Thursday, 19 December 2024

KBC Sunrise Market Commentary

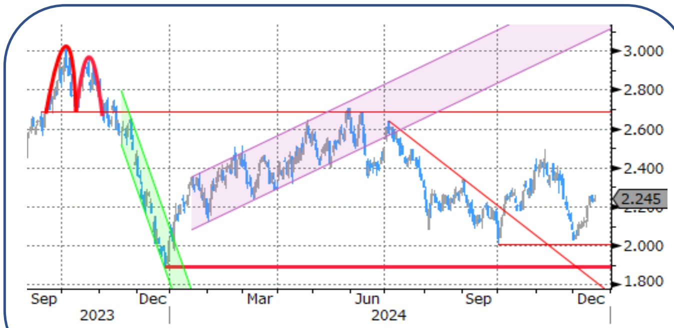
Markets

- The Fed lowered policy rates yesterday from 4.5%-4.75% to 4.25-4.5%, a level chair Powell said is still "meaningfully restrictive". The decision was expected but not unanimous. **Cleveland Fed Hammack voted to keep rates steady** which given the circumstances had a lot to say for. The economy is doing fine with GDP forecasts left unchanged at a very decent 1.9-2.1% over the policy horizon. PCE inflation was revised higher to 2.5% from 2.1% in 2025 before easing towards the 2% goal by 2027. Core PCE faced a similar upward adjustment. The FOMC moved from seeing risks to both inflation gauges as broadly balanced in September to skewed to the upside. In the same vein, uncertainty about both was now much higher. Asked why the Fed did cut, Powell noted the labour market is still cooling, be it gradually, while the inflation story was "broadly on track". The language in the statement on future cuts changed in a hawkish way though with the bold part being the addition: *"In considering **the extent and timing** of additional adjustments to the target range for the federal funds rate, the Committee will carefully assess incoming data, the evolving outlook, and the balance of risks."* **Powell said this signals the Fed is at or near a point to slow the pace of further adjustments.** He added that after having cut a cumulative 100 bps the Fed is now "significantly closer to neutral", warranting a cautious stance. In the updated dot plot, the median rate forecast shifted up by 50 bps over the horizon, meaning next year is now showing two 25 bps rate cuts instead of four. In addition, the policy rate is expected to remain above an upwardly revised neutral rate (to 3%) in 2025-2027. **It's higher for longer all over again.** Powell at the very end of the presser, while labeling it as not a likely outcome, did not even want to rule out a rate hike next year. US yields surged between 8.8 (30-yr) and 14.1 (5-yr) bps on the Fed's hawkish pivot and may have more room to run in the current momentum. US money markets not even fully price in two cuts next year. The dollar closed at the highest level in two years against the euro. EUR/USD finished at 1.0353 compared to the 1.0491 open. Critical support at 1.0335 (November intraday correction low) is at risk. The trade-weighted index topped 108 for the first time since November 2022.
- Multiple central banks convene today. We already had Japan (see below). Next up is Sweden, Norway and the Czech Republic. In core markets, attention shifts from the Fed to the **Bank of England.** The intermediate meeting is without updated forecasts though. The status quo at 4.75% is all but certain. Governor Bailey's guidance for 2025 is way more interesting. This week's stronger-than-expected wage growth and stubborn inflation pressures (core, services) leave the central bank little wiggle room. Money markets barely price in two cuts next year. It's keeping sterling locked near recent highs against the euro around EUR/GBP 0.823. If Bailey is only a fraction as hawkish as Powell yesterday, a test of EUR/GBP 0.8203 is on the cards.

