



## Sunrise

Wednesday, 24 February 2016

### Rates: Bond losses erased after data and drop oil/equities

Core bonds yesterday once more showed their resilience and reversed initial selling waves. Some Fed governors still don't exclude a March rate hike, but markets ignore it. As the eco calendar is uneventful, sentiment on risk and technicals may drive markets, but in a context of strong underlying bond sentiment.

### Currencies: dollar trading mixed as global sentiment deteriorates

Yesterday, the dollar and euro showed both signs of underlying weakness. EUR/USD didn't profit from risk-off sentiment and tested the 1.10 area. USD/JPY remains under pressure. Today, global sentiment will remain the driver for USD trading. Cable dropped temporary below 1.40 as Brexit uncertainty, global risk-off sentiment and the lower oil price continue to weigh.

### 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     | ↗ |

- A new drop in the oil price weighed on **US equities** yesterday. The S&P ended 1.25% lower as energy shares and materials were hit hard. **This morning, most Asian shares trade lower too.** Chinese stocks reversed their losses, trading currently slightly higher.
- Fed policymakers should be prepared to consider raising interest rates in March** despite recent financial market volatility, Fed's **George** said yesterday, adding that there is no fundamental shift in the outlook. Fed's **Fischer** said it is **too early to tell whether the recent market volatility will have any impact on US growth and inflation.**
- Donald Trump won yesterday the Nevada Republican Caucus in a convincing way**, claiming victory in the third state in a row and reinforcing his status as front-runner for the Republican presidential nomination. Next week, on Super Tuesday, 11 states will hold primaries and caucuses.
- Saudi oil minister Ali Al-Naimi said yesterday he was confident more nations would join the pact to freeze output at existing levels** in talks expected next month, but ruled out production cuts. The crude oil prices dropped sharply yesterday with the Brent trading currently below \$33/barrel.
- Bank of Japan governor **Kuroda** said this morning that **they would not push interest rates further into negative territory without considering the impact of such a move on the economy and consumer prices**, adding that achieving negative rates itself is not their primary purpose.
- Today, the **eco calendar is thin** with only the UK CBI distributive trades report, US new home sales and US Markit services PMI. Fed's Lacker, Kaplan and BoE's Cunliffe are scheduled to speak.

# Rates

|    | US yield | -1d     |
|----|----------|---------|
| 2  | 0,7539   | 0,0039  |
| 5  | 1,2031   | -0,0229 |
| 10 | 1,726    | -0,0241 |
| 30 | 2,5835   | -0,0221 |

*Initial selling waves (profit taking?) turned around as eco data print weak and oil prices drag equities lower*

*Peripheral spread narrowing, but Ireland continues to widen ahead of elections*

|    | DE yield | -1d     |
|----|----------|---------|
| 2  | -0,5250  | 0,0010  |
| 5  | -0,3280  | 0,0130  |
| 10 | 0,1810   | 0,0000  |
| 30 | 0,8510   | -0,0216 |

*SNB Jordan: monetary policy has limits*

*ECB Nouy concerned about a lot in banking word including profitability*

*Fed Fischer: too early to draw conclusions from turmoil*

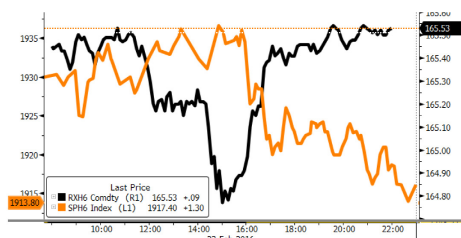
*Fed George: Rate hike on the table in March*

## Bond losses erased after data and drop oil/equities

Yesterday, global bonds initially lost ground in two selling waves, one late in the European morning and one early in the US trading session. Eventually, they recovered later in the US session. US Consumer confidence was awful, while also the Richmond Fed manufacturing index unexpectedly fell back in negative territory. At the same time, **oil fell off a cliff** after comments of **Saudi oil minister Ali al-Naimi**: "The rebalancing of oil demand and supply will start as low prices squeeze out the production of oil that is the most expensive to extract and sell." So no change in strategy of the Saudis that was put in place last year to gain market share from shale oil producers. The comments dragged equities down too. In a daily perspective, US yields fell 1.6 to 3.4 bps, the 5-yr slightly outperforming. German yields were virtually unchanged across the curve. On the intra-EMU bond market, yields spreads narrowed by 3-to-6 bps for the periphery while Ireland's underperformance continued (+4 bps).

