



## Sunrise

Wednesday, 31 August 2016

### Rates: Fed Rosengren and ADP decisive for trading

Today's eco calendar is jam-packed, but markets will probably be most sensible to comments from voting FOMC member Rosengren and the US ADP employment report. The tone of the comments and strength of ADP will determine whether US Treasuries will further reposition towards a September rate hike.

### Currencies: More dollar strength

Following a pause on Monday, the US dollar made some further headway yesterday, especially during the US session. Stronger US and weaker EMU data today might play again in the advantage of the dollar, but the rate markets lag in discounting a greater chance of rate hike. That may hinder the dollar's advance.

### Calendar

## Headlines

S&P	→
Eurostoxx50	↗
Nikkei	↗
Oil	↘
CRB	→
Gold	↘
2 yr US	→
10 yr US	→
2 yr EMU	→
10 yr EMU	→
EUR/USD	→
USD/JPY	↗
EUR/GBP	↘

- **US Equities reversed yesterday part of Monday's gains**, with the S&P falling 0.2% led by utilities. This morning, **Asian shares** trade mixed. **Japanese stocks outperform**, gaining more than 1%, supported by a weaker yen.
- Bank of Japan board member Funo said **the central bank will make full use of its existing policy tools to encourage household and companies to start spending** again and shed their deflationary mindset. Funo sounded upbeat on the economic prospects saying the tightening job market will encourage firms to raise wages.
- **British consumer morale recovered in August some of its post-Brexit slump**, but the level remains however at its second-lowest since 2014, the GfK index showed. After a few weeks of holidays, **UK Prime Minister Theresa May will meet members of her government today** to discuss how Britain will leave the EU.
- **Growth in Japan's industrial production stalled in July**, undershooting the market consensus which was looking for a 0.8% M/M increase. Sluggish factory output is another setback for policymakers, but the ministry maintained its assessment that production is seesawing, but a pickup is seen in some parts.
- **Crude oil prices dropped almost 2% yesterday** with the Brent falling to its lowest level in two weeks (\$48.30/barrel) on renewed uncertainty over a potential output freeze and higher US API inventory data. **Gold** prices dropped to its lowest level in two months, around \$1318/barrel, as the stronger US dollar weighs.
- Today, the **eco calendar** contains the first estimate of **euro zone HICP inflation** for August, the **euro zone unemployment rate** and German unemployment figures, the US **ADP employment report**, Chicago PMI and US pending home sales. Central bankers are active too with **Fed's Rosengren, Evans and Kashkari** and ECB's Praet and Villeroy scheduled to speak. **Spanish caretaker PM Rajoy faces a confidence vote in parliament**.

# Rates

## Price action limited ahead of big data

Core bonds trade ended close to unchanged as disappointing EMU eco data (EC confidence data, German CPI), comments by Fed Fischer and strong US consumer confidence only marginally impacted trading. Initial losses on the back of positive risk sentiment were undone after Fed vice-chair Fischer didn't repeat Friday's reference to a September rate hike in a BB TV interview.

Crashing oil prices (high inventory data) probably limited the potential impact from strong US consumer confidence. At the end of the day, changes on the German yield curve ranged between +0.5 bps (2-yr) and -2.4 bps (30-yr). The US yield curve moved up to 1.5 bps higher (30-yr) with the front end of the curve outperforming (2-yr: -0.8 bps). On intra-EMU bond markets, 10-yr yield spread changes versus Germany were limited between 0 and +2 bps.

### Uneventful core bond trading

	US yield	-1d
2	0,8014	-0,0196
5	1,1896	-0,0048
10	1,5766	-0,0085
30	2,2385	0,0058

	DE yield	-1d
2	-0,6160	0,0150
5	-0,5150	-0,0060
10	-0,0850	-0,0330
30	0,4344	-0,0352

## US ADP employment report: foretaste of payrolls

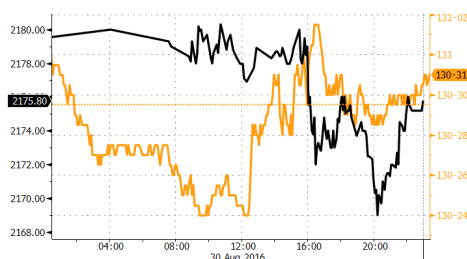
The **eco calendar heats up today**, both in the US and euro zone with the first estimate of EMU HICP inflation for August, the euro zone unemployment rate, German unemployment rate and claims, US ADP employment report, the US Chicago PMI and pending home sales. Central bankers are active too with Fed's Rosengren, Evans and Kashkari and ECB's Coeuré & Villeroy scheduled to speak. Germany (Schatz), Norway (Bonds), Finland (syndication?) and Portugal (Bonds) will tap the market.

