19 December 2018

Danske Daily

Trade talks still on track

Market movers today

- **All eyes will be on the FOMC meeting tonight**. It hasn't become less exciting after the recent market rout and US President Donald Trump's frequent expressions of clear dissatisfaction with the rate hikes. Despite the recent decline in US stocks a rate hike is widely expected. Focus will instead be on the Fed's projections (the dot plot) for 2019 and the language in the statement. The market is currently priced for less than one hike next year, and even if the Fed softens the rate path and the language, we believe they will be perceived as hawkish compared to market pricing. See also *FOMC Preview – Fed set to hike again but removing more forward guidance*, 14 December 2018.
- In the **UK** inflation for November is expected to decline slightly from 2.4% to 2.3% (consensus). On core inflation consensus is a decline to 1.8% y/y from 1.9% y/y in October.
- **Sweden** releases confidence indicators for both consumers and businesses, see page 2.
- The **Bank of Japan** ends its two-day monetary policy meeting early Thursday morning European time. We expect the Bank of Japan to keep its 'QQE with yields curve control' policy unchanged.

Selected market news

US stock markets stabilised yesterday and closed with minor gains after past days' sell-offs. Trading is mixed in Asia this morning as investors await the FOMC tonight.

The oil price dropped substantially yesterday and Brent oil touched USD 56/bbl for the first time since October 2017. The decline in the oil price appears to be driven by a combination of supply and growth concerns. The latter clearly also represents a supporting factor for the rally in global fixed income markets where the 10-year US Treasury yield declined 4bp yesterday to the lowest close since May at 2.807%, while the 10-year Japanese government bond yield has dropped to around 0.01% this morning.

The Italian government has made a deal with the EU Commission on the budget for 2019. The new budget reduces the deficit to 2.04% and according to Italian officials there has been a technical agreement on the budget. We still need an official statement from the EU Commission, but that should come today. This leaves room for more convergence between Italy and the core-EU markets.

US Treasury Secretary Steven Mnuchin last night said that the US and China are planning to hold trade talks in January in order to try to make an agreement before the current tariff truce runs out on 1 March next year. We continue to look for a deal between the US and China within next 3-6 months. See *China Weekly Letter - Improvement in Trade War, deterioration in Tech War* (14 December).

Selected reading from Danske Bank

- *FOMC Preview - Fed set to hike again but removing more forward guidance*
- *FX Strategy - NOK year-end weakness creates opportunities for 2019*
- *Finland Research: Shakier outlook into election year 2019*
- *Euro Area Research: Is the Phillips curve finally coming alive in 2019?*
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Scandi markets

Sweden: Todays' business and consumer confidence surveys by the NIER are among the last macro data from Sweden before year end. Not a significant market mover in itself, but it will still be interesting to see whether it points towards weaker sentiment for the third month in a row, and particularly whether consumer confidence continues to weaken. There are quite substantial differences across industries. What's holding up the ETI is manufacturing when the confidence indicator at 115 remains not very far from highs? Manufacturers reported very favourable order backlogs, and strong performance for production volumes. Other industries are now lagging behind. Construction has of course experienced a downturn and business conditions for services producers appear to have moderated as well.

Other than this, the never-ending story of government-formation lingers on, where the Speaker is expected to give notice whether we will have a third PM-vote before or (more probable) after the Christmas break.

Fixed income markets

As the oil price continues to decline and the economic data is on the soft side combined with plenty of Brexit uncertainty, then there is not much holding German government bonds back from a continued rally other than valuation and modest liquidity. Furthermore, the supply of German government bonds will increase next year as German government earlier on Tuesday published their funding outlook for 2019. There will be an increase in the funding as the government is taking over the funding need 'due to the German government is funding FMS Wertmanagment through German government bonds'. This raises the funding by EUR 20bn (only bonds, no linkers) to EUR 156bn.

Tonight we get statement from the FOMC. A rate hike is priced in and thus focus it will be the 'forward guidance'. We expect that 2-3 hikes will come in 2019, and thus the US yield curve will continue to flat or invert in this case.

FX markets

In focus for USD today will clearly be the Fed. In light of recent softness in pricing, we see risks titled towards a hawkish surprise. That said, we stress that a key risk is that the so-called 'dots' are lowered further out which could be seen as somewhat dovish. But, all in all, we see risks for some USD support here as Fed confirms it is determined to get to 'neutral'. EUR/USD remains stuck in the 1.13 range near term as carry and cyclical divergence counter EUR backing from ECB 'normalisation' but risks into Fed are tilted to the downside.

In the Scandies, the NOK has seen a horrible start to the week with heavy selling both Monday and Tuesday. In the short term we are left with heightened volatility, thin Christmas markets and very wide ranges. Much of the NOK weakness in recent sessions has been driven by NOK/SEK selling. In that light, we identify key levels to be 1.0368 (support) and 1.0475 (resistance). For EUR/NOK, we look for 9.9939 (resistance) and 9.8046 (support). That said we still recommend investors to look for signs of stabilisation in order to enter or increase NOK longs. For more information see *FX Strategy. NOK year-end weakness creates opportunities for 2019*.

EUR/DKK crept higher again yesterday fixing at 7.4675. Since 1999, EUR/DKK has fixed at 7.4670 or higher on only 20 days and on 13 of them Danmarks Nationalbank (DN) bought DKK in FX intervention. In addition, EUR/DKK FX forward outright is now trading above the 7.46038 central rate out to around 6M – another rare situation. EUR/DKK will likely continue to trade at elevated levels until we see risk sentiment in financial markets turn around for the better. That remains our view for 2019 and where we stick to our view that EUR/DKK will fall to 7.4550 in 6-12M.

Key figures and events

Wednesday, December 19, 2018				Period	Danske Bank	*Consensus*	Previous
9:00	SEK	Consumer confidence	Index	Dec			97.5
9:00	SEK	Economic Tendency Survey	Index	Dec			106.7
9:00	SEK	Manufacturing confidence	Index	Dec			116.2
9:15	SEK	NIER economic forecasts					
10:30	GBP	PPI - input	m/m|y/y	Nov		*1.6%|6.2%*	0.8%|10.0%
10:30	GBP	CPI	m/m|y/y	Nov		*0.2%|2.3%*	0.1%|2.4%
10:30	GBP	CPI core	y/y	Nov		*1.8%*	1.9%
14:30	USD	Current account	USD bn	3rd quarter			-101.5
14:30	CAD	CPI	m/m|y/y	Nov			...|2.4%
16:00	USD	Existing home sales	m (m/m)	Nov		*5.2*	5.22|0.014
16:30	USD	DOE U.S. crude oil inventories	K				-1208
20:00	USD	FOMC meeting	%		**2.50%**	*2.50%*	2.25%
20:30	USD	FOMC press conference					
22:45	NZD	GDP	q/q|y/y	3rd quarter		*0.6%|2.8%*	1.0%|2.8%

Source: Bloomberg, Danske Bank

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