



Thursday, 13 December 2018

Rates: Will Bunds continue to decline as ECB meets?

Core bonds are moving lower on the uptick in risk sentiment with the US and China showing progress in trade talks. Investor focus shifts to the ECB meeting of today. With markets already positioned on the dovish side, we expect a balanced message from Draghi given probable GDP/CPI forecast downgrades.

Currencies: ECB meeting probably won't be a game-changer for euro trading

There was again no news topic important enough to give clear directional guidance for trading yesterday in the major FX cross rates. Today, the ECB will take center stage. Draghi might keep a cautiously positive tone, but is unlikely to trigger a euro rally. Sterling rebounded as PM survived a confidence vote, but hurdles for further GBP gains remain high.

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 equities** ended in green on upbeat trade expectations. Nasdaq (+0.95%) outperformed. **Asian stock markets** are surfing along the green wave. China (+1.5%) outperforms.
- **Shipments of US soybeans are heading for China** following the country's first significant purchase since both countries began imposing tariffs. The move is regarded an important gesture of China toward easing tensions.
- **Theresa May survived a vote of no confidence** triggered by her Conservative Party last night. She received backing of 200 party members, 117 opposed her. May cannot face another Tory triggered vote for at least a year.
- **The Brazilian central bank left its benchmark rate unchanged at 6.5%** saying the domestic economy is gradually recovering but the global outlook remains challenging. CPI is at "comfortable levels" despite the recent sell-off of the real.
- China detained Canadian businessman Michael Spavor on suspicion of harming the country's state security. The announcement follows the detention on Monday of Canada's Michael Kovrig on the same grounds, a move considered reprisal for the arrest of Huawei's CFO Meng Wanzhou.
- **EU's economy commissioner Pierre Moscovici said it's wrong to compare France with Italy** following the former's recent expansion of the deficit. Exceeding the 3% limit is allowed in a "limited, temporary, exceptional way" and cannot last 2 consecutive years. France's deficit in 2017 amounted to 2.8%.
- **Today's** a heyday for central bank watchers as the Swiss National Bank, Norges Bank and the ECB hold their December meeting. Also watch for statements from the European Council concerning Italy and Brexit. The US, Italy and Spain tap the bond market.

Rates

Will Bunds continue to decline as ECB meets?

	US yield	-1d
2	2,77	0,01
5	2,77	0,03
10	2,91	0,03
30	3,15	0,02

	DE yield	-1d
2	-0,57	0,04
5	-0,25	0,05
10	0,28	0,05
30	0,86	0,03

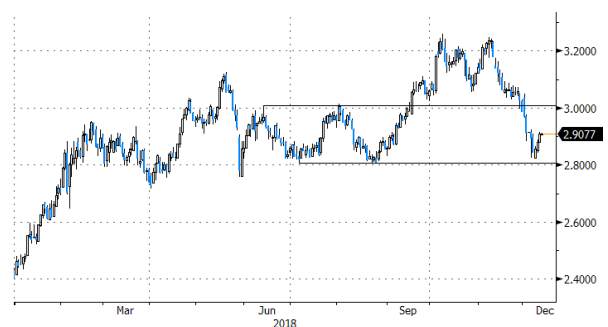
Global core bonds ended higher yesterday with German Bunds underperforming US Treasuries. German Bunds finally gave in to the uplift of risk sentiment after resilience of the previous days. The German yield curve moved higher with the belly of the curve underperforming. Changes range from +3.2 bps (30-yr) to +4.7 bps (5-yr). The US yield curve edged up as well with changes from +0.8 bps (2-yr) to +3.1 bps (10-yr). **Italian BTP's rallied after the Italian government reached an agreement to lower its budget deficit to a manageable 2.0%.** The Italian 10-yr yield fell below 3.0% for the first time since September. The Italian/German 10-yr yield spread decreased 17 bps to 272 bps.

Asian markets this morning show the uplift in sentiment continues today with all equity indices opening in green. China outperforms its peers on a first (practical) sign that the US and China are genuinely working on a trade deal as Chinese food importers have bought US soybeans for the first time in months. US Treasuries opened neutral with a small desire to continue the downward trend of late. We expect a similar opening for the Bund, with investors eying the ECB's rate decision this afternoon, followed by president Draghi addressing the public. The ECB fixed the guidelines of its policy at the June meeting. Policy rates are expected to remain unchanged at least through the Summer of 2019, net asset purchases will end by the turn of the year and the reinvestments of maturing bonds from the APP portfolio will last as long as deemed necessary. Focus will be on president Draghi's comments afterwards. **We expect that the ECB will downwardly adjust its growth/inflation forecasts, but Draghi will try to keep a balanced message to avoid large market swings. He recently fiercely defended the view that underlying inflationary pressures are building because of rising wages, a closing output gap and the ECB's very accommodative policy.** Investors will also be looking for new hints on a possible new round of TLTRO's. From a market point of view, it's probably hard for Draghi to surprise of the dovish side of current positioning. We expect any market impact to be small whatsoever.

