



Sunrise

Tuesday, 05 December 2017

Rates: Front end US yield curve rises further

The main item on today's agenda is the US non-manufacturing ISM which is expected to remain very strong. In theory, that's negative for US treasuries, but we don't expect a strong reaction. The front end of the US yield curve continues to underperform, discounting already two rate hikes for 2018 going into next week's FOMC meeting.

Currencies: Dollar rebound stalls despite rising interest rate support

The dollar profited temporary from the tax bill approval in the US Senate yesterday, but the rally stalled as US equities turned south. Today's eco data probably won't cause a big directional USD move. Even so, the ongoing rise in ST US yields is making USD shots expensive and should protect the USD downside going into the payrolls and next week's Fed meeting.

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 ended varied with Nasdaq (-1%) underperforming** as a last-minute change to Senate Republicans' tax-overhaul plan may mean higher taxes for corporations, including IT firms. **Asian bourses trade mixed overnight.**
- A carefully choreographed divorce deal between London and Brussels was **derailed at the eleventh hour after Northern Ireland's hardline Unionists rejected Theresa May's agreement** to potentially keep the province aligned with EU law after Brexit. EUR/GBP rose back above 0.88.
- **Growth in China's services sector activity picked up to a three-month high in November (PMI: 51.9)**, buoyed by a solid rise in new business, though the rate of expansion remained moderate and weaker than the long-run trend.
- **The Reserve Bank of Australia kept its policy rate unchanged at 1.5%**, but a shift in the inflation language signalled that the central bank is arguably offering a less dovish tone. AUD/USD rises from 0.76 to 0.7650.
- The **Reserve Bank of New Zealand's** new assumption that global inflation will stay lower for longer means it **is more exposed to the risk of prices picking up**, Acting Governor Spencer said. NZD/USD moves higher towards 0.69.
- European Finance Ministers shifted power from the north of the continent to the south, providing a boost to opponents of austerity policies. **They chose Portugal's FM Centeno to lead the Eurogroup** to succeed Dijsselbloem.
- **Today's eco calendar** contains November services PMI's in EMU (final), the UK and the US (ISM). EMU retail sales are also up for release.

Rates

Bear flattening in US vs bear steepening in Europe

	US yield	-1d
2	1,81	0,03
5	2,16	0,03
10	2,37	0,01
30	2,78	0,00

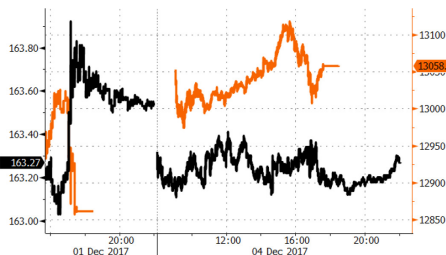
	DE yield	-1d
2	-0,70	0,00
5	-0,33	0,02
10	0,34	0,04
30	1,17	0,05

One-off repositioning on US Senate tax vote

Global core bonds lost part of Friday's gains yesterday. The move was limited to a one-off repositioning in the Asian or European opening with the positive US Senate tax bill vote the main incentive. It's now up to House and Senate lawmakers to find common ground for a bill, preferable before year-end. More worrying headlines on the US political scene about Mueller's investigation into Russia-links in Trump's presidential campaign team perhaps hampered a more enthusiastic reaction. Core bond trading was rather lethargic after the opening move and confined to a tight sideways range. The US Note future slightly outperformed the Bund in the process as US equity markets went off in a swoon going into the US closes. Investors probably have Friday's payrolls and next week's FOMC meeting in mind. The European eco calendar contained only second tier and slightly disappointing data (PPI, Sentix investor confidence).

In a daily perspective, the German yield curve bear steepened with yields up to 5.3 bps (30-yr) higher. The US yield curve bear flattened with yield changes ranging between +3.5 bps (2-yr) and +0.2 bps (30-yr). On intra-EMU bond markets, 10-yr yield spreads versus Germany ranged between +1 bp and -1 bp with Spain/Italy (-4 bps) and Greece (-11 bps) outperforming.

Today's eco calendar contains the final EMU services PMI (expected to be confirmed at 56.2) and the US non-manufacturing ISM. The ISM is expected to decline from a record high 60.1 in October to 59 in November. That remains a very strong reading, but markets lately didn't get lured into reacting on strong activity data.



