



Sunrise

Thursday, 27 April 2017

Rates: Will Draghi trigger new Bund sell-off?

The ECB is expected to keep its policy unchanged. However, Draghi's language at the press conference might reveal more optimism on economic growth and hints about a future unwinding of the ECB's current very accommodative monetary policy stance. The market reaction could be a copy of the one after the March policy meeting (bear steepening).

Currencies: Trump tax plan no help for the dollar. Focus turns to Draghi

Yesterday, the euro fell prey to modest profit taking. However, the lack of details of the Trump tax plan prevented further USD gains. The BOJ left its policy unchanged with little impact on the yen. Today's focus will be on the ECB meeting. If Draghi would sound more optimistic, he might inspire some further unintended euro gains.

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 equities ended marginally weaker** as they were not impressed by Trump's tax plan. **Overnight, Asian stock markets also correct lower** with China marginally underperforming (-0.5%).
- **The Trump administration said it was no longer considering pulling out of NAFTA.** Mexico, Canada and the US will soon begin talks over renegotiating the agreement.
- President Trump's top economic team unveiled what they called the biggest tax cut in US history, **proposing a sharp reduction in corporate taxes and a simplification of individual rates** they said would unleash economic growth.
- **The BoJ kept its policies unchanged while lowering its inflation forecast.** Any exit from its unprecedented monetary easing remains far away. The central bank made a small increase to its growth forecasts for this fiscal year and next.
- **Global oil discoveries fell to a record low in 2016**, the International Energy Agency says, raising fresh concerns about the potential for a petroleum-supply shortage as soon as 2020.
- **Profits earned by China's industrial firms rose 23.8% in March** from a year earlier, buoyed by a continued construction boom, though the pace of growth eased from multi-year highs seen in previous months.
- **Today's eco calendar** heats up with US trade balance, durable goods orders, weekly jobless claims, German Inflation, EMU EC economic confidence and central bank meetings in EMU and Sweden. Italy and the US tap the market.

Rates

After the stormy weather, bonds find their composure

German Bunds higher on short covering ahead of ECB meeting

US Treasuries rise on disappointment about tax plan

Peripherals underperform on profit taking

Trading on markets calmed down yesterday after two hectic days. Some bottom fishers/short coverers were active in most markets. The Bund gradually moved higher. **A very temporary dip is visible on the charts when US Treasury Secretary Mnuchin spoke about the tax plan. Lack of detail and the suggestion that growth would offset the impact of the cuts on the deficit eventually hit equities and pushed US Treasuries to minor gains.** We shouldn't qualify yesterday's price action as a countermove, but more as a short covering ahead of today's ECB meeting and reaction on the US's tax plan.

In a daily perspective, the German yield curve shifted 1.4 bps (2-30-yr) to 2.6 bps (10-yr) lower. Changes on the US yield curve ranged between flat (2-yr, benchmark change) and -2.8 bps (10-30-yr). **On intra-EMU bond markets,** 10-yr yield spreads widened for most credit with Spain (+5 bps) and Italy (+7 bps) underperforming, likely due to profit taking and upcoming supply (Italy).

	DE yield	-1d
2	-0,69	-0,01
5	-0,34	-0,02
10	0,35	-0,03
30	1,11	-0,01

	US yield	-1d
2	1,28	-0,01
5	1,84	-0,02
10	2,31	-0,02
30	2,97	-0,02

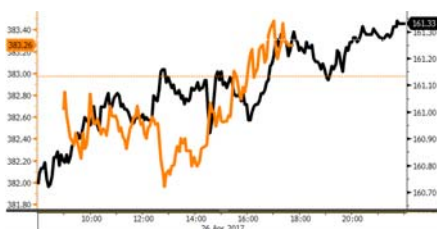
Busy eco calendar and ECB meeting

German CPI report expects sharp rebound. Too sharp?

