



Sunset

Wednesday, 15 February 2017

Headlines

- **Most European equity markets eke out some gains, but US stock markets for the first time have difficulties to continue their record race on stronger than expected US eco data. Tightening fears taking over?**
- **US consumer prices beat expectations and recorded their biggest increase in nearly four years in January**, rising 0.6% m/m and 2.5% y/y. The **so-called core CPI**, which strips out food and energy costs, rose 0.3% last month, lifting it to **2.3 % y/y in January**.
- US **Retail sales notched up better than expected growth last month (0.4% vs 0.6% expected)**, marking the fifth consecutive month of higher consumer spending. December retail sales were upwardly revised from 0.6% m/m to 1% m/m. **The US empire manufacturing unexpectedly improved to 18.7** in February, the highest level since Oct2014.
- **UK unemployment declined and a measure of the number of people in work rose to a record**, pushing the labour market closer to "full capacity". Despite the increase in employment, and labour shortages in some areas, **that's not being fully reflected in wages**. Basic pay growth slowed to 2.6% from 2.7%, weaker than forecast.
- **US industrial production slightly disappointed in January, the only demerit to today's strong batch of US eco data**. They declined by 0.3% m/m, from a downwardly revised 0.6% m/m in December. Manufacturing production rose in line with expectations, by 0.2% m/m.
- **Sweden's central bank** held its benchmark interest rate at -0.50% and its QE programme unchanged, but **indicated that it could loosen policy further if necessary**. *"The Executive Board is still prepared to make monetary policy more expansionary if the upward trend in inflation were to be threatened and confidence in the inflation target weakened"*.
- **US defence secretary James Mattis has said Nato is a "fundamental bedrock" for Washington**, as he pushes to reassure allies about Donald Trump's commitment to the organisation.
- **The EU and Canada secured clearance for their contentious free trade deal** and the removal of import duties that supporters say will boost growth and jobs on both sides of the Atlantic.

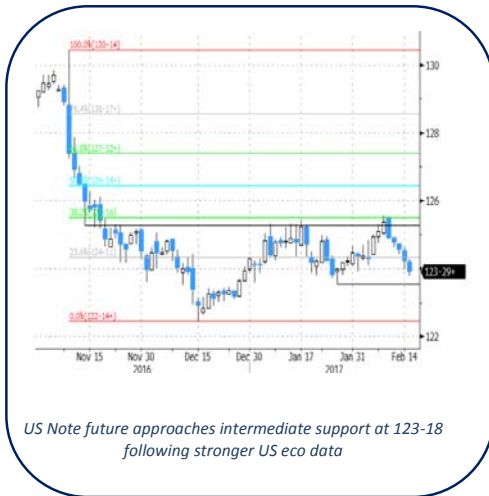
Rates

Strong data deal US Treasuries another blow

Global core bonds suffered another blow following strong US eco data. The combination of yesterday's Yellen comments and today's data pushed the odds of a March rate hike from 28% to 42%. US Treasuries underperformed German Bunds. The US Note future approaches intermediate support at 123-18. **At the time of writing**, the US yield curve shifts 1.6 bps (2-yr) to 4.2 bps (5-yr) higher. The German yield curve bear steepens with yields 0.8 bps (2-yr) to 3.1 bps (30-yr) higher. **On intra-EMU bond markets**, 10-yr yield spread changes versus Germany ranged between -3 bps and +3 bps with Greece underperforming (+22 bps). Greek bonds suffered as Eurogroup Dijsselbloem said yesterday evening that talks between Greece and its creditors have **not**

sufficiently progressed to reach an agreement at the February 20 Eurogroup meeting. Italy marginally suffered as people familiar with the matter said that former PM Renzi is pushing for September elections.

Intraday, trading was confined to narrow ranges in European dealings amid an empty calendar. **Dynamics changed in US dealings as US headline and core inflation unexpectedly rose further above the Fed's 2%-target.** On top, **retail sales continued their positive run** at the start of the year with an upward revision to the December numbers. **An impressive surge of the February empire manufacturing survey**, to the highest level in more than 2 years, was the icing on the cake. The US Note future lost more ground with Trump's "phenomenal" fiscal stimulus plans and Yellen's warning (don't wait too long to hike rates) in mind. Rate markets aligned further with the Fed's scenario of 3 rates hikes in 2017 and even start to attach a decent chance to a March move (42%). **US industrial production slightly disappointed** and was the demerit to today's eco releases. Later today, Fed chairwoman Yellen holds her second testimony, this time in the US House of Representatives. Will lawmakers ask specifically to the possibility of a March tightening?



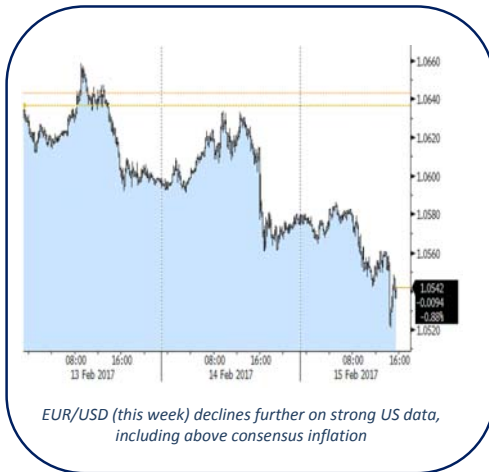
Currencies

Dollar extends gains on very strong US data

Today, the dollar stayed well bid in Europe, building on yesterday's post-Yellen gains. The dollar rally accelerated early in the US as the US data (Empire Manufacturing, CPI and retail sales) all came out much stronger than expected, but some profit taking kicked in going into the US equity market opening. USD/JPY trades in the 114.60/70 area. EUR/USD changes hands in the 1.0550/60 area.

