

Monday, 11 May 2020

Rates: Supply-related steepening

This week's eco calendar is backloaded. Focus initially turns to the heavy mid-month US supply operation which could cause some additional steepening. Asian stock markets copy WS gains this morning with China and South Korea lagging on a fresh increase of virus cases. Rating agency Moody's kept the Italian rating unchanged at Baa3 (stable outlook).

Currencies: dollar gains slightly as US yields bottom

On Friday, US yields and the dollar gained modest ground even as the US economy lost 20.5 mln jobs. EUR/USD is holding north of the 1.08. Ongoing institutional uncertainty in the wake of the German court ruling probably makes a sustained rebound difficult. For now sterling, hardly profits from first steps in the UK to ease the lockdown measures.

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	↔

- **Wall Street** inched higher on Friday despite a horrible April payrolls report. The DJI (+1.91%) outperformed. **Asian stocks** rise in lockstep with Australia and Hong Kong taking the lead (up to 2%).
- **The US job numbers will get even worse**, White House advisor Kudlow said in the wake of the April job report. He thinks the contraction hasn't fully run its course and there will be positive numbers only in the second half of the year.
- The **UK will start to ease lockdown measures from Wednesday on**, allowing outdoor time for sports and trips to parks and beaches. Some (primary) schools and shops will reopen in June.
- **SNB President Jordan said the central bank has been engaging in the FX market "substantially"** and could still cut interest rather into deeper negative territory as the coronavirus pandemic exerts "enormous" upward pressure on the franc.
- **Rating agency Moody's left Italy's Baa3 rating** (one notch above junk) **and outlook** (stable) **unchanged** last Friday. DBRS Morningstar didn't alter Italy's investment grade (BBB) rating but downgraded its outlook to negative.
- **South Korea** reported 34 new cases on Sunday after days of no infections. The new cluster was linked to a popular nightlife district, prompting its mayor to **immediately shut bars and nightclubs and reinstate social distancing**.
- **Today's economic calendar** is extremely thin with key data backloaded. A new week of Brexit talks starts today. Several ECB and Fed speeches are due. The US taps the bond market.

Rates

Focus turns to US supply operation

	US yield	-1d
2	0.16	0.02
5	0.33	0.03
10	0.68	0.04
30	1.39	0.05

	DE yield	-1d
2	-0.78	-0.02
5	-0.76	-0.01
10	-0.54	0.01
30	-0.07	0.01

Core bonds initially extended Thursday's gains in the run-up to the April US payrolls report. The damage was huge (-20500k) but in line with forecasts after clues from weekly jobless claims and ADP employment. The unemployment rate jumped to 14.7% with White House advisor Hasset later warning that it will rise to around 20% next month. The surge in earnings was statistical in nature. **US Treasuries lost some ground after the release and slid further into the close as US equities gathered momentum (1.5%-2%).** It also helped that the **US Fed Funds Future curve slightly retraced from discounting negative policy rates.** That caused the US 2-yr yield to set an all-time low on Thursday. Fed governors in general oppose to negative policy rates which create downward pressure on profitability in the financial sector and thus limit credit expansion. **The late weakness in US Treasuries could finally also be influenced by this week's huge mid-month supply operation.** The US yield curve eventually bear steepened with yields rising by 2 bps (2-yr) to 5.4 bps (30-yr). The German yield curve steepened as well with changes varying between -1.3 bps (2-yr) and +1.4 bps (30-yr). 10-yr yield spread changes vs Germany narrowed by up to 3 bps with Italy (-8bps) outperforming. **Rating agency Moody's eventually decided to keep the Italian rating at the lowest possible investment grade tier (Baa3) with a stable outlook.**

Asian stock markets follow WS's example with China and South Korea lagging on a new increase in virus cases. EC President von der Leyen threatened to sue Germany for not abiding to EU law. The comments come after the German Constitutional court gave the ECB a 3 month ultimatum to fix its QE programme. It thinks that the ECJ had overstepped its powers by backing the ECB's asset purchases. **Core bonds remain near Friday's sell-off lows.**

Today's eco calendar only contains second-tier events. The US Treasury starts its supply operation with a \$42bn 3-yr Note auction. **The US yield curve faces some more steepening pressure ahead of 10-yr and 30-yr sales later this week.** The eco calendar is backloaded with US retail sales, Empire Manufacturing (May), industrial production and Michigan consumer confidence all on Friday. Chinese retail sales, investments and industrial production data will be published as well that day.

