



Sunset

Friday, 21 October 2016

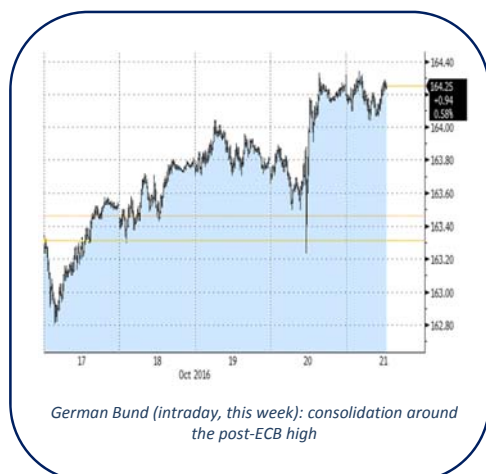
Headlines

- **European equity markets** trade marginally lower. US stock markets even opened up to 0.5% in the red. General Electric's results slightly beat expectations, but they cut the outlook as the sluggish economy crimps industrial demand.
- **Britain is on course to borrow billions of pounds more than planned this year**, leaving Chancellor of the Exchequer Philip Hammond little room for generosity as he prepares new budget plans to help the economy cope with Brexit.
- Long-term euro zone inflation projections remain well anchored near the European Central Bank's target, but GDP growth will be weaker than earlier thought, the **ECB's Survey of Professional Forecasters** showed.
- **Italian Prime Minister Matteo Renzi** said he would not change his 2017 budget plan even if the European Commission says it breaches EU rules on fiscal consolidation.
- **A new cigarette king is in the making.** British American Tobacco offered to buy the 58% in Reynolds American it doesn't already own for \$56.50 a share, 20% over yesterday's close but only just above this year's peak. The deal would create the largest publicly traded tobacco company, surpassing Altria, bringing Camels and Lucky Strikes under one roof and underscoring the industry's consolidation as smoking rates in the developed world decline.
- **Tonight, rating agency DBRS decides on Portugal's BBB- rating. On Sunday, Spanish Socialists vote on whether or not to abstain when PM Rajoy makes a new minority government bid.**

Rates

Bund consolidates after post-ECB correction

Global core bonds traded uneventful in a session devoid of eco data, events and central bank speeches. The Bund move higher following the ECB meeting proved to be a one-off. ECB President Draghi ruled out eternal QE and an abrupt stop of APP in March 2017, suggesting that the central bank will announce tapering at its December meeting. At the time of writing, changes on the German yield curve range between -0.4 bps (30-yr) and +0.8 bps (5-yr). Changes on the US yield curve vary between +0.4 bps (2-yr) and -2.5 bps (10-yr/30-yr). The US 10-yr and 30-yr yields face difficulties holding above key resistance levels at 1.75% and 2.5% respectively, suggesting that the downside in the US Note future (129-26 area) becomes a tough nut to crack as well.



On intra-EMU bond markets, 10-yr yield spread changes narrow up to 2 bps in a quiet session. Markets count down to two specific events. **First, rating agency DBRS updates the Portuguese BBB- rating tonight.** A downgrade into junk makes Portuguese debt in theory ineligible for the ECB's PSPP programme though Draghi suggested yesterday that the ECB could make an exception: *"Having said that, we should acknowledge the remarkable progress that's been achieved in Portugal..."* Portuguese bonds rallied going into the verdict, anticipating an unchanged decision. **Second, Spanish Socialists' decide on Sunday on whether or not supporting a minority PP-government.** A positive vote could end the 10-month political deadlock. A negative vote paves the way for a third consecutive general election, around Christmas. Spanish bonds traded rather stable this year despite the political crisis, so the impact on Monday could be muted, especially in case of a "yes" vote.

Currencies

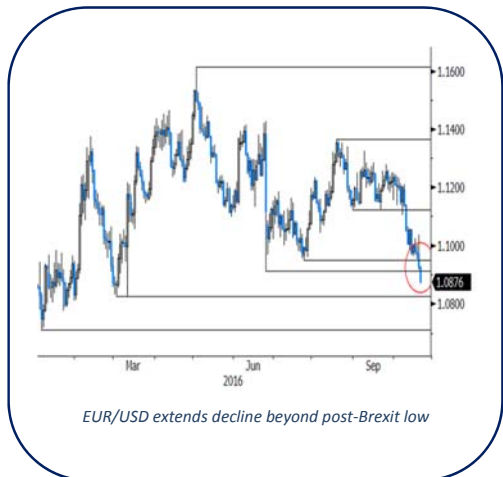
USD stays well bid even as sentiment turns risk-off

Today, there were no macro data to guide trading. The dollar remained in favour with EUR/USD declining further after breaking the post-Brexit low. USD/JPY failed to join the overall USD rally as global investor sentiment faltered.

