



Sunrise

Thursday, 18 January 2018

Rates: US reflationary spirits back alive

Surging US stock markets, hawkish comments by Fed Mester and a very robust Beige Book revived reflationary spirits and caused an underperformance of US Treasuries. The US 5-yr yield is near key resistance at 2.42% (2011 top). The Bund could continue to outperform as ECB members downplay speculation on communication changes at next week's meeting.

Currencies: Dollar bottoms, but technical confirmation is still needed

The dollar finally rebounded yesterday. The US currency received additional interest rate support, as risk sentiment improved and as the Beige Book sounded positive on the economy. ECB governors continue to show their unease with the recent sharp euro rally. In this respect, we keep a close eye on comments from the ECB Coeure today.

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 stock markets eked out impressive gains yesterday (+1%), lifted by Apple's announcement to repatriate cash and invest in the US economy.** Asian stock markets started well, but grind lower with Japan underperforming (-0.5%).
- **White House Chief of Staff Kelly said that Republican leaders have the votes to avert a government shutdown** and push through a stopgap measure until Feb 26.
- **Australian employment** jumped past expectations to **match the longest run of monthly gains on record**, yet unemployment still edged up as more people looked for work putting an unwelcome brake on wages and inflation.
- The White House has "zero anxiety" about the prospect of former senior adviser **Steve Bannon testifying to the special counsel** overseeing the Russia investigation, an administration official.
- Economic activity across the US expanded into 2018, **with tight labor markets and modest wage and price growth**, according to the **Fed's Beige Book**.
- **Apple has pledged to invest more than \$30bn to expand its American operations** in the wake of last month's US tax cut, even as it makes an estimated \$38bn one-off tax payment on the repatriation of its overseas profits.
- **Today's eco calendar** heats up in the US with housing starts, building permits, Philly Fed Business outlook and weekly jobless claims.

Rates

Apple and Fed revive reflationary spirits

	US yield	-1d
2	2,04	0,03
5	2,40	0,05
10	2,59	0,05
30	2,85	0,03

	DE yield	-1d
2	-0,57	0,00
5	-0,13	0,00
10	0,56	0,00
30	1,29	0,00

Global core bond trading was uneventful during yesterday's European trading session. **Dynamics changed in US dealings** when core bonds lost ground. **US Treasuries underperformed German Bunds. Surging US equities on Apple headlines, hawkish comments by voting Fed-member Mester** (3 or more hikes in 2018) **and an upbeat assessment of the US economy in the Beige Book contributed to the move.** The market implied probability of a 3 rate hike scenario in 2018 rose above 50% for the first time. US yields increased between 2.9 bps (2-yr) and 5.7 bps (7-yr) on a daily basis. **The US 2-yr yield rose further above 2%, to the highest level since 2008. The 5-yr yield is very close to 2.42% resistance (2011 top).** The German yield curve ended virtually unchanged compared to Tuesday's close. 10-yr yield spread changes versus Germany were marginal with Italy (+3 bps) underperforming.

Asian stock markets started strong in line with WS yesterday, but several indices grind lower into the Asian close. Japan underperforms (-0.5%). The US Note future trades stable, suggesting a neutral opening for the Bund.

Today's eco calendar heats up in the US with housing data, jobless claims and Philly Fed Business outlook. Activity data failed to impact trading lately. Apple's announcement might dominate headlines and revive reflationary spirits (negative US Treasuries). US Congress faces a January 19 deadline to reach a spending deal and avoid a government shutdown. A final agreement is unlikely and Republicans will probably consider a stopgap spending bill and short term extension until Feb 16. **In previous government shutdown spells, which is not our base scenario this time, US Treasuries tended to profit from safe haven flows.** Speeches by ECB members (Weidmann, Coeuré and Villeroy) are potentially interesting. **Several ECB members tried to talk the euro lower recently,** dampening speculation that the ECB could already change its communication strategy at next week's meeting and causing an **outperformance of the Bund vs the Note future.**

Technical considerations remain at play as well for the Bund and US Note future. German yields are close to resistance levels, respectively at -0.55% (2-yr), -0.06% (5-yr), 0.62% (10-yr) and 1.38% (30-yr), but a break higher is unlikely ahead of next week's ECB meeting. **We argue in favor of some consolidation near the highs (in yield terms). Medium term, we closely follow German trade union negotiations about pay rises. German wages are expected to be pivotal to start an upward spiral in EMU price dynamics and could be a bearish signal for Bunds.** Strong global growth, rising inflation expectations and the global push to monetary normalization are **bearish factors for bonds medium term.** The US 10-yr yield's new trading range is between 2.5% and 2.63% (2017 top).



