



Sunset

Wednesday, 04 October 2017

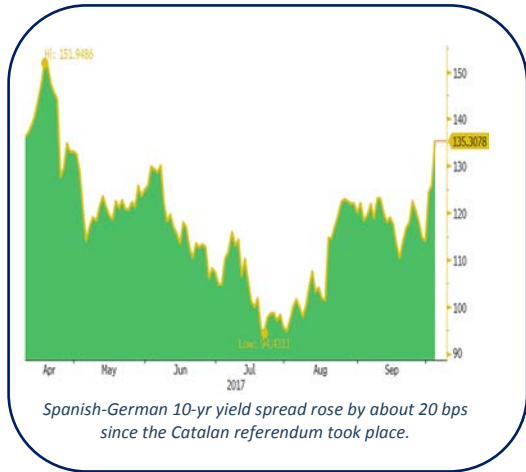
Headlines

- **European stock markets lost up to 0.5% with Spain underperforming (-2%)** as sources indicated that Catalonia will declare independence on Monday. **US stock markets opened with minor losses.**
- **The pace of hiring in the US private sector slowed to its weakest pace in 13 months last month**, as Hurricane Irma and Harvey disrupted businesses across a large swath of the south-eastern US. Non-farm private employers added 135,000 jobs from August to September, according to a report from payroll processor ADP.
- **America's service industries expanded in September at the fastest clip in 12 years (from 55.3 to 59.8)**, signalling vibrancy across the bulk of the economy following two major hurricanes, a survey from the ISM showed.
- **Catalonia will move on Monday to declare independence from Spain, a regional government source said**, as the EU nation nears a rupture that threatens the foundations of its young democracy and has unnerved financial markets.
- **Firms in the UK's important services sector reported better than expected growth in September (53.6 from 53.2)** in the closely-watched PMI survey, but warned of potential difficulties ahead as new business growth fell to its lowest level in more than a year. **The final EMU services PMI was upwardly revised from 55.6 to 55.8.**
- **President Donald Trump's tax plan would let US companies take bigger, faster deductions on capital investments**, a step some experts said would deplete Washington's policy arsenal by using up a tax break normally reserved for fighting recessions.
- **President Vladimir Putin said Russia may agree to extend a deal with OPEC to curb oil supplies beyond March to the end of 2018**, though he'll wait to make a decision until nearer the end of the existing pact.
- **The ECB's supervisors want lenders to be fully covered against losses from new loans that have gone sour**, in a move that could hurt credit creation in weaker economies in the region.
- **The National Bank of Poland kept its policy rate unchanged at 1.5%**. NBP governor Glapinski holds a press conference later today.
- A month before a snap parliamentary election, **Iceland's central bank cut its key interest for the fifth time in little more than a year, from 4.5% to 4.25%**, in a move to offset the impact of lower inflation. **The Reserve Bank of India kept its policy rates unchanged at 6%.**

Rates

Volatile session, but limited changes after all

Core bonds had a constructive session helped by a volatile mild risk off sentiment and technical factors. The Bund outperformed US Treasuries, but this time in a sphere of (modestly) falling yields. The tide turned in the afternoon session on the core bond markets and gains melted partly away.



The Bund started strong on **Spanish developments**. The German Dax opened at an all-time high in a catch-up move (German markets closed for Day of the Unity yesterday), but couldn't sustain at these levels with other European indices losing ground (Spain underperforming). However, by the time of writing our report, the Dax is again upwardly oriented. The Bund managed to eke out additional gains because of technical reasons. The German 10-yr yield tried already a few days to break through 0.5% resistance, but didn't succeed, encouraging some bulls to take profit on shorts/open long positions. **However in lockstep with rising equities, the Bund lost again some ground in the afternoon session.** The **EMU final PMI** stayed nearly unrevised and **EMU retail sales** were weaker, but markets ignored the eco data, just like the **US ADP employment report** that was bang in line with (modest) expectations.

