



Sunset

Friday, 22 September 2017

Headlines

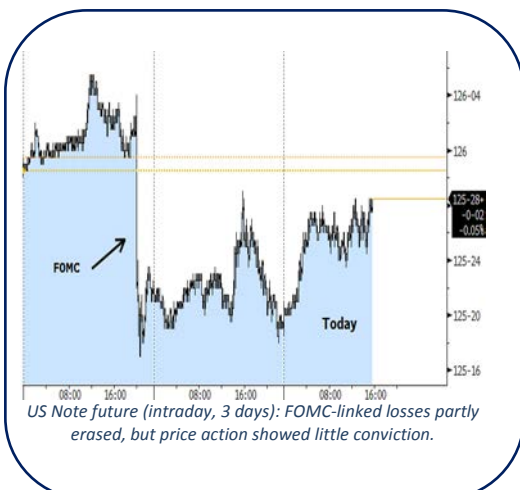
- **European equities** opened weak as Asian risk off sentiment carried over to EMU, but equities gradually went up, well into positive territory on the back of strong EMU PMI's. **Later on, risk sentiment deteriorated again, helped by another Trump tweet, pushing equities back to yesterday's closing levels.**
- **Eurozone business activity accelerated to the strongest pace since May**, putting upward pressure on prices, according to a survey that highlights the expectations that the European Central Bank will soon begin easing its bond buying programme. Composite PMI index rose to 56.7 in Sept., from 55.7 in August, the strongest gain in 6 years.
- **Mario Draghi** has made a fresh plea to eurozone governments to reform their labour markets and improve the prospects of young people, saying higher unemployment rates for younger workers had high costs for society. Mario Draghi was silent on policy-sensitive issues.
- **San Francisco Fed Williams** called rates still low in the US, could see another rate hike in December and expects gradual increases of rates in the next couple of years. However, everything depending how the economy fares. Williams, who did a lot of research on the natural rate, said 2.5% is the new normal for the long run or neutral rate.
- **Uber's license to operate taxis in London was revoked**, a surprise decision that will affect the 3.5 million people and 40,000 drivers who use the app in the city. If the decision stands, Uber appeals, it will have a considerable impact on the company's global business. London is one of Uber's most established markets.
- **"The recent euro appreciation may have a more limited dampening effect on inflation than what would be implied by historical averages"** based on recent research, ECB Vice President Constancio said .

Rates

German bonds underperform US Treasuries

US Treasuries eked out some gains in the Asian session, as risk-aversion linked to North-Korean nuclear test threats, dominated trading. They kept the gains, but moved sideways further out. **The Bund opened higher, reflecting US Treasury gains, but soon slid lower as risk sentiment improved and EMU PMI business confidence largely exceeded expectations.** It confirms the buoyancy of the euro area economy. The Bund bottomed even before noon and struggled higher to erase losses, maybe helped by declining equities. All in all, the bond moves are minor, but more than half of the post FOMC losses on Wednesday have now been recouped.

Central bankers gave a number of interesting comments that were however largely ignored. **San Francisco Fed Williams is on board of the majority group inside the FOMC. He sees a rate hike this year as likely and calls current rates still low.** He also expects gradual rate increases in the next years, but, **most**



important, sees 2.5% as the new normal (meaning the long run or neutral rate). ECB Constancio said that the strong euro might have less impact on (lower) inflation than historical experience would suggest. This could be called hawkish coming from the dovish ECB vice chairman, as it lessens fears that QE tapering would push inflation lower via a stronger euro. Mario Draghi didn't touch sensitive issues in his speech and later today, we hear the views of Fed governors George (hawk) and Kaplan (rather dove).

At the time of writing, US yields decline between 0.7 bps (2-yr) and 2.7 bps (10-yr), while German yields are little changed (between flat and +0.5 bps). On intra-EMU bond markets, 10-yr yield spreads versus Germany are unchanged.

Currencies

Data support euro. Dollar continues to struggle

Dollar sentiment remained fragile as (geopolitical) uncertainty and a cautious risk-off mood deprived the dollar of highly needed interest rate support. At the same time, the euro was supported by very strong EMU PMI's. At the end of the day, the moves are modest. Still, the conclusion survives that the dollar fails to profit from the Fed's commitment to continue policy normalisation. This especially applies to EUR/USD. The pair trades in the 1.1975 area. USD/JPY hovers near the 112 big figure.