From a technical point of view, 0.18% (German 10y yield) and 2.78/2.8% (US 10y yield) are the lines in the sand. A break lower would, especially in the US and taking into account the inversion at the 2y-5y, signal heightened fears of a nearby end to the economic & monetary cycles. For now, our hypothesis remains that the correction on rate markets the past month resulted in a too dovish positioning going into the final ECB & Fed meetings of the year.



German 10-yr yield finally profits from the uptick in sentiment



US 10-yr yield: technical rebound away from 2.78%/2.8% support, but Fed will have final say next week

Currencies

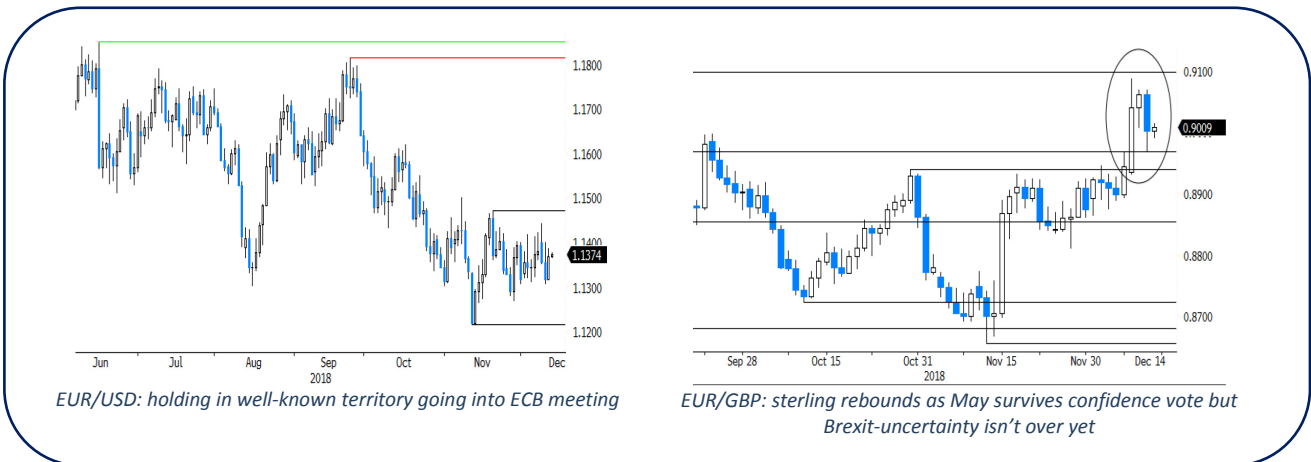
ECB meeting unlikely to be a FX gamechanger

R2	1,1815	-1d
R1	1,1621	
EUR/USD	1,1369	0,0052
S1	1,1187	
S2	1,1119	

R2	0,93067	-1d
R1	0,91	
EUR/GBP	0,9002	-0,0060
S1	0,8700	
S2	0,862	

The EUR/USD trading pattern **yesterday** was similar to what happened of late. The news headlines caused some moderate intraday swings but wasn't able to push the pair out of the established ranges. Early euro softness reversed on headlines that Italy might agree a 2% 2019 budget deficit. Easing tensions in the trade talks between the US and China and a positive risk sentiment were rather neutral for EUR/USD trading. US CPI data were exactly in line with expectations. The euro was also little affected by the **Brexit saga (drama)** as it developed in the UK yesterday afternoon. **EUR/USD closed a rather dull session at 1.1369 (from 1.1317)**. Trading in the USD/JPY cross rate was even less inspiring. A risk-on sentiment and higher US yields failed to inspire any further USD/JPY gains. The pair finished at 113.29 (from 113.38). **Overnight**, Asian equities join the risk rebound from the US yesterday. The dollar shows no clear directional bias. The yuan continues a cautious rebound (USD/CNY 6.8650). EUR/USD trades little changed (1.1370). USD/JPY gains a few ticks (113.45). US data (import prices and claims) **later today** are second tier. The focus will be on the ECB meeting. Chairman Draghi has to walk a thin line. He will probably admit risks to growth, but the new ECB-forecasts will stay strong enough for Draghi to conclude that inflation will move closer to target at the end of the policy horizon. Question is whether the market will believe this rather positive scenario. The ECB communication might help to put a floor for European yields. This is a tentative euro positive, but we don't expect today's meeting to be a game-changer for EUR/USD. The focus will soon turn to next week's Fed meeting. **Of late, the 1.1450/1.15 area proved to be a tough resistance. We don't see a trigger for a break ST.**

Sterling trading was at the mercy of the headlines on the **leadership vote within the Conservative party** yesterday. Sterling started the session on a weak footing, but rebounded intraday as markets saw a good chance of PM May surviving. This is exactly what happened. Even so, sterling couldn't maintain gains below the EUR/GBP 0.90 level. PM May will try to get new concessions from EU leaders at a summit **today**. However, it is unlikely that this process will yield many GBP-supportive headlines. So yesterday's sterling rebound might be short-lived.



