



Sunrise

Friday, 17 March 2017

Rates: ECB doesn't have to follow Fed's playbook

ECB Nowotny said after European trading that the ECB doesn't have to follow the Fed's playbook when normalizing monetary policy. He suggests that the ECB could hike (deposit) rates before ending QE. This could weigh on the Bund in the opening. Today's eco calendar only contains second tier US eco data, suggesting consolidation ahead of the weekend.

Currencies: From dollar softness to euro strength

The dollar initially stabilized yesterday after the post-FOMC setback. Later in the session, hawkish comments from ECB's Nowotny propelled EUR/USD to the highest level in one month. We look out how far the post-FOMC USD correction has to go. Will today's US consumer confidence be strong enough to block the USD correction?

Calendar

Headlines

| | |
|--------------|---|
| 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 | ➡ |

- **US equities returned part of the FOMC-gains** and closed slightly lower on the day. **Overnight**, most Asian stock markets trade positive with Japanese stocks underperforming (-0.4%).
- **The ECB might move away from loose monetary policy in a different way than the Fed**, ECB Nowotny said. The US model was to finish bond purchases first, but this model might not transfer well to Europe.
- **Moody's improved to outlook on Brazil's Ba2-rating from negative to stable** driven by expectation that downside risks are abating and macroeconomic conditions stabilizing, with the economy showing signs of recovery, inflation falling and the fiscal outlook clearer.
- The Czech central bank is **likely to end** a regime to keep the crown weak **around the middle of the year**, **Vice-Governor Hampl** was quoted as saying, **adding a later exit was also possible**.
- Greece and its international creditors remain divided over the terms of a review of the country's bailout programme, a senior euro zone official said, **a gap that will prevent Athens from getting fresh financial aid at Monday's Eurogroup**.
- **Conservatives in Congress are pushing Donald Trump to block the IMF from participating in a European-led bailout of Greece**, as his administration signalled it would take a tougher line with global institutions.
- **Today's eco calendar** is uneventful with only US industrial production and University of Michigan consumer confidence. G20 finance chiefs gather in Germany and Donald Trump meets Angela Merkel.

Rates

US Treasuries reverse some of Thursday's juicy gains

Bund additionally hit by Dutch election results & Nowotny comments

Peripherals cannot gain sustainably on Dutch election results

| | US yield | -1d |
|----|----------|------|
| 2 | 1.33 | 0.03 |
| 5 | 2.04 | 0.05 |
| 10 | 2.53 | 0.04 |
| 30 | 3.14 | 0.04 |

| | DE yield | -1d |
|----|----------|------|
| 2 | -0.79 | 0.03 |
| 5 | -0.29 | 0.07 |
| 10 | 0.47 | 0.08 |
| 30 | 1.22 | 0.06 |

Production to have rebounded

Upside risks Michigan consumer sentiment

FOMC gains partly erased; Nowotny hits Bund

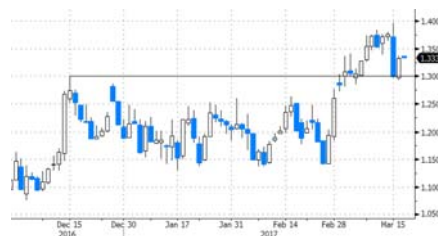
Global core bonds lost ground yesterday, reversing part of Wednesday evening's post-FOMC gains. Bunds underperformed US Treasuries, as the failure of the far-right Dutch candidate Wilders to win the elections weighted extra on the Bund, as well as late session comments of ECB Nowotny. He said the ECB exit may be different from the Fed with the deposit rate hike possibly preceding asset tapering. Not all rates should be increased simultaneously, he added. ECB executive member Praet already contradicted Nowotny, saying that the sequence of the exit is well defined in the forward guidance. Nowotny pushed the Bund 40/50 ticks lower in after-trade. Praet's response was ignored. In a daily perspective, the German yield curve trades 3 bps (2-yr) to 3.4 bps (10-yr) higher. The US yield curve bear steepens with yields 3.3 bps (2-yr) to 4.7 bps (10-yr) higher. On intra-EMU bond markets, 10-yr yield spread changes versus Germany widened up to 3 bps with Portugal underperforming (+27 bps), perhaps in the run-up to tomorrow's rating decision by S&P (BB+, stable outlook).

