



**Tuesday, 25 February 2020**

### Rates: Exhaustion move on bond market?

Fear of the spreading coronavirus hurt risk sentiment badly yesterday with core bonds profiting. US Treasuries significantly outperformed German Bunds with the US 10-yr yield near the all-time low. Tensions ease this morning with bonds off yesterday's best levels. Corona sentiment remains key, but can we label yesterday's price action as an exhaustion move?

### Currencies: Loss of interest rate support weighs on USD despite risk-off

Yesterday, the dollar underperformed against the euro and the yen. The sharp decline in interest rate support reduced the safe haven appeal of the US currency. The decline in US yields can't go on at the same pace. As such, the USD decline might slow too. That said, the dollar might enter a more neutral trading pattern after recent strong gains.

### 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	↔

- **WS** printed the biggest slide in 2y as a surge in corona cases outside China rattled investors. The Nasdaq underperformed (-3.71%). The selloff in **Asia** is slowing with Japanese equities plunging (-3.22%) in catch-up mode.
- **The head of the WHO** said although an increase in the number of cases outside of China is "deeply concerning", it is **still too early to label the infectious coronavirus a pandemic** but countries should be "in a phase of preparedness".
- **Trump's administration is asking Congress for \$2.5bn in supplemental funding to battle the fast-spreading coronavirus.** The funds would be deployed to develop, manufacture and distribute vaccines and treatments for US patients.
- **The Fed's Mester asserted although the coronavirus epidemic** poses a threat to the US economy, it **doesn't yet justify any shift in monetary policy** as it is still difficult to assess the magnitude of the economic consequences.
- **Saudi Arabia's energy minister Bin Salman disclosed OPEC hasn't decided yet on whether to extend or modify its deal on output cuts** as oil prices continue to grind lower amid intensified growth concerns.
- **The PBOC will consider new measures to battle the coronavirus epidemic** e.g. lenders will be encouraged to special loan quotas in a bid to step up support to the real economy, Bloomberg reported citing a central bank official.
- **Today's economic calendar** contains US/French confidence data. A speech from Fed's Clarida is due. Hungary decides over monetary policy. The UK, US, Italy tap the bond market. Spain is likely to issue a new 30y bond.

# Rates

## Exhaustion move on core bond market?

	US yield	-1d
2	1.25	-0.11
5	1.24	-0.11
10	1.37	-0.10
30	1.86	-0.08

	DE yield	-1d
2	-0.67	-0.04
5	-0.66	-0.05
10	-0.48	-0.05
30	0.00	-0.05

The start of the new trading week was a rude awakening for investors. The rapid spreading of the coronavirus outside China triggered pandemical fears and caused full-blown risk aversion across markets. Core bonds profited from the safe haven bids. US yields declined by 8 bps (30-yr) to 11.4 bps (5-yr). The US 30-yr yield set a new all-time low with 5- and 10-yr tenors dropping below the 2019 bottoms. Markets now discount a June rate cut, but that's not what officials are hinting at right now. Voting Cleveland Fed governor Mester joined ranks of those who believe that the US economy remains in a good place while admitting that the corona outbreak serves as a downside risk. She endorsed Fed's Brainard proposal to shift to flexible inflation averaging. German yields lost 3 bps (2-yr) to 5 bps (10-yr) in a daily perspective. The German 30-yr yield turned negative for the first time since October with the 10-yr yield dropping below -0.41%/-0.44% intermediate support. 10-yr yield spread changes vs Germany widened by 3 bps with Greece and Italy (+11 bps) underperforming. Other winners yesterday included gold (highest level since 2013) and JPY while stock markets (US: -3.5%; Europe: -4%) and oil prices were on the losing side of the equation.

