



Thursday, 02 May 2019

Rates: Fed cuts IOER; soft inflation transient?

A disappointing US manufacturing ISM and a 5 bps IOER cut by the Fed were offset by Fed Chair Powell's suggestion that soft inflation was transient. US Treasuries eventually closed a tad softer. Today's session is probably less interesting, bridging yesterday's Fed with tomorrow's payrolls and non-manufacturing ISM. The US S&P 500 shows a bearish engulfing pattern.

Currencies: Fed Powell blocks further decline of the dollar, for now.

The dollar traded in the defensive in the run-up to the yesterday's Fed policy decision, but rebounded as Fed's Powell signaled that there is currently no case for a rate cut. The dollar rebounded during the press conference. Still the US currency remains vulnerable as soft US price and/or activity data might easily revive calls for a Fed rate cut.

Calendar

Headlines

- **US equities** lost ground (-0.75%) yesterday after setting fresh record highs earlier in the trading day. **Asian shares** are trading mixed with mainland Chinese and Japanese bourses closed.
- **The US Fed left its policy rate unchanged** at 2.25%-2.50%. Fed chief Powell added that he sees **no immediate need to move interest rates either higher or lower**. The Fed expects inflation to rebound and the economy to stay healthy.
- **The US and China concluded productive trade talks in Beijing yesterday**, with some sources expecting a deal by the end of next week, incl. the removal of some of the US import tariffs. Negotiations continue in Washington next week.
- **UK PM May and Labour leader Corbyn have both signalled to edge closer to a Brexit deal**. May said she could move on one of her key red lines and allow the UK to maintain a joint customs regime with the EU, a key Labour demand.
- **US April ISM Manufacturing fell to 52.8** from 55.3 in March (vs. 55 consensus), with new orders and employment dragging sentiment down. **ADP employment change beat expectations in April with a 275k growth**, up from 129k in March.
- **Bank of Canada chief Poloz said he still foresees a need for policy interest rates to rise**, once factors that are currently slowing the economic expansion will vanish. He does think accommodative rates are needed for now.
- **Today's economic calendar** contains this week's jobless claims in the US. The Bank of England holds its April policy meeting. Norway and Sweden print April Manufacturing PMI's. ECB chief economist Praet speaks.

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	👉

Rates

	US yield	-1d
2	2.30	0.04
5	2.32	0.02
10	2.50	0.00
30	2.91	-0.02

	DE yield	-1d
2	-0.58	0.00
5	-0.41	0.00
10	0.01	0.00
30	0.66	0.00

Fed cuts IOER; soft inflation transient?

Japanese (Golden Week), Chinese and most European markets (both Labour Day) were closed yesterday. The US trading session nevertheless turned out to be interesting. **US Treasuries ignored a strong April ADP employment report (+275k vs +180k expected), but profited from an unexpectedly strong decline in the US manufacturing ISM (52.8 from 55.3 vs 55 expected).** The April reading was the weakest since October 2016 with details (eg new orders and employment) showing more signs of softness. **US Treasuries received a second push in the back after the Fed's policy rate announcements.** The target bounds remain unchanged (2.25%-2.5%), **but the Fed has cut the Interest Rate on Excessive Reserves (IOER) by 5 bps from 2.4% to 2.35%.** Fed Chair Powell downplayed the significance afterwards at the press conference. **It's mainly to avoid that the Fed Funds effective rate (weighted average of overnight bank rates) would surpass the upper end of the policy range.** The effective rate gently increased to 2.45% in past sessions, which is the widest since the introduction of IOER (2008) and suggests a tightening of liquidity. **US Treasuries hit an air pocket after Powell said that some of the reasons behind current low inflation appear to be "transient or idiosyncratic".** The Fed wants to keep its wait-and-see attitude with **currently no strong trigger to move rates in either direction.** The US yield curve eventually flattened with yield changes varying between +3.8 bps (2-yr) and -2.5 bps (30-yr).

