

**Wednesday, 20 March 2019**

### Rates: Fed to deliver soft message

Fed chair Powell is expected to announce the end of the balance sheet run-off by the end of the year. Communication on the future composition of the BS is a wildcard. We expect the total amount of rate hikes in the dot plot to fall from 3 to 1. Most should be discounted on rate markets, but this soft message creates space for more bonds gains over the MT.

### Currencies: Dollar has discounted by and large a soft Fed

Today's currency price action will be driven solely by the Fed. Recent dollar weakness suggests that a dovish Fed is probably discounted. We anticipate sideways trading ahead of the Fed with some risks of EUR/USD profit taking afterwards. UK PM May is running out of time to find consensus on the length of the brexit deadline extension.

### Calendar

## Headlines

- **US equities** started strong but eventually closed unchanged following reports that some **US officials are concerned China is pushing back against American demands**. Asian bourses are mixed with China (-0.5%) underperforming.
- Despite concerns of Chinese stalling in trade talks, **US Trade representative Lighthizer and Treasury Secretary Mnuchin are to travel to China next week** for another round of high-level discussions with Chinese Vice Premier Liu He.
- **Chinese President Xi Jinping will sign agreement with Italy and France** over the next days to enhance synergies and trade relationships with the EU on its Belt and Road initiative.
- **Czech National Bank's vice governor Mora** told Bloomberg yesterday that he expects **one more rate hike this year, but it probably won't happen at next week's policy meeting** (Mar 28).
- **RBA Bullock** worries that the large influx of supply on the Sydney apartment market might **exacerbate declines in housing prices and worsen households' financial positions**. She called on **banks to loosen lending conditions**.
- **Canada's Liberal government presented a pre-election budget including over \$10bn in spending** to counter the worsening economic backdrop and prop up voter support for the scandal-hit PM Trudeau and his government.
- **Today's economic calendar** centres on the FOMC's verdict. The US central bank is expected to join the ECB's dovish swing. UK inflation data and a German Bobl auction are the other items on the agenda.

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	➔

# Rates

## Fed to deliver dovish signal

	US yield	-1d
2	2,47	0,02
5	2,42	0,01
10	2,61	0,01
30	3,02	0,00

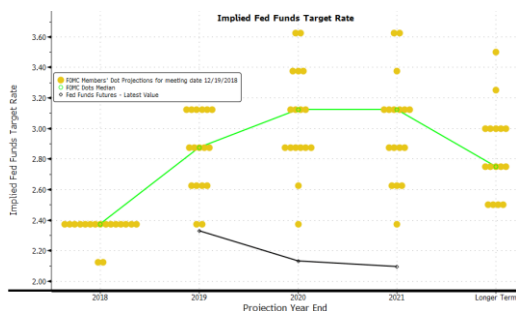
	DE yield	-1d
2	-0,53	0,00
5	-0,31	0,01
10	0,10	0,01
30	0,76	0,01

**Global core bonds ceded some ground yesterday.** The main move occurred around European noon after China Central Television reported the country would firmly implement major reforms and deepen supply-side structural reform. The fact that such headline manages to impact trading is more of an indication of low volume action ahead of tonight's Fed meeting than anything else. Economic data printed mixed. The German yield curve bear steepened in a daily perspective with yields adding 0.2 bps (2-yr) to 1.4 bps (30-yr). The US yield curve bear flattened with yields ending 1.7 bps (2-yr) to 0.4 bps (30-yr) higher. 10-yr yield spread changes vs Germany ended close to unchanged with Portugal and Italy (+3 bps) underperforming.

Asian stock markets are mixed this morning after WS's late swoon with China underperforming (-0.5%). Media reports on US-Sino trade talks are mixed. Some US officials are concerned that China is pushing back against American demands, but key officials (Lighthizer, Mnuchin) will travel to China next week to continue high levels talks with vice premier Liu He. Core bonds tread water going into the European opening. **The sole focus of today is tonight's FOMC meeting.**

Fed chair Powell already suggested in front of US Congress **to halt the balance sheet run-off by the end of the year.** That's much sooner than the Fed originally had in mind and market participants had expected until the turn of last year. Communication on the composition of the Fed's portfolio is a wildcard. The Fed might opt to continue to let its MBS-portfolio run off, but replace them by US Treasuries. Another factor the Fed might tweak is the duration of its Treasury portfolio. Shortening it would be considered hawkish and vice versa. Apart from this, we expect **the Fed's plotted rate hikes to drop from 3 currently (2 in 2019 and 1 in 2020) to 1 (in 2019)** taking into account weaker growth and inflation forecasts. **The Fed's feared inflation overshoot didn't happen last year, putting governors at ease to take a more wait-and-see approach as the economy shows first signs of sputtering.** Markets remain even softer positioned with unchanged rates this year and a rate cut in 2020.