From a technical point of view, the German 10-yr yield is trying to find a fresh equilibrium. **For US yields, the Fed's unlimited QE announcement is the de facto start of curve control probably reducing volatility. A trading range between 0.5% and 0.8% opened up.**



German 10-yr yield tries to find fresh equilibrium



US 10-yr yield: unlimited QE by the Fed de facto start of curve control?

Currencies

USD gains a few ticks on (slightly) higher US yields

R2	1.125	-1d
R1	1.1109	
EUR/USD	1.0839	0.0005
S1	1.0770	
S2	1.0636	

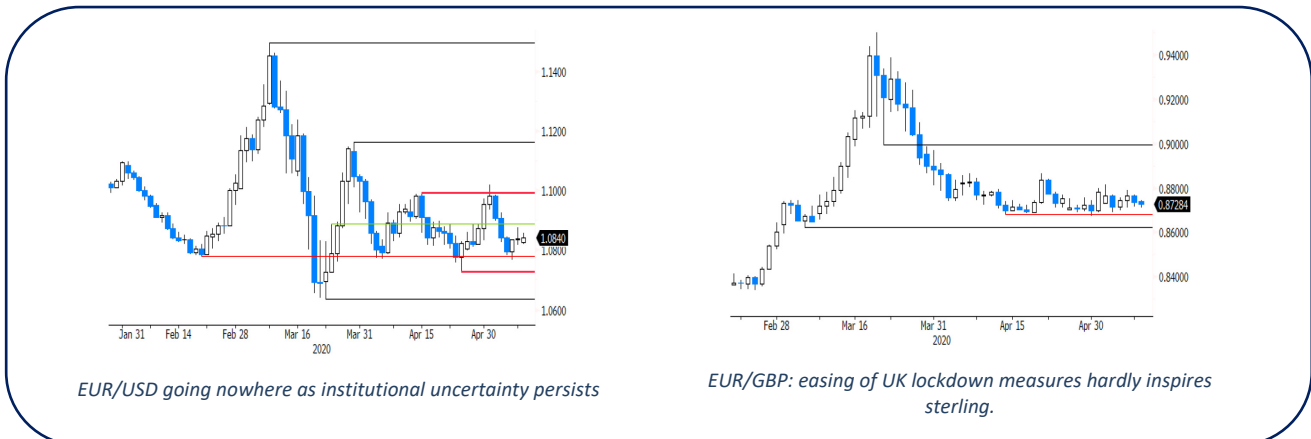
R2	0.9212	-1d
R1	0.9033	
EUR/GBP	0.8736	-0.0027
S1	0.8621	
S2	0.8569	

Global sentiment stayed positive on Friday, resulting in smooth price action in the major FX cross rates. The disconnect between (equity) markets and the data continued. Mounting evidence of an unprecedented steep economic decline as illustrated by a loss of 20.5 mln jobs in the US in April, hardly affected markets. On the contrary; US yields regained a few bp after the report, slightly supporting USD/JPY (close 106.65). Still, price moves in the major USD crosses were confined to well-known ranges. EUR/USD hovered in the 1.08 figure closing little changed at 1.0839. Moody's left the Italian Baa3 rating unchanged.

This morning, Asian equities join WS's rally on Friday. Mainland China indices underperform even as the PBOC indicated to keep a supportive monetary policy in place in its quarterly report. The yuan loses a few ticks (USD/CNY 7.0825). USD/JPY is trading higher after a tentative bottoming last week, testing the 107 area. The Aussie is holding on the recent gains, but the 0.6550/70 area proves to be a tough resistance.

Today's calendar thin. Later this week, US bond supply might be a topic for the bond markets with some potential spill-over effects to FX. **Will the dollar profit (albeit modestly) from a (limited) rise in US yields?** In Europe, Moody's review of the Italian credit rate is out of the way, but the issue of German court ruling on the ECB QE stays in the headlines. During the weekend, the ECB and the European Commission pushed back on the ruling and indicated that rulings on ECB policy should be done at a European level. Even so, the debate illustrates to complexity of the EU institutional framework which is no help in a time of crisis. Last week, EUR/USD dropped below 1.08 after the German court ruling, but the 1.0727 correction low was left intact. Institutional issues probably will continue cap any sustained euro rebound. We expect EUR/USD to hold in the lower part of the 1.0727/1.1018 trading range for now.

EUR/GBP hovered sideways in the mid 0.87 area on Friday. During the weekend, UK PM Johnson announced 'first careful steps' to easing the lockdown rules. Details will be given later today. At least for now, sterling isn't impressed. The UK isn't a frontrunner on the path to a restart of the economy. Brexit also lingers with EU-UK talks still in a stalemate. We expect the EUR/GBP 0.8680/0.87 support to hold.



