Sunrise

Tuesday, 11 April 2017

Rates: Risk aversion dominates thin agenda at start trading week

Overnight, risk sentiment deteriorated on most Asian stock markets. A stronger opening of the Bund will result in an immediate test of 0.2% support for the German 10-yr yield. We don't anticipate a sustained break lower even if risk aversion provides some short term safe haven flows.

Currencies: Dollar cannot build on Friday's positive price action

EUR/USD hovers listless close to 1.06, but USD/JPY is sliding back towards the key 110, helped by some risk-off sentiment in Asian session (lower equities and lower US yields). We nevertheless aren't convinced the Asian trend should infect European and US markets too much. That should keep USD/JPY north of 110.

Calendar

Headlines

- **US equities flat lined** in the first trading session of the week. **Overnight Asian risk sentiment deteriorated** with China underperforming (-1%).
- The Federal Reserve's plans to raise US interest rates gradually are aimed at sustaining full employment and near-2-% inflation **without letting the economy overheat, Fed Chair Yellen** said.
- **ECB policy is *"appropriate and a reassessment is not warranted at this stage,"* VP Constancio said.** The risk of a regional (Portuguese) real estate bubble is limited, while advocating targeted measures to avoid potential problems.
- A **Moody's** report titled *'Credit Profiles Resilient to Rising Household Debt and Stretched Housing Affordability'* focused on **Australia, Canada, New Zealand and Sweden - all AAA rated countries where home prices and household debt have soared** in the last three years.
- **BoJ Governor Kuroda** said the central bank aims for a moderate acceleration of inflation **driven by increases in wages and corporate earnings.** At this stage, they haven't increased as much as hoped for despite a tightening job market.
- **South Africa's central bank said the scope for interest-rate cuts is limited** as current policy should be enough to bring inflation to within target range. Price-growth expectations remain *"uncomfortably close to 6%"*, SARB said.
- **Today's eco calendar** contains EMU industrial production, German ZEW, US NFIB small business optimism and UK inflation data. The Netherlands and the US tap the market ECB Visco and Fed Kashkari are scheduled to speak.

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

France underperforms as Mélenchon overtakes Fillon

Mild risk off sentiment as French tail risk (extreme left vs extreme right) increases

Bund outperforms US Note future

French assets underperform

	US yield	-1d
2	1,25	-0,04
5	1,87	-0,05
10	2,34	-0,04
30	2,97	-0,04

Global core bonds profited from safe haven flows yesterday. The Bund outperformed the US Note future. Latest French election polls provided the bid for Bunds and caused French underperformance (stocks and bonds). Geopolitical tensions (Syria, North-Korea) also simmer on the background. Extreme-left candidate Mélenchon gains ground and currently polls third, overtaking Fillon with 18%. Frontrunners Macron and Le Pen still lead the bunch with around 24%. Mélenchon's rise increases the tail risk of a presidential run-off vote between extreme left and extreme right which is the worst outcome from a market point of view. **Brent crude continued its impressive rally, but couldn't counter the safe haven flows.** Since the end of March, the oil price rose from $50/barrel to $56/barrel. Since the start of US dealings, core bond trading remained confined to narrow ranges.

In a daily perspective, the German yield curve dropped 3.4 bps (30-yr) to 2.1 bps (10-yr) lower. Declines at the US yield curve were smaller, varying between -2 bps (5-yr) and -1.3 bps (2-yr). **On intra-EMU bond markets**, 10-yr yield spread changes versus Germany widened with Italy/Ireland (+4 bps; supply ahead) and France (+6 bps vs +3 bps for Belgium; Mélenchon) underperforming.

Yellen confirms change of heart, but slightly more cautious

	DE yield	-1d
2	-0,84	-0,03
5	-0,51	-0,03
10	0,20	-0,05
30	0,97	-0,05

After US closure, **Fed chairwoman Yellen** spoke in a public discussion. She **confirmed the change of heart at the Fed,** referred to by several other governors last week. The focus is now on gradually raising interest rates unless the economy begins to deteriorate. Up until recently, the Fed acted the other way around: keeping policy unchanged unless the economy shows clear signs of improving. While emphasizing this change of heart, Yellen nevertheless stroke a note of caution: *"Where before we had our foot pressed down on the gas pedal trying to give the economy all the oomph we possibly could, now [we're] allowing the economy to kind of coast and remain on an even keel.* ***To give it some gas, but not so much that we're pressing down hard on the accelerator."*** The US Note future gains some ground overnight.

