



Sunrise

Monday, 24 July 2017

Rates: New upward potential Bund, especially if German 10y yield drops below 0.5%

Draghi's dovish performance on Thursday, the risk-off correction on European stock markets (Thursday/Friday) and the volatile, but downwardly oriented, oil price (Friday ahead of today's OPEC vs non-OPEC meeting) suggests some more consolidation in the Bund (correction higher). The German 10-yr yield tests important support (0.5%).

Currencies: Dollar continues fighting an uphill battle

Dollar weakness continues to dominate USD trading. Political uncertainty in the US weighs on the US currency and Draghi's comments didn't prevent further by-default euro buying. Today's US and EMU confidence data probably won't change the established USD negative trend. We don't expect a meaningful comeback of the dollar ahead of the Fed policy decision.

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	↗

- **European equities** were hard hit on Friday, as the euro continued to gain ground against the dollar. **US equities** ended little changed after recouping early losses. **Asian equities** trade mostly slightly positive overnight with the exception of the Japanese equities which are hit by yen strength.
- **Japanese PMI business confidence** weakened slightly in July. The headline index fell to 52.2 from 52.4 in June. Levels above 50 suggest expanding activity.
- **A new EU competition investigation into Germany's top carmakers** threatens the credibility of the entire industry, a German minister has warned, after Brussels confirmed it was probing suspected collusion on technology.
- **Better growth in China, the euro zone and Japan is making up for a slower US economy**, Trump's stalled economic promises and a faltering UK, the IMF said. 2017/18 global growth was confirmed at 3.5%/3.6%.
- **Greece's sovereign credit rating's (B-) outlook was raised to positive** by S&P, boosting the government in Athens, as it ponders a return to bond markets. The IMF agreed to a new \$1.8B conditional loan for Greece on Thursday.
- **Brent oil** stabilized around \$48/barrel overnight, after dropping sharply on Friday and ahead of a meeting between OPEC and non-OPEC regarding production cuts later today.
- **Today**, the market calendar contains the **EMU and US July PMI business surveys**, the US Existing Home sales and speeches of **ECB Smets** and **BoE Brazier**. OPEC meets non-OPEC countries to discuss production cuts.

Rates

Modest gains for core bonds despite sharply lower oil prices and European equities

Euro strength helps Bunds only modestly

Peripherals continued to trade calm

	US yield	-1d
2	1,34	-0,01
5	1,81	-0,01
10	2,24	-0,02
30	2,81	-0,02

	DE yield	-1d
2	-0,64	0,00
5	-0,18	-0,02
10	0,51	-0,02
30	1,28	-0,01

Euro strength to start weighing on EMU manufacturing confidence?

EMU services confidence to recoup some ground?

US Existing Home Sales to stabilize near cycle highs?

Main uncertainty: Will ECB drop its easing bias on APP?

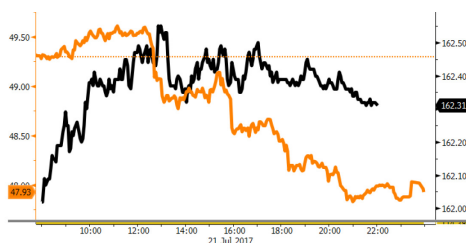
Core bonds eke out modest gains

Global core bonds traded with an upward bias on Friday, helped by falling oil prices, a stronger euro and maybe some late reaction on Draghi's dovish performance on Thursday. This occurred in a context of favourable technicals. The gains were limited though and volumes traded low, suggesting that one shouldn't draw too many conclusions from the daily price action. In such market it shouldn't surprise that the moves between various markets were not synchronized. The Bund reached its daily highs when the oil price only started to fall. US Treasuries moved still a bit higher when oil dropped, but these additional gains were meagre given the extent of the oil price drop. Similarly, the Bund rallied in the morning session, when stocks stabilized and stabilized when stocks hit the skids. There were no eco releases of importance.

In a daily perspective, German yields fell slightly, flattening the curve till the 10-yr tenor. Yields fell about 2.2 bps in the belly, but were marginally higher at the 2-yr (+0.2 bps) and lower in the belly of the curve (-2.4 bps). **US yields fell 1.2 to 2.1 bps till the 10-yr tenor**, flattening the curve, while the 30-yr fell 1.7 bps. **On intra-EMU bond markets**, 10-yr yield spreads versus Germany were little changed with the exception of Portugal (-7bps).

