Friday, 10 January 2025

KBC Sunrise Market Commentary

Markets

- The partial absence of US investors due to a national day of mourning for ex-president Carter and the empty economic calendar kept markets squarely focused on the UK. Gilt yields gapped another 12 bps higher at the open before paring most of those gains into the close. The earlier surge nevertheless means multi-year or even -decade highs. **Breeden from the Bank of England was the first to comment** but wouldn't go much further than saying they are monitoring what is happening and that the moves reflect a lot of "global factors". The genie appears to be out of the bottle for sterling. EUR/GBP tested the 0.84 big figure. The pound has the easing of the gilt sell-off to thank for avoiding the technical break (EUR/GBP 0.8368). Cable's picture looks much more dire. The 2024 GBP/USD low of 1.23 was cracking and succumbs in Asian trading this morning. GBP/USD 1.228 trades at the weakest level since November 2023 and marches closer to an important support area around 1.225 (38.2% retracement on the 2022-2024 ascent). Rates in Europe added a few basis points in a bear flattening move (up to 3 bps in Germany) compared to a liquidity-thinned bull steepening in the US with moves from -2 bps to flat. Currency markets ex GBP were a sea of calm.
- Asian-Pacific dealings lacking much other news revolve mostly around the PBOC announcement (see News & Views) to suspend bond buying. All eyes are on US economic agenda for today. The University of Michigan's consumer confidence indicator (January) is scheduled but it's the **December payrolls report** that'll get most of the market attention. We think risks to the 165k consensus are **skewed to the upside.** The front end of the US curve is at a stalemate with markets already positioned more hawkish than the Fed (40 bps of cuts priced in compared to 50 bps in the dot plot). Similarly we do not think that a downside surprise would suddenly prompt a material dovish rebalancing. Recent Fed speak was clearly in favour of a prolonged pause at the current level of rates. The long end is most vulnerable for further losses in case of a topside surprise. Important resistance in the 10-yr yield is located at 4.73%. A break implies a return towards the 2023 high of 5.02%. **Dollar strength remains our base case.** With the euro not yet ripe for a rebound from its own making, south is the past of least resistance in EUR/USD. 1.0226 is the reference to watch.

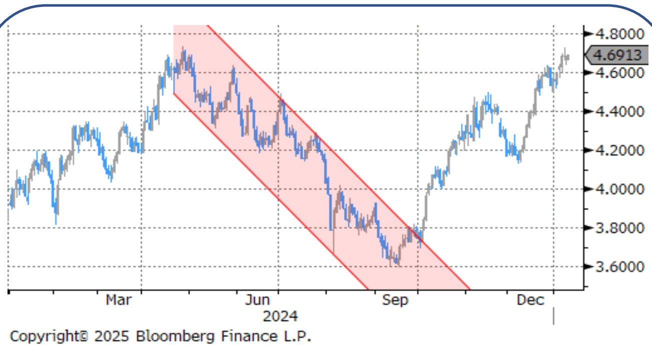
News & Views

- **The People's Bank of China (PBOC) this morning announced that it suspends its Treasury Bond purchases.** In explaining the move, the PBOC said that supply of bonds has fallen compared to demand, **triggering a shortage in the market.** Bond purchases since last year gained in significance as a tool to manage market liquidity as the central bank tried to ease monetary conditions to support the ailing economy. However, the subsequent sharp decline in yields is seen as a factor **putting additional pressure on the currency.** The run on (long-dated) bonds can also be seen as a sign of investor doubts on the ability of authorities to address current deflationary trends. **Chinese authorities showed unease with the financial stability risks** related to a stretched bond positioning in the market (risk for a crash). The central bank left the timing open of a resumption of its program which. It will take place at a proper time depending on supply and demand in the government bond market. In a first reaction, the 10-y Chinese government bond yield jumped 4 bps to 1.68%, but the gain dwindled as trading continued. The yuan trades little changed near recent lows at USD/CNY 7.332.
- **Inflation in Mexico declined eased further in December printing at 0.38% M/M and 4.21% Y/Y.** The latter marked the **lowest level since February 2021.** Core inflation reaccelerated to 0.51% M/M and 3.65% Y/Y. The central bank of Mexico aims to keep inflation at 3.0% with a 1.0% tolerance band. The data most likely will allow the bank to **continue its easing cycle.** The central bank cut its policy rate in December by 25 bps to 10%. It started its easing cycle in March of last year at 11.25%. The Minutes of the December policy meeting yesterday showed that a majority of the board members leaned to **considering larger rate cuts.** "In view of the progress on disinflation, larger downward adjustments could be considered in some meetings, albeit maintaining a restrictive stance," the minutes said. The Mexican peso, which suffered from overall USD strength in the second half of last year, remains in the defensive. At USD/MXN, the local currency holds within reach of the weakest levels since mid-2022 reached at the end of last year.

