



Sunrise

Tuesday, 26 January 2016

Rates: Risk sentiment makes a turn for the worse

Oil prices started sliding again with Brent crude below \$30/barrel. Late night weakness on US equity markets spreads to Asia with Chinese stocks up to 7% lower. The Bund opened significantly higher and tests resistance around 161.71/94 (contract high). We don't expect a break higher though.

Currencies: dollar losing slightly ground as risk-off trade resumes

Yesterday, the dollar drifted cautiously lower as oil and equities turned back south. Sterling reacted in a similar way. Today, there are plenty of eco data in the US, but USD trading will most probably again be at mercy of global market developments. Chinese equities crash.

Calendar

Headlines

S&P	↓
Eurostoxx50	↓
Nikkei	↓
Oil	→
CRB	↗
Gold	↗
2 yr US	↓
10 yr US	↓
2 yr EMU	→
10 yr EMU	↓
EUR/USD	↗
USD/JPY	↓
EUR/GBP	↗

- **The 2-day US equity rebound ran into resistance** yesterday with the S&P losing 1.5% led by a sell-off in energy shares as the oil price dropped lower. This morning, **sentiment in Asia weakened further** with Chinese indices losing up to 7% and the Nikkei ending almost 2.5% lower.
- The rebound in crude oil prices ran into resistance yesterday. **This morning, both the Brent and WTI oil price fell back below \$30/barrel** as Saudi Arabia signalled no willingness to change its strategy, despite calls from the OPEC Secretary General and Russia showing its readiness to cooperate.
- **The head of the ESM, Klaus Regling, ruled out a haircut for Greek debt**, but said extending debt maturities and deferring interest are options that could be used to make Greek debt more manageable. He added however that the country must complete the first review of its progress of structural reforms before deciding on how to restructure its sovereign debt.
- **A group of influential German economists urged the country's judges to take a stand against one of the ECB's crisis-fighting tools.** Their recommendation relates to the rejection by the European Court of Justice of a German group's challenge to the ECB's freedom to buy government bonds.
- **Philips swung to a net loss in the fourth quarter of last year**, but said that its operational performance continued to improve as it works toward the separation of its lightning division. For this year, they continue to expect modest comparable sales growth. After the US close, Apple announces its earnings.
- Today, the **eco calendar** contains the US **Richmond Fed index**, US **Conference Board's consumer confidence**, S&P CS house prices and the US Markit services PMI. BoE members testify on the Financial Stability Report.

Rates

Bonds trade with upward bias on lower oil/equity prices

Global core bonds eked out modest gains as oil prices and equities fell lower again, following a short squeeze at the end of last week. Most of the US equity and oil losses came at the end of trading and erased Friday's equity gains. Oil dropped again below \$30/barrel overnight. In a daily perspective, the US yield curve bull flattened with yields 1.2 bps (2-yr) to 5.1 bps (30-yr) lower. The German yield curve shifted in similar fashion with yields up to 3 bps lower at the 30-yr tenor and the 2-5-year sector nearly flat. On intra-EMU bond markets, 10-yr yield spread changes versus Germany were nearly flat (-1 bp to +2 bps) with Greece underperforming (+23 bps) as it is under pressure on the Schengen issue end despite Friday evening's rating upgrade from C+ to BBB-by S&P (stable outlook). The German ifo indicator, the only important release, disappointed, but didn't affect trading. The upcoming FOMC meeting (Wednesday) and the blizzard that hit the US east coast also kept many investors sidelined, making it a traditional quiet, low volume Monday session.

Core bonds erase more of the post ECB losses as risk rally fizzled out already.

Peripheral spreads barely move

	US yield	-1d
2	0,8401	-0,0453
5	1,4155	-0,0803
10	1,982	-0,0786
30	2,7694	-0,0552

	DE yield	-1d
2	-0,4430	0,0010
5	-0,2413	-0,0234
10	0,4680	-0,0190
30	1,2327	-0,0420

ECB Draghi defended the ECB's unconventional policy saying that these measures lowered borrowing costs by 80 bps. The bigger risk, Draghi said, was doing nothing. The FT put the comments against the German unease with this policy and remarked that Jens Weidmann wouldn't vote in March, an element we would think is not very important. No really new info.