US durables good, but maybe not as good as expected

ECB to lay low. Possible surprises: risk assessment/slight tweak FG

The **EU Commission confidence data for April should be strong** with additional modest gains in April. **More important are the German April inflation data, following the surprisingly sharp March drop.** The market expects a rebound. Conventional wisdom suggests that the late timing of Easter was partly responsible for March dip (together with higher energy and food prices) and thus will now be offset by a rebound in prices to 1.9% Y/Y from 1.5% Y/Y in March. **We agree with consensus on the rebound, but see risks on the strength of the rebound.** Needless to say that it is a key variable for the bond market, even it may ST be overshadowed by the ECB meeting. The **March US durable goods report** may affect markets. It is a volatile series that is difficult to forecast and thus often surprises. The headline may be positively influenced by Boeing orders (which are already reported), but offset by weakness in car orders. Core orders weakened modestly recently. **Therefore, we expect a positive report that may fall shy of the high expectations though.** The ECB meeting is the key event (see our preview at the KBC research App). Given lingering political uncertainty about the French elections, **we expect the ECB to lay low and to try to avoid volatility.** The current policy stance will be confirmed (APP till end 2017 at €60B/month and forward guidance). The **risk assessment might be upgraded** to broadly balanced from tilted to the downside and there's **a small chance that the reference to even lower rates is scrapped** from the forward guidance. However, we think that the June and September meetings will be crucial.



Bund future (Black) & EuroStoxx (orange): Slight upward bias Bunds, but in a tight range.



German 10-yr yield: Any surprise by Draghi .may be enough to send it to the topside or the downside again.

Italy and US tap market

R2	163,99	-1d
R1	162,49	
BUND	161,19	0,21
S1	158,73	
S2	158,28	

The Italian treasury sells the on the run 5-yr BTP (€2-2.5B 1.2% Apr2022) and 10-yr BTP (€2.25-2.75B 2.2% Jun2027). The bonds cheapened marginally in the run-up to the auction, but trade rather expensive on the Italian curve. The amount on offer is rather low suggesting no difficulties though.

The US Treasury continued its end-of-month refinancing operation with a strong \$15B 2-yr FRN auction and a weak \$34B 5-yr Note auction. The 5-yr Note auction stopped with a tail and the bid cover (2.34) was light. Bidding details showed a weak indirect bid while the direct and dealer bids were close to average. The Treasury ends its refinancing operation today with a \$28B 7-yr Note auction. Currently, the WI trades around 2.13%.

Will Draghi trigger new Bund sell-off?

Risk sentiment is rather neutral overnight. Asian stock markets trade a tad weaker, but Brent crude, the Japanese yen and the US Note future give no firm guidance. We expect a neutral opening for the Bund.

Trading is generally subdued ahead of an ECB meeting, but today **it might be different with German (regional) CPI data on the agenda. A significant Easter-related rebound is expected which trigger more bets on an early normalization process by the ECB.** In such scenario, the German yield curve could bear steepen with a further reduction of asset purchases in H2 2017 in mind. **The ECB is expected to keep its policy unchanged.** The upcoming 2nd round of French presidential elections and subdued EMU core inflation warrant such stance. **However, Draghi's language at the press conference might reveal more optimism on economic growth and hints about a future unwinding of the ECB's current very accommodative monetary policy stance. In that case, the market reaction could be a copy of the one after the March policy meeting (bear steepening, stronger euro).** If Draghi manages to hold a very soft stance, we think that the market reaction will be less outspoken, with Bunds reversing some of this week's earlier losses.

Technically, the US 5- and 10-yr yield **recaptured lost support levels (1.8% and 2.3% respectively), which allows them to turn higher in the old trading bands** as the Fed prepares another rate hike in June and will start to run-off its balance sheet before the end of the year. The German 10-yr yield is already back in its old 0.2%-0.5% trading range as markets no longer discount a Brexit tail risk and perhaps start looking forward to the ECB's normalisation process (this Summer?).



German Bund: Brexit no longer an issue. Focus turns to ECB's normalization policy.



US Note future: new sell-on-upticks as yields regained lost support levels

Currencies

Rise of EUR/USD and USD/JPY slows as does the risk-rally

Trump Tax plan doesn't help USD.

R2	1,13	-1d
R1	1,1145	
EUR/USD	1,0902	-0,0043
S1	1,0778	
S2	1,0341	

BOJ constructive on the economy, but inflation target still far away

USD/JPYT stabilizes in the low 111

CAD and MXN rebound

ECB policy statement in focus today

Will Draghi be soft enough to prevent further euro gains?