Calendar

Thursday, 13 December		Consensus	Previous
US			
14:30	Import Price Index MoM/YoY (Nov)	-1.0%/1.3%	0.5%/3.5%
14:30	Import Price Index ex Petroleum MoM (Nov)	-0.1%	0.2%
14:30	Export Price Index MoM/YoY (Nov)	-0.3%/--	0.4%/3.1%
14:30	Initial Jobless Claims	226k	231k
14:30	Continuing Claims	1649k	1631k
Japan			
03:00	Tokyo Avg Office Vacancies (Nov)	1.98A	2.20
UK			
01:01	RICS House Price Balance (Nov)	-11%A	-10%
EMU			
13:45	ECB Deposit Facility Rate	-0.40%	-0.40%
Germany			
08:00	CPI EU Harmonized MoM/YoY (Nov F)	0.1%/2.2%	0.1%/2.2%
France			
08:45	CPI EU Harmonized MoM/YoY (Nov F)	-0.2%/2.2%	-0.2%/2.2%
Norway			
10:00	Deposit Rates	0.75%	0.75%
Sweden			
09:30	Unemployment Rate SA (Nov)	6.2%	6.0%
Switzerland			
09:30	SNB Sight Deposit Interest Rate	-0.75%	-0.75%
09:30	SNB 3-Month Libor Lower Target Range	-1.25%	-1.25%
09:30	SNB 3-Month Libor Upper Target Range	-0.25%	-0.25%
Events			
13-14DEC	European Council meets		
10:30	Spain to Sell Bonds		
11:00	Italy to Sell Bonds		
19:00	U.S. to Sell USD16 Bln 30-Year Bonds		

10-year	Close	-1d	2-year	Close	-1d	Stocks	Close	-1d	
US	2,91	0,03	US	2,77	0,01	DOW	24527,27	157,03	
DE	0,28	0,05	DE	-0,57	0,04	NASDAQ	7098,312	66,48	
BE	0,76	0,01	BE	-0,52	0,02	NIKKEI	21816,19	213,44	
UK	1,28	0,09	UK	0,75	0,06	DAX	10929,43	148,92	
JP	0,06	0,00	JP	-0,14	-0,01	DJ euro-50	3107,97	52,65	
IRS	EUR	USD	GBP	EUR	-1d	-2d	USD	-1d	-2d
3y	0,00	2,89	1,24	Eonia	-0,3600	0,0000	Libor-1	2,4324	0,0000
5y	0,29	2,87	1,32	Euribor-1	-0,3680	0,0000	Libor-3	2,7790	0,0000
10y	0,89	2,95	1,47	Euribor-3	-0,3120	0,0000	Libor-6	2,8806	0,0000
				Euribor-6	-0,2410	0,0030			
Currencies	Close	-1d	Currencies	Close	-1d	Commodities	Close	-1d	
EUR/USD	1,1369	0,0052	EUR/JPY	128,78	0,46	CRB	181,20	-0,60	
USD/JPY	113,29	-0,09	EUR/GBP	0,9002	-0,0060	Gold	1250,00	2,80	
GBP/USD	1,2629	0,0142	EUR/CHF	1,1294	0,0053	Brent	60,15	-0,05	
AUD/USD	0,722	0,0014	EUR/SEK	10,3335	0,0472				
USD/CAD	1,335	-0,0040	EUR/NOK	9,7451	0,0357				

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Contacts

Brussels Research (KBC)		Global Sales Force	
Mathias Van der Jeugt	+32 2 417 51 94	Corporate Desk(Brussels)	+32 2 417 45 82
Peter Wuyts	+32 2 417 32 35	Institutional Desk(Brussels)	+32 2 417 46 25
Mathias Janssens	+32 2 417 51 95	CBC Desk (Brussels)	+32 2 547 19 19
Dieter Lapeire	+32 2 417 25 47	France	+32 2 417 32 65
Dublin Research		London	+44 207 256 4848
Austin Hughes	+353 1 664 6889	Singapore	+65 533 34 10
Shawn Britton	+353 1 664 6892		
Prague Research (CSOB)		Prague	+420 2 6135 3535
Jan Cermak	+420 2 6135 3578		
Jan Bures	+420 2 6135 3574		
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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