



Sunrise

Wednesday, 24 August 2016

Rates: Core bonds stabilize as summer mood continues

Core bonds ignored yesterday a number of fairly interesting items and closed virtually unchanged. Today's calendar is razor thin and unattractive, making us think that sideways trading will continue going into Friday's Jackson Hole speech of Yellen.

Currencies: Dollar decline slows

Yesterday, the dollar decline slowed. Sterling tries a technical rebound. Today, the eco calendar is thin. So, more technical trading might be on the cards as the countdown to Yellens's speech at Jackson hole continues.

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 opened higher yesterday with the S&P testing its record high**, but gains were mitigated towards the end of the session. **This morning, Asian shares trade mixed.** Japanese stocks outperform as USD/JPY trades slightly higher.
- **The board of directors at 8 of the 12 regional Fed banks sought last month to increase the discount rate to 1.25% from 1%**, the minutes of the discount rate meeting showed. It was the first time since the Fed raised rates in December that a majority of regional boards backed a discount-rate increase.
- **Brent crude oil prices rebounded late yesterday** after reports suggested Iran will attend a meeting of Opec producers in Algeria next month and may support coordinated action to prop up the market. The oil price reversed part of its gains overnight though with the Brent trading currently around \$49.5/barrel.
- **The use of China's currency in international payments bounced back in July** after a dip in June. The renminbi's use in Swift payments rose to 1.9% last month, but remains well below last year's high of 2.79%.
- **Rating agency Standard & Poor's lowered the outlook on Mexico's BBB+ rating to negative from stable** saying that a downgrade might come in the next two year if the government's debt or interest burden deteriorated. The peso weakened after the decision.
- Today, **the eco calendar is thin** with only US existing home sales and FHFA house price data. Germany, the US and Sweden will tap the market.

Rates

| | US yield | -1d |
|----|----------|---------|
| 2 | 0,7657 | 0,0000 |
| 5 | 1,1413 | -0,0016 |
| 10 | 1,5509 | 0,0000 |
| 30 | 2,2328 | 0,0000 |

Core bond yields stabilize

Peripheral bond yield spread widen slightly underperform

Lot of interesting news ignored.

| | DE yield | -1d |
|----|----------|---------|
| 2 | -0,6250 | -0,0010 |
| 5 | -0,5160 | 0,0020 |
| 10 | -0,0950 | 0,0000 |
| 30 | 0,4046 | 0,0000 |

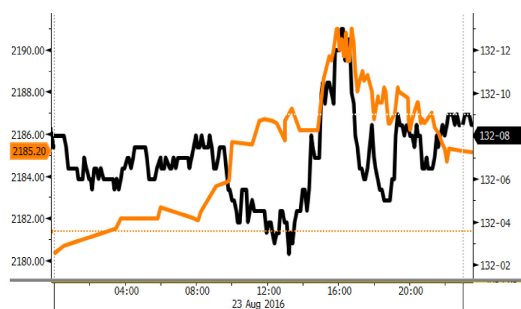
Existing Home sales & house prices for release

Core bonds barely move in quiet summer trading

Yesterday was probably one of the most boring trading sessions in the core bond markets this summer despite some interesting eco data and events. Investors are apparently unwilling to take positions ahead of the Jackson Hole speech of Yellen on Friday. In a daily perspective, German and US yields were less than 1 basis point higher/lower across the curve. European equities traded strong and US ones started strong, tested the highs, but slid lower for the remainder of the day. Oil jumped higher in late European trading (see headlines), but stabilized and didn't materially affect core bonds. **Eco data were mixed**: EMU consumer confidence unexpectedly weakened in August, while in the US New Home sales were much stronger than expected in July at multi-year high, but both the Richmond Fed manufacturing survey as the Markit PMI were a good deal weaker than expected. Market reactions: none. **The US 2-year Note auction** went very well. Finally, the **Minutes of the US Fed discount meeting (July 25)** showed that 8 out of 12 regional governors asked for a discount rate hike. In June there were six requests. **ECB Coeuré** said that the lack of structural reforms or fiscal initiatives may force the ECB to act despite risks. **In intra-EMU bond markets**, modest profit taking continued with 10-year yield differentials up 1 to 2 bps.

