05 February 2018

# Danske Daily

## Market movers today

- **The main focus starting this week is whether the sharp sell-off in both bond markets and equity markets continues on the back of the 'inflation scare' flaring up in markets.**
- **On the global agenda today, ECB's Weidman speaks in Frankfurt at 10.00CET. The final Euro PMI service indices with more country details are released at 10.00CET followed by Euro area retail sales at 11.00CET.**
- **US ISM non-manufacturing at 16.00CET will give more insights into the strength of the US service sector.**
- **Rest of the week Fed speeches and Bank of England meeting are the key things to watch. The Fed speeches will be particularly interesting following the job report Friday showing higher wage growth.**
- **In Scandi, attention today turns to Norwegian housing prices at 11.00CET. Rest of the week Norwegian inflation and GDP numbers and Swedish industrial orders/ production and household consumption are the main economic figures in focus.**

## Selected market news

Service PMIs released for China and Japan overnight both came out stronger than expected showing healthy expansion in service sector activity in both economies. Despite these news and the overall strong global economic backdrop equity markets continued to sell off overnight with major Asian stock indices down 1-2% and futures in Europe and US down as well.

Overnight, Japan's prime minister Abe supported continuation of easing by Bank of Japan by saying that he still expects dynamic quantitative easing and that the economy has not completely escaped deflation yet. Bank of Japan governor Kuroda was out saying that there is no change to approach in quantitative easing.

Following the US jobs report on Friday a number of Federal Reserve officials made comments about monetary policy. Kashkari stood out the most as he hinted that the high wage growth number if a sign that wage pressures were building could warrant more hikes this year and thus struck a more hawkish tone on monetary policy than usual. Kaplan and Williams made hawkish and dovish comments respectively.

The Iranian oil minister Zanganeh said this weekend that Iran can increase oil production swiftly if OPEC decides to end production cuts following the planned June review of the production cut deal. On Friday, the US oilrig count rose further to 765 indicating future rise in US production. The price on Brent crude has dropped below USD68/bbl level overnight partly owing to the positive supply fundamentals and partly to the above mentioned weak sentiment in equity markets.

### Selected readings from Danske Bank

- *Strategy - Don't throw out the inflation baby with the capital tide*
- *Flash Comment Denmark - Small drop in FX reserve - large increase in government deposits*

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## Scandi markets

**Norway.** We are not quite so sure how housing prices fared in January (published at 11.00). Revised data show housing prices levelling off in Q4 rather than falling sharply as suggested by the previous series. The change of methodology does, however, increase monthly volatility, so we expect a small correction again in December, with prices falling 0.2-0.3% m/m. This does not change our view that housing prices are stabilising, as suggested by the decrease in the stock-to-sales ratio, but it may sow fresh doubts about the housing market after all the optimism in the wake of the revised data.

## Fixed income markets

The FI sell-off intensified after non-farm on Friday, and the market has now priced in a relatively steep money market curve in EUR and price in almost three US rate hikes in 2018. However, we might still be going into a more pronounced bear market, though we would keep an eye on the impact on global equity markets. If the negative sentiment continues, it should be supportive for global fixed income. We are back to a risk on/risk off market.

So far the 5Y mark has been the focal point on the European curve. It has been the classic textbook reaction when monetary policy is about to change. However, the market may now move the turning or focal point further out on the curve. 1) The impact from the US curve will be higher in the 10Y segment, 2) there is much more room for repricing both the real rate, inflation expectations and the term and volatility in the 10Y segment than in the 5Y segment. For now we could start to see a steeper 5y10y EUR curve. For more see *Government Bonds Weekly*, 2 February 2018.

This week the scheduled EGB supply will slow down significantly from EUR25bn last week to approximately EUR6.5bn – and average duration will be lower. The week will also be characterised by modest coupons and redemptions of just EUR5.2bn compared to EUR53.1bn this week. The January syndication season has more or less come to an end, and of the scheduled syndications in Q1 we only have the 15Y Finland left. This is probably due in the coming week or the week after. Austria kicks off the scheduled week with taps in the 10Y and 3 benchmark bonds and Germany will tap in the 10Y Feb-28 Bund on Wednesday and the DBRi linker Apr-26 on Tuesday.

Today, RD and Nykredit will kick off the February 2018 refinancing auctions of non-callable bullet bonds. The total auction amount is DKK 122bn. Of this, DKK 66bn, DKK 30.9bn and DKK 16.7bn is expected to be sold in the 1Y, 3Y and 5Y segments, respectively. For more details on the refinancing auctions, see *presentation* and auction *overview*. We anticipate reasonable demand for 5Y non-callables at the auction due to low expected supply for the rest of the year and solid interest ahead of the auction. In outright terms 5Y non-callables still offer the highest excess carry vs. swaps and DGBs, though risk-adjusted 3Y non-callables look more attractive than earlier. We maintain our buy recommendation on 5Y non-callable bullets, though the potential for further spread performance is limited.