Business confidence in focus

This **week's market calendar** is interesting with **key economic data** releases, the **FOMC meeting** (Wednesday), and some **auctions (Belgium, Italy, US)**. The **earnings season** is in full swing. **Today, attention goes to the business sentiment data (Markit) and to a meeting between OPEC and non-OPEC countries in Russia**. The EMU business sentiment indicators showed an unexpected mixed picture (at high levels) in June. The manufacturing PMI still improved (unabatedly since September 2016), but the services PMI declined. This surprised because the stronger euro suggested some decline in the euro sensitive export (manufacturing) sector. The more domestically oriented services sector was expected to be well underpinned by domestic demand. **Given the additional euro strength, we see downside risks for the manufacturing sector in July, but maybe some rebound in services confidence, as domestic demand fundamentals remain strong**. Last month, markets ignored the EMU PMI report. In the US, the Markit PMI gets less attention due to the presence of the (similar) ISM confidence indicators. The US PMI's have constantly lagged the ISM's performance. Dollar weakness should help the manufacturing confidence, but the inability of Trump to advance his pro-growth agenda may weigh on the services sector. The **US existing home sales** are expected slightly lower, offsetting the slight gain in May. Existing Home sales are still near cycle highs. The relative lack of houses for sales hinder a further increase. We have no reason to distance us from consensus.



Bund future (black) and Brent oil (orange) (intraday): Bund future trades before oil price sinks.



Brent oil cannot break above \$50/barrel threshold. Correction followed. OPEC meets with non-OPEC producers today.

R2	165,55	-1d
R1	164,13	
BUND	162,29	0,55
S1	160,17	
S2	159,1	

Belgium kicks off EMU supply

The Belgian debt agency taps three on the run OLO's: 7-yr OLO 79 (0.2% Oct2023), 10-yr OLO 81 (0.8% Jun2027) and 30-yr OLO 78 (1.6% Jun2047) for a combined €2.2-2.8B. Bonds on offer gave no concession in the run-up to the auction in ASW spread terms. The 7- and 30-yr OLO's trade normal on the Belgian curve while the 10-yr OLO is rather cheap. We expect a plain vanilla auction. Belgium is well advanced with this year's funding plans. They already raised €25.69B of the 2017 €35B OLO funding target (73.4%). **Italy is the only other EMU country to tap the market this week with BTP€I and CTZ-auctions on Wednesday and a regular BTP auction on Friday.** Exact lines and amounts on offer still need to be announced, but we assume it will be 5- and 10-yr auctions.

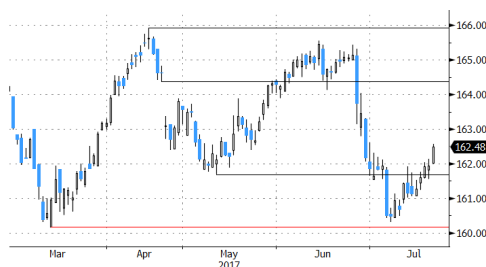
The US Treasury starts its end-of-month refinancing operation tomorrow with a \$26B 2-yr Note auction. The auction is followed by a \$15B 2-yr FRN auction and a \$34B 5-yr Note auction on Wednesday and a \$28B 7-yr Note auction on Thursday.

Weak stocks, low oil price and dovish Draghi

Asian stock markets trade mixed overnight with Japan underperforming and China outperforming. Brent crude stabilizes after Friday's heavy losses The US Note future stabilizes too. We expect a neutral opening for the Bund.

Today's eco calendar is interesting with EMU PMI's. We expect a mixed outcome with downside risks for the manufacturing PMI and upside risks for the services release. That's an ambiguous signal for markets. **Draghi's dovish performance on Thursday, the risk-off correction on European stock markets (Thursday/Friday) and the volatile, but downwardly oriented, oil price (Friday ahead of today's OPEC vs non-OPEC meeting) suggests some more consolidation in the Bund (correction higher).** Cautiousness ahead of Wednesday's FOMC meeting should also benefit the US Note future in thin trading conditions.