**US rate markets are positioned for a soft message.** Ending the BS run-off and lower dots are probably discounted. The accents of Powell's press conference or possible details on the composition of the Treasury portfolio are wildcards. **Current positioning might dampen the immediate market impact, but we expect the Fed to create fertile breathing ground for additional bond gains over the medium term, flattening the curve.** The US 10-yr yield can drift lower in the 2.49%-2.8% broad sideways channel.



December dot plot including median Fed projections (green) and current market expectations (black)



US 10-yr yield losing intermediate support (2.61%) ahead of dovish anticipated Fed meeting.

# Currencies

R2	1,1815	-1d
R1	1,1621	
<b>EUR/USD</b>	<b>1,1352</b>	<b>0,0015</b>
S1	1,1187	
S2	1,1119	

R2	0,93067	-1d
R1	0,91	
<b>EUR/GBP</b>	<b>0,8556</b>	<b>0,0002</b>
S1	0,8500	
S2	0,8314	

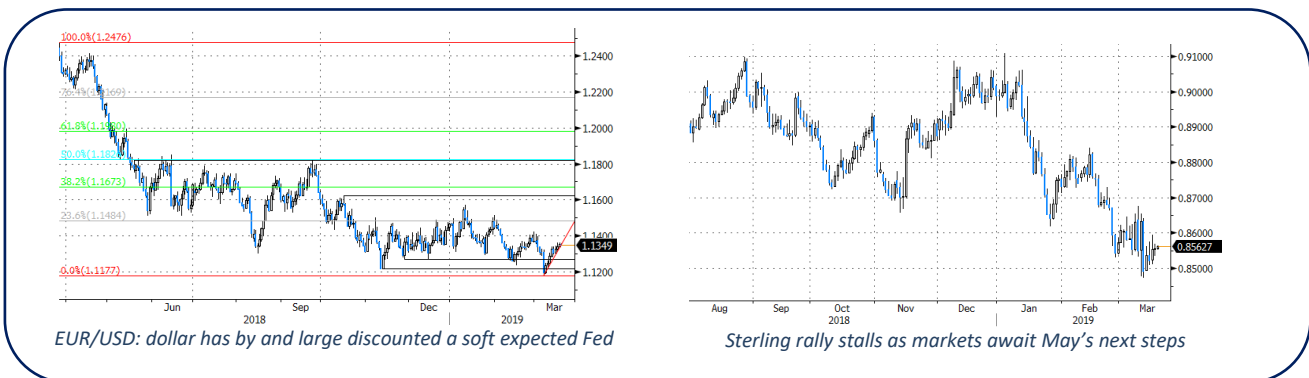
## Soft Fed discounted after recent USD weakness?

EUR/USD was well bid yesterday. The couple eked out gains as investors avoided excessive USD long exposure ahead of a cautious expected Fed meeting (tonight). At the same time, euro buying found support in a positive surprise of Germany's ZEW confidence (expectations component) and an overall constructive risk climate. **However, the latter was shaken by conflicting reports on trade later on.** Some US officials are concerned China is resisting US demands. China also stepped back from earlier trade promises it made, saying they do so because there haven't been any assurances from the US that tariffs would be lifted. The EUR/USD uptrend stalled. The pair closed at 1.1352 (from 1.1337). USD/JPY closed a choppy trading session stable at 111.39.

**Asian markets are trading mixed this morning.** Chinese equities underperform following the trade reports. The Chinese yuan opened slightly lower but has recovered most losses soon after. The Aussie (AUD/USD 0.708) similarly staged a turnaround after slipping as the RBA said that risks to financial stability have become "elevated". Minutes of the BoJ showed disagreement among its members over monetary easing. One member said the BoJ should avoid market expectations of no change in policy to be fixed to "an excessive degree". USD/JPY is trading at 111.55, up from 111.40.