US 5-yr yield about to test 2011 top (2.42%)



German Bund: consolidation ahead of next week's ECB meeting?

Currencies

Dollar looking for a bottom?

R2	1,2643	-1d
R1	1,2297	
EUR/USD	1,2186	-0,0074
S1	1,1713	
S2	1,1554	

R2	0,9307	-1d
R1	0,9033	
EUR/GBP	0,8811	-0,0078
S1	0,8690	
S2	0,8657	

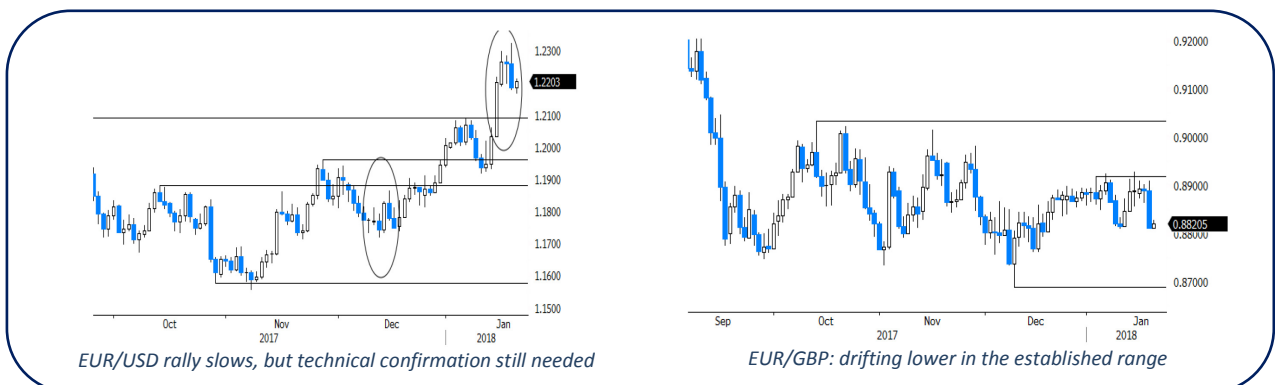
The EUR/USD rally was a bit exhausted yesterday after setting a new correction top in Asia. ECB members Constancio and Nowotny warned that a sudden rise of the euro complicates the ECB's effort to bring inflation back to target. EUR/USD tested the 1.22 mark early in US trading. The 2-yr US/GE yield spread rose to a cycle top of over 2.60 %. EUR/USD closed the session at 1.2186. USD/JPY finished at 111.29.

Asian equities opened strong overnight, but struggle to maintain the early gains. The dollar is holding most of yesterday's gains on higher US yields. The Japan 10-yr yield nears the 0.10% mark, blocking a further decline of the yen. USD/JPY holds in the low 111 area. The EUR/USD decline also slows. EUR/USD hovers near 1.22. The Aussie dollar fails to profit from strong November/December job growth. An overnight attempt to clear AUD/USD 0.80 failed.

US housing starts and permits are forecast to ease slightly. The Philly Fed business outlook is also expected slightly softer from 27.9 to 25.0. Activity data are not the focus of markets these days. So, any market reaction to these data will probably only be of intraday significance. Yesterday, the dollar finally rebounded. **Equities, Fed comments and the Beige book were supportive, but there is no guarantee but there is no guarantee that this is enough to trigger a sustained bigger correction already at this stage.** We keep a close eye at an appearance from ECB's Coeure. Will he also warn on the impact of a too fast rise of the euro?

