



Sunrise



Wednesday, 19 April 2017

Rates: Can overbought conditions halt the core bond rally?

Today's eco calendar is empty apart from final EMU inflation data which we don't expect to influence trading. Sentiment remains positive for core bonds, but both the Bund and the US Note future are in overbought conditions, suggesting some consolidation around current levels instead of continuation of the rally.

Currencies: Sterling jumps sharply higher as PM May calls early elections

Yesterday, USD softness persisted as US yields declined further. EUR/USD regained the 1.07 barrier. Today, the calendar is thin so there is probably no trigger to change the dollar's fortunes. Sterling jumped sharply higher as PM May announced early elections. Markets apparently expect the election outcome to provide more stability for the Brexit negotiations.

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 equity markets closed up to 0.3% lower with the Dow Jones underperforming (-0.5%). Overnight,** most Asian stock markets lose ground as well with China underperforming (-1%).
- **The German government believes an interest rate increase by the ECB would help to reduce Germany's often-criticised export surplus,** the Funke Mediengruppe newspaper chain reported.
- Another Federal Reserve policymaker backed an emerging US central bank plan to begin trimming its bond holdings later this year, as **Kansas City Fed George warned against waiting too long in order to "overheat" labour markets.**
- **US President Trump** signed a new "Buy American, Hire American" executive order aimed at cracking down on skilled worker visa abuse and **forcing US government agencies to buy more domestically produced products.**
- Primary dealers have been asked to respond to questions on **the potential demand, pricing and other factors for 40-, 50-, or 100-year bonds,** as part of the **US Treasury's** latest quarterly survey.
- **The IMF raised its 2017 global growth forecast** from 3.4% to 3.5% due to manufacturing and trade gains in Europe, Japan and China, but warned that protectionist policies threaten to choke a broad-based recovery.
- **Today's eco calendar** remains thin with only final EMU inflation data. ECB members Coeure, Praet, Hansson and Fed governor Rosengren are scheduled to speak. The Fed releases its Beige Book and Germany taps the market.

Rates

Strong gains for US Treasuries and moderate once for Bunds

No real strong risk off climate

Capitulation as investors leave Trump's reflation trade?

Peripheral spreads narrow

	US yield	-1d
2	1,17	-0,03
5	1,71	-0,06
10	2,18	-0,07
30	2,85	-0,06

	DE yield	-1d
2	-0,87	-0,01
5	-0,53	-0,01
10	0,17	-0,02
30	0,89	-0,03

No data of interest

US Earnings season continues

Fed's Beige book most interesting event

ECB Coeuré, Praet and Fed Rosengren wildcards

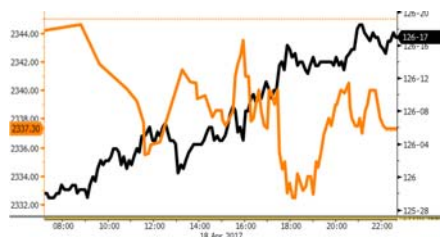
Yields continue to drop, as (US) longs capitulate

Global core bonds resumed their month-long rally which was interrupted during the Easter holidays. The Bund traded volatile, but sideways well into the US session, only disrupted by **UK PM May's call for snap elections** (June 8). During US dealings, **the Bund started to track US Treasuries which were at that point already modestly higher**. US eco data printed mixed, but didn't trigger a strong bond reaction. **Oil prices** dropped lower, but in an erratic way, while bonds dropped at a gradual pace. **EMU equities** dropped after the opening, but side-lined afterwards. The **yen strengthened a bit** but nothing too much. So, one could say that the **climate was risk-off, but only moderately so**. Core bonds rose more than one would expect when taken other market moves into consideration. The upleg occurred **despite the US Treasury calling for comments on the possible issuance of very long tenors** and despite **Kansas Fed George**, admittedly a hawk, calling to start the Fed's balance sheet tapering quickly and continue without reconsideration at each meeting. On top of that the **IMF forecast** reflects a bright global outlook. **In this respect, the bull flattening of the curve is strange too. Safe haven flows often go into the shorter end of the curve. Therefore, it looks more likely that traders and investors are massively leaving the reflation trade and start building back their long positions, a kind of capitulation trade. Where will it stop?**

