Danske Bank

24 November 2017

Danske Daily

Market movers today

- In the US, Markit PMIs for November are due for release. The large gap between Markit and ISM manufacturing narrowed in October and we expect this trend to continue (driven by both variables). Hence, we estimate that Markit PMI rose to 55.6. We estimate the service index stayed around its current level of 55.3.

- German Ifo expectations figures are due for release today.

- In Japan, November PMI figures for the export-heavy manufacturing sector are due out on Friday. The manufacturing sector has looked solid for more than a year now with industrial production up 4.2% y/y and PMI just below 53.

- In Sweden, October retail sales follow today. In Sweden, PPI data is released at 09:30 CET.

Selected market news

It has been a relatively quiet session overnight on financial markets as the US celebrated Thanksgiving. The sell-off in Chinese equities which send the CSI 300 index 2.5% lower yesterday has lost steam and trading in Asian markets is rather mixed this morning as Japan returns from holiday. Chinese equity indices are still lower this morning, but the negative momentum has eased. In Japan, the large equity indices trade higher and USD/JPY sees some support and trades slightly higher.

The minutes from the ECB meeting on 26 October, released yesterday, revealed that 'several members' (probably Benoît Coeuré, Francois Villeroy and Jens Weidmann) favoured delinking the forward guidance on QE from the requirement of a sustained rise in inflation and instead link it to the overall monetary policy stance (new QE purchases, QE stock and reinvestments and forward guidance in policy rates). If that view is becoming more prominent in the Governing Council over coming months, it would open up the possibility for the ECB to end the QE programme in 2018, even without a clear pick-up in inflation.

The latest PMI surveys From Europe and Japan indicate that the global business cycle is likely to underpin growth in coming quarters: Yesterday, PMI surveys from France, Germany and the aggregate euro zone came out very strong and continue to paint an optimistic picture for growth in Europe in coming quarters. In Japan, the Nikkei manufacturing PMI index, released early this morning, rose to the highest level since March 2014 indicating that the manufacturing sector is likely to continue to support GDP growth.

Selected readings from Danske Bank

- *Research: What if Swedish Housing Prices Drop 15-20%?*

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Arne Lohmann Rasmussen on the prospects for the global bond markets

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Important disclosures and certifications are contained from page 4 of this report.

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Scandi markets

Sweden. PPI data due to be released at 09:30 CET. We have seen producer (and import) price inflation trending lower this year. The recent SEK depreciation should eventually prompt a turn around on import prices. For a discussion on this, see this week's Reading the Market Sweden, 23 November.

Fixed income markets

Yesterday, the Danish government put forward a new proposal for the funding of social housing loans, which has been agreed with the Danish mortgage banks. Earlier this year, the government proposed to move the funding from the Danish mortgage banks and back to the government, where they fund old and new social housing loans through the issuance of Danish government bonds in order to save on the margin paid to the mortgage banks as well as obtain lower funding costs. However, the proposal was met with a lot of critique, and thus the government has today put forward a new proposal for the funding of the social housing loans. We expect this proposal to be passed in the parliament given the agreement with mortgage banks.

Going forward the loans will remain with the Danish mortgage banks (Realkredit Danmark, BRF and Nykredit as well as Kommunekredit). However, the government will provide a direct government guarantee to the loans, and the mortgage banks will open new capital centres (cover pools), where they will issue govt. guaranteed mortgage bonds. This will give them a lower risk weight, and thus the new bonds should trade with a tight spread to DGBs and tighter than Kommunekredit, which does not have an explicit govt. guarantee. This will have an impact on both government bonds and callable mortgage bonds. As we see it – then the government will still prepay callable high-coupon loans and fund these with short-dated non-callable mortgage bonds (but with a govt. guarantee). Hence, 30Y callables like 3% 2044 from RD, BRF and Nykredit will be prepaid. They will also do buy-back in the low-coupon bonds such as 1.5% 2047 going forward, but how fast the buy-back of these bonds will happen is uncertain. Issuance of government bonds in 2018 will be smaller by at least 10bn as the loans are no longer funded by issuing government bonds. Hence, as we see it this is positive for 1% 2047, 5Y non-callables and Danish government bonds going into 2018.

Finally, the refinancing auctions are starting to come to an end, with much lower supply today as the last auction day for non-callable bonds. RD will be selling both 1Y (DKK and EUR), 3Y and 5Y non-callable bonds and BRF will sell 1Y bonds. Nordea Kredit and Nykredit have ended their non-callable auctions and DLR still has an auction on 5 December. Today, Nykredit will also be selling DKK2.7bn in a DKK FLT CIBOR6M Apr'22 and we expect to see good demand as yesterday's auction showed very strong demand for DKK12bn 10Y capped floaters.

FX markets

EUR/USD was bid again yesterday, closing in on the high end of the range (1.1479-1.1880) we have been looking for the cross to stay within ahead of year-end. We have previously stressed that it would require a shift in rhetoric from the ECB to break the 1.1880 level (the early October high) and, while yesterday's ECB minutes were largely balanced, they did reveal that the Governing Council is considering the option of decoupling the forward guidance on QE from the requirement of a sustained rise in inflation and instead linking it to the overall monetary policy stance. This is key for the euro as it opens up the possibility for the ECB to end the QE programme in 2018 even without a clear pickup in inflation and could pave the way for the next 'wave' of ECB 'normalisation' trades. This would in turn lift the euro quite substantially in our view as it would open for support from rates and flows alike, see *FX Edge: Power of flows* (23 August). Near term, we still deem that it is too early for a sustained move higher in EUR/USD but a break of 1.1880 is clearly a risk now.

USD/JPY trades slightly higher this morning after the cross has been trading very close to the 111 figure over the past 24 hours. The sell-off in USD/JPY in the ahead of Thanksgiving might to some extent be explained by investors reducing risk ahead of holidays and USD/JPY could see some support today as US and Japanese investors return to the market. However, we still see risks skewed to the downside in the short term, as speculative accounts are very short JPY and as the flattening pressure on the US yield curve is likely to remain a headwind for the cross. Technically, a clean break below the 111 could open up for a test of 110.

Key figures and events

Friday, November 24, 2017				Period	Danske Bank	Consensus	Previous
-	EUR	Moody's may publish Estonia's debt rating					
8:00	DKK	Retail sales	m/m|y/y	Oct			0.9%|3.1%
9:30	SEK	PPI	m/m|y/y	Oct			0.4%|4.3%
10:00	DEM	IFO - business climate	Index	Nov		116.5	116.7
10:00	DEM	IFO - current assessment	Index	Nov		125.0	124.8
10:00	DEM	IFO - expectations	Index	Nov		108.8	109.1
15:45	USD	Markit PMI manufacturing, preliminary	Index	Nov	55.6	55.0	54.6
15:45	USD	Markit PMI service, preliminary	Index	Nov	55.3		55.3

Source: Bloomberg, Danske Bank

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