US president Trump suggested that Puerto Rico's staggering \$74B debt will be wiped out (default) to help the island recover from the effects of the hurricane Maria, estimated at \$95B of damages. This might have serious implications for the big municipal market and could help safe-haven US Treasuries. However, once more there was no firm evidence that it effectively played a role. **Fed Fischer**, who leaves office later this month, continues to expect a tightening US labour market to lift wages and prices even though the process can take longer than anticipated. **He is yesterdays' man for markets** and thus unimportant. **Gold and the yen** rose in the morning session, but lost (part) of the gains in the afternoon, confirming **that volatile risk sentiment was behind market movements.**

The German Finanzagentur tapped the on the run 10-yr Bund (€3B 0.5% Aug2027). Total bids amounted €3.75B, slightly below the €4.07B average at the previous 4 Bund auctions. The Bundesbank set aside €0.59B for secondary market operations, resulting in an official bid cover of 1.6. The auction had no tail.

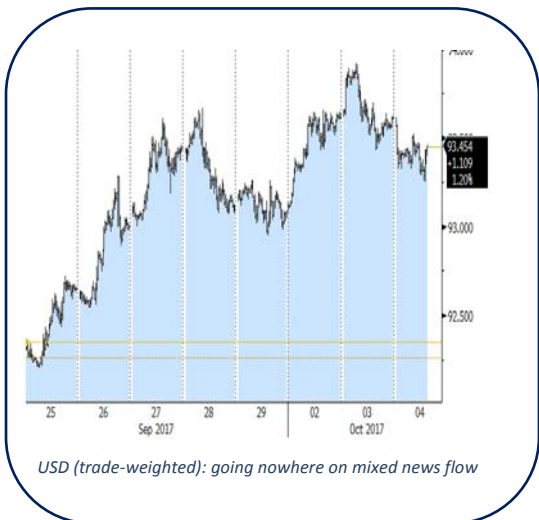
Currencies

Dollar going nowhere on conflicting stories

Today, USD traders faced several conflicting issues including strong EMU eco data, uncertainty on Catalonia and the US debate on who will succeed Yellen at the helm of the Fed. EUR/USD and USD/JPY hovered up and down. In the end, the trade-weighted dollar is little changed from the start in Europe. EUR/USD is changing hands in the 1.1770 area. USD/JPY tries to hold 112.50 area.

Overnight, Asian equities ex-Australia continued their uptrend. The Japan services PMI indicated modest growth, but didn't hurt the yen. The dollar declined slightly further as the political debate on a successor for Fed's Yellen intensified. There were rumours that chances of Fed member Powell, also on the shortlist, were growing. USD/JPY dropped to the mid 112 area. In the same vein, EUR/USD settled again in the upper half of the 1.17 big figure.

European FX traders faced a complex environment. The EMU PMI's were strong but rising tensions on Catalonia were a negative for euro sentiment. The rebound of European equities stalled and German bunds outperformed US Treasuries, widening the interest rate differential in favour of the dollar.

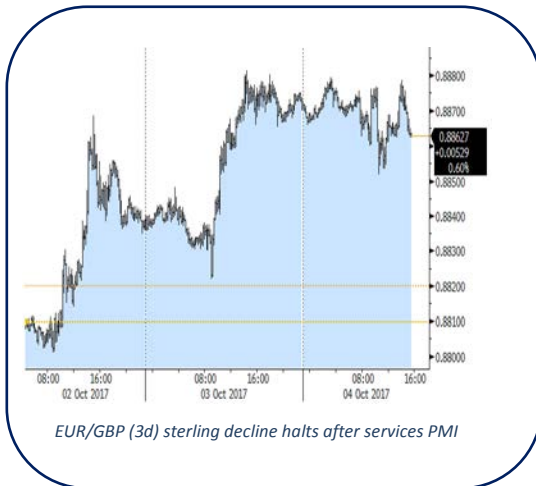


However, it didn't help the US currency. EUR/USD gradually reversed an early dip and returned to the 1.1770/80 area. USD/JPY traded with a negative bias as core bond yields declined and as risk sentiment turned cautiously negative. Uncertainty on the successor of Fed Chair Yellen kept USD bulls side-lined. USD/JPY drifted (temporary?) below 112.50.

