



Tuesday, 12 May 2020

Rates: Fed governors to rule out possibility of negative rates

US Treasuries continued their supply-related underperformance ahead of tonight's 10-yr Note sale. The eco calendar remains thin, but Fed governors will be grilled on the fact that the Fed Funds Future curve discounts (marginally) negative rates in 2021. We expect Fed members to categorically rule out the possibility.

Currencies: Uncertainty on easing of UK lockdown measures weighs on sterling

The dollar mostly outperformed yesterday as risk sentiment turned more cautious and as (LT) yields rose. EUR/USD drifted back sought to the 1.08 area. A brief dip lower this morning was easily reversed but the EUR/USD picture remains fragile. Sterling underperformed as the UK government failed to bring a clear message on the restart of the economy.

Calendar

Headlines

- **US equities** ended mixed with the DJI down 0.45% but the Nasdaq 0.7% in the green. Most **Asian-Pacific markets** print declines. Australia (-1.7%) underperforms amid increasing trade tensions with China.
- **China suspended meat imports from four Australian companies** that make up 35% of the country's beef exports to China. Tensions between the two escalated recently as Australia called for a probe into the origins of the pandemic.
- WH advisor Kudlow and National Security Advisor O'Brien wrote to the Labor Secretary that they **don't want him to invest the government retirement fund in a fund that tracks Chinese stocks, calling it "risky and unjustified"**.
- **State governor Cuomo** declared the critical phase of the virus in New York over and **laid out plans for a phased reopening beginning on Friday**. NY will be divided in 10 regions and will have to satisfy seven criteria before opening.
- **Several Fed officials downplayed the potential use of negative rates**. Chicago Fed's Evans said he's not anticipating them while Bostic from Atlanta sees sub-zero rates as one of the "weaker tools in the tool kit".
- **Germany's main business organisation (BDI)** in a paper jointly issued by its Italian and French counterparts **called for more "fiscal solidarity"**, adding that the pandemic risks collapsing the EU export market, affecting all member states.
- **Today's economic calendar** contains US April NFIB small business optimism and CPI data. A slew of Fed and ECB speeches are due. Germany and the US tap the bond market.

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

	US yield	-1d
2	0.17	0.02
5	0.34	0.02
10	0.71	0.03
30	1.40	0.03

	DE yield	-1d
2	-0.75	0.03
5	-0.73	0.03
10	-0.51	0.03
30	-0.05	0.02

Fed governors to rule out negative policy rates

Core bond trading was confined to narrow ranges yesterday. Both the German Bund and the US Note future slightly fainted during US hours. **US Treasuries underperformed in a supply-related move.** This week sees record US issuance. The US Treasury kicked off with a \$42bn 3-yr Note auction, but 10-yr and 30-yr deals will follow. Treasury Secretary Mnuchin stressed the increased reliance of issuance of (longer term) debt as plotted out in last week's quarterly refunding statement. Yesterday's 3-yr sale in any case was well digested. The US yield curve bear steepened with yields rising 1.7 bps (2-yr) to 3.3 bps (30-yr). The German yield curve bear flattened with yields adding 2.8 bps (2-yr) to 2.2 bps (30-yr). 10-yr yield spread changes vs Germany barely changed with Greece (-5 bps) outperforming. No relief rally in peripherals thus after the Eurogroup decided on the ESM Pandemic Credit Line (up to 2% of 2019 GDP; no conditionality). Italian BTP's didn't react to Moody's keeping the lowest possible investment grade rating (Baa3).

Most Asian stock markets lose ground this morning, ignoring WS's late sprint yesterday. Fox Business reported that **US President Trump will pull federal money (retirement funds) out of Chinese equities** which risks retaliating Chinese measures and weighing on the countries trade relationship. **China on his part has suspended meat imports from four Australian abattoirs (35% of Australian beef exports to China),** probably in response to the Australian government's blame game with regard to the origin of the Covid-19 virus. Core bonds trade a tad stronger this morning.

Today's eco calendar contains US NFIB Small Business Optimism and CPI inflation. Several Fed governors are scheduled to speak. **It will be interesting to hear comments on the negative (yield) part of the Fed Funds Future curve (2021). We expect Fed governors to categorically rule out negative policy rates. In combination with more US supply (\$32bn 10-yr Notes), there is thus room for additional underperformance of US Treasuries.** Tomorrow's speech by Fed Chair Powell will be closely watched in this respect as well. This week's eco calendar is generally 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

EUR/GBP tries to rebound off 0.87 support

R2	1.125	-1d
R1	1.1109	
EUR/USD	1.0807	-0.0032
S1	1.0770	
S2	1.0636	

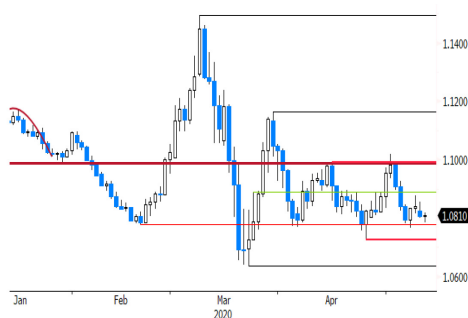
R2	0.9212	-1d
R1	0.9033	
EUR/GBP	0.8762	0.0026
S1	0.8621	
S2	0.8569	

Global sentiment turned more cautious yesterday. Uncertainty on the pace of the easing of lockdown measures worldwide dented risk appetite. The dollar was in good shape with trade-weighted USD (DXY) regaining the 100 mark. The yen was a remarkable underperformer after a solid performance of the Japanese currency of late. The USD/JPY rise accelerated as US yields jumped higher later in USD dealings (close 107.66). EUR/USD drifted to the low 1.08 area. Overall USD strength and the political bickering on the ruling of the German Court on the ECB PSPP programme kept EUR/USD in the defensive (close at 1.0807).