In August, **euro zone HICP inflation** is expected to extend its upward trend, with the consensus looking for an increase from 0.2% Y/Y to 0.3% Y/Y. If confirmed, this would be the highest rate of inflation since January. Core inflation, on the contrary, is expected to stay stable for a second straight month, at 0.9% Y/Y. We believe that the risks for the headline reading are on the downside due to the drop in the oil price in July. The **EMU unemployment rate** is expected to renew its downward trend, falling from 10.1% to 10.0% in July, following a stabilisation at 10.1% in June. We have no reasons to distance ourselves from the consensus. In Germany, the number of people unemployed is expected to have dropped slightly in August. In the US, the **ADP report** might already give an indication ahead of Friday's non-farm payrolls. In August, ADP employment is expected to have increased by 175 000, down slightly from the 179 000 in July. We believe that hiring will continue its recent trend and have therefore **no reasons to distance ourselves from the consensus**. ADP hiring has been much more stable recently than the official BLS reading, a trend we expect to continue in August. Finally, the **Chicago PMI** is forecast to have dropped slightly in August, from 55.8 to 54.0. In August, regional indicators were overall poor so we see risks for a weaker Chicago PMI too.

### Downside surprise from EMU CPI?

### US ADP Employment near expectations?

### Downside risks Chicago PMI



US Note future (orange) and S&P future (black) intraday (two days): modest initial losses reversed after Fischer comments



Brent crude: oil price suffers setback after strong month

## German, Portuguese and Finnish (?) supply

**The German Finanzagentur holds a €4B 2-yr Schatz auction (0% Sep2018).** Total bids averaged €6.56B at the previous 4 Schatz auctions despite ever lower, record, negative yields. Therefore, we think that this auction will pass without difficulties as well. **The Portuguese treasury puts the 3.85% Apr2021 and 2.875% Jul2026 OT's on offer from a combined €0.75-1B.** Both bonds cheapened in ASW spread terms going into the auction and trade normal on the Portuguese curve. The looming credit rating decision by DBRS in October (last agency above junk, important for ECB QE, but DBRS sounded downbeat on Portugal recently) could slightly hamper demand, but we expect a plain vanilla auction overall. **The Republic of Finland is expected to launch a new 7-yr bond (€3B Sep2023) via syndication, probably today.**

R2	170	-1d
R1	168,86	
<b>BUND</b>	<b>167,64</b>	0,0500
S1	165,63	
S2	163,61	

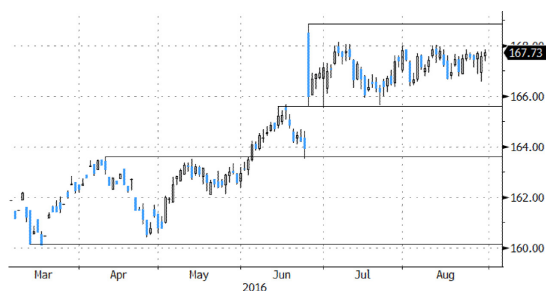
## Fed Rosengren and ADP report key for trading

**Overnight, most** Asian equity markets trade mixed with Japan further outperforming on recent yen weakness. The US Note future trades a touch lower, but we expect neutral risk sentiment at the start of the trading session.

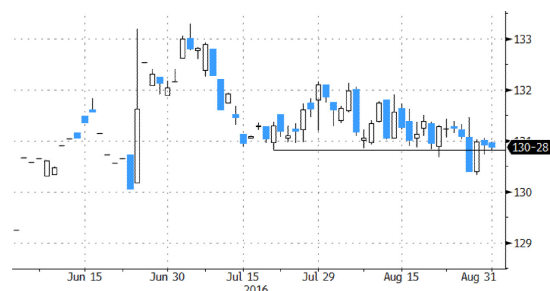
**There's a lot on the eco calendar today, both in EMU and US (see above), but the US side of the story will probably be the most relevant. A first important event is a speech by Boston Fed Rosengren, currently a voter.** The Fed governor is rather neutral so any comments in favour or against a near term rate hike could trigger repositioning. During the US trading session, we look out for the ADP employment report and (to a lesser extent) Chicago PMI. We expect the ADP to print near consensus, but a decent/strong reading could already be welcomed by markets as a herald of decent payrolls on Friday.

