



Sunrise

Wednesday, 03 January 2018

Rates: Bear steepening in opening session of the year

Global core bonds started the New Year on a weak footing with bear steepening of both the US and German yield curves. Trading will be mainly guided by the US eco calendar today with US manufacturing ISM and FOMC Minutes. We hold our short positions in both the US Note future and the Bund even if FOMC Minutes give increased attention to low inflation.

Currencies: EUR/USD nears 2017 top

Recently, the dollar suffered. Ongoing strong global growth suggested that other CB's, including the ECB, might come closer to policy normalization. Interest rate differentials narrowed in favour of the euro. Today's US events (ISM/ Fed Minutes) probably won't change the global context. The EUR/USD might slow ahead of Friday's payrolls

Calendar

Headlines

S&P	↗
Eurostoxx 50	↗
Nikkei	→
Oil	→
CRB	↗
Gold	↗
2 yr US	↗
10 yr US	↑
2yr DE	→
10 yr DE	↗
EUR/USD	↗
USD/JPY	↗
EUR/GBP	→

- **US stock markets eked out gains on the first trading day of the new year.** The Nasdaq significantly outperformed, closing above 7000 for the first time ever. **Asian risk sentiment is positive as well overnight with Japan closed.**
- **The ECB may end its stimulus programme this year** if the EMU economy continues to grow strongly, **ECB Nowotny** said. He also **warned of European stock market bubble risks.**
- **Britain has held informal talks about joining the Trans-Pacific Partnership.** The proposal would make the UK the first member that does not border the Pacific Ocean or the South China Sea.
- **Brent crude rose above \$67/barrel for the first time since 2015 yesterday,** supported by **tensions in Iran.** Separate data showed **a record net long position has been accumulated** by hedge funds and other money managers in the five biggest futures and options contracts covering crude, gasoline and heating oil.
- **Donald Trump has embarked on a foreign policy offensive** on his return to the White House, piling pressure on Iran, Pakistan, North Korea and the Palestinians as he switches his focus beyond tax reform and other domestic priorities.
- **South Korea can "in principle" consider measures to boost investment overseas if won rises sharply,** a government official, who declined to be named on internal policy, said by phone.
- **Today's eco calendar** contains German unemployment data, the UK construction PMI, the US manufacturing ISM and FOMC Minutes.

Rates

Bear steepening in opening session of the NY

Global core bonds started the New Year on a weak footing. Both the Bund and US Note future sold off with US Treasuries underperforming, partly catching up with Bund weakness in the illiquid final trading days of last year. Higher oil prices (see graph) and hawkish comments by ECB Coeuré & Nowotny might have been at play. The ECB members warned that APP won't be extended beyond September and Nowotny added bubble risks on European stock markets. A strong US equity market opening inflicted additional losses on mainly the US Note future. The eco calendar was empty apart from Markit's confirmation the final EMU manufacturing PMI at a very high 60.6.

	US yield	-1d
2	1,92	0,04
5	2,25	0,04
10	2,46	0,06
30	2,81	0,07

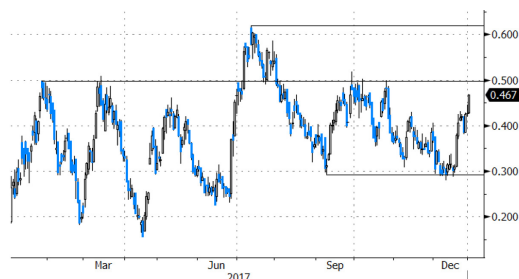
	DE yield	-1d
2	-0,61	0,02
5	-0,19	0,02
10	0,47	0,04
30	1,32	0,05

In a daily perspective, both the US and German yield curves bear steepened. US yields increased by 3.6 bps (2-yr) to 7.4 bps (30-yr) while German yields added 1.7 bps (2-yr) to 5.1 bps (30-yr). 10-yr yield spreads versus Germany ended narrowly mixed with Portugal (+3 bps) and Italy (+5 bps) underperforming. Italian president Mattarella dissolved parliament last week, preparing for early parliamentary election (March 4) which could result in a political deadlock. Therefore, more underperformance is possible. Irish spreads remained steady despite the Treasury's announcement of a near term €3-4bn syndicated bond sale (May2028; likely today).

Asian stock markets trade positive overnight in line with the US yesterday. The US Note future and Brent crude trade stable, suggesting a neutral opening for the Bund. Trading will be mainly guided by the US eco calendar today with US manufacturing ISM and FOMC Minutes. The ISM is expected to have remained strong in December, in line with other global PMI/ISM's already published. A stabilization at 58.2 is forecast. The market reaction to activity data was muted of late. FOMC Minutes might show more insight in the Fed's determination to hike rates three times this year. A potential risk to this scenario is increased cautiousness by Fed members to mysteriously low inflation. That might cause an uptick in US Treasuries, but we don't expect such move to last and eye a test of the 123-12+ low in the US Note future. We think that the Fed will hike rates in March. The market implied probability of that scenario is 70%.

German Bund sentiment deteriorated sharply since the end of last month.

Strong present and expected growth warrants such move. We think that the ECB will have to change its guidance on APP and interest rates in 2018, acknowledging these developments. We hold our short positions and target the September low (159.78).