German Bund (black) & Dax (orange) intraday: one-off repositioning in European opening followed by range bound action, especially in the Bund



Eonia overnight bank lending rates returning back to normal after unexpected spike at the end of last month. Due to month-end or year-end distortion/funding squeeze?

Front end of US yield curve rises further

R2	165,18	-1d
R1	163,92	
BUND	163,23	-0,52
S1	161,91	
S2	160,24	

Asian stock markets trade mixed overnight, though risk sentiment is deteriorating towards the end of the session. The US Note future and Brent crude give no indication for the start of trading, suggesting a neutral opening for the Bund.

The main item on today's agenda is the US non-manufacturing ISM which is expected to remain very strong. In theory, that's negative for US treasuries, but we don't expect a strong reaction. **The front end of the US yield curve continues to underperform, discounting already two rate hikes for 2018 going into next week's FOMC meeting.** We expect the new dot plot to show the Fed's determination to hike rates 3 times next year. **Rate markets are for the first time in the current tightening cycle (rapidly) catching up with FOMC forecasts.**

Technically, US Treasuries will probably trade in the 123-27 to 125-14+ range going forward (March 2018 contract!). This corresponds with a 2.3%-2.47% band in yield terms. The **German Bund** set a new contract high, but this wasn't confirmed by a drop of the German 10-yr yield below 0.3%. **We don't anticipate such move and suggest putting short positions around current levels. Strong current and expected growth and the ECB's slow normalisation process warrant such move.**



German Bund: New contract high, but break needs to be confirmed with move of German 10y yield below 0.3%.



US Note future (March contract!): sideways ahead of key Fed meeting next week. How will the 2018 dot plot look like?!

Currencies

Dollar rebound stalls despite higher ST yields

Tax-driven reflation trade eases during yesterday's session

Dollar returned most of the initial gains

Dollar looking for a bottom after yesterday evening's setback

Aussie and kiwi dollar gain as CB's keep a less dovish tone

EMU PMI's and US ISM top the eco calendar today

Global sentiment probably remains the driver for USD trading short-term

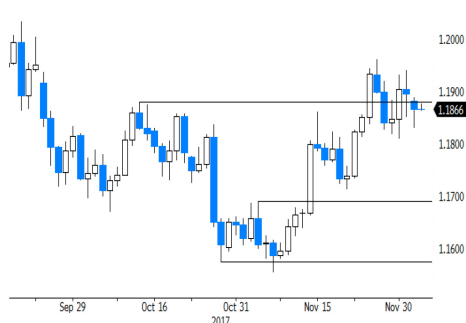
R2	1,2225	-1d
R1	1,2092	
EUR/USD	1,1866	-0,0030
S1	1,1554	
S2	1,1331	

European (and US) markets initially reacted in a positive way to the approval of the US tax bill. European equities jumped higher. ST US yields rose further and the dollar extended cautious gains. USD/JPY tested the 113 area. The gain of the dollar against the euro was again more limited. Later in US dealings, tax optimism dwindled, reversing most of the intraday 'reflation trade'. The dollar returned a big part of the early gains. USD/JPY closed the session at 112.41 (from 112.17 on Friday). EUR/USD finished the day at 1.1866 (from 1.1896).

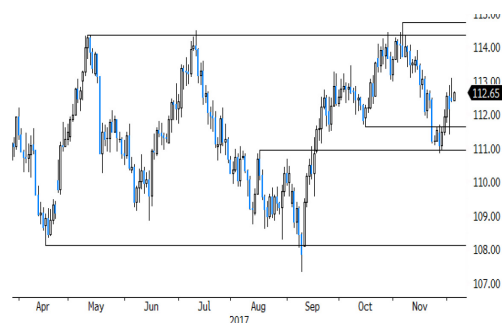
Asian equity indices show a mixed picture. A new setback in US tech stocks also affects (parts of) the Asian markets. **The dollar 'bottoms' after the late session setback in the US yesterday evening.** USD/JPY trades in the 112.60 area. EUR/USD is changing hands near 1.1870 area. The **RBA** as expected left its policy rate unchanged at 1.50%, but expects that a stronger labour market could see some lift in wage growth over time. Better than expected retail data also supported the Aussie dollar. **AUD/USD trades in the mid 0.76 area.** The kiwi dollar made some modest gains after **RBNZ's Spencer** indicated that the bank could give more weight to output employment and financial stability.