Asian stock markets recover slightly from yesterday's beating apart from Japan's catch-up move returning from a long weekend (-3%). Other markets find breathing space as well after yesterday's sharp repositioning which could suggest we might end up labelling them as an exhaustion move on the bond market. Core bonds are off yesterday's best levels. Today's eco calendar contains US consumer confidence and Richmond Fed manufacturing index. We don't expect February US confidence already to be negatively impacted by corona while the Richmond Fed gauge could show a similar positive sign as measures for the NY and Philadelphia regions did earlier. So overall, we expect US eco data to be decent/good. Speeches by Fed Clarida and ECB Hernandez de Cos serve as wildcards while the US, Italy and Spain (30-yr syndication?) tap the bond market.

**Technically:** core bond yields failed to take out resistance levels at the start of the year, at -0.18% (July high)/-0.15% (38% retracement of Feb '18 – Sep '19 decline) for the German 10-yr yield and 1.94% for the US 10-yr yield. The Chinese coronavirus took markets hostage via risk aversion, pulling core bond yields below first support. The Chinese return to trading after Lunar NY holidays temporary ended the decline since mid-January, but the rapid spreading outside of China caused fresh stress across markets. The US 10-yr yield arrived at key 1.43%. The German 10-yr yield dropped below -0.41%/-0.44%.



German 10-yr yield below intermediate support at: -0.41%/-0.44%



US 10-yr yield nears all-time low (1.32%)

# Currencies

## Loss of interest rate support weighs on USD

R2	1.1199	-1d
R1	1.0864	
<b>EUR/USD</b>	<b>1.0854</b>	<b>0.0007</b>
S1	1.0778	
S2	1.0581	

R2	0.8798	-1d
R1	0.8676	
<b>EUR/GBP</b>	<b>0.8396</b>	<b>0.0025</b>
S1	0.8275	
S2	0.8117	

The corona risk-off guided global FX yesterday, but **parts of the market deviated from the standard script**. Most striking, the **dollar was in the defensive**. The sharp decline in US yields reduced its relative safe haven appeal. The decline in USD/JPY wasn't that surprising (close 110.72 from 111.61), but the USD also lost (modest) ground against the euro (1.0854 from 1.0847), which is in bad shape of late, as the Fed has much more room to cut rates than the ECB. Other risk-off repositioning was mostly in line with the standard script. **Smaller, less liquid currencies** suffered. **The Swiss franc** touched strongest level since 2015 against the euro, but EUR/CHF rebounded on suspected SNB interventions (close 1.0625).

**This morning**, Japan has to catch up on yesterday's sell-off as it reopens after a holiday. The sell-off on Chinese markets slows. Korea rebounds and US equity futures also try a comeback after yesterday's steep losses.

**The yuan is trading slightly stronger (USD/CNY 7.0150)**. The dollar also bottoms is line with US yields (USD/JPY 110.80 area; EUR/USD 1.0850).

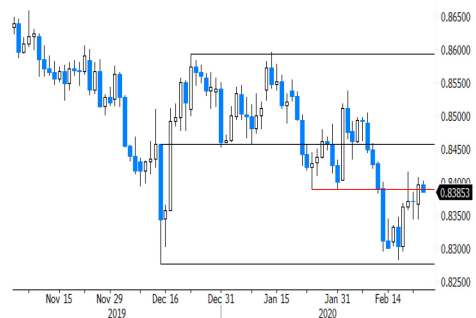
**Today**, French business confidence and the details of German Q4 growth are on the agenda. In the US, consumer confidence (Conf. board) will be published. Data will probably be overshadowed by the corona-driven market dynamics. There might be an asymmetric risk for US consumer confidence, with the **dollar being vulnerable to a negative surprise**.

**Yesterday**, the USD struggled against other majors on the sharp decline in US yields. The latter can't continue at the same pace even if markets maintain the view that the Fed will likely be forced to step in. Yesterday, we advocated that some more **erratic (neutral) trading pattern in the likes of EUR/USD or USD/JPY as the corona story develops**. Considering yesterday's price action, we maintain that assessment. The **EUR/USD** technical picture **deteriorated substantially** of late, but the 1.0778 level survived. It's too early to call of the EUR/USD alert, but the pressure is easing, at least temporarily.