News & Views

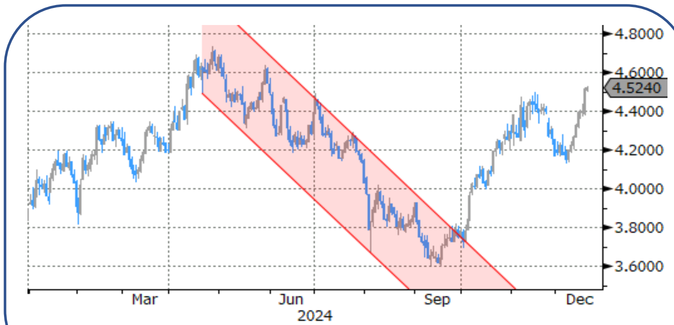
- **The Bank of Japan kept rates steady at 0.25% this morning.** The decision was widely expected after the likes of Reuters and Bloomberg cited sources that the central bank was leaning towards the status quo. Tamura dissented and voted for a hike as the economy and prices were moving as expected and inflation risks were increasing. With the economy "likely to keep growing at a pace above its potential growth rate" and inflation expected to be sustainably at target as projected in the October outlook, **a third hike is coming nevertheless.** Governor Ueda during the presser confirmed this but said they wanted more information on wage hikes first. The lack thereof today was the reason why they held rates. **Since these wage negotiations (shunto) only take place in February/March, a January rate hike suddenly is being questioned as well.** The yen, which was already pressured by a strong USD, extends losses on Ueda's comments. USD/JPY shoots higher to 156.3. Verbal interventions are probably incoming.
- **New Zealand GDP contracted a much bigger than expected 1% Q/Q in the third quarter this year.** It followed a downwardly revised 1.1% (from -0.2%) in Q2, meaning the country technically entered a recession. GDP was 1.5% smaller than in 2024Q3. Part of the steep decline was statistically inspired with adjustments to earlier readings having caused a higher comparison base. Details do show a **weak performance across the board** from household consumption (-0.3% Q/Q), capital formation (-2.9%) and government consumption (-1.9%). Exports (-2.1%) dropped more than imports (-0.4%) did. The kiwi dollar tumbled on the release with the dollar compounding the downleg in NZD/USD. The pair closed at 0.562. Swap rates slipped 5 bps at the front end of the curve.

Graphs



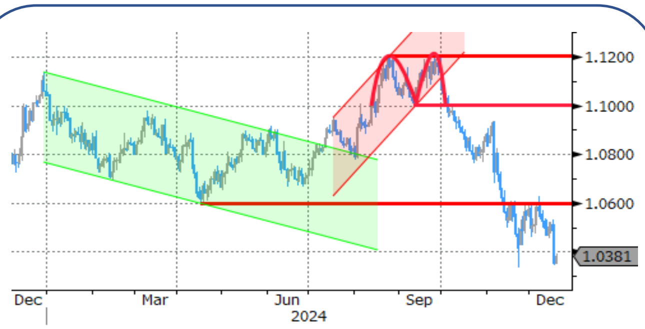
GE 10y yield

The ECB delivered a fourth rate cut in December and dropped the reference to keeping policy restrictive. Updated inflation forecasts barely changed while the growth outlook deteriorated. Sticking with a data-dependent approach, **we think the ECB eyes back-to-back 25 bps rate cuts in January and March** after which a proper evaluation on neutral interest rates is necessary. Money market positions remains too dovish. **The German 10-yr yield is bottoming out.**



US 10y yield

The Fed eased policy rates by 25 bps in December but added that **"the extent and timing"** of further cuts depend on incoming data. Updated rate forecasts above an upwardly revised neutral rate (3%) and higher inflation forecasts with risks firmly skewed to the upside complete the Fed's hawkish twist. **Higher for longer is back** and lifted both the front and long end of the curve. The 10-yr yield is on track for a test of the YtD high at 4.73%.



EUR/USD

Solid October US data started an impressive USD comeback. Trump's election victory later added to by default USD strength through fiscal and trade expectations. Money markets significantly reduced Fed rate cut bets as a result and saw their view validated by a hawkish central bank in December. With the euro on the ropes, the November correction low of 1.0335 is at risk.

EUR/GBP

The BoE delivered a second **hawkish cut** in November. The expansionary Labour budget lifted the BoE's GDP and CPI forecasts. It forced Bailey to backtrack on his earlier call for an activist approach and instead **sounded cautious on future cuts.** The economic picture between the UK and Europe diverged **to the benefit of sterling.** EUR/GBP sets new YTD lows and is heading to the post-brexit low of 0.8203.