Most Asian stock markets are positively oriented this morning despite late WS weakness (up to -0.75%). **The US S&P 500 shows a technical bearish engulfing signal, suggesting a short term trend reversal (correction lower).** The US Note future trades near yesterday's intraday lows. The eco calendar only contains final EMU manufacturing PMI's, US weekly jobless claims and final durable goods orders. **We don't expect the data to guide trading. The session could be a transitory one, bridging yesterday's Fed with tomorrow's US-non manufacturing ISM and payrolls.**

Long term view: markets concluded that the ECB missed out on this cycle. They even start pondering the possibility of an additional deposit rate cut. The downtrend in the German 10-yr remains in place so far. **Regarding Fed policy, markets now discount a >50% probability of a Fed rate cut by December.** The US 10-yr yield earlier this month returned above the lower bound of the previous 2.5%-2.79%. This turned the picture more neutral again, but the move lacks conviction.



US S&P 500 points bearish engulfing pattern. Short term trend reversal?!



US 10-yr yield regained previous support area after several failed tests, but move lacks conviction

Currencies

Powell blocks further USD loss, at least for now.

R2	1.1815	-1d
R1	1.1621	
EUR/USD	1.1196	-0.0019
S1	1.1110	
S2	1.0864	

R2	0.93067	-1d
R1	0.91	
EUR/GBP	0.8580	-0.0025
S1	0.8500	
S2	0.8314	

The dollar traded soft in the run-up to the Fed decision yesterday. The ADP job report was strong but the US manufacturing ISM signalled a sharp slowdown in the sector, weighing on the dollar. The USD dropped (temporarily) further as the Fed acknowledged recent decline in both headline and core inflation. However, **US yields and the USD rebounded as Fed's Powell later indicated that this decline was seen as transitory**. The FOMC agreed that there was no case for a rate move in either direction. EUR/USD dropped from the 1.1265 area to close at 1.1196. USD/JPY also reversed an initial decline to finish the session at 111.38.

Asian equity markets are trading mixed to slightly higher, but key Japan and mainland China markets are closed. The dollar shows no clear trend (DXY near 97.60; USD/JPY near 111.55). EUR/USD tries to regain the 1.12 handle. Risky assets are slightly supported by headlines (CNBC) that the US and China are close to a trade deal.

Later today, the final EMU manufacturing PMI's are expected to confirm a sluggish momentum in the sector. In the US, the jobless claims, productivity and labour cost data and the final March order data will be published. However, **USD traders will look forward to tomorrow's US payrolls**. Headlines on trade and/or Brexit remain wildcards.

Earlier this week, the euro was supported by better than expected EMU data while the dollar traded in the defensive ahead of the Fed meeting. **Fed's Powell didn't give in to calls for a (precautionary) rate cut**. This might prevent further USD selling for now. That said, **calls for a Fed rate cut will easily resurface if US activity and/or price data would soften further**. We retain the working hypothesis that **sustained USD gains from current levels won't be easy**. A break of EUR/USD below the 1.1110 support area might be difficult.

Yesterday, sterling gained some ground on rumours that the conservatives and labour were coming **closer to a Brexit deal**. EUR/GBP dropped below the 0.86 level. Today, the focus for sterling trading will be on **local elections in the UK**. **The BoE will also announce its policy decision and publish an inflation report**. The BoE will probably continue to support the idea of a limited tightening longer term, but stay on hold as long as uncertainty on (the consequences of) Brexit persists. The day-to-day momentum is GBP-constructive, but we don't preposition for a big leap higher.



EUR/USD: Fed Powell blocks further USD decline, but US currency probably remains vulnerable to soft US data.