There was no real trigger for the initial two selling waves. Two central bankers made interesting and sensible comments which nevertheless might have played a role. **SNB Jordan** suggested that CB's unconventional measures have their limits. **ECB's Nouy** was concerned about the profitability of banks and observed a trend to greater risk-taking. A few days ago, **ECB Constancio** suggested that the ECB would take into account the negative effects on banks from eventual further ECB measures. **Taken this all together, it wouldn't be too surprising that some longs decided to take profit, as the ECB's March easing actions could fall short of high expectations.**

During US dealings, **Fed vice president Fischer** said that he remained uncertain whether recent market turmoil signalled global economic woes that would slow the US economy. Therefore, it is too early to draw conclusions. Despite his comments, it looks like the March meeting comes too early for a second rate hike. **Kansas Fed George**, the number one hawk inside the FOMC, seems to disagree when she **said yesterday that a rate hike should absolutely on the table in March**. "At this point I would not say that the data have suggested there has been a fundamental shift in the outlook." **The comments had little impact.**



*Bund (black) and S&P future (orange) (intraday): Initial losses erased by eco data and weakness oil/equities*



*Oil tries to form bottom, but jury is still out*

US-German

## Agenda includes US New Home Sales and Services PMI

*Downside risks New Home sales*

Wednesday, 24 February 2016

After having increased for three consecutive months, **US new home sales** are forecast to have dropped by 4.4% M/M in January (to 520 000). Following very strong data in the previous month (10.8% M/M increase),

we believe that the **risks are for a more significant correction**. After the sharp drop in the US Markit manufacturing PMI, **the services PMI** might get a little more attention. Following two consecutive monthly declines, the consensus expects a marginal uptick.

## Germany breaks with tradition; taps off the run Bund

|             |               |        |
|-------------|---------------|--------|
| R2          | 167           | -1d    |
| R1          | 166,16        |        |
| <b>BUND</b> | <b>165,53</b> | 0,1000 |
| S1          | 163,25        |        |
| S2          | 162,86        |        |

### The German Finanzagentur taps the off the run 30-yr Bund (€1B 2.5% Jul2044).

This year, the German debt agency breaks with its tradition of only tapping on the run bonds. Throughout 2016, they've scheduled 4 taps of this off the run long Bund. In the run-up to the auction, the Bund traded relatively stable in ASW spread terms. It trades normal on the German curve and we expect that investors should be able to digest the low amount on offer. **The US Treasury started its end-of-month refinancing operation yesterday with an uneventful \$26B 2-yr Note auction. Today, the Treasury continues its refinancing operation with a \$34B 5-yr Note auction and a \$13B 2-yr FRN auction.**

## Today: Neutral view, but sentiment still positive

**Overnight**, Asian markets trade lower though losses remain contained given yesterday's weakness in Europe and the US. The oil price holds a minor downward bias following heavy losses (see above). The US Note future trades stable despite these weaker equities and lower oil. We believe that the Bund could still open stronger though.

**Today's eco calendar** contains only second tier eco data. Speeches of Richmond Fed Lacker and Dallas Fed Kaplan are worth watching, but unlikely to influence trading. Markets only attach a 10% probability to a rate hike in March. **Weakness in stock markets and oil prices continue to be supportive for core bonds. Underlying sentiment remains strong.** The Portuguese government approved in the first reading the government's 2016 budget bill which takes into account recent EU recommendations. This could prove slightly beneficiary for Portuguese bonds. Ireland could remain under pressure going into this weekend's election.

**Technically**, the US Note future's first test to drop firmly below the steep uptrend line failed, suggesting still some momentum. Nevertheless, we expect sideways trading ahead, roughly between 129 and 133. The picture for the Bund is more or less similar. Short-term range: 163.25-166.16.



German Bund: Range trading ahead?