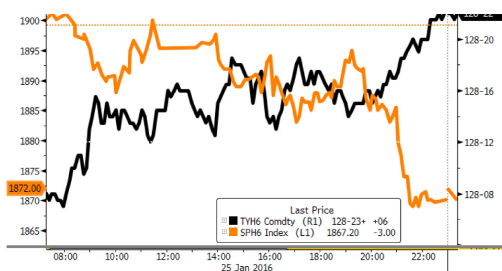
Focus on US eco data, as two-day FOMC meeting starts

The US Conference Board's consumer confidence is forecast to have stabilized in January following a limited rebound in December and significantly weakening in October and November. As labour market conditions continued to improve and lower oil prices are boosting consumers' spending power, we believe that the risks are for an upward surprise, despite market turmoil. Also Michigan consumer confidence and the weekly Bloomberg indicator have picked up somewhat recently. The US Richmond Fed business index, on the contrary, is forecast to have weakened in January, from 6 to 2, following a significant rebound in December. We believe that the risks are for a stronger outcome following the pick-up in orders last month. Both S&P CS house prices and the FHFA house price index are forecast to have increased further in November. Finally, the Markit services PMI is forecast to have dropped slightly in further in January, following a significant decline in December.

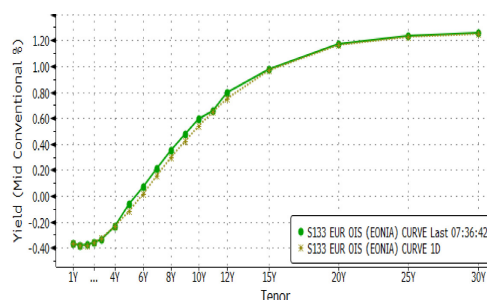
European eco calendar empty.

US Consumer confidence to have stabilized, while risks for Richmond Fed on the upside

FOMC meeting starts.



US Note future (black) and S&P future (orange): Still nice inverse correlation. Renewed equity weakness pushes bonds higher



Eonia curve: 2-year trades at -0.38 bps, suggesting that the market already priced in more than 20 bps cut in depo!!

R2	162	-1d
R1	161,94	
BUND	161,55	0,2800
S1	160,38	
S2	156,4	

Today: Risk aversion strikes back

Overnight, Asian equity markets trade up to 5% lower (China) extending yesterday evening's WS losses. Risk sentiment took a turn for the worse as oil prices started sliding again. Brent crude trades back below \$30/barrel. The US Note future trades with an upward bias, suggesting a stronger opening for the Bund as well.

Today's eco calendar contains US consumer confidence and Richmond Fed Manufacturing. Risks are on the upside of expectations. **However, if risk sentiment on equity markets deteriorates further and the new down-leg of oil prices continues, we think the Bund/US Note future might be resilient to stronger data and supply.** The US Treasury starts its end-of-month refinancing operation tonight with a \$26B 2-yr Note auction. Currently, the WI trades around 0.855%. A new test of the recent highs of the Bund (161.71-94) and US Note future (129-09+) is likely against the back of risk aversion, but we don't anticipate a break higher ahead of tomorrow's FOMC meeting.

We hold our view that there is little value in the Bund/US Note future when 10-yr yields drop respectively below 0.50% and 2%. The front end of European yield curves is expected to remain near record low levels as we expect at least a 10 bps deposit rate cut at the March ECB meeting, while markets discounts already more than 20 bps rate cut, not necessarily all in March (see graph above).



German Bund: failed test of contract high on dovish Draghi.



US Note future: Driven by oil price

Currencies

Dollar drifts marginally lower as post-Draghi rally halts

R2	1,106	-1d
R1	1,0985	
EUR/USD	1,0859	0,0048
S1	1,0711	
S2	1,0524	

Asian equities sharply lower

Moves in the major currency cross rates are limited

Plenty of US eco data, but probably with limited impact on the dollar

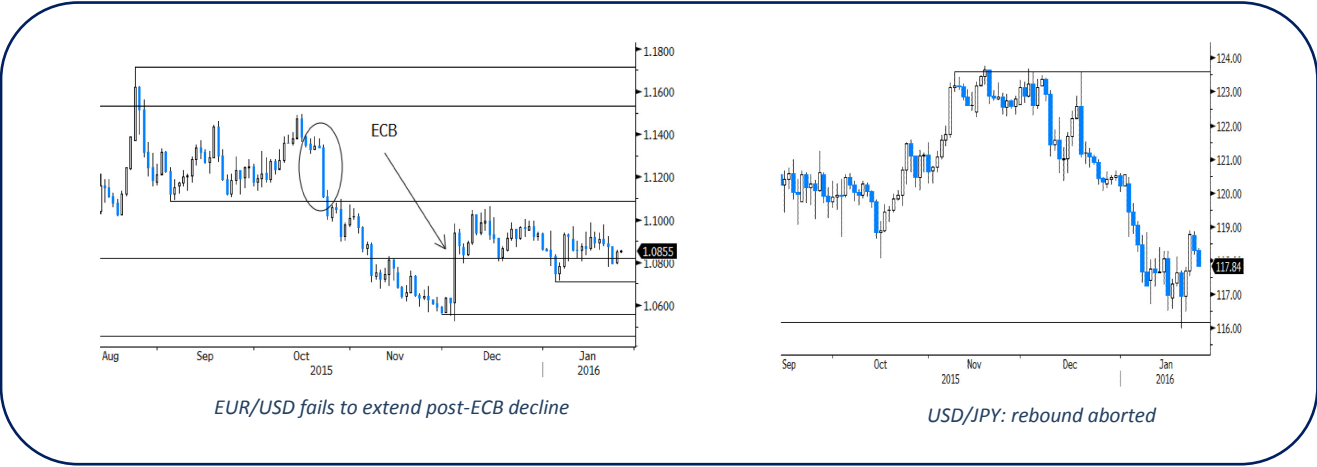
Countdown to the FOMC will probably keep USD trading range-bound

