best level against the euro since the weak July payrolls report (Aug 2). **EUR/USD changes hands at 1.0820, preparing for a test of 1.0778 support.** In the run-up to US elections, by default USD-strength could continue not only because of yield and economic divergence, but also because of **a negative Trump-premium for the USD's counterparts** fearing a very hawkish trade policy. We expect current market to continue today given the thin eco calendar (only Richmond Fed business survey). Speeches by BoE Bailey and ECB Lagarde are wildcards for trading.

### News & Views

- Brazil's central bank chief Campos Neto** sees **"this huge de-anchoring" of inflation expectations** from the 3% target as he explained last month's decision to return to rate hikes to 10.75% after the 4-month pause that followed a cutting cycle (from 13.75% to 10.50%). The inflation convergence towards target has stalled, he said. **Services inflation is a particular worry** and a **tight labour market** indicates that it needs to be monitored closely. It's "a puzzle" to the central bank governor why the labour market continues to be this strong. He said the **fiscal narrative** is only part of the answer. With economic growth having consistently surprised to the upside, Campos Neto thinks there is a **structural element** as well following the range of reforms implemented over the past 5 to 10 years. The central bank's next meeting is November 6, in between the US elections and the Fed meeting but that doesn't necessarily means they won't act, especially with the Brazilian real hovering close to record lows (USD/BRL 5.7).
- Bank of England rate setter Megan Greene** in an Op-ed for the Financial Times said she **favoured a gradual approach to monetary easing.** Her comments contrast with those of governor Bailey who called for a more activist stance. Greene said rate hikes have spurred consumers to save more. This **higher-than-historical savings rate of >10%** easily tops that in the US (5%) and was also driven out of precaution in the wake of successive (pandemic and energy) shocks. Real consumption as a result is a mere 1.5% above pre-Covid levels compared to 13% in the US even as **British real incomes have been rising for more than a year now.** For Greene there's a risk that lowering the policy rate may trigger the exact opposite move, **releasing pent-up demand** that's currently stored in savings. One opposing risk factor is the **full impact of higher mortgage rates that has yet to pass through.** But given the uncertainty, Greene said the central bank should move cautiously.

# Graphs



## GE 10y yield

The ECB delivered a third rate cut in October as the outlook deteriorated and inflation is expected to reach the target sooner than thought. **Another reduction in December is highly likely** even though Lagarde refrained from official guidance. The path towards neutral (2-2.5%) should eventually aid an ailing economy. Against this background and with a little help from ongoing strong US data, the 2% support in the 10-yr yield looks solid.



## US 10y yield

The Fed kicked off its easing cycle with a 50 bps move, turning the **focus** from inflation to a potential slowdown in growth/employment. **Strong US September payrolls suggest the economy doesn't need more aggressive Fed support for now (25 bps steps will do)**, but the debate might resurface as the economic cycle develops. 3.60% acted as strong support before a rebound (and resumption of fiscal-related steepening trend) kicked in.



## EUR/USD

**EUR/USD twice tested the 1.12 big figure as the dollar lost interest rate support at stealth pace.** Bets on fast and large rate cuts trumped traditional safe haven flows into USD. An ailing euro(pean economy) offset some of the general USD weakness. After **solid early October US data, the dollar regained traction, with EUR/USD breaking the 1.1002 neckline.** Targets of this pattern are near 1.08.



## EUR/GBP

The BoE delivered a **hawkish cut** in August. Policy restrictiveness will further unwind gradually, starting November 7. The economic picture between the UK and Europe also diverged **to the benefit of sterling.** **BoE Bailey's call for an activist approach doesn't get backed by the data so far.** EUR/GBP is testing the 0.83 support zone ahead of the first Labour budget due October 30.

# Calendar & Table

Tuesday, 22 October		Consensus	Previous
<b>US</b>			
14:30	Philadelphia Fed Non-Manufacturing Activity (Oct)	4.1	-6.1
16:00	Richmond Fed Manufact. Index (Oct)	-17	-21
16:00	Richmond Fed Business Conditions (Oct)	--	-3
<b>UK</b>			
08:00	Central Government NCR (Sep)	--	11.0b
08:00	PSNB ex Banking Groups (Sep)	17.5b	13.7b
<b>EMU</b>			
06:00	EU27 New Car Registrations (Sep)	-6.10%A	-18.30%
<b>Belgium</b>			
11:00	Consumer Confidence Index (Oct)	--	-7
<b>Hungary</b>			
14:00	<b>Central Bank Rate Decision</b>	<b>6.50%</b>	<b>6.50%</b>
<b>Events</b>			
Q3 earnings	General Motors (12:30), 3M (bef-mkt) ...		
01:00	RBNZ Assistant Governor Silk Speaks on Financial Markets		
15:00	ECB's Centeno Speaks in Washington		
15:05	<b>ECB's Knot Speaks in New York</b>		
15:15	BOE's Greene Speaks		
15:25	<b>BOE's Bailey Speaks</b>		
15:45	BOE's Greene Speaks		
15:45	ECB's Holzmann Participates in Panel		
16:00	<b>ECB's Lagarde Speaks With Bloomberg TV's Lacqua</b>		
16:00	Fed's Harker Speaks at Fintech Conference		
19:00	<b>ECB's Villeroy speaks in New York</b>		
20:00	<b>ECB's Rehn Speaks in Washington</b>		
21:15	BOE's Breeden Speaks		
21:15	ECB's Lagarde, Panetta Speak		

10-year	Close	-1d	2-year	Close	-1d	Stocks	Close	-1d	
US	4.20	0.11	US	4.03	0.08	DOW	42931.6	-344.31	
DE	2.28	0.10	DE	2.18	0.07	NASDAQ	18540.01	50.46	
BE	2.87	0.11	BE	2.31	0.07	NIKKEI	38507.94	-446.66	
UK	4.14	0.08	UK	4.05	0.05	DAX	19461.19	-196.18	
JP	0.98	0.02	JP	0.45	0.01	DJ euro-50	4941.22	-45.05	
IRS	EUR	USD	GBP	EUR	-1d	-2d	USD	-1d	-2d
3y	2.29	3.73	3.81	€STR	3.4150	0.0000			
5y	2.31	3.67	3.72	Euribor-1	3.1450	-0.0020	SOFR-1	4.7516	-0.0021
10y	2.44	3.73	3.76	Euribor-3	3.1380	-0.0630	SOFR-3	4.6460	0.0215
				Euribor-6	2.9720	-0.0560	SOFR-6	4.4746	0.0408
Currencies	Close	-1d	Currencies	Close	-1d	Commodities	Close	-1d	
EUR/USD	1.0815	-0.0052	EUR/JPY	163.13	0.65	CRB	281.07	1.52	
USD/JPY	150.84	1.31	EUR/GBP	0.8329	0.0002	Gold	2738.90	8.90	
GBP/USD	1.2985	-0.0067	EUR/CHF	0.9368	-0.0031	Brent	74.29	1.23	
AUD/USD	0.6659	-0.0047	EUR/SEK	11.4223	-0.0095				
USD/CAD	1.3831	0.0032	EUR/NOK	11.8451	-0.0272				

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