## FX markets

The strong US job report sent EUR/USD towards 1.24 on Friday, but the cross recovered decently in late trading – an illustration that good US news is currently seen as a global positive and/or not something that will cause the Fed to tighten much more/faster. At a time when the euro is very sensitive to ECB communication it is worth watching out for comments e.g. from Draghi today on the currency, which is now in effective terms back at levels prior to negative rates and QE. We see EUR/USD consolidating around the 1.25 level for now but maintain the pair is a buy on dips.

USD/JPY bounced above 110 on Friday for the first time since 24 January supported by BoJ's fixed price operation and the strong US jobs report. The correlation between US fixed income market and USD/JPY has broken and USD/JPY is currently caught between two opposing forces as rising US yields currently weighs on global equity markets. The BoJ's fixed price operation announced on Friday reaffirmed that the yield curve control remains in place and should help underpin USD/JPY for now. We expect USD/JPY to trade within the range of 108.25-110.84 in the near term. Speculative short JPY positions were slashed substantially in the week ending 30 January, according to the *IMM data*. Investors are still very short JPY though, but last week's sell-off indicates there may be some room on the upside for USD/JPY from a positioning point of view. Next focus point for JPY will be the announcement about the BoJ's leadership. Japan's government will likely present its nominees around mid- to late February at the earliest.

EUR/GBP ended last week slightly higher driven by a sell-off in GBP/USD after strong US data. For GBP, attention this week will be on the Bank of England (BoE) meeting on Thursday where focus will be on the BoE's inflation projection in the short-term. The oil price has increased while sterling has strengthened, and while we reckon that the net effect is likely around zero for inflation, market is now pricing in 55% probability of a rate hike already in May. We think the appetite for making a big signal shift at this meeting is low and that the BoE might take a wait-and-see approach. This could send EUR/GBP slightly higher this week. Overall, we still expect EUR/GBP to trade within the 0.8650-0.90 range in the near term.

NOK suffered in late Friday trading on the back of risk (incl. oil) selling off after the US non-farm release. We had been arguing that the balance of risk last week was for a NOK correction given the external environment. While EUR/NOK broke through the 100D moving average that we referred to, we still think any NOK setbacks marks a buying opportunity from a strategic basis. This week's data calendar is heavy in Norway: house prices (today), inflation and Q4 GDP. Overall, we see upside risk to these releases relative to consensus. If one believes global risk appetite settles, then long NOK this week also seems like a reasonable tactical trade. For more information see *Reading the Markets Norway*, 5 February 2018.

**Key figures and events**

| Monday, February 5, 2018 | | | | Period | Danske Bank | Consensus | Previous |
|---|---|---|---|---|---|---|---|
| 1:30 | JPY | Markit PMI services | Index | Jan | | | 51.1 |
| 2:45 | CNY | Caixin PMI service | Index | Jan | | *53.5* | 53.9 |
| 8:30 | SEK | PMI services | Index | Jan | | | 64.6 |
| 9:15 | ESP | PMI services | Index | Jan | | *55.1* | 54.6 |
| 9:45 | ITL | PMI services | Index | Jan | | *56.0* | 55.4 |
| 9:50 | FRF | PMI services, final | Index | Jan | | *59.3* | 59.3 |
| 9:55 | DEM | PMI services, final | Index | Jan | | | 57.0 |
| 10:00 | EUR | ECB's Weidmann speaks in Frankfurt | | | | | |
| 10:00 | EUR | PMI composite, final | Index | Jan | | *58.6* | 58.6 |
| 10:00 | EUR | PMI services, final | Index | Jan | | *57.6* | 57.6 |
| 10:30 | EUR | Sentix Investor Confidence | Index | Feb | | *34.5* | 32.9 |
| 10:30 | GBP | PMI services | Index | Jan | **54.6** | *54* | 54.2 |
| 11:00 | EUR | Retail sales | m/m\|y/y | Dec | | *-1.0%\|1.8%* | 1.5%\|2.8% |
| 11:00 | NOK | Housing prices | m/m | Dec | **-0.2%** | | |
| 15:45 | USD | Markit PMI service, final | Index | Jan | | | 53.3 |
| 16:00 | USD | ISM non-manufacturing | Index | Jan | | *56.5* | 56.0 |

*Source: Bloomberg, Danske Bank*

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### Date of first publication

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