Overnight, Asian equity markets joined yesterday's post-Yellen rally. Japanese stocks profited from the decline of the yen and outperformed. USD/JPY traded in the 114.35 area. In Parliament, PM Abe said that president Trump acknowledged that monetary policy tries to end deflation and is not FX manipulation. The PBOC strengthened the fixing of the yuan to USD/CNY 6.8632, despite overall USD strength, indicating that the PBOC aims to tighten monetary policy. EUR/USD hovered in the 1.0580 area, near yesterday's closing levels.

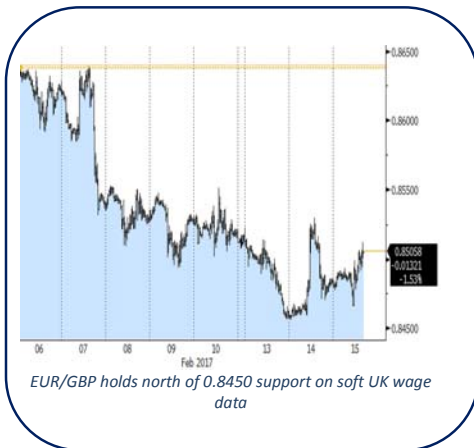
There was little in the way of a EMU specific story today. Risk sentiment remained constructive in line with the US yesterday and Asia this morning. **Core yields preserved yesterday's gains and so did the dollar.** USD/JPY basically hovered sideways in the mid 114 area. The dollar gained slightly further ground against the euro. EUR/USD touched an intraday low in the 1.0543 area, but the decline slowed later in the European morning session. The EUR/USD price pattern still suggests some underlying euro softness even as we didn't see any additional EMU negative headlines. Maybe uncertainty on Greece weighed slightly (Greek spreads widened again).



The early morning US data were very strong with retail sales, the empire manufacturing survey and inflation all beating consensus by a substantial margin. Especially the rise in inflation caught the eye with January headline inflation at 2.5% Y/Y and core inflation at 2.3% Y/Y. US yields/yield differentials and the dollar jumped higher. EUR/USD dropped to the 1.0521 area. USD/JPY jumped to the high 114 area. However, the USD rally slowed going into the US equity market opening and ahead of Fed's Yellen Testimony before the House. EUR/USD trades currently in the 1.0550/60 area. USD/JPY changes hands in the 114.60/70 area. The gradual, but protracted USD rebound continues.

Sterling declines slightly after soft UK wage data

Yesterday, UK price data painted a mixed picture, but sterling reacted to a softer than expected CPI. **Today, the reaction to the labour data was a bit similar.** The jobless claimed declined sharply and job creation in the 3 months to December printed at a stronger than expected 37K. So, the UK labour market remains solid. Even so, wage growth disappointed and slowed from 2.8% Y/Y to 2.6% Y/Y. The market reacted to the price signals rather than to the activity data. EUR/GBP was slightly under pressure this morning as the decline of EUR/USD weighed. Sterling lost some ground after the UK labour data. EUR/GBP revised the 0.85 area, but the move had no momentum and petered out very soon. Later in the session the strong US data pressured cable (high 1.23 area). However contrary to what was often the case of late, **there was no negative fall-out from EUR/USD on EUR/GBP. EUR/GBP trades currently in the 0.8505/10 area within reach of the intraday top. So, the 0.8450 support area looks 'safe' for now'.**



16:00 CET

Daily EMU spread changes (bps)

	5-yr			10-yr			30-yr		
	Yield	Spread	Change	Yield	Spread	Change	Yield	Spread	Change
Germany	-0,41%			0,38%			1,20%		
Greece (2-10-20)	9,93%	1034	58,8	7,79%	741	22,4	8,13%	693	11,8
Portugal	1,93%	234	0,0	4,09%	371	3,2	5,02%	383	0,8
Italy	0,91%	133	-0,5	2,25%	186	-0,3	3,38%	219	-2,8
Spain	0,30%	71	-1,4	1,68%	130	-0,5	3,02%	183	-0,6
Ireland (4-10-30)	-0,23%	18	-0,4	1,10%	71	1,1	2,21%	102	0,8
Belgium	-0,08%	33	-0,8	0,89%	51	-2,7	1,93%	74	-1,0
France	0,11%	53	-1,6	1,05%	67	-1,7	2,11%	92	-1,3
Austria	-0,33%	8	-0,1	0,64%	26	-0,4	1,62%	42	0,5
Netherlands	-0,27%	15	-0,4	0,70%	32	-0,2	1,32%	12	-0,3
Finland	-0,36%	5	-1,5	0,56%	18	-1,7	1,32%	12	-1,4
US	1,99%	240	2,2	2,50%	212	1,5	3,09%	189	0,5
UK	0,50%	91	-2,0	1,30%	92	-2,3	2,01%	81	-2,0

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)		Prague	+420 2 6135 3535
Jan Cermak	+420 2 6135 3578		
Jan Bures	+420 2 6135 3574		
Petr Baca	+420 2 6135 3570		
Bratislava Research (CSOB)		Bratislava	+421 2 5966 8820
Marek Gabris	+421 2 5966 8809		
Budapest Research		Budapest	+36 1 328 99 85
David Nemeth	+36 1 328 9989		

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