USD records slight losses as equity rebound stalls

On Monday, trading on global markets was mainly driven by the gyrations in the oil price. Oil declined early in Europe and during the US session capping the rebound in global equities. This oil-driven setback weighed slightly on the dollar. However with USD/JPY closing the session at 118.30 and EUR/USD holding in the 1.0850 area, the losses of the US currency were limited.

This morning, Asian equities fall sharply with Chinese equity indices showing losses of up to 5.0%. Oil extends its slide with Brent again trading below \$ 30 p/b. The PBOC continues to stabilize the yuan and fixed it again marginally stronger. However, renewed uncertainty on the equity markets this time weighs on the off shore yuan (USD/CNH at .61673 currently). The rebound of the Hong Kong dollar halted, too. The Canadian dollar (USD/CAD 1.4310) and the Aussie dollar (AUD/USD 0.6935) also suffer from the decline in the oil price, but for the Aussie dollar, the losses are moderate. The dollar trades again marginally lower against the yen (USD/JPY at 117.90), but is stable vs the euro (1.0850 area).

Today, focus is on US eco data with house prices, the services PMI, Richmond Fed manufacturing index and consumer confidence. We see upward risks for consumer confidence and for the Richmond Fed index. However, just one day before the FOMC meeting, a really big surprise is needed to cause a meaningful rebound of the dollar. Equities and oil will again be at least as important even as the link between the dollar and developments in other markets has loosened. This is especially the case for EUR/USD, which has settled in a tight range of late. The negative sentiment on Asian markets suggests some downside risk for the dollar today. However, with investors counting down to tomorrow's FOMC decision and to the BOJ meeting on Friday, we also expect any decline of the dollar to remain limited. It's a bit waiting for Godot.



EUR/USD fails to extend post-ECB decline

USD/JPY: rebound aborted

From a technical point of view, EUR/USD failed to regain important resistances at 1.1087 (breakdown) and 1.1124 (62% retracement from the October high). Earlier this month, EUR/USD failed also to sustain below 1.0796 support (07 Dec low). This area was again tested yesterday and on Friday, but a break didn't occur.

Next support is at 1.0711/1.0650 (correction low/76% retracement off 1.0524/1.1060) and at 1.0524. On the upside, 1.0985/1.1004 (reaction top) is a first reference. This level was left intact even as sentiment was outright risk-off before the ECB meeting. Next resistance comes in at 1.1060/1.1124 (15 Dec top/62% retracement). We expect this resistance to be strong and difficult to break. After the ECB announcement, we look to sell EUR/USD on upticks for return action lower in the range. **The picture for USD/JPY remains negative below 120, but the pair tries to build a bottom.** Still, we think that a sustained return above 120 will be difficult.

R2	0,7755	-1d
R1	0,7715	
EUR/GBP	0,7644	0,0088
S1	0,7525	
S2	0,7313	

Sterling turns back south

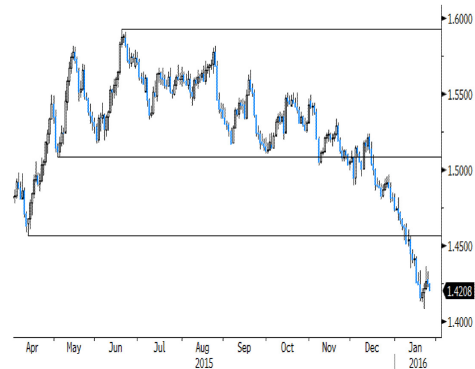
At the end of last week, the sterling rebounded nicely as oil and global equities surged. Poor UK eco data were ignored. However, this risk-on rally stalled yesterday. **Especially oil underwent a substantial setback. This left its traces on sterling.** EUR/GBP rebounded north of 0.76 and closed the session at 0.7614 (from 0.7526 on Friday). Cable also lost gradually ground throughout the day, but with the dollar also trading in the defensive, the decline developed in a gradual way. The pair closed the session at 1.4249 (from 1.4265 on Friday). **The UK January CBI industrial trends survey painted a mixed picture.** Orders declined more than expected, but the quarterly business survey showed signs of a rebound. We didn't see any lasting impact on sterling.