Unenticing market calendar

After having increased for four consecutive months, **US existing home sales** are forecast to have dropped slightly in July, by 1.3% M/M to a total number of 5.50 million. Following strong sales in the previous months, we believe that a limited dip is likely, although the trend will remain positive. **FHFA house prices** are still June data, so quite outdated. The consensus is looking for an increase by 0.3% M/M, up from 0.2% M/M in May, but we see risks for a stronger increase spurred by increasing activity.



T-Note future (black) & S&P future (orange) (intraday): T-Note hovered listless in narrow range. S&P eases after the cash open, as highs are too tough to crack before Yellen



S&P test highs, but recedes afterwards. Longer term, S&P upward momentum gas sharply eased down

Bund and US 5-year Note auctions

| | | |
|-------------|---------------|--------|
| R2 | 170 | -1d |
| R1 | 168,86 | |
| BUND | 167,68 | 0,0000 |
| S1 | 165,63 | |
| S2 | 163,61 | |

The Treasury started its end-of-month financing operation with a stellar 2-year Note auction. The auction stopped (0.76%) a full basis point below the WI at the moment of the stop (80% allocation at the high yield). The bid/cover of 2.83 was above average (awful 2.52 last month) and the buy-side takedown was very well, especially the direct bidding. This bodes well for **today's 5-year Note auction**. The issue is currently trading at 1.135%. The auction will pay-down about \$1B taking into account a \$35B maturing issue.

The **German debt Agency will tap the 0% Oct2021 for an amount of €4B**. It is the first re-opening after it sold €5B of the new issue in July. At the initial auction, the average yield was 0.51% and the official bid/cover 1, after the Bundesbank retained about 1.614B for its market regulation. Currently the bond yields -0.523%, not far away from the yield at auction. Positively, there is currently little fresh supply, but on the other hand many investors may be not active. **So, while the issue may again be undersubscribed, it shouldn't as usual have little impact on the secondary market.**

More range-trading ahead of Yellen?

Overnight, Asian equity markets trade again mixed. Japanese equities are doing well while Chinese equities trade weaker and the other marginally stronger. The dollar is little changed and so are US Treasuries. This suggests a fairly neutral opening of core bonds. European equities may still open somewhat lower on the slide of US equities after the European closure.

Today's eco calendar is thin and unattractive. No eco data in EMU and only existing Home sales, no strong market mover, in the US. The Bund and 5-year T-Note auctions are interesting, but unlikely to trigger much follow up action. That didn't even happen yesterday when there were some interesting items. In this context, we expect technically inspired sideways trading today and probably even into Yellen's speech on Friday. Traders may look intraday for impetus to the equity and oil markets, but also these may be range-bound. On top of it, the correlation between these markets and bonds diminished sharply. **Technically**, the T-Note future rebounded when approaching key support (131-19+), suggesting that it needs a strong driver to break eventually, which is not on today's radar. The Bund is moving nicely in its 200 ticks sideways range with 168 first resistance that may invite some traders to go short. Longer term, the range has boundaries between 168.86 and 165.63.



German Bund: sideways between 165.63 and 168.86



US Note future: Rebound when support approached. More range-trading?

Currencies

Dollar reversed earlier losses in technically inspired trading.

USD/JPY and EUR/USD range-bound.

| | | |
|---------|--------|--------|
| R2 | 1,1428 | -1d |
| R1 | 1,1366 | |
| EUR/USD | 1,1289 | 0,0001 |
| S1 | 1,1234 | |
| S2 | 1,1046 | |

USD/JPY 100 decent support, at least for now.

Major FX cross rates range-bound

Only second tier (US) eco data.