French OAT future (orange) and German Bund (black): Nice correlation last week, but latest French election news causes French underperformance and triggers safe haven flows

Brent crude continues its comeback, approaching $56/barrel

Calendar heats up

EMU industrial production is expected to have risen 0.1% M/M and 1.9% Y/Y in February following a stronger 0.9% M/M (and 0.6% Y/Y in January. National data were mixed with strong German (0.8% M/M) and Italian production (1% M/M), but weakness in France (-1.6% M/M), Ireland (-15.54%) and to a lesser extent Spain. Taken it together, **the risks remain on the downside of expectations.** The

Mixed eco data?

Downside risks for EMU production and US NFIB

Upside risks German ZEW (expectations)

German ZEW investors' sentiment (expectations) is expected to have risen slightly to 14.8 in April from 12.8 previously, while current conditions remain strong at 77.3. The expectation index hovers already for a few months around current levels. Given that the German cycle looks at its peak (see high current conditions) that's no real surprise. Given the advance of equities and the rise in the Sentix survey, we nevertheless dare put **the risks slightly on the upside of expectations.** Finally the **US NIFB small business sentiment** is expected to have slid marginally in March to 104.7 from 105.3 in February. The index has risen tremendously following Trump's victory. There may be some early disappointment on Trump's scorecard till now after the failure to repeal Obamacare and the expected delay in the fiscal stimulus plan. So, **risks might be on the downside,** but without inflicting to much damage to confidence.

Netherlands and US tap market

The US Treasury started its refinancing operation with a weak $24B 3-yr Note auction. Today, the US Treasury continues its refinancing with a $20B 10-yr Note auction. Currently, the WI trades around 2.34%. **The Dutch debt agency taps the on the run DSL (2.5% Jan2033) for €0.75-1.25B.** The bond on offer didn't cheapen going into the auction and trades rather expensive on the curve. While the amount on offer is relatively low, we expect a mediocre auction.

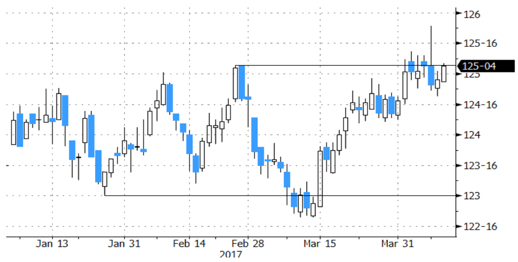
R2	164,40	-1d
R1	163,31	
BUND	163,21	0,55
S1	158,28	
S2	157,28	

Risk aversion dominates at start trading week

Overnight, risk sentiment deteriorated on most Asian stock markets after yesterday's neutral WS session. China underperforms (-1%). Other risk-off barometers also suggest a stronger opening for the Bund. The Japanese yen, the US Note future and gold trade higher. We don't think that there's a direct link with Yellen's comments (see above). **A stronger opening of the Bund will result in a test of 0.2% support in the German 10-yr yield. As with US yields last Friday, we don't anticipate a sustained break lower even if deteriorating risk sentiment provides some ST safe haven flows.** Today's eco data are expected to be mixed and insignificant for trading.

Last Friday's technically very important session suggest that US Treasuries will eventually face new downward pressure, even if risk aversion took over at the start of this week. From a technical point of view, both the US 5-yr (1.8% and 10-yr (2.3%) yields managed to stay above the lower bound of their respective trading ranges after intense tests. We expect yields to move back higher in the range, **targeting 2.14% and 2.64% respectively implying a sell-on-upticks environment for US Treasuries.** Markets still have to align with the Fed's tightening scenario and didn't take into account effects of the start of the run-off the balance sheet ahead of the year-end.

German Bund: New contract high. German 10-yr yield about to test key support (0.2%)



US Note future: Sell-on-upticks as 2.3% yield support survived intense test and markets need to align with Fed

Currencies

Dollar cannot build on post-payrolls gains

USD/JPY remains in danger zone

R2	1,1145	-1d
R1	1,0906	
EUR/USD	1,0589	-0,0003
S1	1,0341	
S2	1,0000	

USD: Uneventful trading yesterday with poor close

The dollar traded fairly uneventful in a news-poor Monday session. Some follow through USD/JPY buying during the Asian session and some minor French election-related risk-off spiced the sideways trading session that ended with some marginal dollar weakening against euro and yen. EUR/USD hovered between about 1.0570 and 1.0608, closing at 1.0596. USD/JPY made a trip to 111.60 from 111.10 in Asian trading, but gradually eased to opening levels before a final down-move pushed it just below 111 with a 1.1094 close. **Concluding, an uneventful session, but with a bit of a nasty taste as USD/JPY couldn't build on Friday's gains, despite US equities closing unchanged.**

Overnight: Yen higher on risk off and Yellen

Overnight, Yellen said the Fed is shifting from its post-crisis exercise of healing the economy to one aimed at holding on to the progress made (see above). While her comments are quite neutral according to us, US yields are 2 to 3 bps lower overnight. Asian equities are mostly down with some close to flat. The **yen is gaining ground** together with other safe havens like US Treasuries and gold. USD/JPY slid from 110.95 to an intraday low at 110.60 and trades now slightly higher at 110.67. **EUR/USD** trades with a slight dollar positive bias, but at 1.0584 from 1.0595 at the opening that doesn't mean much.