Today, there are not important UK eco data on the agenda. Overnight, **BoE's Forbes said that the latest fall in oil prices gives the BoE 'the luxury to of a bit more time, to check whether wages will pick up.** Overall Forbes sounded relatively positive on the labour market. However, it doesn't help sterling this morning, The decline in oil and the sell-off on Asian equity markets is sending sterling back south.

In a longer term perspective, uncertainty on Brexit and global negative risk sentiment are important drivers for sterling weakness. As long as these issues aren't solved, a sustained sterling rebound is unlikely. **The medium term technical picture of sterling against the euro remains negative as EUR/GBP broke above the 0.7493 Oct top. Next resistance stands at 0.7875.** A return below 0.74 would be a first indication that sterling enters calmer waters.



EUR/GBP: regains 0.76 barrier



Cable to resume downtrend

Calendar

Tuesday, 26 January		Consensus	Previous
US			
15:00	FHFA House Price Index MoM (Nov)	0.5%	0.5%
15:00	S&P/CS 20 City MoM SA (Nov)	0.80%	0.84%
15:00	S&P/CS Composite-20 YoY (Nov)	5.64%	5.54%
15:45	Services PMI (Jan P)	54.0	54.3
15:45	Composite PMI (Jan P)	--	54.0
16:00	Consumer Confidence Index (Jan)	96.5	96.5
16:00	Richmond Fed Manufact. Index (Jan)	2	6
Japan			
00:50	PPI Services YoY (Dec)	A: 0.4%	0.2%
Sweden			
09:30	PPI MoM/YoY (Dec)	--/--	-0.1%/-1.5%
Events			
	Philips (07:00), Siemens (07:00) Proctor & Gamble (bef mkt), Johnson & Johnson (12:45), 3M (13:30), Apple (aft mkt) Announce Q1 Earnings		
11:45	BoE Members including Carney Speak on Financial Stability Report		
	US Federal Reserve Starts two-day FOMC meeting		
Italy	CTZ & BTPei Auction (€1-1.5bn 0% Aug 2017 CTZ, €0.5-1bn 2.35% Sep 2024 BTPei, €0.5-1bn 3.1% Sep 2026 BTPei)		
US	2Yr Notes Auction (\$26B)		

10-year	td	-1d	2-year	td	-1d	STOCKS	-1d
US	1,98	-0,08	US	0,84	-0,05	DOW	15885 15885,22
DE	0,47	-0,02	DE	-0,44	0,00	NASDAQ	for Exch - NQI #VALUE!
BE	0,75	-0,03	BE	-0,38	0,00	NIKKEI	16709 16708,90
UK	1,70	-0,02	UK	0,41	-0,02	DAX	9736,15 9736,15
JP	0,23	-0,01	JP	-0,02	-0,01	DJ euro-50	3002 3001,78

						USD	td	-1d
IRS	EUR	USD (3M)	GBP	EUR	-1d	Eonia EUR	-0,238	0,003
3y	-0,089	1,056	1,006	Euribor-1	-0,23	0,00	Libor-1 USD	0,51 0,51
5y	0,142	1,343	1,269	Euribor-3	-0,15	-0,01	Libor-3 USD	0,59 0,59
10y	0,778	1,828	1,700	Euribor-6	-0,07	-0,01	Libor-6 USD	0,74 0,74

Currencies			-1d	Currencies			-1d	Commoditie	CRB	GOLD	BRENT
EUR/USD	1,08585	0,0048		EUR/JPY	127,92	-0,47			163,8033	1114,26	29,52
USD/JPY	117,805	-0,97		EUR/GBP	0,7643	0,0087	-1d		4,66	13,45	-3,22
GBP/USD	1,4199	-0,0100		EUR/CHF	1,0999	0,0035					
AUD/USD	0,6928	-0,0093		EUR/SEK	9,3044	0,04					
USD/CAD	1,4306	0,0166		EUR/NOK	9,5212	0,09					

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
Joke Mertens	+32 2 417 30 59	Institutional Desk	+32 2 417 46 25
Mathias van der Jeugt	+32 2 417 51 94	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)			
Jan Cermak	+420 2 6135 3578	Prague	+420 2 6135 3535
Jan Bures	+420 2 6135 3574		
Petr Baca	+420 2 6135 3570		
Bratislava Research (CSOB)			
Marek Gabris	+421 2 5966 8809	Bratislava	+421 2 5966 8820
Budapest Research			
David Nemeth	+36 1 328 9989	Budapest	+36 1 328 99 85

ALL OUR REPORTS ARE AVAILABLE ON WWW.KBCCORPORATES.COM/RESEARCH

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 data of the report and are subject to change without notice.