Overnight, risk sentiment soured in Asia. Press reports said that North Korea might retaliate on Trump's speech and trade measures, by testing a hydrogen bomb in the Pacific. The renewed geopolitical tensions caused a modest risk-off repositioning. Asian equity indices declined, bonds gain and the yen outperformed. USD/JPY declined from the mid 112 area to trade in the high 111 area at the start of European trading. The dollar also declined slightly further against the euro. EUR/USD rebounded north of 1.1950.

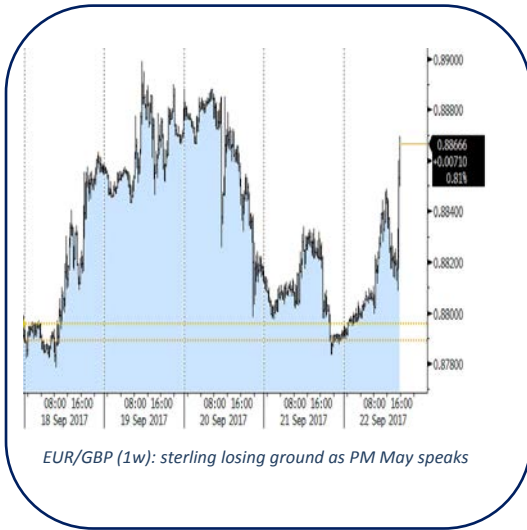
European equity markets opened with modest losses, but the risk-off sentiment from Asia evaporated almost immediately. The EMU September PMI's were rock-solid with the composite PMI in France and Germany reaching a new cycle top. European yields rose slightly. At the same time, US yields maintained a tentative downward bias. EUR/USD rebounded to the psychological barrier of 1.20, but a sustained break didn't occur. The dollar even regained some ground towards the end of the European morning session. EUR/USD dropped back to the 1.1960/75 area. USD/JPY tried to regain the 112 big figure. ECB's Constancio said that the appreciation of the euro may have a more limited dampening impact on inflation than what would be implied by historical averages, but the euro hardly reacted.

Early in the US, president Trump reacted sharply to the overnight 'threats' from North Korea. There was no immediate market reaction, but risk sentiment gradually deteriorated as US trading developed. For now, the negative impact on the dollar remains modest. EUR/USD trades in the 1.1970 area. USD/JPY hovers around 112.



Sterling under pressure at the start of May's speech

During the morning session, sterling was at the mercy of the broader swings in the euro and the dollar as **UK markets awaited UK PM May's Brexit speech in Florence this afternoon**. EUR/GBP drifted higher as the euro was well bid after the strong PMI's. The pair filled offers just below 0.8850. Cable lost a few ticks on overall USD softness. However, at start of PM May's Brexit speech, intraday changes were limited. CBI trends orders were softer than expected but ignored. PM May's Brexit speech is still ongoing at the moment of writing. She only brought some general considerations on the relationship between the EU and the UK. **For now we didn't see much concession from May. Sterling is losing ground as the speech proceeds**, but this can still change when May addresses more concrete issues on the Brexit process. EUR/GBP trades currently in the 0.8860 area. Cable trades in the 1.3515 area.



EUR/GBP (1w): sterling losing ground as PM May speaks

16:00 CET

Daily EMU spread changes (bps)

	5-yr			10-yr			30-yr		
	Yield	Spread	Change	Yield	Spread	Change	Yield	Spread	Change
Germany	-0.26%			0.45%			1.28%		
Greece (2-10-20)	2.91%	316	-2.6	5.56%	511	0.8	6.60%	533	-0.4
Portugal	0.94%	120	0.2	2.42%	197	-0.4	3.61%	233	1.5
Italy	0.72%	97	-0.5	2.10%	165	-0.6	3.29%	202	-1.8
Spain	0.27%	53	0.3	1.61%	116	-0.5	2.87%	159	-1.0
Ireland (4-10-30)	-0.38%	-12	-0.7	0.74%	29	-0.5	1.86%	58	-0.9
Belgium	-0.18%	7	-0.2	0.73%	28	-0.4	1.77%	49	-1.4
France	-0.15%	10	-0.2	0.73%	28	-0.3	1.82%	54	-0.9
Austria	-0.23%	2	-0.1	0.62%	17	-0.1	1.58%	30	-0.2
Netherlands	-0.30%	-5	-0.1	0.57%	12	-0.5	1.28%	1	-0.5
Finland	-0.14%	12	0.0	0.61%	16	-0.3	1.38%	10	-1.0
US	1.86%	211	-3.1	2.24%	179	-2.9	2.78%	151	-1.7
UK	0.76%	101	-1.8	1.35%	90	-1.3	1.92%	64	-1.0

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