Yesterday, **sterling slightly underperformed both against the dollar and the euro**. The risk-off and uncertainty on the UK-EU trade talks weighed on the UK currency. The market again anticipates BoE rate cut later this year to counterbalance the potential economic fall-out of corona. Today, the CBI retail data are expected solid, but we don't expect them to change fortunes for the sterling. The ERU/GBP 0.8276 is a solid support. We expect more consolidation in the 0.8350/0.8450 range.



EUR/USD rebounds off 1.0778 support as dollar 'suffers' loss of interest rate support.



EUR/GBP: 0.8276 proves to be tough resistance for sterling.

# Calendar

Tuesday, 25 February		Consensus	Previous
<b>US</b>			
15:00	House Price Purchase Index QoQ (4Q)	--	1.10%
15:00	FHFA House Price Index MoM (Dec)	0.40%	0.20%
15:00	S&P CoreLogic CS 20-City MoM SA/YoY (Dec)	0.41%/2.80%	0.48%/2.55%
<b>16:00</b>	<b>Conf. Board Consumer Confidence (Feb)</b>	<b>132.1</b>	<b>131.6</b>
16:00	Conf. Board Expectations (Feb)	--	102.5
16:00	Conf. Board Present Situation (Feb)	--	175.3
16:00	Richmond Fed Manufact. Index (Feb)	10	20
<b>Japan</b>			
00:50	PPI Services YoY (Jan)	2.30%A	2.10%
<b>UK</b>			
12:00	CBI Retailing Reported Sales (Feb)	3	0
12:00	CBI Total Dist. Reported Sales (Feb)	10	11
<b>Germany</b>			
08:00	GDP SA QoQ/WDA YoY (4Q F)	0.00%/0.40%	0.00%/0.40%
<b>France</b>			
08:45	Business Confidence (Feb)	103	104
08:45	Manufacturing Confidence (Feb)	99	100
08:45	Production Outlook Indicator (Feb)	-6	-5
<b>Events</b>			
25FEB	Spain is likely to issue new 30y bond		
25FEB	World Bank President Malpass delivers a speech at NABE conference		
09:00	ECB's Hernandez de Cos speaks in Madrid		
11:00	Italy to Sell Bonds		
19:00	US to Sell USD40 Bln 2-Year Notes		
<b>21:15</b>	<b>Fed's Clarida Speaks at NABE Conference in Washington</b>		

10-year	Close	-1d		2-year	Close	-1d		Stocks	Close	-1d
US	1.37	-0.10		US	1.25	-0.11		DOW	27960.8	-1031.61
DE	-0.48	-0.05		DE	-0.67	-0.04		NASDAQ	9221.28	-355.31
BE	-0.24	-0.03		BE	-0.61	-0.02		NIKKEI	22605.41	-781.33
UK	0.54	-0.03		UK	0.41	-0.11		DAX	13035.24	-544.09
JP	-0.10	-0.04		JP	-0.19	-0.03		DJ euro-50	3647.98	-152.40
IRS	EUR	USD	GBP	EUR	-1d	-2d		USD	-1d	-2d
3y	-0.38	1.21	0.64	Eonia	-0.4540	0.0000		Libor-1	1.6268	0.0000
5y	-0.34	1.20	0.64	Euribor-1	-0.4770	0.0010		Libor-3	1.6793	0.0000
10y	-0.14	1.30	0.69	Euribor-3	-0.4140	0.0010		Libor-6	1.6748	0.0000
				Euribor-6	-0.3570	-0.0010				
Currencies	Close	-1d		Currencies	Close	-1d		Commodities	Close	-1d
EUR/USD	1.0854	0.0007		EUR/JPY	120.19	-0.80		CRB	170.57	-4.08
USD/JPY	110.72	-0.89		EUR/GBP	0.8396	0.0025		Gold	1676.60	27.80
GBP/USD	1.2924	-0.0040		EUR/CHF	1.0625	0.0009		Brent	56.30	-2.20
AUD/USD	0.6605	-0.0022		EUR/SEK	10.5645	0.0253				
USD/CAD	1.3293	0.0068		EUR/NOK	10.156	0.0933				

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