US production and consumer sentiment in focus

The EMU calendar contains only second tier reports which won't affect markets. The US production and Michigan consumer sentiment data have some, albeit modest, market moving potential. US industrial production is expected to have rebounded in February (0.2% M/M) following a weather-related 0.3% M/M drop in January. Also this month, manufacturing output (0.5% M/M) is expected to outperform overall production, as utility output again lagged. Mining should be a positive as the number of active drilling rigs continued to recover. We have no reasons to distance ourselves from consensus. Michigan consumer sentiment is expected to have increased slightly in March to 97 from 96.3. Strong labour market, strong equities and lower gasoline prices are favourable for sentiment to improve with strong risks on the upside of consensus. Our expectation is underpinned by some outperformance of the Bloomberg and Conference board measures of confidence.



Bund future (black) & S&P future (orange) (intraday): Bunds slides lower in the morning and in late evening (Nowotny comments)



US 2-yr yield rebounds after touching key yield support at 1.30%. Suggesting post-FOMC move was one off?

Consolidation ahead of the weekend?

| | | |
|-------------|---------------|--------------|
| R2 | 164.40 | -1d |
| R1 | 163.12 | |
| BUND | 159.36 | -0.94 |
| S1 | 158.28 | |
| S2 | 157.28 | |

Overnight, most Asian stock markets trade positive with China and Japan underperforming. The Bund lost ground after European trading and is expected to open lower. Comments by ECB Nowotny, who said that the ECB doesn't necessarily have to follow the Fed's example when normalizing policy, inflicted some damage. However, we don't expect the comments to harm Bunds all day long. The US Note future trades marginally higher.

Today's eco calendar only contains US industrial production and Michigan consumer confidence, but we don't expect them to impact trading much. Consolidation ahead of the weekend is likely. Technically, US yields failed to break key resistance levels in the run-up to the Fed-meeting and suffered a significant setback afterwards. **We expect the US 10-yr yield to trade in the 2.3%-2.64% range, perhaps even until after the French elections. In the near-term, the US Note future probably has more upward potential. Longer term, we keep our scenario of 4 rate hikes in 2017 unchanged.**

Last week's ECB meeting and Bund sell-off comforted our call that another "calibration" of the ECB's QE programme will happen in H2 2017. Therefore, we have a long term bearish view on Bunds as well. Technically, the German 10-yr yield moved at a rapid pace from the 0.2% lower bound of the sideways range towards the 0.5% upper bound, but a break didn't occur. **Like in the US, we expect range trading ahead of the French elections.**



German Bund: Sell-off after ECB meeting halts.



US Note future: Fed less hawkish than markets expected. Downside protected ahead of French elections?

Currencies

Dollar stabilizes after post-Fed setback

Euro jumps on hawkish comments from ECB's Nowotny

| | | |
|---------|--------|--------|
| R2 | 1.1145 | -1d |
| R1 | 1.0874 | |
| EUR/USD | 1.0779 | 0.0045 |
| S1 | 1.0341 | |
| S2 | 1.0000 | |

USD/JPY fails to rebound after post-FOMC correction

EUR/USD trades at one month high

Eco calendar is moderately interesting

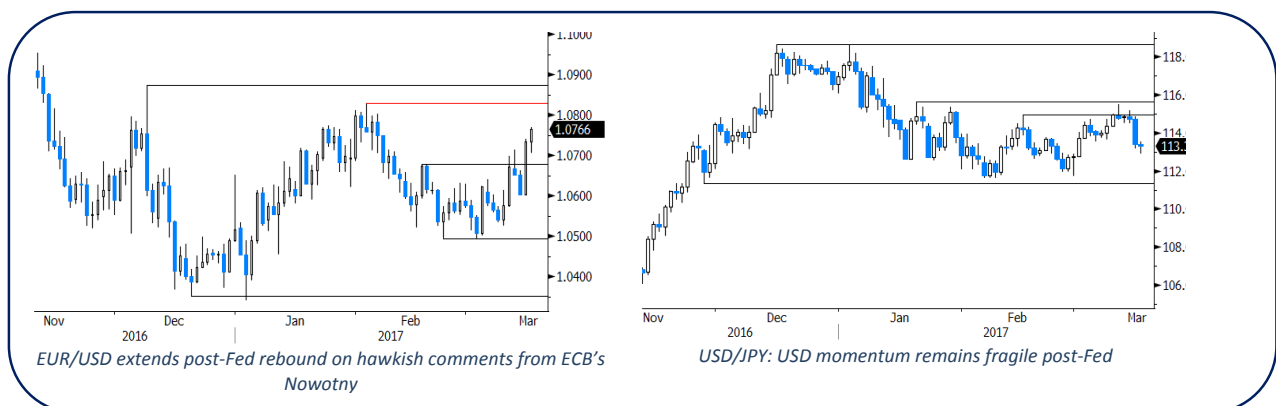
EUR/USD the test resistance in the 1.0829/74 area

Euro extends gains on Nowotny comments

Yesterday, the dollar initially stabilized versus euro and yen, following substantial losses in the aftermath of the FOMC decision. European equities started strongly, but gave back half of the initial gains. So, no full-blown risk-on session. Late in the session, the euro was propelled by comments ECB's Nowotny who said rates could be raised before the end of the APP. The comments were soon dismissed by ECB's Praet, but the euro maintained its gains. EUR/USD closed the session at 1.0766 (from 1.0734). The swings in USD/JPY were much more modest. USD/JPY finished the session at 113.31 (from 113.38).