In a daily perspective, the German yield curve flattened with yields changes ranging between flat (2-yr) and -4.4 bps (30-yr). US Treasuries outperformed and yields dropped between 4.1 bps (2-yr) and 8.2 bps (10-yr). On the intra-EMU markets, 10-yr yield spreads versus Germany were mixed. Spain and Italy outperformed (-3/-4 bps), while Belgium and Greece underperformed (+3/+15 bps).

Fed's Beige Book & Central bank speakers

The market calendar remains razor thin and unattractive. EMU final March CPI and the February trade balance won't **set the direction for bond trading**. **Earnings reports** include Morgan Stanley and Blackrock. Wild cards are the **appearances of ECB Coeuré, Praet and Boston Fed Rosengren**. The former two back Draghi's policy. No policy changes are expected at the April 27 ECB meeting. **Boston Fed Rosengren** favoured 4 rate hikes in 2017. We will closely listen whether he backtracks on that rather aggressive stance. The **Fed's Beige book** is more interesting than usual as the divide between the survey data and the hard data has rarely been wider, causing uncertainty about Q1 GDP.



T-note future (black) & S&P future (orange): Strong bond rally and modest losses US equities



US 10-yr yield drops further, as longs capitulate after break 2.30%. End of reflation trade (for bonds?)

R2	164,40	-1d
R1	163,99	
BUND	163,78	0,24
S1	161,88	
S2	158,28	

Germany taps off the run 30-yr Bund

The German Finanzagentur taps the off the run 30-yr Bund (€1B 2.5% Aug2044). Total bids at the previous 4 30-yr Bund auctions averaged only €1.1B amid mostly higher auction yields than today will be the case. The bond didn't cheapen in ASW spread terms going into the auction, but is rather attractive compared to surrounding bonds at the very long end of the German yield curve. Nevertheless, we fear another toilsome auction.

Little downside Bund ahead of French elections

Overnight, most Asian stock markets lose some ground with China underperforming. The US Note future and Brent crude trade stable though suggesting a neutral opening for the Bund.

Today's eco calendar is empty apart from final EMU inflation data which we don't expect to influence trading. **Last week's risk aversion pushed the US 5- and 10-yr yield below key support levels (respectively 1.8% and 2.3%). The German 10-yr yield lost 0.2% support yesterday.** Geopolitical concerns (North Korea & Syria), doubt about the implementation of Trump's pro-growth agenda and French presidential elections (1st round on April 23) probably prevent return action (higher yields) this week as the eco calendar is irrelevant for trading apart from Friday's euro area PMI's. **However, both the Bund and US Note future entered overbought conditions, suggesting that the core bond rally could lose some steam. We expect consolidation around current levels.**

Our medium term strategy remains that US yields will recapture lost support levels and afterwards turn higher in the old trading bands as the Fed prepares another rate hike in June and will run-off its balance sheet before the end of the year.



German Bund: New contract high. German Bund sets new contract high. Overbought conditions



US Note future: risk aversion dominates, boosting core bonds with yields below key levels

Currencies

Dollar continues to fight an uphill battle

EUR/USD regains 1.07 handle

R2	1,1145	-1d
R1	1,0906	
EUR/USD	1,0720	0,0077
S1	1,0341	
S2	1,0000	

Eco data probably remain of second tier importance for USD trading

US yields to decide on USD direction

Decline US yields continues to weigh on dollar

On Tuesday, global equity softness was again more negative for the dollar than for the euro. The US eco data were mixed with no impact on USD trading. Later in the session, the dollar came under further pressure as the decline in core/US bond yields accelerated. USD/JPY failed to sustain north of 109 and closed the session at 108.43, but Monday's correction low (108.13) was left intact. The dollar also lost ground against the euro. EUR/USD rebounded north of 1.07 and closed the session at 1.0730. Are investors reducing euro shorts ahead of the French presidential election?