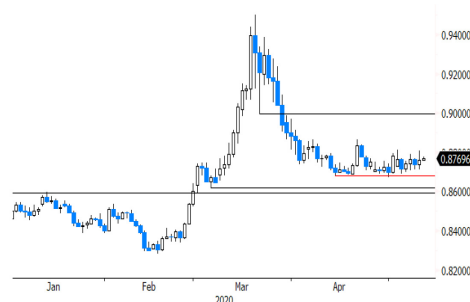
This morning, Asian markets also started in cautious risk-off mode. Investors ponder the consequences of new local outbreaks of the corona virus. Early in Asian trading, the **Aussie dollar** lost half a big figure as China suspended imports for meat from four Australian abattoirs, raising fears for trade tensions to flare up. However, the move was rather easily reversed later AUD/USD is again trading in the 0.6480 area. The yen regains some ground after yesterday's setback (USD/JPY 107.40 area). EUR/USD dropped temporarily to the 1.0785 area (AUD-driven?) but also reversed its decline (currently 1.0815).

Today, the US NFIB small business confidence and the CPI data are interesting but probably with no lasting impact on trading. **Several Fed governors will speak**. Given recent market pricing of negative FF rates, markets will look for clues whether negative rates are indeed an option for the Fed. For now we don't expect the Fed to give a clear sign in that direction. The US 10-y bond auction is a wildcard. Question is whether higher yields due to big supply should be seen as USD supportive. 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 to 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.**

Sterling underperformed yesterday. EUR/GBP was propelled higher to test the 0.88 area. Confusing communication of the UK government on the easing of the lockdown and persistent headlines on the stalemate in the UK-EU trade negotiations were negatives for sterling. EUR/GBP closed at 0.8762. There are no important UK data today. The EUR/GBP 0.87 area proved to be quite a solid bottom of late. Some further EUR/GBP gains are possible short-term.



EUR/USD holding tight range. Picture remains fragile



EUR/GBP: tentative signs of bottoming off the 0.87 support?

Calendar

Tuesday, 12 May		Consensus	Previous
US			
12:00	NFIB Small Business Optimism (Apr)	83.0	96.4
14:30	CPI MoM/YoY (Apr)	-0.80%/0.40%	-0.40%/1.50%
14:30	CPI Ex Food and Energy MoM/YoY (Apr)	-0.20%/1.70%	-0.10%/2.10%
14:30	Real Avg Hourly/Weekly Earning YoY (Apr)	--/--	1.60%/0.70%
France			
08:30	Bank of France Ind. Sentiment (Apr)	40	--
China			
03:30	PPI YoY (Apr)	-3.10%A	-1.50%
03:30	CPI YoY (Apr)	3.30%A	4.30%
Norway			
08:00	GDP Mainland QoQ (1Q)	-1.90%	0.20%
08:00	GDP QoQ (1Q)	--	1.60%
Events			
11:30	Germany to Sell EUR 4 Bln of 2027 Bonds		
15:00	Fed's Bullard Speaks on the Economic Outlook		
16:00	Fed's Harker Discusses the Impact of Covid-19		
16:00	Fed's Quarles Appears Before Senate Banking Committee		
16:30	ECB's Stournaras on German Court's decision		
19:00	US to Sell USD32 Bln 10-Year Notes		
23:00	Fed's Mester takes Part in a Moderated Q&A		

10-year	<u>Close</u>	<u>-1d</u>		2-year	<u>Close</u>	<u>-1d</u>	Stocks	<u>Close</u>	<u>-1d</u>
US	0.71	0.03		US	0.17	0.02	DOW	24221.99	-109.33
DE	-0.51	0.03		DE	-0.75	0.03	NASDAQ	9192.344	71.02
BE	0.07	0.03		BE	-0.48	0.04	NIKKEI	20366.48	-24.18
UK	0.27	0.03		UK	0.01	0.01	DAX	10824.99	-79.49
JP	-0.01	-0.02		JP	-0.17	-0.04	DJ euro-50	2883.75	-24.36
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	-0.32	0.26	0.36	Eonia	-0.4560	0.0000			
5y	-0.29	0.36	0.41	Euribor-1	-0.4460	0.0050	Libor-1	0.1980	0.0000
10y	-0.12	0.66	0.52	Euribor-3	-0.2580	-0.0120	Libor-3	0.4346	0.0000
				Euribor-6	-0.1470	-0.0020	Libor-6	0.6880	0.0000
Currencies	<u>Close</u>	<u>-1d</u>		Currencies	<u>Close</u>	<u>-1d</u>	Commodities	<u>Close</u>	<u>-1d</u>
EUR/USD	1.0807	-0.0032		EUR/JPY	116.36	0.86	CRB	122.67	-2.07
USD/JPY	107.66	1.01		EUR/GBP	0.8762	0.0026	Gold	1698.00	-15.90
GBP/USD	1.2335	-0.0075		EUR/CHF	1.0516	-0.0007	Brent	29.63	-1.34
AUD/USD	0.6489	-0.0043		EUR/SEK	10.6754	0.0877			
USD/CAD	1.4007	0.0080		EUR/NOK	11.1414	0.0667			

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	
Jan Cermak	+420 2 6135 3578		
Jan Bures	+420 2 6135 3574		
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 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.