Today's economic calendar is extremely thin. **The Fed meeting tonight will have market's undivided attention. We expect the central bank to reduce its anticipated 2019 rate hikes from 2 to 1 with no hikes penciled in for 2020 (vs. 1 in December).** Powell will probably also announce the end of the balance sheet run-off by the end of the year. **We believe the dollar at the current levels has discounted a soft Fed.** That might result in sideways EUR/USD trading ahead of the Fed with some risks of profit-taking afterwards. More so because any further sustained rebound in EUR/USD probably needs better EMU data first.

Sterling entered calmer waters yesterday after the UK's Speaker of the House thwarted May's Brexit strategy. Markets are now awaiting the PM's next steps which would consist of asking the EU to extend the deadline. Reports suggest she seeks at minimum a 3m extension. It is unclear however how the EU will respond at the summit tomorrow. We don't expect the Brexit process to be clarified soon and stay cautious on sterling. **The 0.8490/0.85 area might become a ST floor for EUR/GBP.**



# Calendar

Wednesday, 20 March		Consensus	Previous
<b>US</b>			
12:00	MBA Mortgage Applications	--	2.3%
19:00	<b>FOMC Rate Decision</b>	<b>2.25%/2.50%</b>	<b>2.25%/2.50%</b>
<b>Japan</b>			
07:00	Machine Tool Orders YoY (Feb F)	--	-29.3%
08:00	Convenience Store Sales YoY (Feb)	--	0.8%
<b>UK</b>			
10:30	CPIH YoY (Feb)	1.8%	1.8%
10:30	<b>CPI MoM/YoY (Feb)</b>	<b>0.4%/1.8%</b>	<b>-0.8%/1.8%</b>
10:30	<b>CPI Core YoY (Feb)</b>	<b>1.9%</b>	<b>1.9%</b>
10:30	RPI MoM/YoY (Feb)	0.7%/2.5%	-0.9%/2.5%
10:30	RPI Ex Mort Int.Payments (YoY) (Feb)	2.5%	2.5%
10:30	PPI Input NSA MoM/YoY (Feb)	0.6%/4.1%	-0.1%/2.9%
10:30	PPI Output NSA MoM/YoY (Feb)	0.1%/2.2%	0.0%/2.1%
10:30	PPI Output Core NSA MoM/YoY (Feb)	0.2%/2.3%	0.4%/2.4%
10:30	House Price Index YoY (Jan)	2.4%	2.5%
12:00	CBI Trends Total Orders (Mar)	5	6
12:00	CBI Trends Selling Prices (Mar)	--	22
<b>Germany</b>			
08:00	PPI MoM/YoY (Feb)	0.2%/2.9%	0.4%/2.6%
<b>Belgium</b>			
15:00	Consumer Confidence Index (Mar)	--	-7
<b>Events</b>			
11:30	Germany to Sell 4 Billion Euros of 0% 2024 Bonds		

10-year	Close	-1d	2-year	Close	-1d	Stocks	Close	-1d	
US	2,61	0,01	US	2,47	0,02	DOW	25887,38	-26,72	
DE	0,10	0,01	DE	-0,53	0,00	NASDAQ	7723,946	9,47	
BE	0,54	0,01	BE	-0,44	0,00	NIKKEI	21608,92	42,07	
UK	1,19	-0,01	UK	0,75	-0,01	DAX	11788,41	131,35	
JP	-0,04	0,00	JP	-0,16	0,00	DJ euro-50	3409	21,06	
IRS	EUR	USD	GBP	EUR	-1d	-2d	USD	-1d	-2d
3y	-0,09	2,51	1,14	Eonia	-0,3680	0,0010	Libor-1	2,4878	0,0000
5y	0,10	2,48	1,23	Euribor-1	-0,3670	0,0000	Libor-3	2,6326	0,0000
10y	0,59	2,62	1,39	Euribor-3	-0,3100	0,0000	Libor-6	2,6706	0,0000
				Euribor-6	-0,2320	-0,0010			
Currencies	Close	-1d	Currencies	Close	-1d	Commodities	Close	-1d	
EUR/USD	1,1352	0,0015	EUR/JPY	126,47	0,13	CRB	185,24	0,38	
USD/JPY	111,39	-0,04	EUR/GBP	0,8556	0,0002	Gold	1306,50	5,00	
GBP/USD	1,3268	0,0013	EUR/CHF	1,1343	-0,0011	Brent	67,61	0,07	
AUD/USD	0,7088	-0,0016	EUR/SEK	10,451	-0,0126				
USD/CAD	1,332	-0,0014	EUR/NOK	9,6804	-0,0091				

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