Overnight, most Asian equities are trading with modest losses. The yen remains strong with USD/JPY holding in the mid 108 area. **The Japanese 10-year yield** remains around 0.0%, away from the 0.1% BOJ target, but that is no negative for the yen. **EUR/USD maintains yesterday's gains, holding in the 1.0720/25 area.** So, **by default dollar softness remains the name of the game.** The **Aussie dollar** is ceding further ground against a declining USD. Overall negative sentiment on risk, a further decline in the Iron ore price and a soft performance of Chinese equities all weigh on the Aussie dollar. AUD/USD is trading in the 0.7525 area.

Today, the market calendar remains thin. There are no important eco data in the US. In the euro area, the final March CPI and the February trade balance are no market movers. Or is there risk for an upward revision for the CPI?. **Earnings reports** include Morgan Stanley and Blackrock. Wild cards are the **appearances of ECB Coeuré, Praet** and **Boston Fed Rosengren**. The former two are well behind Draghi's policy. **Rosengren** favoured 4 rate hikes in 2007. We will closely listen whether he backtracks on that rather aggressive stance. The **Fed's Beige book** is a bit more interesting than usual as the divide between the survey data and the hard data has rarely been wider.

Yesterday, by default dollar softness still dominated FX trading. The move was reinforced by a further decline in US bond yields. Contrary to what was the case of late, USD weakness was mainly visible in USD/EUR and less in USD/JPY. **We look out whether this pattern continues.** We don't see much room for a sustained EUR/USD rebound. Even so, dollar softness combined with some profit taking on euro shorts a head of the French elections might cause a (temporary ?) bid for the euro.



EUR/USD: rebounds in the range. USD softness prevails, but a modest euro short-squeeze is probably also in play



USD/JPY holding below the 110 support. Technical picture remains bearish, but tentative signs of bottoming

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For the overall USD performance we continue to keep a close eye on the US bond markets. We maintain the view that the correction on the US bond markets has gone far enough. However for now there is no trigger for U-turn. So, it is still too early to position for a rebound of the dollar.

From a technical point of view, USD/JPY broke through the 110 key support, after having failed to regain the 111.36/60 previous range bottom. We downgraded our USD/JPY assessment to bearish, as long as the pair doesn't regain 112.20 (neckline ST double bottom). Next key support (62% retracement) comes in at 107.18.

EUR/USD extensively tested the topside of the MT range (1.0874/1.0906 area) late March, but the test was rejected. EUR/USD returned lower in the 1.0875/1.05. The move did meet support in the 1.06 area as the dollar traded weakish of late. The picture is turning more neutral as the pair returns to the middle of the ST range. We slightly prefer to sell EUR/USD on upticks in case of a return higher in the range as we see room for a broader USD comeback.

Sterling propelled as PM calls early elections

R2	0,8881	-1d
R1	0,8854	
EUR/GBP	0,8359	-0,0110
S1	0,8314	
S2	0,8304	

Yesterday sterling **briefly fell-off a cliff on headlines that UK PM May would make a statement.** Rumours on early elections were confirmed as the UK PM called a vote for June 8. **Initial sterling weakness was reversed and the UK currency started an impressive rebound.** The UK government is largely expected to get a much bigger majority. Markets consider it as a source of stability. It might give room of manoeuvre in the Brexit negotiations. The jury is still out whether the new political context will really lead to a more balanced Brexit outcome. Anyway, it was used to further reduce sterling shorts. EUR/GBP tumbled more than one big figure (even as the euro traded fairly strong). The pair closed the session at 0.8356. The gain in cable was even more spectacular. The pair closed the session at 1.2824 area, a level not seen since October last year.