Overnight, Asian equities are mostly slightly higher. Post-Fed dollar correction and expectations that Fed policy normalisation will continue in a very gradual way is supporting regional equities ex-Japan. USD/JPY is holding yesterday's post-Fed consolidation pattern (lower half of the 113 big figure). EUR/USD maintains the gains recorded on the Novotny comments and trades in the 1.0775 area, near a one month high.

Today, there are only second tier eco data in Europe. In the US, production and Michigan consumer sentiment have some market moving potential. US February industrial production is expected to have rebounded (0.2% M/M) following a weather-related 0.3% M/M drop. Michigan consumer sentiment is expected slightly higher at 97 from 96.3. A strong labour market, strong equities and lower gasoline prices support sentiment. So, we see upside risks. Yesterday, the dollar stabilised after the post-Fed correction, but failed to regain ground. On the contrary, the US currency lost further ground against euro as markets ponder the chances of an early change in the ECB policy. In a longer term perspective, policy divergence between the Fed and the ECB will probably remain big enough to support further USD gains. Yellen suggested that, considering the eco developments, the Fed policy might be relatively close to the 'dot-path'. The day-to-day USD momentum remains soft though and the euro is in better shape. So we look out/wait for strong enough US data that might put a floor on the current USD correction. Interesting to see whether a strong consumer confidence can help this process.



Global context. EUR/USD 1.0874 resistance remains the line in the sand with intermediate resistance at 1.0829. We maintain the view that a sustained break of EUR/USD above this area will be difficult, even after Wednesday's Fed message. The US/German (EMU) interest rate differential remains at an absolute

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high level. Especially at the short end of the curve, the differential might even re-widen. **The fundamentals/ interest rate differentials are also supportive for USD/JPY, but of late the momentum/technical picture is not really convincing. We maintain the working hypothesis that the 111.60 range bottom should hold.**

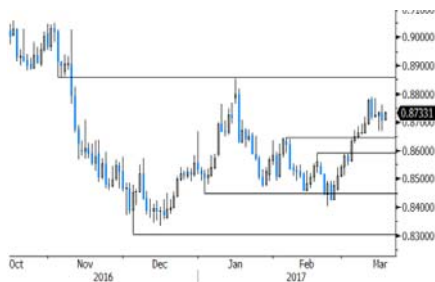
| | | |
|---------|--------|---------|
| R2 | 0.8881 | -1d |
| R1 | 0.8854 | |
| EUR/GBP | 0.8716 | -0.0023 |
| S1 | 0.8592 | |
| S2 | 0.8304 | |

EUR/GBP: Balance of sterling rebound and euro strength

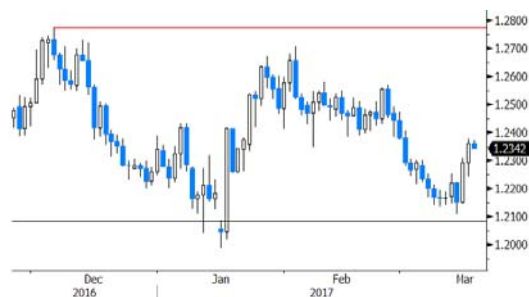
EUR/GBP and cable held very tight ranges yesterday as investors awaited the BoE's policy decision. The BoE as expected left its policy unchanged. However, Kristin Forbes dissented in favour of a rate hike and the Minutes contained **a note of concern on inflation.** "Some members noted that it would take relatively little further upside news on the prospects of activity or inflation for them to consider that a more immediate reduction in policy support might be warranted." **This took sterling traders awry and triggered some frenetic sterling buying.** EUR/GBP dropped from 0.8740 to about 0.8680/70. Later in the session, EUR/GBP regained some ground on the Nowotny comments. EUR/GBP closed the session at 0.8710 (from 0.8732). The combination of USD softness and GBP strength propelled cable to close the session at 1.2360 (from 1.2291).

There are no important eco data in the UK today. Both sterling and the euro were in good shape yesterday. This balance might persist and some EUR/GBP consolidation might be on the cards. Despite yesterday's somewhat more hawkish BoE approach, we don't see a real risk for BoE tightening anytime soon. So, any rebound of sterling shouldn't go too far.