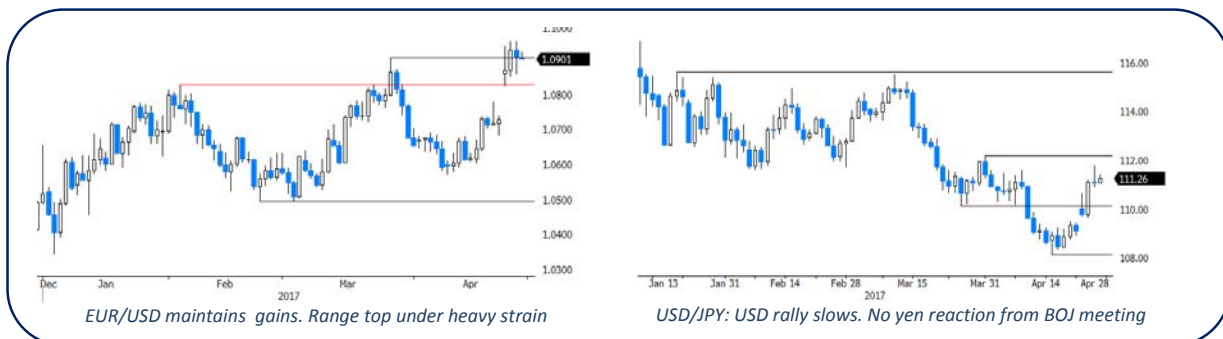
Tax plan no help for USD. Focus turns to Draghi

On Wednesday, the combined rally of EUR/JPY, USD/JPY and EUR/USD continued in Asia, but the post-Macron risk trade slowed in Europe. This caused some profit taking on the euro as investors reduced positions ahead of the Trump tax plan and the ECB policy meeting today. The Trump tax plan didn't bring additional info. The announcement triggered a slight setback in US equities and in the dollar. EUR/USD reversed part of intra-day losses and finished the session at 1.0904 (from 1.0926). USD/JPY closed the session little changed at 111.09.

Overnight, the BOJ as expected left its **policy unchanged**. The bank is rather upbeat on the economy. Still, It cut its inflation forecast for this fiscal year, suggesting that no policy tightening is to be expected anytime soon. The Bank expects the 2% target to be reached during the fiscal year 2018/19. The reaction of the yen is modest. USD/JPY hovers in the 111.20/25 area. Asian equities trade with limited losses following WS. EUR/USD hovers little changed in the 1.09 area. The CAD and MXN rebound as Trump said he doesn't intend to scrap the NAFTA pact.

Today, the eco calendar is well filled. In EMU, the EC confidence data and the German inflation data take centre stage. German HICP inflation is expected to rebound to 1.9 % Y/Y from a surprise drop to 1.5% Y/Y. We consider the expected rebound as quite strong. A lower than expected figure might be slightly negative for the euro. The US calendar heats up with the trade balance, the durable goods orders and the weekly jobless claims. For the durable orders, we see downside risks. The key feature for the (FX) trading will be the ECB meeting. (see our preview). Given uncertainty about the French elections, **we expect the ECB to try to avoid volatility**. So, the core of its current policy will be confirmed. It is possible that the **risk assessment is upgraded** to broadly balanced from tilted to the downside. There is **a small chance that the reference to even lower rates is scrapped** from the forward guidance. However, we think that the June and the September meetings will be crucial.

In a day-to-day perspective, the eco data might be mixed for EUR/USD trading. Market disappointment on the Trump tax plan might be slightly negative for the dollar. As was the case last month, the ECB will try to avoid hints about policy normalisation. However, hints on an improvement in the economic context might be seen as opening the door for a change in policy. **In such a scenario, EUR/USD might revisit the recent highs. Even a test of the 1.10 barrier might be on the cards.**



This week, FX trading was driven by the global risk trade as (European) political event risk eased. This supported USD/JPY but also EUR/USD and EUR/JPY. Market speculation that the decline in EMU political event risk could bring forward the ECB normalisation process supports the euro, too. ECB's Draghi will downplay this speculation. **Question is whether the (FX) market will believe it.** At the same time, Trump's tax plan is no immediate support for the dollar. **So, for now, a cautiously euro positive momentum might persist. From a technical point of view,** This week's rebound of USD/JPY suggests a bottoming out process might have started, but the pair needs to regain the 112.20 level (neckline ST double bottom) to improve the picture. **EUR/USD extensively tested the topside of the MT range (1.0874/1.0906 area) late March. The pair returned to the range top after the French election and set minor new highs. We look out how this test turns out. If EUR/USD would regain the 1.10 barrier, next resistance comes in in the 1.1145/1.13 area (US pre/post-election swings).**