The **eco calendar** contains the final EMU (services) PMI's, EMU retail sales and the US non-manufacturing ISM. EMU PMI's are expected to confirm the strong growth momentum (57.5 for the composite PMI). Retail sales are expected to have declined in October (-0.7% M/M and 1.6% Y/Y). We don't expect the EMU data to have a lasting impact on the euro. **The US non-manufacturing ISM is expected to ease slightly from 60.1 to 59, still a very high level.** Last week's manufacturing ISM showed a similar pattern. We have no reason to take a different view from the consensus. Of late, markets mostly reacted rather muted to (US) activity data. **Investors are more sensitive to price data.**

The dollar showed a mixed picture last week, rebounding against the yen but holding relatively soft against the euro. Yesterday, the pattern initially continued, but the USD rebound was aborted by a new up-tick in US equity volatility later in the session yesterday. **The US 2-yr yield continues an astonishing rise (currently above 1.80%!), but it was only of little help for the dollar of late.** Even so, it should at least help to put a floor for the US currency as USD shorts are becoming ever more expensive. We don't expect a really big directional move ahead of next week's Fed policy decision/statement.



EUR/USD: rally aborted, but no clear trend yet



USD/JPY: rally slows. Technical picture turned neutral again

Tuesday, 05 December 2017

That said, except for high profile negative news from the US (or negative risk sentiment) we see no reason for EUR/USD to rise beyond the 1.1961/1.20 area. The downside of USD/JPY looks better protected, but the rebound might slow if it isn't supported by developments on other markets.

From a technical point of view: EUR/USD set a post-ECB low mid-November, but dollar momentum wasn't strong enough. EUR/USD regained the 1.1880 MT correction top, opening the way for a full retracement to the 1.2092 top. A return below 1.1713 would signal that the rebound in EUR/USD is aborted. **For now, there is no clear technical signal. The USD/JPY momentum** deteriorated early November. USD/JPY dropped below the 111.65 neckline, but there was no aggressive follow-through selling. Last week the pair even succeeded a nice rebound, calling off the downside alert. **The pair again hovers in the 110.84/114.73 consolidation range. We amend our ST bias on the pair from negative to neutral.**

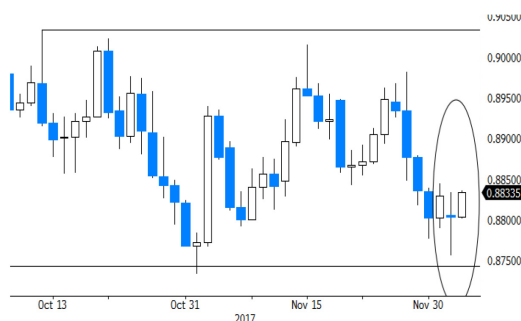
R2	0,9307	-1d
R1	0,9033	
EUR/GBP	0,8803	-0,0026
S1	0,8743	
S2	0,8657	

Sterling hit by last-minute Brexit failure

Brexit headlines caused a rollercoaster ride for sterling yesterday. UK PM May met with EU Commission president Juncker. EUR/GBP initially hovered in the 0.8825 area. Around noon there were press headlines from several sources that EU's **Barnier had indicated that negotiations on the separation issues were headed for a breakthrough. Sterling jumped higher across the board as markets assumed that Brexit negotiations could move to the content of the new relationship between the UK and the EU post Brexit. However, at a joined press conference, UK PM May and EC's Juncker said that progress had been made, but no final agreement was reached. Sterling reversed most of the intraday gains. EUR/GBP finished the session at 0.8803. GBP closed the session at 1.3480.**

Overnight, BRC UK retail sales rebounded to 0.6% Y/Y. However, it doesn't help sterling. The UK currency remains under pressure. Markets are disappointed on yesterday's last minute failure to reach a separation deal. Both parties are still trying to reach a deal to be proposed to the EU summit next week. Yesterday's failure is the perfect illustration of the difficult balancing act that PM May faces and will continue to face during the next stages of the negotiations. **Today, the UK services PMI will be published.** A slight decline from 55.6 to 55 is expected. The report probably will only be of intraday significance for sterling trading. The focus remains on Brexit. Sterling remains in the defensive, unless there is hard evidence of a deal.