Calendar heats up, but most second tier data

Downside risks EMU production, but upside risk ZEW sentiment

Downside risk US small business sentiment

Mixed data: no market mover?

EMU industrial production is expected to have risen 0.1% M/M and 1.9% Y/Y in February following a stronger 0.9% M/M (and 0.6% Y/Y in January. **Risks remain on the downside of expectations**. The **German ZEW investors' sentiment** (expectations) is expected to have risen slightly to 14.8 in April from 12.8 previously, while current conditions remain strong at 77.3. Given the advance of equities and the rise in the Sentix survey, we nevertheless dare to put **the risks slightly on the upside of expectations**. Finally the **US NIFB small business sentiment** is expected to have slid marginally in March to 104.7 from 105.3 in February. There may be some early disappointment on Trump's scorecard till now so, **risks might be on the downside. The eco data are no strong market movers**

EUR/USD: Nice dollar move on payrolls suggesting the pair may slide towards 1.05 support area or even the cycle lows at 1.0340, but yields should go up

USD/JPY struggled to keep above the key 110 area. Friday's price action brought little solace for the dollar

No strong catalyst for today's trading

Friday's dollar price action was constructive, as was the rejection of key US yield supports (1.80% for the 5-yr and 2.30% for the 10-yr). This suggested that US

yields and widening yield differentials may give the dollar again support. The proof of the pudding is in the eating though and yesterday's price action didn't really support the notion that the dollar is back on the winning side. EUR/USD stabilizes with election risk and geopolitical risk keeping the euro dollar balance intact. The dollar didn't get rate support. On the contrary, yields are down at the onset of European trading. We don't expect much of the eco data. So, sentiment and geopolitical issues will simmer at the background giving FX markets some intraday momentum. We don't see a catalyst for EUR/USD or USD/JPY to take out significant technical barrier, even if EUR/JPY remains dangerously close to the 110 level.

Technicals: Danger USD/JPY not away yet

From a technical point of view, USD/JPY failed to regain the 111.36/60 previous range bottom and approached three times the key 110 support area, but rebounded each time. A decline below 110 would signal more trouble ahead. **Friday's price action is a slight positive for the dollar, but we remain cautious on USD/JPY as long as the pair doesn't trade sustainably above 112.20** (neckline ST double bottom). **EUR/USD extensively tested the topside of the MT range (1.0874/1.0906 area) two weeks ago, but the test was rejected. EUR/USD returned lower in the 1.0875/1.05 trading range with the odds now for a test of the downside of the range.**

Sterling doing somewhat better

R2	0,8881	-1d
R1	0,8854	
EUR/GBP	0,8527	-0,0022
S1	0,8403	
S2	0,8304	

Today, the UK eco calendar is busy and interesting from a market point of view. Overnight, the **BRC like for like sales disappointed** as they dropped 1% Y/Y while a 0.3% M/M drop was expected. A further sign that consumer spending is losing momentum. However, it didn't impact sterling that remained fairly stable against euro and dollar. More important will be the **CPI and PPI data for March**. The market expects CPI at 0.3% M/M and 2.3% Y/Y unchanged from February, while the core CPI is expected to have eased slightly to 1.9% Y/Y from 2% previously. The weaker sterling is behind the trend increase in inflation, but that trend may pause in March due to some special factors like the late Easter and lower fuel prices. **We side with consensus, but any stronger outcome may stimulate expectations on the timing of a rate hike and supports sterling.** Similarly both input and output PPI are expected to have slowed in March, even as input prices remain at very high levels. Output price risks are on the upside. Sterling gradually gained ground versus the euro. If inflation surprises on the upside, some more gains are possible. However, EUR/GBP intermediate support looms at 0.8484, a level which won't be easily broken. **Mid-March, sterling found a better bid after** higher than expected UK inflation and a more hawkish tone from the BoE. **We changed our short-term bias on EUR/GBP from positive to neutral. The EUR/GBP 0.88/0.84 range should guide trading for now. Last week, sterling rally/short-squeeze ran into resistance, but we see no trigger for a real change in sentiment.**