Calendar

Monday, 11 May		Consensus	Previous
US			
11MAY-15MAY	Mortgage Delinquencies (1Q)	--	3.77%
11MAY-15MAY	MBA Mortgage Foreclosures (1Q)	--	0.78%
Italy			
10:00	Industrial Production MoM/WDA YoY (Mar)	-20.00%/-18.3%	-1.20%/-2.40%
China			
10MAY-15MAY	Money Supply M2 YoY (Apr)	10.30%	10.10%
10MAY-15MAY	New Yuan Loans CNY (Apr)	1300.0b	2850.0b
Norway			
08:00	CPI MoM/YoY (Apr)	0.10%/-0.40%	0.00%/0.70%
08:00	CPI Underlying MoM/YoY (Apr)	-0.40%/2.10%	0.30%/2.10%
08:00	PPI including Oil MoM/YoY (Apr)	--/--	-7.5%/-12.6%
Sweden			
06:00	PES Unemployment Rate (Apr)	4.80%	4.20%
Switzerland			
10:00	Total Sight Deposits CHF (May 8)	--	663.8b
Events			
11-15MAY	Brexit talks to continue all week		
12:45	ECB Executive Board member Mersch Speaks		
14:00	BOE's Breeden Speaks on Webinar		
18:00	Fed's Bostic Discusses the Response to Covid-19		
19:00	US to Sell USD42 Bln 3-Year Notes		

10-year	Close	-1d	2-year	Close	-1d	Stocks	Close	-1d	
US	0.68	0.04	US	0.16	0.02	DOW	24331.32	455.43	
DE	-0.54	0.01	DE	-0.78	-0.02	NASDAQ	9121.32	141.66	
BE	0.04	-0.01	BE	-0.53	-0.01	NIKKEI	20390.66	211.57	
UK	0.24	0.00	UK	-0.01	0.00	DAX	10904.48	145.21	
JP	0.01	0.01	JP	-0.17	-0.02	DJ euro-50	2908.11	27.51	
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	-0.33	0.26	0.35	Eonia	-0.4560	0.0000	Libor-1	0.1980	0.0000
5y	-0.30	0.35	0.39	Euribor-1	-0.4510	-0.0060	Libor-3	0.4346	0.0000
10y	-0.12	0.64	0.47	Euribor-3	-0.2460	0.0120	Libor-6	0.6880	0.0000
				Euribor-6	-0.1450	-0.0310			
Currencies	Close	-1d	Currencies	Close	-1d	Commodities	Close	-1d	
EUR/USD	1.0839	0.0005	EUR/JPY	115.5	0.40	CRB	124.74	2.16	
USD/JPY	106.65	0.37	EUR/GBP	0.8736	-0.0027	Gold	1713.90	-11.90	
GBP/USD	1.241	0.0048	EUR/CHF	1.0523	-0.0019	Brent	30.97	1.51	
AUD/USD	0.6532	0.0037	EUR/SEK	10.5877	-0.0406				
USD/CAD	1.3927	-0.0046	EUR/NOK	11.0747	-0.0255				

If you no longer wish to receive this mail, please contact us: "kbcmarketresearch@kbc.be" to unsubscribe

Contacts

Brussels Research (KBC)		Global Sales Force	
Mathias Van der Jeugt	+32 2 417 51 94	Corporate Desk(Brussels)	+32 2 417 45 82
Peter Wuyts	+32 2 417 32 35	Institutional Desk(Brussels)	+32 2 417 46 25
Mathias Janssens	+32 2 417 51 95	CBC Desk (Brussels)	+32 2 547 19 19
Dieter Lapeire	+32 2 417 25 47	France	+32 2 417 32 65
Dublin Research		London	+44 207 256 4848
Austin Hughes	+353 1 664 6889	Singapore	+65 533 34 10
Shawn Britton	+353 1 664 6892		
Prague Research (CSOB)		Prague	+420 2 6135 3535
Jan Cermak	+420 2 6135 3578		
Jan Bures	+420 2 6135 3574		
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		

ALL OUR REPORTS ARE AVAILABLE VIA OUR KBC RESEARCH APP (iPhone, iPad, Android)

This non-exhaustive information is based on short-term forecasts for expected developments on the financial markets. KBC Bank cannot guarantee that these forecasts will materialize and cannot be held liable in any way for direct or consequential loss arising from any use of this document or its content. The document is not intended as personalized investment advice and does not constitute a recommendation to buy, sell or hold investments described herein. Although information has been obtained from and is based upon sources KBC believes to be reliable, KBC does not guarantee the accuracy of this information, which may be incomplete or condensed. All opinions and estimates constitute a KBC judgment as of the data of the report and are subject to change without notice.