German 10-yr yield rapidly approaching the upper bound of last year's trading range.



Brent crude closes in on the 2015 high, supported by tensions in Iran

Currencies

EUR/USD nears 2017 top

R2	1,2225	-1d
R1	1,2092	
EUR/USD	1,2059	0,0047
S1	1,1713	
S2	1,1554	

Overnight, the dollar shows no clear trend even as risk sentiment stays positive. USD/JPY holds in the lower half of the 112 big figure. EUR/USD hovers in the mid 1.20 area. **Today, German labour data** are expected to improve further with the unemployment rate declining to 5.5%. **The US manufacturing ISM is expected unchanged at a high 58.2.** (FX) traders will keep an eye at the price indicators of the report. This evening, the minutes of last month's FOMC meeting will be published. Markets will also look for the Fed's assessment on ongoing low inflation. At least, it didn't cause a major change to the 2018 Fed dot plot.

Recently, the dollar suffered as the global recovery could force other major CB's (including ECB) to join policy normalisation. Today's data probably won't change market sentiment. **That said, good US data might slow the recent USD decline ahead of Friday's payrolls.** It also won't be that easy for EUR/USD to set new cycle high without really high profile news. At the same time, higher core yields and/or a risk-on sentiment as such were not enough to support the dollar of late.

Global picture USD: The outcome of the Dec Fed & ECB meetings didn't provide directional guidance for EUR/USD. A narrowing in the (LT) interest rate differentials finally propelled EUR/USD to the topside of the 1.1554/1.2090 range end 2017. A sustained break would improve the ST picture. For now we don't preposition for such a break. Quite some good news on the euro/bad news on the dollar should be discounted at current levels. Price data remain in focus.

EUR/GBP tried to regain the 0.89 mark yesterday on a softer than expected manufacturing PMI, but the attempt failed. **Today, only the UK construction PMI** is on the agenda (expected little changed at 53). More technical trading might be on the cards. A slowdown of the EUR/USD rally might cap the topside of EUR/GBP short-term.

Global picture EUR/GBP: The EUR/GBP decline stalled even as the EU agreed to start the next stage of Brexit negotiations. The pair settled in a 0.8760/0.8960 consolidation range. Recent UK data were mixed. We don't expect the BoE to raise interest rates anytime soon. The EUR/GBP 0.8700/60 support looks solid. Ongoing euro strength or soft UK data might keep EUR/GBP 0.90 on the radar further down the road. We keep a EUR/GBP buy-on-dips approach in case of return action to the 0.87 area.



Calendar

Wednesday, 3 January		Consensus	Previous
US			
16:00	Construction Spending MoM (Nov)	0.5%	1.4%
16:00	ISM Manufacturing (Dec)	58.2	58.2
20:00	FOMC Meeting Minutes	--	--
UK			
10:30	Markit/CIPS UK Construction PMI (Dec)	53.0	53.1
Germany			
09:55	Unemployment Change ('000's) (Dec)	-13k	-18k
09:55	Unemployment Claims Rate SA (Dec)	5.5%	5.6%
10:00	CPI Brandenburg MoM / YoY (Dec)	--/--	0.4%/1.6%
Spain			
09:00	Unemployment MoM Net ('000s) (Dec)	-58.9	7.3
Norway			
08:00	Unemployment Rate AKU (Oct)	4.0%	4.0%

10-year	<u>Close</u>	<u>-1d</u>		2-year	<u>Close</u>	<u>-1d</u>	Stocks	<u>Close</u>	<u>-1d</u>
US	2,46	0,06		US	1,92	0,04	DOW	24824,01	104,79
DE	0,47	0,04		DE	-0,61	0,02	NASDAQ	7006,898	103,51
BE	0,69	0,05		BE	-0,49	0,01	NIKKEI	22764,94	0,00
UK	1,29	0,10		UK	0,50	0,06	DAX	12871,39	-46,25
JP	0,05	0,00		JP	-0,13	0,00	DJ euro-50	3490,19	-13,77
IRS	<u>EUR</u>	<u>USD</u>	<u>GBP</u>	EUR	<u>-1d</u>	<u>-2d</u>	USD	<u>-1d</u>	<u>-2d</u>
3y	0,00	2,20	0,92	Eonia	-0,3700	-0,0240			
5y	0,32	2,28	1,09	Euribor-1	-0,3680	0,0000	Libor-1	1,5643	0,0000
10y	0,91	2,44	1,36	Euribor-3	-0,3290	0,0000	Libor-3	1,6943	0,0000
				Euribor-6	-0,2710	0,0000	Libor-6	1,8371	0,0000
Currencies	<u>Close</u>	<u>-1d</u>		Currencies	<u>Close</u>	<u>-1d</u>	Commodities	<u>Close</u>	<u>-1d</u>
EUR/USD	1,2059	0,0047		EUR/JPY	135,41	0,17	CRB	194,72	0,85
USD/JPY	112,29	-0,34		EUR/GBP	0,8873	-0,0013	Gold	1316,10	6,80
GBP/USD	1,359	0,0087		EUR/CHF	1,1718	0,0012	Brent	66,57	-0,30
AUD/USD	0,783	0,0025		EUR/SEK	9,8492	0,0236			
USD/CAD	1,2512	-0,0033		EUR/NOK	9,8011	-0,0497			

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