Technically, the German 10-yr yield retests previous resistance (0.5%). A move lower suggests a return to this year's sideways range (0.2%-0.5%) and means that markets want more specific clues on a possible September APP-announcement by the ECB. Given Summer trading conditions, this could only come at the end of August (Jackson Hole?).



German Bund: technical picture again neutral. More upside if German 10-yr yield drops back below 0.5%.



US Note future: Cautiousness ahead of the FOMC meeting?

Currencies

USD fights an uphill battle

Dollar still haunted by US political uncertainty

By default euro buying persists despite soft Draghi assessment

EMU eco data probably won't be a game-changer

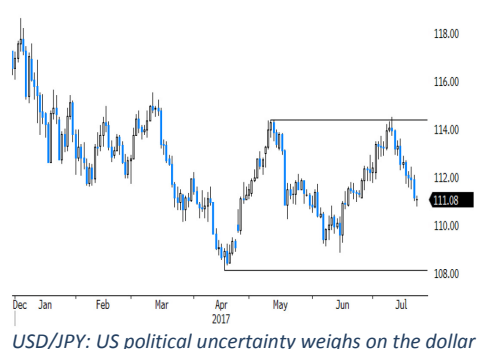
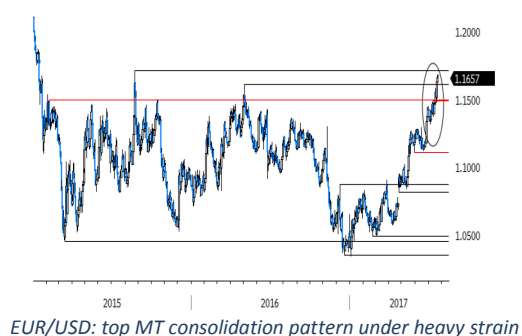
The dollar to remain in the defensive going into the Fed policy decision

R2	1,1811	-1d
R1	1,1714	
EUR/USD	1,1663	0,0032
S1	1,1119	
S2	1,0839	

R2	0,9142	-1d
R1	0,9049	
EUR/GBP	0,8974	0,0008
S1	0,8757	
S2	0,8652	

On Friday, overall dollar weakness continued to dominate FX trading. Uncertainty on the potential political fall-out of the investigations against president Trump and people close to him are weighing on the dollar. At the same time, the euro extended a by default rally. Draghi's comments on the ECB press conference can only be considered as soft, but he also didn't seem overly worried on the recent euro strength. EUR/USD closed the session at 1.1683 (from 1.1631). USD/JPY finished the week at 111.13 (from 111.61 on Thursday evening).

Today, attention goes to the business sentiment data (Markit) and to a meeting between OPEC and non-OPEC countries in Russia. The EMU business sentiment indicators showed an unexpected mixed picture (at high levels) in June. The manufacturing PMI still improved, but the services PMI declined. **Given the additional euro strength, we see downside risks for the manufacturing sector in July, but maybe some rebound in services confidence, as domestic demand fundamentals remain strong. The EMU data probably won't be a game-changer for euro trading, unless they show a really big surprise.** If data would be unexpectedly strong, they might reinforce euro positive momentum. **The focus will be on the US side of the story.** Political uncertainty is probably here to stay and won't help the dollar short-term. **Markets will also look forward to the Fed policy decision on Wednesday.** The Fed will confirm its intention to continue policy normalisation and might even give some concrete hints on the start of the reduction of the balance sheet. **At the same time they probably can't ignore the recent softening in inflation.** There is already quite some negative news discounted for the dollar after the recent setback, **but we see no trigger yet for a positive U-turn on the US dollar.** For that to happen, the dollar needs some really positive news. Strong US eco data next week might bring some relief, but that's still far away. For now there is not good reason to try to catch the falling knife.



USD: technical picture worsens further

EUR/USD rebounded above the 1.1300/66 resistance at the end of June. The payrolls and other recent data were not good enough to trigger a sustained USD rebound. Finally EUR/USD broke beyond the 1.1489/1.15 resistance, paving the way to the LT-correction tops at 1.1616/1.1714. **A break would end the long consolidation that followed the sharp decline of EUR/USD in 2014/early 2015. Such a key area is not easy to break. We don't preposition for a break, but the pressure is mounting.** Return action below 1.13 would be a first indication of a loss in upside momentum.