Calendar & Table

Thursday, 19 December		Consensus	Previous
US			
14:30	Philadelphia Fed Business Outlook (Dec)	2.8	-5.5
14:30	**Initial Jobless Claims**	**230k**	**242k**
14:30	Continuing Claims	1892k	1886k
16:00	Existing Home Sales Total/MoM (Nov)	4.08m/3.00%	3.96m/3.40%
17:00	Kansas City Fed Manf. Activity (Dec)	-1	-2
Japan			
19DEC	**BOJ Target Rate**	**0.25%A**	**0.25%**
UK			
13:00	**Bank of England Bank Rate**	**4.75%**	**4.75%**
Germany			
08:00	GfK Consumer Confidence (Jan)	-22.5A	-23.3
France			
08:45	Business Confidence (Dec)	96	96
08:45	Manufacturing Confidence (Dec)	98	97
08:45	Production Outlook Indicator (Dec)	-14	-14
Belgium			
11:00	Consumer Confidence Index (Dec)	--	-8
Czech Republic			
14:30	**Repurchase Rate**	**4.00%**	**4.00%**
Norway			
10:00	**Deposit Rates**	**4.50%**	**4.50%**
Sweden			
09:30	**Riksbank Policy Rate**	**--**	**2.75%**

10-year	Close	-1d		2-year	Close	-1d	Stocks	Close	-1d
US	4.51	0.12		**US**	4.35	0.11	**DOW**	42326.87	-1123.03
DE	2.25	0.02		**DE**	2.03	-0.02	**NASDAQ**	19392.69	-716.37
BE	2.85	0.01		**BE**	2.21	-0.01	**NIKKEI**	38813.58	-268.13
UK	4.56	0.03		**UK**	4.46	0.01	**DAX**	20242.57	-3.80
JP	1.08	-0.01		**JP**	0.61	0.01	**DJ euro-50**	4957.28	14.70
IRS	EUR	USD	GBP	**EUR**	-1d	-2d	**USD**	-1d	-2d
3y	2.15	4.14	4.23	**€STR**	2.9170	-0.2470			
5y	2.17	4.07	4.09	**Euribor-1**	2.7620	-0.0130	**SOFR-1**	4.3578	-0.0232
10y	2.25	4.02	4.06	**Euribor-3**	2.8520	-0.0130	**SOFR-3**	4.3470	-0.0109
				Euribor-6	2.6520	-0.0120	**SOFR-6**	4.3094	0.0251
Currencies	Close	-1d		Currencies	Close	-1d	Commodities	Close	-1d
EUR/USD	1.0353	-0.0138		**EUR/JPY**	160.26	-0.74	**CRB**	292.01	1.08
USD/JPY	154.8	1.34		**EUR/GBP**	0.8234	-0.0020	**Gold**	2653.30	-8.70
GBP/USD	1.2574	-0.0136		**EUR/CHF**	0.9329	-0.0037	**Brent**	73.39	0.20
AUD/USD	0.6218	-0.0119		**EUR/SEK**	11.5229	0.0221			
USD/CAD	1.4447	0.0137		**EUR/NOK**	11.7894	0.0413			

Contacts

KBC Economics – Markets Brussels		Global Sales Force	
Mathias Van der Jeugt	+32 2 417 51 94	Corporate Desk(Brussels)	+32 2 417 45 82
Peter Wuyts	+32 2 417 32 35	Institutional Desk(Brussels)	+32 2 417 46 25
Mathias Janssens	+32 2 417 51 95	CBC Desk (Brussels)	+32 2 547 19 51
		France	+32 2 417 32 65
		London	+44 207 256 4848
		Singapore	+65 533 34 10
CSOB Economics – Markets Prague		Shanghai	+86 21 68236128
Jan Cermak	+420 2 6135 3578	Hong Kong	+852 2525 9232
Jan Bures	+420 2 6135 3574	**Prague**	+420 2 6135 3535
Petr Baca	+420 2 6135 3570		
CSOB Economics – Markets Bratislava		**Bratislava**	+421 2 5966 8820
Marek Gabris	+421 2 5966 8809		
K&H Economics – Markets Budapest		**Budapest**	+36 1 328 99 85
David Nemeth	+36 1 328 9989		

Discover more insights at www.kbceconomics.be