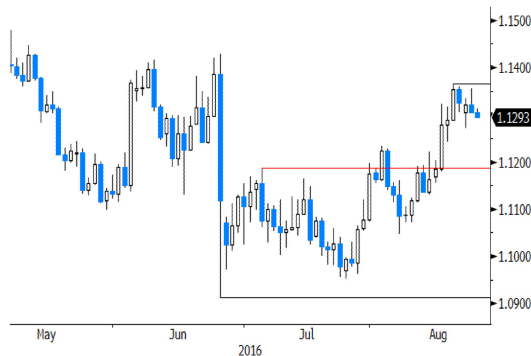
Technical trading ahead of Yellen's Jackson Hole speech is expected.

Dollar decline slows, but no clear trend yet

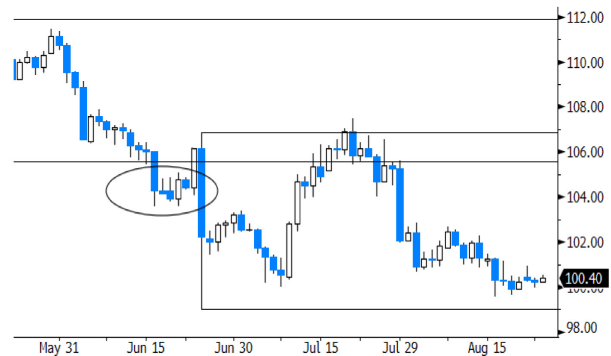
On Tuesday, currency traders experienced another uneventful session. The dollar stayed under slight pressure in Asia, but the decline slowed in Europe. USD/JPY stabilised close to the 100 mark. EUR/USD held a tight range mostly in the lower half of the 1.13 big figure. Later, the dollar rebounded cautiously. The Minutes of the Fed discount meeting showed that a majority of the regional Fed governors asked for a hike of the discount rate ahead of the July meeting. It was marginally USD supportive. EUR/USD closed the session at 1.1305 (from 1.1320). USD/JPY finished day at 100.24 (from 100.33).

Overnight, Asian equities trade mixed, but the moves remain limited. There is again no high profile macro-economic news to guide trading. Japanese equities gain about 0.5% as USD/JPY holds north of the psychological barrier of 100 (currently trading near 100.40). Brent oil is drifting back below \$50 p/b after an intraday rebound yesterday, but there is no clear impact on currency markets. EUR/USD hovers near yesterday's closing levels in the 1.13 area. The Aussie and the Kiwi dollar make a small step backward on overall USD strength. The CAD tries to sustain below USD/CAD 1.30 as oil holds near recent highs.

Today, the eco calendar is empty in Europe and thin in the US. After having increased for four consecutive months, **US existing home sales** are forecast to have dropped slightly in July, by 1.3% M/M to a total number of 5.50 million. Following strong sales in the previous months, we believe that a limited dip is likely, but the trend remains positive. **FHFA house prices** are still June data, so quite outdated and no market mover. The consensus is looking for an increase by 0.3% M/M, up from 0.2% M/M in May. Eventual surprises should only be of intraday significance. **The focus for USD trading remains on Yellen's speech on Friday**. Markets apparently prepare for the Fed chair signalling that rates might stay substantially lower for long, compared the what was the case in previous cycles. **In this context, the dollar might stay in the defensive going into Yellen's speech**. That said, yesterday's USD price action suggests that this soft scenario is maybe already discounted at current levels. **So, more technical trading without a clear direction might be on the cards for EUR/USD and for USD/JPY**.



EUR/USD: pre-Yellen rally running into resistance



USD/JPY struggling to stay north of 100 pivot

Wednesday, 24 August 2016

Of late, **an improvement in US eco data and ongoing constructive risk sentiment didn't help the dollar much**. Markets are not convinced that the Fed will take decisive steps toward policy normalisation anytime soon. **EUR/USD even rebounded north of the post Brexit sideways range as the Minutes from the July Fed meeting showed no consensus to raise rates soon**. The moves in EUR/USD remain modest (low volatility), but **the short-term momentum remains slightly USD negative going into the Jackson hole speech of Yellen**. EUR/USD 1.1428 (24 June top) is the first short term resistance. Overall dollar weakness also weighs on USD/JPY. Speculation on further BOJ easing hardly weakens the yen for now. The USD/JPY 99/100 was a strong support of late as markets fear BOJ action in case of a swift break. The downside in USD/JPY remains vulnerable though if the Fed stays muted on the timing of a next rate hike or if global sentiment on risk would turn less positive.