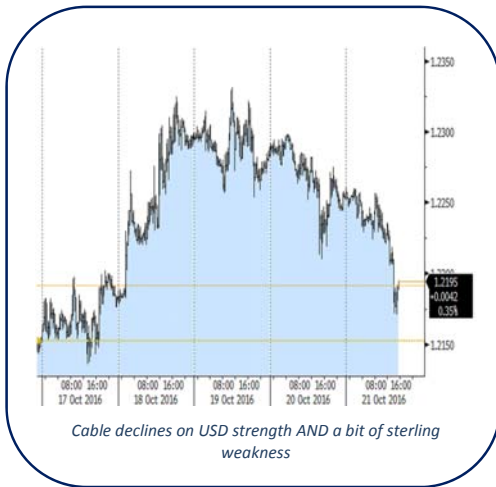
Overnight Asian equities traded mixed, mostly slightly in negative territory, as investors faced diffuse signals. Dollar strength was the most dominant feature. The trade-weighted dollar (DXY) reached the highest level since March. USD/JPY again tried to regain the 104 big figure even as global equity sentiment dwindled. Dollar strength also pushed USD/CNY to the highest level since 2010. CNY weakness causing additional market chatter on Chinese capital outflows. EUR/USD dropped below the 1.0952/13 support, the lowest level post-Brexit.

There was again no macro-economic news to guide trading on European markets. Interest rates and currency markets looked for a new equilibrium in the wake of yesterday's ECB press conference. Core bond yields rose marginally, but spreads between Europe/Germany and the US changed barely. **EUR/USD continued the post-ECB decline and drifted further below the 1.09 handle.** USD/JPY was the exception to the rule of global dollar strength and even started a gradual intraday downtrend south of 104.

No real change of scenario during the US trading hours. The (trade-weighted) dollar remains well bid near the recent highs. EUR/USD holds near the new post Brexit lows and trades currently in the 1.0870 area. USD/JPY changes hands at about 103.60. The deterioration in global risk sentiment caps the USD/JPY topside.



Sterling takes small step backward



Today's sterling moves were modest, especially compared to yesterday's swings during the ECB's press conference. Sterling initially traded sideways, but some 'minor' issues triggered a gradual intraday decline. **BAT's bid for the outstanding shares of Reynolds** with an important part of the payment in cash, was negative for sterling (especially against the dollar). Mid-morning, the **monthly UK public finance data** added to the sterling-sceptical sentiment. The budget deficit was substantially wider than expected and questions the government's intention to substantially reduce this year's shortfall. It also raises doubts whether the government has much room to support the economy in case of an economic setback due to Brexit. The budget data reinforced the intraday sterling decline. **The fragile risk sentiment and negative headlines on the Brexit process coming from the EU summit didn't help sterling neither.** EUR/GBP touched an intraday low around 0.8887 this morning, but rebounded and trades currently around 0.8935. Cable also drifted south, both because of dollar strength and sterling weakness. The pair trades currently around 1.2175.

16:00 CET

Daily EMU spread changes (bps)

	5-yr			10-yr			30-yr		
	Yield	Spread	Change	Yield	Spread	Change	Yield	Spread	Change
Germany	-0,50%			0,00%			0,60%		
Greece	#VALUE!	#VALUE!	#VALUE!	8,44%	844	-0,3	#VALUE!	#VALUE!	#VALUE!
Portugal	1,79%	228	-7,1	3,18%	318	-2,7	4,10%	350	-3,6
Italy	0,35%	85	-1,5	1,36%	136	-0,9	2,46%	186	-2,2
Spain	0,11%	61	-1,7	1,10%	110	-0,3	2,20%	160	-1,8
Ireland	#VALUE!	#VALUE!	#VALUE!	0,46%	45	0,4	1,29%	69	-0,7
Belgium	-0,43%	7	-0,6	0,23%	22	-0,5	1,15%	55	-0,9
France	-0,38%	12	-0,6	0,28%	27	-0,5	1,07%	47	-0,3
Austria	-0,40%	10	-0,2	0,18%	18	-0,6	0,94%	34	0,3
Netherlands	-0,42%	8	-0,8	0,11%	10	0,0	0,66%	6	-0,1
Finland	-0,46%	4	-0,0	0,13%	13	0,2	0,65%	5	-0,3
US	1,24%	174	-1,7	1,73%	173	-2,1	2,48%	188	-2,4
UK	0,46%	96	-1,0	1,06%	106	-1,9	1,70%	110	-2,4

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
Joke Mertens	+32 2 417 30 59	Institutional Desk	+32 2 417 46 25
Mathias van der Jeugt	+32 2 417 51 94	France	+32 2 417 32 65
Dublin Research		London	+44 207 256 4848
Austin Hughes	+353 1 664 6889	Singapore	+65 533 34 10
Shawn Britton	+353 1 664 6892		
Prague Research (CSOB)			
Jan Cermak	+420 2 6135 3578	Prague	+420 2 6135 3535
Jan Bures	+420 2 6135 3574		
Petr Baca	+420 2 6135 3570		
Bratislava Research (CSOB)			
Marek Gabris	+421 2 5966 8809	Bratislava	+421 2 5966 8820
Budapest Research			
David Nemeth	+36 1 328 9989	Budapest	+36 1 328 99 85

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