EUR/GBP: drifting lower in the 0.85/0.87 ST consolidation pattern

Calendar

Thursday, 2 May		Consensus	Previous
US			
13:30	Challenger Job Cuts YoY (Apr)	--	0.4%
14:30	Initial Jobless Claims	215k	230k
14:30	Continuing Claims	1660k	1655k
14:30	Nonfarm Productivity (1Q P)	2.2%	1.9%
14:30	Unit Labor Costs (1Q P)	1.5%	2.0%
16:00	Durable Goods Orders (Mar F)	--	2.7%
16:00	Cap Goods Ship Nondef Ex Air (Mar F)	--	-0.2%
UK			
10:30	Markit/CIPS UK Construction PMI (Apr)	50.3	49.7
13:00	Bank of England Bank Rate	0.750%	0.750%
EMU			
10:00	Markit Eurozone Manufacturing PMI (Apr F)	47.8	47.8
Germany			
08:00	Retail Sales MoM/YoY (Mar)	-0.5%/2.9%	0.5%R/4.7%
Italy			
09:45	Markit/ADACI Italy Manufacturing PMI (Apr)	47.8	47.4
Norway			
09:00	DNB/NIMA PMI Manufacturing (Apr)	56.8	56.8
Spain			
09:15	Markit Spain Manufacturing PMI (Apr)	51.2	50.9
Sweden			
08:30	Swedbank/Silf PMI Manufacturing (Apr)	52.8	52.8
Events			
2019Q1 earnings	Under Armour (12:55), PG&E (bef-mkt), Kellogg (14:00), Activision (aft-mkt) ...		
13:00	Bank of England Inflation Report		
13:30	BOE's Carney speaks at press conference in London		
19:30	ECB's Praet Speaks in Vienna		

10-year	Close	-1d		2-year	Close	-1d		Stocks	Close	-1d
US	2.50	0.00		US	2.30	0.04		DOW	26430.14	-162.77
DE	0.01	0.00		DE	-0.58	0.00		NASDAQ	8049.64	-45.75
BE	0.45	0.00		BE	-0.52	0.00		NIKKEI	22258.73	0.00
UK	1.15	-0.04		UK	0.74	-0.02		DAX	12344.08	0.00
JP	-0.04	0.00		JP	-0.15	0.00		DJ euro-50	3514.62	0.00
IRS	EUR	USD	GBP	EUR	-1d	-2d		USD	-1d	-2d
3y	-0.13	2.36	1.09	Eonia	-0.3590	0.0000				
5y	0.04	2.35	1.17	Euribor-1	-0.3670	0.0000		Libor-1	2.4805	0.0000
10y	0.51	2.50	1.33	Euribor-3	-0.3100	0.0000		Libor-3	2.5756	0.0000
				Euribor-6	-0.2310	0.0000		Libor-6	2.6220	0.0000
Currencies	Close	-1d		Currencies	Close	-1d		Commodities	Close	-1d
EUR/USD	1.1196	-0.0019		EUR/JPY	124.76	-0.26		CRB	183.66	-0.59
USD/JPY	111.38	-0.04		EUR/GBP	0.8580	-0.0025		Gold	1284.20	-1.50
GBP/USD	1.305	0.0018		EUR/CHF	1.1397	-0.0035		Brent	72.18	0.12
AUD/USD	0.7015	-0.0033		EUR/SEK	10.6827	0.0414				
USD/CAD	1.3446	0.0058		EUR/NOK	9.7101	0.0320				

If you no longer wish to receive this mail, please contact us: "kbcmarketresearch@kbc.be" to unsubscribe

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		

ALL OUR REPORTS ARE AVAILABLE VIA OUR KBC RESEARCH APP (iPhone, iPad, Android)

This non-exhaustive information is based on short-term forecasts for expected developments on the financial markets. KBC Bank cannot guarantee that these forecasts will materialize and cannot be held liable in any way for direct or consequential loss arising from any use of this document or its content. The document is not intended as personalized investment advice and does not constitute a recommendation to buy, sell or hold investments described herein. Although information has been obtained from and is based upon sources KBC believes to be reliable, KBC does not guarantee the accuracy of this information, which may be incomplete or condensed. All opinions and estimates constitute a KBC judgment as of the date of the report and are subject to change without notice.