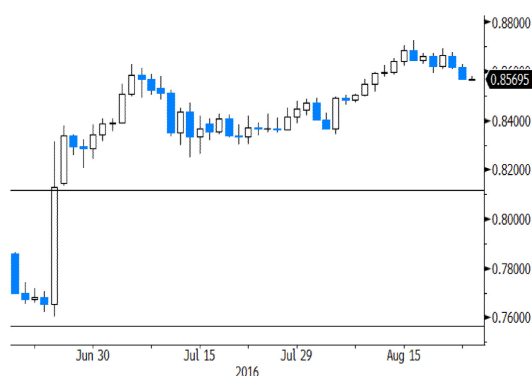
Sterling rebounds slightly

| | | |
|---------|---------------|--------|
| R2 | 0,8815 | -1d |
| R1 | 0,8725 | |
| EUR/GBP | 0,8567 | 0,0002 |
| S1 | 0,8344 | |
| S2 | 0,8251 | |

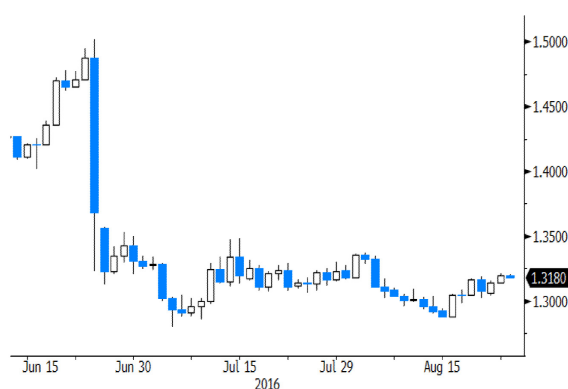
Yesterday morning in Asia, sterling extended Monday's 'technical' rebound. Investors further reduced sterling shorts. EUR/GBP drifted below the 0.8600 mark. Cable tested the 1.32 area. **The sterling rebound slowed in Europe, even as sentiment on risk improved**. The CBI industrial orders were better than expected (-5 vs -10 expected). Selling prices were also higher. However, the report didn't help sterling much, but the intraday decline of EUR/USD also pushed EUR/GBP further south. EUR/GBP closed the session at 0.8566 (from 0.8617). Cable finished the day at 1.3198.

Overnight, sterling stabilises against the dollar, but gains slightly ground against the euro as EUR/USD is losing a few ticks. Later today, only the BBA data on the loans for home purchases will be published. A substantial further decline is expected. This trend was already in place before Brexit. We don't expect much negative fall-out from it on sterling.

Of late, the first UK hard eco data from the post Brexit area were not too bad. At the same time, we have the impression that sterling has already discounted quite some negative news. We keep a negative/cautious bias on sterling longer term. **Short term, it looks that the decline of sterling is taking a breather. Even a technical rebound is possible**



EUR/GBP: sterling declines slows, at least temporary



GBP/USD looking for a short-term bottom

Calendar

| Wednesday, 24 August | | Consensus | Previous |
|----------------------|---|--------------------|--------------------|
| US | | | |
| 13:00 | MBA Mortgage Applications | -- | -4.0% |
| 15:00 | House Price Purchase Index QoQ (2Q) | -- | 1.3% |
| 15:00 | FHFA House Price Index MoM (Jun) | 0.3% | 0.2% |
| 16:00 | Existing Home Sales Total / MoM (Jul) | 5.50m/-1.3% | 5.57m/1.1% |
| Japan | | | |
| 07:00 | Leading Index CI (Jun F) | A 99.2 | 98.4 |
| 07:00 | Coincident Index (Jun F) | A 111.1 | 110.5 |
| UK | | | |
| 10:30 | BBA Loans for House Purchase (Jul) | 38000 | 40103 |
| Germany | | | |
| 08:00 | GDP SA QoQ YoY (2Q F) | 0.4% / 1.8% | 0.4% / 1.8% |
| France | | | |
| 18:00 | Total Jobseekers (Jul) | 3505k | 3525.7k |
| 18:00 | Jobseekers Net Change (Jul) | -20.5 | 5.4 |
| Belgium | | | |
| 15:00 | Business Confidence (Aug) | 0.8 | 1.0 |
| Norway | | | |
| 10:00 | Unemployment Rate AKU (Jun) | 4.7% | 4.7% |
| Events | | | |
| | Cabinet Office Monthly Economic Report for August | | |
| Germany | BoBl Auction (€4B 0% Oct2021) | | |
| US | 5Yr Notes (\$34B) & 2Yr FRN (\$13B) Auction | | |
| Sweden | Bond Auction (SEK3B 3.5%; 2022 & SEK0.5B 2.25% 2032) | | |