R2	0,8881	-1d
R1	0,8854	
EUR/GBP	0,8471	-0,0055
S1	0,8314	
S2	0,8304	

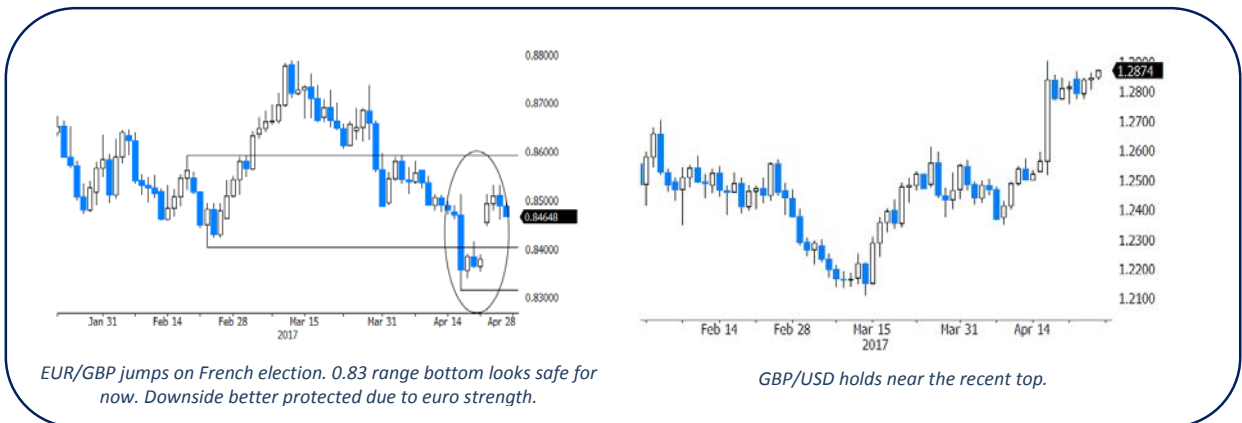
Cable continues to challenge recent top

Yesterday, the focus of sterling trading was on external factors, including on the Trump tax plan. Euro profit taking dominated the price action in EUR/GBP. EUR/GBP closed the session at 0.8487. Initially, the dollar held relatively strong against sterling, but cable regained some ground on USD softness after the Trump Tax plan. The pair closed the session at 1.2848.

Today, the UK calendar contains the CBI retail data/distributive reported sales. A slight decline in the sales momentum is expected. However, the figure will have to be really negative to trigger a meaningful decline of sterling. Sterling took a good start against the euro and the dollar this morning. However, if the euro would stay well bid on the ECB policy statement, it could also help to put a floor for the EUR/GBP. Cable currently profits from USD softness.

Early last week, EUR/GBP dropped below EUR/GBP 0.84 support, (temporary) improving the sterling picture. The pair came within reach of the key 0.8305 support (Dec low), but no real test occurred. After this week's rebound, the range bottom is better protected. Longer term, Brexit-complications remain a potential negative for sterling. Of late, this was not the focus of sterling trading.

Nevertheless on technical considerations we are inclined to reconsider a cautious EUR/GBP buy-on-dips approach.