The USD/JPY rally ran into **resistance** in May and the pair returned lower in the 108.13/114.37 range. The post-Fed USD rebound pushed the pair above the **112.13 correction top, but follow-through gains remain modest. USD/JPY 114.37 resistance was tested, but the test was rejected. The pair is currently drifting lower in the broader consolidation pattern between 114.50 on the topside and 108.83/13 on the downside. A test of the downside is of the range is becoming ever more likely?. This suggests a pause in the recent USD/JPY uptrend.** We stay cautious on USD/JPY long positions despite the recent decent performance.

Calendar

Monday, 24 July		Consensus	Previous
US			
15:45	Markit US Manufacturing PMI (Jul P)	52.2	52.0
15:45	Markit US Services PMI (Jul P)	54	54.2
15:45	Markit US Composite PMI (Jul P)		53.0
16:00	Existing Home Sales / MoM (Jun)	5.57m/1.4%	5.62m/1.1%
Japan			
02:30	Nikkei Japan PMI Mfg (Jul P)	--	52.4
EMU			
10:00	Markit Eurozone Manufacturing PMI (Jul P)	57.2	57.4
10:00	Markit Eurozone Services PMI (Jul P)	55.4	55.4
10:00	Markit Eurozone Composite PMI (Jul P)	56.2	56.3
Germany			
09:30	Markit/BME Germany Manufacturing PMI (Jul P)	59.2	59.6
09:30	Markit Germany Services PMI (Jul P)	54.3	54.0
09:30	Markit/BME Germany Composite PMI (Jul P)	56.3	56.4
24JUL-28JUL	Import Price Index MoM / YoY (Jun)	--/--	-1.0%/4.1%
France			
09:00	Markit France Manufacturing PMI (Jul P)	54.6	54.8
09:00	Markit France Services PMI (Jul P)	56.7	56.9
09:00	Markit France Composite PMI (Jul P)	56.4	56.6
Events			
	Meeting between OPEC and Non-OPEC members in St-Peterburg		
Q2 earnings	Philips (07:00), Haliburton (12:50), Alphabet (Aft-mkt),...		
11:30	Belgium to Sell 0.2% 2023, 0.8% 2027 and 1.6% 2047 Bonds		
18:00	BOE Brazier speaks in Liverpool		
18:00	ECB's Frank Smets Speaks in Munich on the ECB's policy since 2014 (IFO)		

10-year	<u>Close</u>	<u>-1d</u>		2-year	<u>td</u>	<u>-1d</u>	Stocks	<u>Close</u>	<u>-1d</u>
US	2,24	-0,02		US	1,34	-0,01	DOW	21580,07	-31,71
DE	0,51	-0,02		DE	-0,64	0,00	NASDAQ	6387,754	-2,25
BE	0,78	-0,02		BE	-0,47	0,00	NIKKEI	19975,67	-124,08
UK	1,18	-0,03		UK	0,27	-0,02	DAX	12240,06	-207,19
JP	0,07	0,00		JP	-0,12	0,00	DJ euro-50	3451,71	-47,78
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	-0,03	1,70	0,68	Eonia	-0,3610	0,0010			
5y	0,25	1,88	0,86	Euribor-1	-0,3740	0,0000	Libor-1	1,2322	0,0050
10y	0,90	2,21	1,23	Euribor-3	-0,3310	0,0010	Libor-3	1,3144	0,0019
				Euribor-6	-0,2720	0,0020	Libor-6	1,4531	-0,0029
Currencies	<u>Close</u>	<u>-1d</u>		Currencies	<u>Close</u>	<u>-1d</u>	Commodities	<u>Close</u>	<u>-1d</u>
EUR/USD	1,1663	0,0032		EUR/JPY	129,61	-0,55	CRB	176,66	-1,74
USD/JPY	111,13	-0,78		EUR/GBP	0,8974	0,0008	Gold	1261,00	8,90
GBP/USD	1,2997	0,0024		EUR/CHF	1,1030	-0,0034	Brent	48,06	-1,24
AUD/USD	0,7916	-0,0042		EUR/SEK	9,6126	0,0473			
USD/CAD	1,2539	-0,0050		EUR/NOK	9,3463	-0,0116			

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