In the US, the ADP labour report showed a modest net growth of 135 000 private jobs in September, in line with consensus. ADP said the dip in job growth was in part due to the impact from the hurricanes. There was no dollar reaction, but the dollar tried to bottom going into the start of US equity trading. **Maybe uncertainty on the financial position of Puerto Rico was also a slightly dollar negative.** EUR/USD trades currently in the 1.1770 area. USD/JPY trades near 112.50 awaiting the US non-manufacturing ISM.

Sterling decline blocked by decent services PMI

Sterling hovered near the recent lows against the euro early today. EUR/GBP held a tight range in the 0.8875 area. Cable tried to move a bit further away from yesterday's correction low (1.3222) but this was due to dollar softness. On Monday and Tuesday, the manufacturing and the services PMI's were reported weaker than expected and weighted on the UK currency. **Today, the services PMI rebounded from 53.2 to 53.6, while a** stabilization was expected. The details from the report were not strong, but upward price pressures persist. **The report fits a scenario of a limited BOE tightening in the near future. However, the BOE will act very cautiously.** Sterling rebounded, but the move was limited given the recent correction. EUR/GBP trades in the 0.8865 area. Cable hovers around 1.3275. The text of May's speech at the conservative party conference was released just before noon. The PM said she is seeking a Brexit deal that works, but the government is also preparing for a no-deal scenario. The impact on markets was very limited.



Daily EMU spread changes (bps)

	5-yr			10-yr			30-yr		
	Yield	Spread	Change	Yield	Spread	Change	Yield	Spread	Change
Germany	-0.29%			0.44%			1.27%		
Greece (2-10-20)	3.21%	350	2.6	5.59%	516	2.1	6.60%	533	2.9
Portugal	0.98%	128	1.0	2.42%	198	3.6	3.66%	239	1.7
Italy	0.74%	103	1.3	2.17%	173	3.0	3.35%	207	3.5
Spain	0.39%	69	5.5	1.75%	132	5.5	2.98%	171	6.9
Ireland (4-10-30)	-0.39%	-9	0.9	0.71%	27	0.1	1.86%	58	0.0
Belgium	-0.21%	8	1.3	0.72%	28	1.2	1.77%	50	1.7
France	-0.01%	28	1.3	0.73%	30	0.9	1.83%	56	0.9
Austria	-0.18%	12	0.3	0.61%	17	1.0	1.57%	29	1.0
Netherlands	-0.33%	-4	0.7	0.56%	12	0.5	1.28%	1	0.1
Finland	-0.17%	13	0.9	0.61%	17	0.6	1.38%	11	0.2
US	1.92%	221	1.8	2.32%	189	2.8	2.87%	159	3.0
UK	0.78%	107	1.4	1.36%	92	2.8	1.92%	64	3.5

Contacts

Brussels Research (KBC)		Global Sales Force	
Piet Lammens	+32 2 417 59 41	Brussels	
Peter Wuyts	+32 2 417 32 35	Corporate Desk	+32 2 417 45 82
Mathias van der Jeugt	+32 2 417 51 94	Institutional Desk	+32 2 417 46 25
Dublin Research		France	+32 2 417 32 65
Austin Hughes	+353 1 664 6889	London	+44 207 256 4848
Shawn Britton	+353 1 664 6892	Singapore	+65 533 34 10
Prague Research (CSOB)		Prague	+420 2 6135 3535
Jan Cermak	+420 2 6135 3578		
Jan Bures	+420 2 6135 3574		
Petr Baca	+420 2 6135 3570		
Bratislava Research (CSOB)		Bratislava	+421 2 5966 8820
Marek Gabris	+421 2 5966 8809		
Budapest Research		Budapest	+36 1 328 99 85
David Nemeth	+36 1 328 9989		

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