Graphs

GE 10y yield

The ECB delivered a fourth rate cut in December and dropped the reference to keeping policy restrictive. Inflation forecasts barely changed while the growth outlook deteriorated. Sticking with a data-dependent approach, **we think the ECB eyes 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 rebounded to 7-month highs in a steepening trend.**



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. **The dollar dominates.** The November correction low of 1.0335 is under test.

EUR/GBP

The BoE's hawkish cut in November was followed by a dovish hold in December where one of the status quo voters is close in switching sides. We think current market pricing of about two rate cuts in 2025 is too conservative. Meanwhile, **long end underperformance due to fiscal risks** is beating the UK currency down. EUR/GBP's attempt to leave the 0.823 lows is gaining traction.

Calendar & Table

Friday, 10 January		Consensus	Previous
US			
14:30	**Change in Nonfarm Payrolls (Dec)**	**165k**	**227k**
14:30	Change in Private Payrolls (Dec)	140k	194k
14:30	Unemployment Rate (Dec)	4.20%	4.20%
14:30	**Average Hourly Earnings MoM/YoY (Dec)**	**0.30%/4.00%**	**0.40%/4.00%**
14:30	Average Weekly Hours All Employees (Dec)	34.3	34.3
14:30	Labor Force Participation Rate (Dec)	62.50%	62.50%
16:00	**U. of Mich. Sentiment (Jan P)**	**74.0**	**74**
16:00	U. of Mich. Current Conditions (Jan P)	75.1	75.1
16:00	U. of Mich. Expectations (Jan P)	72.7	73.3
16:00	U. of Mich. 1 Yr Inflation (Jan P)	2.80%	2.80%
16:00	U. of Mich. 5-10 Yr Inflation (Jan P)	3.00%	3.00%
Canada			
14:30	**Net Change in Employment (Dec)**	**25.0k**	**50.5k**
14:30	Part Time Employment Change (Dec)	--	-3.6k
14:30	Full Time Employment Change (Dec)	--	54.2k
14:30	Unemployment Rate (Dec)	6.90%	6.80%
14:30	Participation Rate (Dec)	--	65.10%
14:30	Hourly Wage Rate Permanent Employees YoY (Dec)	3.80%	3.90%
Japan			
00:30	Household Spending YoY (Nov)	-0.40%A	-1.30%
France			
08:45	Consumer Spending YoY (Nov)	-0.20%	0.40%
08:45	Industrial Production MoM/YoY (Nov)	-0.10%/-1.30%	-0.10%/-0.60%
Norway			
08:00	CPI MoM/YoY (Dec)	0.10%/2.50%	0.30%/2.40%
08:00	CPI Underlying MoM/YoY (Dec)	0.00%/2.80%	0.10%/3.00%
Sweden			
08:00	Industrial Orders MoM/NSA YoY (Nov)	--/--	1.00%/-1.00%
08:00	Household Consumption MoM/YoY (Nov)	--/--	-0.30%/-1.10%
08:00	Industry Production Value YoY (Nov)	--	-2.00%
08:00	Service Production Value YoY (Nov)	--	1.40%

10-year	Close	-1d		2-year	Close	-1d	Stocks	Close	-1d
US	4.69	0.00		US	4.26	-0.02	DOW	42635.2	0.00
DE	2.57	0.02		DE	2.23	0.03	NASDAQ	19478.88	0.00
BE	3.15	0.04		BE	2.39	0.03	NIKKEI	39190.4	-414.69
UK	4.81	0.01		UK	4.52	0.00	DAX	20317.1	-12.84
JP	1.20	0.02		JP	0.65	0.00	DJ euro-50	5017.91	21.52
IRS	EUR	USD	GBP	EUR	-1d	-2d	USD	-1d	-2d
3y	2.37	4.11	4.30	€STR	2.9200	0.0030			
5y	2.42	4.14	4.23	Euribor-1	2.8830	0.0210	SOFR-1	4.3045	0.0015
10y	2.53	4.20	4.27	Euribor-3	2.7890	0.0070	SOFR-3	4.2898	-0.0033
				Euribor-6	2.6490	0.0100	SOFR-6	4.2497	-0.0103
Currencies	Close	-1d		Currencies	Close	-1d	Commodities	Close	-1d
EUR/USD	1.0300	-0.0018		EUR/JPY	162.87	-0.53	CRB	297.39	0.00
USD/JPY	158.14	-0.21		EUR/GBP	0.8368	0.0022	Gold	2690.80	18.40
GBP/USD	1.2308	-0.0055		EUR/CHF	0.9395	-0.0007	Brent	76.92	0.76
AUD/USD	0.6196	-0.0020		EUR/SEK	11.4896	-0.0173			
USD/CAD	1.4395	0.0019		EUR/NOK	11.7369	-0.0295			

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