Today, there are again no eco data in the UK. PM May will formally ask the House of Commons to support her call for early elections on June 8. The call is expected to get the green light as opposition parties support the call. The day-to-day momentum of sterling is obviously strong. In a longer term perspective, the sterling rally is probably a bit overdone. However, at this stage there is no reason to row against the strong sterling tide.

We had a neutral short-term bias on EUR/GBP. Yesterday sterling dropped below the bottom of the EUR/GBP 0.88/0.84 range. The pair came with reach of the 0.8305 support (Dec low). We look whether this level holds. A break below would be highly significant from a technical point of view. Longer term, Brexit-complications remain a potential negative for sterling. However, this is not the focus of sterling trading at this stage.



EUR/GBP: nearing the key 0.83 support as PM May calls for early elections



GBP/USD jumps above MT range top

Calendar

Wednesday, 19 April	¤	Consensus	Previous
US	¤	¤	¤
13:00	MBA-Mortgage-Applications	--	1.5%
EMU	¤	¤	¤
08:00	EU27-New-Car-Registrations-(Mar)	--	2.2%
11:00	Trade-Balance-SA-(Feb)	18B	15.7b
11:00	<u>CPI-MoM-/YoY-(Mar-F)</u>	-0.8%/1.5%	0.4%/1.5%
11:00	<u>CPI-Core-YoY-(Mar-F)</u>	0.7%	0.7%
Norway	¤	¤	¤
08:00	House-Price-Index-QoQ-(1Q)	--	2.7%
Events	¤	¤	¤
Q1-earnings	Blackrock-(Bef-mkt), Morgan-Stanley-(13:00), Qualcomm-(Aft-mkt), eBay-(22:30)	¤	¤
10:00	ECB-Hansson-on-outlook-for-euro-area-in-Estonia	¤	¤
14:00	ECB-Executive-Board-member-Benoit Coeure speaks in New-York-at-roundtable	¤	¤
16:30	ECB-Executive-Board-member-Peter Praet speaks in New-York-(Minsky-conference)	¤	¤
11:30	Germany-to-Sell-€1B-2.5%-2044-Bonds	¤	¤
18:00	Fed's <u>Rosenberg</u> Speaks-at-Bard-College-Conference--(Minsky-conference)	¤	¤
20:00	<u>U.S.-Federal-Reserve-Releases-Beige-Book</u>	¤	¤

10-year	td	-1d		2-year	td	-1d		Stocks	td	-1d
US	2,18	-0,07		US	1,17	-0,03		DOW	20523,28	-113,64
DE	0,17	-0,02		DE	-0,87	-0,01		NASDAQ	5849,471	-7,32
BE	0,76	0,00		BE	-0,51	0,04		NIKKEI	18432,2	76,94
UK	1,01	-0,03		UK	0,09	-0,02		DAX	12000,44	-108,56
JP	0,01	0,00		JP	-0,22	-0,01		DJ euro-50	3409,78	-38,48
IRS	EUR	USD	GBP	EUR	-1d	-2d		USD	td	-1d
3y	-0,08	1,62	0,60	Eonia	-0,3590	-0,0010				
5y	0,11	1,82	0,74	Euribor-1	-0,3710	0,0010		Libor-1	0,9944	0,0000
10y	0,66	2,14	1,06	Euribor-3	-0,3310	0,0000		Libor-3	1,1584	0,0000
				Euribor-6	-0,2500	-0,0040		Libor-6	1,4032	0,0000
Currencies	td	-1d		Currencies	td	-1d		Commodities	td	-1d
EUR/USD	1,0720	0,0077		EUR/JPY	116,49	0,58		CRB	186,54	-0,85
USD/JPY	108,67	-0,24		EUR/GBP	0,8359	-0,0110		Gold	1286,50	-5,40
GBP/USD	1,2823	0,0258		EUR/CHF	1,0695	0,0004		Brent	54,75	-0,61
AUD/USD	0,7522	-0,0067		EUR/SEK	9,6058	0,0305				
USD/CAD	1,34	0,0083		EUR/NOK	9,1311	0,0226				

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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