EUR/GBP sterling short-squeeze is easing, but no sustained sterling correction yet

GBP/USD: cable turned south again, but inflation will decide whether more downside will follow

Calendar

Tuesday, 11 April		Consensus	Previous
US			
12:00	**NFIB Small Business Optimism (Mar)**	**104.7**	**105.3**
16:00	JOLTS Job Openings (Feb)	5650	5626
UK			
01:01	BRC Sales Like-For-Like YoY (Mar)	A -1%	-0.4%
10:30	**CPI MoM / YoY (Mar)**	**0.3%/2.3%**	**0.7%/2.3%**
10:30	**CPI Core YoY (Mar)**	**1.9%**	**2.0%**
10:30	PPI Input NSA MoM / YoY (Mar)	-0.1%/17%	-0.4%/19.1%
10:30	PPI Output NSA MoM / YoY (Mar)	0.1%/3.4%	0.2%/3.7%
10:30	PPI Output Core NSA MoM / YoY (Mar)	0.2%/2.5%	0.0%/2.4%
10:30	House Price Index YoY (Feb)	6.1%	6.2%
EMU			
11:00	**Industrial Production SA MoM / WDA YoY (Feb)**	**0.1%/1.9%**	**0.9%/0.6%**
11:00	ZEW Survey Expectations (Apr)	--	25.6
Germany			
11:00	ZEW Survey Current Situation (Apr)	77.5	77.3
11:00	**ZEW Survey Expectations (Apr)**	**14.8**	**12.8**
Sweden			
09:30	CPI MoM / YoY (Mar)	0.2%/1.5%	0.7%/1.8%
09:30	CPI CPIF MoM / YoY (Mar)	0.1%/1.6%	0.7%/2.0%
Events			
11:30	Netherlands to Sell 2.5% 2033 Bonds		
17:00	ECB Visco Speaks Before European Parliament		
19:00	US to Sell $20B 10-yr Notes Reopening		
19:45	Fed's Kashkari Participates in Q&A in Minneapolis		

10-year	td	-1d		2-year	td	-1d	Stocks	td	-1d
US	2,34	-0,04		US	1,25	-0,04	DOW	20658,02	1,92
DE	0,20	-0,05		DE	-0,84	-0,03	NASDAQ	5880,926	3,11
BE	0,78	0,01		BE	-0,56	0,01	NIKKEI	18747,87	-50,01
UK	1,08	0,00		UK	0,09	-0,02	DAX	12200,52	-24,54
JP	0,04	-0,01		JP	-0,22	-0,01	DJ euro-50	3480,44	-15,36
IRS	EUR	USD	GBP	EUR	-1d	-2d	USD	td	-1d
3y	-0,08	1,74	0,63	Eonia	-0,3570	-0,0040			
5y	0,14	1,97	0,79	Euribor-1	-0,3740	-0,0010	Libor-1	0,9900	0,0000
10y	0,71	2,31	1,13	Euribor-3	-0,3320	-0,0020	Libor-3	1,1576	0,0000
				Euribor-6	-0,2410	0,0000	Libor-6	1,4296	0,0000
Currencies	td	-1d		Currencies	td	-1d	Commodities	td	-1d
EUR/USD	1,0589	-0,0003		EUR/JPY	117,18	-0,84	CRB	187,63	0,52
USD/JPY	110,66	-0,77		EUR/GBP	0,8527	-0,0022	Gold	1258,50	2,80
GBP/USD	1,2418	0,0029		EUR/CHF	1,0681	-0,0003	Brent	55,86	0,39
AUD/USD	0,7501	0,0009		EUR/SEK	9,616	0,0094			
USD/CAD	1,3319	-0,0095		EUR/NOK	9,1399	-0,0306			

Contacts

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
Mathias van der Jeugt	+32 2 417 51 94	Institutional Desk	+32 2 417 46 25
Dublin Research		France	+32 2 417 32 65
Austin Hughes	+353 1 664 6889	London	+44 207 256 4848
Shawn Britton	+353 1 664 6892	Singapore	+65 533 34 10
Prague Research (CSOB)			
Jan Cermak	+420 2 6135 3578	Prague	+420 2 6135 3535
Jan Bures	+420 2 6135 3574		
Petr Baca	+420 2 6135 3570		
Bratislava Research (CSOB)			
Marek Gabris	+421 2 5966 8809	Bratislava	+421 2 5966 8820
Budapest Research			
David Nemeth	+36 1 328 9989	Budapest	+36 1 328 99 85

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