MT view/technical picture: A BoE driven sterling rebound ran into resistance early last month. Sterling declined again as markets anticipated that the rate cycle would be very gradual and limited. EUR/GBP trades in a 0.8733/0.9033 consolidation range. Brexit headlines cause day-to-day gyrations. **We changed our ST bias on EUR/GBP from positive to neutral mid-November.** The 0.9015/33 area might be tough to break short-term. In case of more positive news on Brexit, return action to the 0.8733 (or below) level is possible ST.



EUR/GBP: downside test rejected as Irish border deal fails last minute



GBP/USD: rally slows

Calendar

Tuesday, 5 December		Consensus	Previous
US			
14:30	Trade Balance (Oct)	-\$47.4b	-\$43.5b
16:00	ISM Non-Manf. Composite (Nov)	59.0	60.1
Japan			
01:30	Nikkei Japan PMI Services (Nov)	--	53.4
01:30	Nikkei Japan PMI Composite (Nov)	--	53.4
Australia			
04:30	RBA Cash Rate Target	1.50%	1.50%
China			
02:45	Caixin China PMI Composite (Nov)	--	51.0
02:45	Caixin China PMI Services (Nov)	--	51.2
UK			
01:01	BRC Sales Like-For-Like YoY (Nov)	--	-1.0%
10:00	New Car Registrations YoY (Nov)	--	-12.2%
10:30	Markit/CIPS UK Services PMI (Nov)	55.0	55.6
10:30	Markit/CIPS UK Composite PMI (Nov)	55.8	55.8
10:30	Official Reserves Changes (Nov)	--	\$30m
EMU			
10:00	Markit Eurozone Services PMI (Nov F)	56.2	56.2
10:00	Markit Eurozone Composite PMI (Nov F)	57.5	57.5
11:00	Retail Sales MoM / YoY (Oct)	-0.7%/1.6%	0.7%/3.7%
Spain			
09:00	Industrial Production MoM (Oct)	0.4%	0.1%
Sweden			
08:30	Swedbank/Silf PMI Services (Nov)	--	61.4

10-year	<u>Close</u>	<u>-1d</u>		2-year	<u>td</u>	<u>-1d</u>	Stocks	<u>Close</u>	<u>-1d</u>
US	2,37	0,01		US	1,81	0,03	DOW	24290,05	58,46
DE	0,34	0,04		DE	-0,70	0,00	NASDAQ	6775,366	-72,22
BE	0,52	0,04		BE	-0,59	0,01	NIKKEI	22622,38	-84,78
UK	1,29	0,05		UK	0,51	0,03	DAX	13058,55	197,06
JP	0,05	0,01		JP	-0,12	0,02	DJ euro-50	3576,22	48,67
IRS	<u>EUR</u>	<u>USD</u>	<u>GBP</u>	EUR	<u>-1d</u>	<u>-2d</u>	USD	<u>-1d</u>	<u>-2d</u>
3y	-0,06	2,09	0,97	Eonia	-0,3190	-0,0280			
5y	0,20	2,20	1,12	Euribor-1	-0,3680	0,0010	Libor-1	1,3794	0,0000
10y	0,81	2,39	1,36	Euribor-3	-0,3260	0,0000	Libor-3	1,4946	0,0000
				Euribor-6	-0,2720	-0,0010	Libor-6	1,6743	0,0000
Currencies	<u>Close</u>	<u>-1d</u>		Currencies	<u>Close</u>	<u>-1d</u>	Commodities	<u>Close</u>	<u>-1d</u>
EUR/USD	1,1866	-0,0030		EUR/JPY	133,38	-0,08	CRB	188,69	-2,00
USD/JPY	112,41	0,24		EUR/GBP	0,8803	-0,0026	Gold	1277,70	-4,60
GBP/USD	1,348	0,0003		EUR/CHF	1,1688	0,0074	Brent	62,45	-1,28
AUD/USD	0,7598	-0,0015		EUR/SEK	9,9906	0,0542			
USD/CAD	1,2673	-0,0012		EUR/NOK	9,8872	0,0332			

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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