**Our preferred scenario for the Fed is a September rate hike. If confirmed by incoming eco data and/or Fed speak, this should weigh on US Treasuries and trigger a further (bear) flattening of the US yield curve.**

**Despite Monday's technical rebound, we expect that the US Note future could break below strong support (130-26) in case of good payrolls on Friday. This would deteriorate the technical picture and pave the way for more losses.** The Bund will take a similar direction as the Note future, but the sideways range between 168.54 and 165.68 looks safe.



German Bund: sideways range between 165.63 and 168.86 remains intact



US Note future (Dec contract!!): Strong payrolls should be able to push contract below 130-26 support

# Currencies

## Dollar dominates US session

*Dollar resumed its ascend after a one day pause, but gains still technically irrelevant*

R2	1,1428	-1d
R1	1,1366	
<b>EUR/USD</b>	<b>1,11485</b>	<b>-0,0018</b>
S1	1,1046	
S2	1,0992	

*Dollar little changed overnight. Neutral risk sentiment at start European trading*

Yesterday, extreme calmness reigned on the FX markets during the Asian and especially European session. The dollar gained a bit, especially against the yen on the back of a positive risk sentiment. The balance shifted further in favour of the dollar in mid-US session as the oil price fell sharply on an API report reporting higher crude inventories and on the back of a very strong US consumer confidence report. Surprisingly, the dollar gains weren't mirrored by a wider rate differential. Weaker EMU economic data played no role and neither did a speech of Fed's Fischer. **In a daily perspective, USD/JPY closed at 102.96, a 96 ticks gain and a new post-Yellen high. EUR/USD closed finally at 1.1143 from 1.1189 previously. We suspect that end-of-month positioning may have influenced moves.**

**Overnight,** Asian equities trade narrowly mixed, with Japan outperforming on the back of a weaker yen. Oil stabilizes after yesterday's hit and the same applies for gold. The overall dollar (DXY) is unchanged, while the T-Note future is a tad below yesterday closing, but up from the lows. Japanese production was weak in July, but didn't affect equities much. USD/JPY traded a bit erratic. It set a new ST high at 103.23 but trades currently at 103.05, 10 ticks above the close. EUR/USD is slightly higher but off intra-day highs and currently trading at 1.1149, virtually unchanged.



EUR/USD: Following a pause on Monday, the dollar gained more ground, but technically still no major change



USD/JPY: Dollar climbs higher and tries to penetrate the 103 big figure on hopes monetary policies will diverge further

## Busy calendar today: ADP employment key report

*Downside risks EMU inflation and Chicago PMI*

*ADP employment robust in August?*

*Fed's Rosengren, Evans and Kashkari and ECB's Coeuré, Praet & Villeroy speak*

*Spanish parliament holds confidence vote*

In August, **euro zone HICP inflation** is expected to extend its upward trend from 0.2% Y/Y to 0.3% Y/Y. This would be the highest rate of inflation since January. Core inflation is expected to stay stable for a second straight month, at 0.9% Y/Y. We believe that the **risks for the headline reading are on the downside** due to the drop in the oil price in July and German's surprisingly low number. The **EMU unemployment rate** is expected to fall from 10.1% to 10.0% in July. We have no reasons to distance ourselves from the consensus. In the US, the **ADP report** might already give an indication ahead of Friday's non-farm payrolls. In August, ADP employment is expected to have increased by 175 000, down slightly from the 179 000 in July. We believe that hiring will continue its recent trend and have therefore **no reasons to distance ourselves from the consensus.** ADP

hiring has been much more stable recently than the official BLS reading, a trend we expect to continue in August. Finally, the **Chicago PMI** is forecast to have dropped slightly in August, from 55.8 to 54.0. In August, regional indicators were overall poor so we see **risks for a weaker Chicago PMI** too. **If the US ADP employment report is not weaker than expected it should give the dollar upside momentum, as it would suggest a strong enough payrolls report on Friday to bolster hopes for a September FOMC rate increase.**

Regarding trading, we keep a positive dollar bias on the back of a reasonable strong ADP report, but are a bit nervous as the US rate markets don't swing further towards a rate hike in September. A weaker EMU inflation report together with rather soft surveys might affect the ECB's position. In this regard the downside risks for inflation may weigh on the euro. In a longer term perspective, EUR/USD should fall below support at 1.1046 to make the technical picture dollar positive.