Over the previous day, the decline of sterling took a breather. EUR/GBP **cleared 0.8592 resistance, improving the MT technical EUR/GBP picture.** We don't expect a sustained EUR/USD rebound, but a combination of temporary euro consolidation and ongoing sterling softness, as the Brexit negotiations are nearing, might trigger some more ST EUR/GBP gains. The 0.8854 correction top is the next key resistance. The nervous swings over the previous days suggest that a clear break beyond 0.8854 will be difficult without important (UK negative) news.



EUR/GBP: euro strength and sterling rebound keeping each other in balance



GBP/USD: rebounds on sterling strength and USD softness

Calendar

| Friday, 17-March | | Consensus | Previous |
|------------------|--|-----------|------------|
| US | | | |
| 14:15 | Industrial Production MoM (Feb) | 0.2% | -0.3% |
| 14:15 | Capacity Utilization (Feb) | 75.5% | 75.3% |
| 14:15 | Manufacturing (SIC) Production (Feb) | 0.5% | 0.2% |
| 15:00 | U. of Mich. Sentiment (Mar-P) | 97.0 | 96.3 |
| 15:00 | U. of Mich. Current Conditions (Mar-P) | 111.0 | 111.5 |
| 15:00 | U. of Mich. Expectations (Mar-P) | 87.1 | 86.5 |
| 15:00 | U. of Mich. 1-Yr Inflation (Mar-P) | -- | 2.7% |
| 15:00 | U. of Mich. 5-10 Yr Inflation (Mar-P) | -- | 2.5% |
| EMU | | | |
| 11:00 | Trade Balance SA (Jan) | 22.0b | 24.5b |
| 11:00 | Construction Output MoM / YoY (Jan) | --/-- | -0.2%/3.2% |
| France | | | |
| 08:45 | Wages QoQ (4Q-F) | 0.1% | 0.1% |
| Belgium | | | |
| 15:00 | Consumer Confidence Index (Mar) | | |
| Events | | | |
| | G-20 meeting in Baden-Baden | -- | -2 |

| 10-year | td | -1d | | 2-year | td | -1d | | Stocks | td | -1d |
|------------|--------|---------|------|------------|---------|---------|--|-------------|----------|--------|
| US | 2.53 | 0.04 | | US | 1.33 | 0.03 | | DOW | 20934.55 | -15.55 |
| DE | 0.47 | 0.08 | | DE | -0.79 | 0.03 | | NASDAQ | 5900.76 | 0.71 |
| BE | 0.94 | 0.04 | | BE | -0.48 | 0.03 | | NIKKEI | 19521.59 | -68.55 |
| UK | 1.25 | 0.04 | | UK | 0.08 | 0.04 | | DAX | 12083.18 | 73.31 |
| JP | 0.08 | 0.01 | | JP | -0.26 | 0.01 | | DJ euro-50 | 3439.96 | 30.64 |
| | | | | | | | | | | |
| | | | | | | | | | | |
| IRS | EUR | USD | GBP | EUR | -1d | -2d | | USD | td | -1d |
| 3y | 0.04 | 1.87 | 0.72 | Eonia | -0.3540 | 0.0000 | | | | |
| 5y | 0.30 | 2.14 | 0.89 | Euribor-1 | -0.3710 | 0.0000 | | Libor-1 | 0.9428 | 0.0145 |
| 10y | 0.89 | 2.49 | 1.26 | Euribor-3 | -0.3290 | 0.0000 | | Libor-3 | 1.1482 | 0.0108 |
| | | | | Euribor-6 | -0.2410 | 0.0000 | | Libor-6 | 1.4382 | 0.0058 |
| | | | | | | | | | | |
| | | | | | | | | | | |
| Currencies | td | -1d | | Currencies | td | -1d | | Commodities | td | -1d |
| EUR/USD | 1.0779 | 0.0045 | | EUR/JPY | 122.16 | 0.56 | | CRB | 184.04 | 0.25 |
| USD/JPY | 113.32 | 0.04 | | EUR/GBP | 0.8716 | -0.0023 | | Gold | 1227.40 | 1.00 |
| GBP/USD | 1.2368 | 0.0085 | | EUR/CHF | 1.0739 | 0.0020 | | Brent | 51.73 | -0.46 |
| AUD/USD | 0.769 | -0.0005 | | EUR/SEK | 9.4997 | -0.0183 | | | | |
| USD/CAD | 1.3316 | 0.0020 | | EUR/NOK | 9.1571 | 0.0400 | | | | |

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