Contacts

| 10-year | td | -1d | 2-year | td | -1d | STOCKS | -1d |
|---------|-------|-------|--------|-------|------|------------|------------------------|
| US | 1,55 | 0,01 | US | 0,77 | 0,02 | DOW | 18547 18547,30 |
| DE | -0,10 | -0,01 | DE | -0,62 | 0,00 | NASDAQ | for Exch - NQI #VALUE! |
| BE | 0,12 | -0,01 | BE | -0,58 | 0,00 | NIKKEI | 16584 16584,49 |
| UK | 0,55 | -0,01 | UK | 0,11 | 0,00 | DAX | 10592,88 10592,88 |
| JP | -0,08 | 0,01 | JP | -0,20 | 0,01 | DJ euro-50 | 2994 2993,73 |

| | | | | | | USD | td | -1d |
|-----|--------|----------|-------|-----------|-------|------|-------------|-------------|
| IRS | EUR | USD (3M) | GBP | EUR | -1d | -2d | Eonia EUR | -0,34 0,001 |
| 3y | -0,198 | 1,042 | 0,426 | Euribor-1 | -0,37 | 0,00 | Libor-1 USD | 0,27 0,27 |
| 5y | -0,133 | 1,148 | 0,484 | Euribor-3 | -0,30 | 0,00 | Libor-3 USD | 0,39 0,39 |
| 10y | 0,268 | 1,391 | 0,709 | Euribor-6 | -0,19 | 0,00 | Libor-6 USD | 0,52 0,52 |

| Currencies | | -1d | Currencies | | -1d | Commoditie | CRB | GOLD | BRENT |
|------------|---------|---------|------------|--------|---------|------------|----------|--------|-------|
| EUR/USD | 1,12895 | -0,0050 | EUR/JPY | 113,34 | -0,16 | | 187,0811 | 1336,8 | 49,4 |
| USD/JPY | 100,41 | 0,29 | EUR/GBP | 0,8562 | -0,0046 | -1d | 0,00 | -2,03 | 0,73 |
| GBP/USD | 1,3178 | 0,0009 | EUR/CHF | 1,0887 | -0,0012 | | | | |
| AUD/USD | 0,7601 | -0,0042 | EUR/SEK | 9,4681 | -0,01 | | | | |
| USD/CAD | 1,2928 | 0,0023 | EUR/NOK | 9,2823 | -0,02 | | | | |

| 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 |
| Joke Mertens | +32 2 417 30 59 | | Institutional Desk | | +32 2 417 46 25 |
| Mathias van der Jeugt | +32 2 417 51 94 | | 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 | | |
| Jan Cermak | +420 2 6135 3578 | | | | +420 2 6135 3535 |
| Jan Bures | +420 2 6135 3574 | | | | |
| Petr Baca | +420 2 6135 3570 | | | | |
| Bratislava Research (CSOB) | | | Bratislava | | |
| Marek Gabris | +421 2 5966 8809 | | | | +421 2 5966 8820 |
| Budapest Research | | | Budapest | | |
| David Nemeth | +36 1 328 9989 | | | | +36 1 328 99 85 |

ALL OUR REPORTS ARE AVAILABLE ON WWW.KBCCORPORATES.COM/RESEARCH

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 date of the report and are subject to change without notice.