Calendar

Thursday, 27 April		Consensus	Previous
US			
-14:30	Advance Goods Trade Balance (Mar)	-\$65.2b	-\$63.9b
-14:30	Durable Goods Orders (Mar-P)	1.3%	1.8%
-14:30	Durables Ex Transportation (Mar-P)	0.4%	0.5%
-14:30	Cap Goods Orders Nondef Ex Air (Mar-P)	0.5%	-0.1%
-14:30	Cap Goods Ship Nondef Ex Air (Mar-P)	0.1%	1.0%
-14:30	Initial Jobless Claims	243k	244k
Japan			
-	BOJ Policy Balance Rate	A-0.100%	-0.100%
-	BOJ 10-Yr Yield Target	A-0.000%	0.000%
UK			
-12:00	CBI Retailing / Total Dist. Reported Sales (Apr)	6/30	9/32
EMU			
-11:00	Economic Confidence (Apr)	108.2	107.9
-11:00	Business Climate Indicator (Apr)	0.82	0.82
-11:00	Industrial Confidence (Apr)	1.3	1.2
-11:00	Services Confidence (Apr)	12.9	12.7
-11:00	Consumer Confidence (Apr-F)	-3.6	-3.6
-13:45	ECB Main Refinancing Rate	0.000%	0.000%
-13:45	ECB Deposit Facility Rate	-0.400%	-0.400%
-13:45	ECB Asset Purchase Target (Apr)	EU60b	EU80b
Germany			
-	CPI Baden-Wuerttemberg MoM / YoY (Apr)	--	0.3%/1.6%
-08:00	GfK Consumer Confidence (May)	9.9	9.8
-09:00	CPI Saxony MoM / YoY (Apr)	--	0.2%/1.8%
-10:00	CPI Bavaria MoM / YoY (Apr)	--	0.4%/1.7%
-10:30	CPI North Rhine-Westphalia MoM / YoY (Apr)	--	0.1%/1.7%
-14:00	CPI MoM / YoY (Apr-P)	-0.1%/1.9%	0.2%/1.6%
-14:00	CPI EU Harmonized MoM / YoY (Apr-P)	-0.1%/1.9%	0.1%/1.5%
Italy			
-10:00	Economic Sentiment (Apr)	--	105.1
-10:00	Manufacturing Confidence (Apr)	107.3	107.1
-10:00	Consumer Confidence Index (Apr)	107.4	107.6
Spain			
-09:00	Unemployment Rate (1Q)	18.60%	18.63%
-09:00	CPI EU Harmonised MoM / YoY (Apr-P)	0.7%/2.3%	1.1%/2.1%
Sweden			
-09:30	Riksbank Interest Rate	-0.500%	-0.500%
Events			
-Q1 earnings	BASF (07:00), Bayer (07:30), Dow Chemical, Samsung, Intel, Alphabet, Amazon, ...		
-11:00	Italy to Sell 1.2% 2022, 2.2% 2027 & Floating 2024 Bonds		
-19:00	US to Sell \$28B 7-yr Notes		

10-year	<u>td</u>	<u>-1d</u>		2-year	<u>td</u>	<u>-1d</u>		Stocks	<u>td</u>	<u>-1d</u>
US	2,31	-0,02		US	1,28	-0,01		DOW	20975,09	-21,03
DE	0,35	-0,03		DE	-0,69	-0,01		NASDAQ	6025,226	-0,27
BE	0,83	0,00		BE	-0,50	-0,03		NIKKEI	19251,87	-37,56
UK	1,08	0,00		UK	0,09	-0,01		DAX	12472,8	5,76
JP	0,02	0,00		JP	-0,20	0,00		DJ euro-50	3578,71	-4,45
IRS	<u>EUR</u>	<u>USD</u>	<u>GBP</u>	EUR	<u>-1d</u>	<u>-2d</u>		USD	<u>td</u>	<u>-1d</u>
3y	-0,02	1,75	0,63	Eonia	-0,3630	-0,0010		Libor-1	0,9922	0,0011
5y	0,22	1,97	0,79	Euribor-1	-0,3730	-0,0020		Libor-3	1,1704	0,0039
10y	0,81	2,29	1,13	Euribor-3	-0,3290	0,0000		Libor-6	1,4236	0,0029
				Euribor-6	-0,2480	0,0000				
Currencies	<u>td</u>	<u>-1d</u>		Currencies	<u>td</u>	<u>-1d</u>		Commodities	<u>td</u>	<u>-1d</u>
EUR/USD	1,0902	-0,0043		EUR/JPY	121,28	-0,62		CRB	181,71	-0,20
USD/JPY	111,25	-0,13		EUR/GBP	0,8471	-0,0055		Gold	1268,40	3,70
GBP/USD	1,2869	0,0033		EUR/CHF	1,0834	-0,0029		Brent	51,63	-0,41
AUD/USD	0,7485	-0,0032		EUR/SEK	9,5583	-0,0297				
USD/CAD	1,3551	-0,0018		EUR/NOK	9,3565	-0,0037				

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