### Mixed performance of sterling

R2	0,8815	-1d
R1	0,8725	
<b>EUR/GBP</b>	<b>0,851</b>	-0,0029
S1	0,8344	
S2	0,8251	

Yesterday, sterling gained minor ground versus the euro but lost slightly against the dollar in an uneventful session. EUR/USD closed at 0.8518, down from 0.8537 on Monday, while cable (GBP/USD) closed at 1.3080 from 1.3106. Initially, sterling was in the defensive as cable moved for a test of the post-Yellen lows 1.3060 at the start of equity trading in Europe. The absence of follow through selling convinced cable shorts to close their positions. **The reaction to the weak lending data was limited though and the rebound of cable simply continued till opening levels were reached.** Later on, the dollar took the initiative and rose across the board (see higher), pushing cable again lower. Stronger US consumer confidence, lower oil prices and weaker gold played a role. The dollar rose more against the euro than against sterling, despite a sharp fall in UK yields. EUR/GBP closed lower, but results were technically insignificant.

**This morning, UK second tier data have been released. Consumer confidence** that got a serious blow in July from the Brexit (from -1 to -12), but recovered in August to -7, slightly better than expected. On the contrary, the **Lloyds business barometer** dropped in August to 16 from 29 in July. It erased part of the July rebound after an awful June reading. We believe business sentiment won't recover in a structural way anytime soon. EUR/GBP and cable are still at yesterday's closing levels, suggesting the data had no impact. Later today, the UK eco calendar is empty, but PM May will meet her government to discuss Brexit. The EMU and US calendars are well-filled and reasonably important. **Therefore, we expect the fade of sterling to depend on what happens with those major currencies. EUR/GBP is currently taking a pause and has difficulties to make a corrective break below the 0.85 big figure.** We don't expect changes to this picture today. The dollar is a tad weaker, pushing cable in the overnight session to 1.31. EUR/GBP is little changed.