Global Picture: The dollar was in the defensive of late as markets prepare for a change in policy from central banks outside the US, especially from the ECB. This propelled EUR/USD despite a huge interest rate differential in favour of the dollar. **Yesterday, the dollar decline finally showed tentative signs of bottoming, but the jury is still out.** A return below previous resistance at 1.2092 is needed to call off the ST alert for the dollar. EUR/USD 1.2598 (62% Retracement) is next important resistance on the charts.

EUR/GBP lost substantial ground yesterday even as there were few UK eco data. The EUR/USD decline was an important factor. This morning, UK RICS house prices were better than expected. There are no other UK data today. The day-to-day momentum of sterling improves, but we hold the view that 0.8760/00 is a strong support area ST.



Calendar

Thursday, 18 January		Consensus	Previous
US			
14:30	Housing Starts / MoM (Dec)	1275k/-1.7%	1297k/3.3%
14:30	Building Permits / MoM (Dec)	1295k/-0.6%	1303k/-1.0%
14:30	Philadelphia Fed Business Outlook (Jan)	25.0	27.9
14:30	Initial Jobless Claims	249k	261k
14:30	Continuing Claims	1900k	1867k
Japan			
05:30	Industrial Production MoM / YoY (Nov F)	A: 0.5%/3.6%	0.6%/3.7%
05:30	Capacity Utilization MoM (Nov)	A: 0.0%	0.2%
UK			
01:01	RICS House Price Balance (Dec)	A: 8%	0
China			
08:00	GDP SA QoQ / YoY (4Q)	1.7%/6.7%	1.7%/6.8%
08:00	GDP YTD YoY (4Q)	6.8%	6.9%
08:00	Retail Sales YoY / YTD YoY (Dec)	10.2%/10.3%	10.2%/10.3%
08:00	Industrial Production YoY / YTD YoY (Dec)	6.1%/6.6%	6.1%/6.6%
08:00	Fixed Assets Ex Rural YTD YoY (Dec)	7.1%	7.2%
Events			
Q4 earnings	Morgan Stanley (13:00), American Express (Aft-Mkt),...		
02:30	China December Property Prices		
09:15	ECB's Weidmann, Coeure, IMF's Lagarde speak in Frankfurt		
10:30	Spain to Sell Bonds		
10:50	France to Sell Bonds		
15:30	ECB's Coeure speaks on a panel in Frankfurt		
18:30	Bank of France's Villeroy holds press conference in Paris		

10-year	Close	-1d		2-year	Close	-1d	Stocks	Close	-1d
US	2,59	0,05		US	2,04	0,03	DOW	26115,65	322,79
DE	0,56	0,00		DE	-0,57	0,00	NASDAQ	7298,279	74,59
BE	0,70	-0,01		BE	-0,48	-0,01	NIKKEI	23763,37	-104,97
UK	1,31	0,01		UK	0,57	-0,01	DAX	13183,96	-62,37
JP	0,08	-0,01		JP	-0,13	0,00	DJ euro-50	3612,78	-9,23
IRS	EUR	USD	GBP	EUR	-1d	-2d	USD	-1d	-2d
3y	0,05	2,35	0,98	Eonia	-0,3630	0,0070	Libor-1	1,5561	0,0000
5y	0,38	2,46	1,15	Euribor-1	-0,3690	0,0000	Libor-3	1,7341	0,0000
10y	0,95	2,60	1,38	Euribor-3	-0,3280	0,0010	Libor-6	1,9041	0,0000
				Euribor-6	-0,2740	-0,0020			
Currencies	Close	-1d		Currencies	Close	-1d	Commodities	Close	-1d
EUR/USD	1,2186	-0,0074		EUR/JPY	135,63	0,21	CRB	196,40	1,30
USD/JPY	111,29	0,84		EUR/GBP	0,8811	-0,0078	Gold	1339,20	2,10
GBP/USD	1,3831	0,0039		EUR/CHF	1,1767	0,0003	Brent	69,38	0,23
AUD/USD	0,797	0,0009		EUR/SEK	9,8103	-0,0487			
USD/CAD	1,2438	0,0003		EUR/NOK	9,6026	-0,0527			

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