EUR/GBP: stable



GBP/USD: still in triangle pattern with key support at 1.2866 1.2798

# Calendar

Wednesday, 31 August		Consensus	Previous
<b>US</b>			
13:00	MBA Mortgage Applications	--	-2.1%
14:15	<b>ADP Employment Change (Aug)</b>	<b>175k</b>	<b>179k</b>
15:45	<b>Chicago Purchasing Manager (Aug)</b>	<b>54.0</b>	<b>55.8</b>
16:00	Pending Home Sales MoM YoY (Jul)	0.7% / 2.2%	0.2% / 0.3%
<b>Canada</b>			
14:30	GDP MoM YoY (Jun)	0.5% / 1.0%	-0.6% / 1.0%
14:30	Quarterly GDP Annualized (2Q)	-1.5%	2.4%
<b>Japan</b>			
01:50	Industrial Production MoM YoY (Jul P)	A0.0%/-3.8%	2.3% / -1.5%
01:50	Loans & Discounts Corp YoY (Jul)	A 2.25%	2.06%
06:00	Vehicle Production YoY (Jul)	A -4.1%	-1.0%
07:00	Annualized Housing Starts (Jul)	A 1.005m	1.004m
07:00	Construction Orders YoY (Jul)	A -10.9%	-2.4%
07:00	Small Business Confidence (Aug)	A 46.3	47.8
<b>UK</b>			
01:01	Lloyds Business Barometer (Aug)	A 16	29
01:05	GfK Consumer Confidence (Aug)	A -7	-12
08:00	Nationwide House Prices MoM YoY (Aug)	A 0.6%/5.6%	0.5% / 5.2%
<b>EMU</b>			
11:00	<b>Unemployment Rate (Jul)</b>	<b>10.0%</b>	<b>10.1%</b>
11:00	<b>CPI Estimate YoY (Aug)</b>	<b>0.3%</b>	<b>0.2%</b>
11:00	<b>CPI Core YoY (Aug A)</b>	<b>0.9%</b>	<b>0.9%</b>
<b>Germany</b>			
08:00	<b>Retail Sales MoM YoY (Jul)</b>	<b>A1.7%/-1.5%</b>	<b>-0.1% / 2.7%</b>
09:55	<b>Unemployment Change (000's) (Aug)</b>	<b>-4k</b>	<b>-7k</b>
09:55	<b>Unemployment Claims Rate SA (Aug)</b>	<b>6.1%</b>	<b>6.1%</b>
<b>France</b>			
08:45	CPI EU Harmonized MoM YoY (Aug P)	0.4% / 0.4%	-0.4% / 0.4%
08:45	Consumer Spending MoM YoY (Jul)	0.3% / 1.1%	-0.8% / 0.6%
<b>Italy</b>			
11:00	CPI EU Harmonized MoM YoY (Aug P)	-0.1%/-0.1%	-1.8%/-0.2%
12:00	Hourly Wages MoM YoY (Jul)	--	0.2% / 0.7%
<b>Belgium</b>			
15:00	GDP SA QoQ YoY (2Q F)	--	0.5% / 1.4%
<b>Norway</b>			
10:00	GDP QoQ (2Q)	0.1%	1.0%
10:00	GDP Mainland QoQ (2Q)	0.3%	0.3%
10:00	Credit Indicator Growth YoY (Jul)	5.0%	4.9%
<b>Spain</b>			
09:00	Total Mortgage Lending YoY (Jun)	--	23.0%
09:00	House Mortgage Approvals YoY (Jun)	--	34.1%
10:00	Current Account Balance (Jun)	--	2.8b
<b>Events</b>			
08:00	<b>ECB's Villeroy Speaks at Frankfurt Event</b>		
09:15	<b>Fed's Rosengren, Evans to Address Financial Conference in Beijing</b>		
09:15	ECB's Praet Speaks at Panel in Beijing		
14:00	<b>Fed's Kashkari Speaks on Fed Structure in St. Paul</b>		
14:45	ECB's Villeroy speaks at conference in Frankfurt		
15:50	Bank of England Bond-Buying Operation Results		
<b>Finland</b>	<b>Expected to Launch New 7Yr Bond Via Syndication (€3.0B Sep2023)</b>		
<b>Norway</b>	<b>Bond Auction (NOK2.0B 1.5% 2026)</b>		
<b>Germany</b>	<b>Schatz Auction (€4B 0% Sep2018)</b>		
<b>Portugal</b>	<b>Bond Auction(€0.75-1B 3.85% Apr2021 &amp; 2.875% Jul2026)</b>		

# Contacts

10-year	td	-1d	2-year	td	-1d	STOCKS	-1d
US	1,58	-0,01	US	0,80	-0,02	DOW	18454 18454,30
DE	-0,09	-0,03	DE	-0,62	0,01	NASDAQ for Exch - NQI	#VALUE!
BE	0,15	0,00	BE	-0,59	0,01	NIKKEI	16887 16887,40
UK	0,64	0,08	UK	0,14	0,01	DAX	10657,64 10657,64
JP	-0,06	0,01	JP	-0,20	0,01	DJ euro-50	3031 3030,75

IRS	EUR	USD (3M)	GBP	EUR	-1d	-2d	USD	td	-1d
3y	-0,192	1,091	0,442	Euribor-1	-0,37	0,00	Eonia EUR	-0,341	0,004
5y	-0,129	1,195	0,488	Euribor-3	-0,30	0,00	Libor-1 USD	0,28	0,28
10y	0,269	1,421	0,693	Euribor-6	-0,19	0,00	Libor-3 USD	0,39	0,39
							Libor-6 USD	0,52	0,52

Currencies	-1d	Currencies	-1d	Commodity	CRB	GOLD	BRENT
EUR/USD	1,1151 -0,0015	EUR/JPY	114,97 0,84		182,8225	1313,4	48,32
USD/JPY	103,15 0,93	EUR/GBP	0,8512 -0,0028	-1d	-1,61	-8,37	-1,06
GBP/USD	1,3093 0,0024	EUR/CHF	1,0961 0,0009				
AUD/USD	0,7512 -0,0051	EUR/SEK	9,5067 0,03				
USD/CAD	1,3090 0,0060	EUR/NOK	9,2945 0,04				

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