US Note future: Ongoing test to break below steep uptrendline suggests still positive momentum

# Currencies

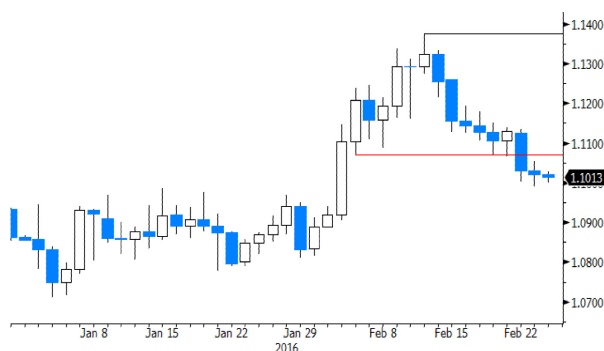
*Dollar and euro both show signs of underlying weakness as sentiment on risk deteriorates.*

|         |         |         |
|---------|---------|---------|
| R2      | 1,1376  | -1d     |
| R1      | 1,1139  |         |
| EUR/USD | 1,10115 | -0,0027 |
| S1      | 1,081   |         |
| S2      | 1,0711  |         |

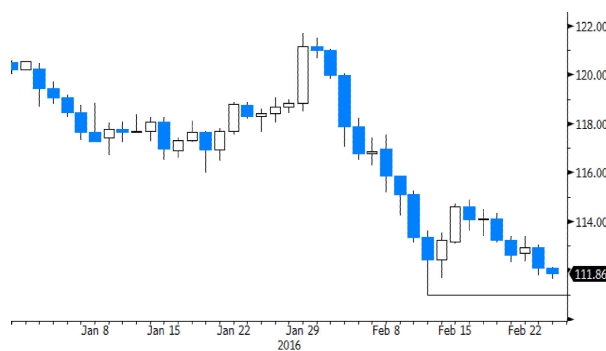
## Dollar trading mixed as risk sentiment deteriorates

On Tuesday, trading in the major currency cross rates showed a mixed picture. The dollar gained marginally further ground against a weak euro. EUR/USD tested the 1.10 barrier. A poor German IFO business climate weighed on the euro. At the same time, the dollar struggled to prevent further losses against the yen as sentiment on risk was (modestly) risk-off. The US consumer confidence was very weak, but only had a limited and temporary impact on the dollar. EUR/USD closed the session at 1.1020 (from 1.1030). USD/JPY finished the day at 111.78 (from 112.36).

**The risk-off correction from the US continues in Asia.** Oil is again a key factor for the deterioration in global investor sentiment. Comments from the oil ministers of Iran and Saudi Arabia illustrated that a deal to cut production is still very far away. Brent oil has dropped below \$33 p/b. Asian equities mostly traded with moderate losses. China rebounds late in the session. The PBOC set the fixing of the yuan marginally weaker (0.04%) against the dollar. The on-shore and offshore yuan are both trading weaker. **Overnight, BoJ's Kuroda made some balanced comments.** He said the BOJ has still plenty of room to cut interest rates further. However, the Bank would not push interest rates further into negative territory without considering the impact such a move could have on the economy and consumer prices. The comments had little impact on the yen. The Japanese currency records moderate additional gains due to the risk-off sentiment. USD/JPY trades in the 111.85 area. **The dollar remains rather strong against the euro, holding in the 1.1010 area.**



EUR/USD holding below 1.1060/70 support



USD/JPY: nearing the 110.98 correction low

*Eco calendar is moderately interesting today*

*Global sentiment and oil will continue to set the tone for USD trading*

**Today**, the eco-calendar is rather thin. There are only second tier eco data in Europe. In the US; the mortgage applications, the Market services PMI and the New home sales will be published. **US new home sales** are forecast to have dropped by 4.4% M/M in January (to 520 000). Following very strong data in the previous month (10.8% M/M increase), we believe that the **risks are for a more significant correction**. After the sharp drop in the Markit manufacturing PMI, **the services PMI** might get a little more attention. Following two consecutive monthly declines, the consensus expects a marginal uptick from 53.2 to 53.5. **Negative US data might fuel global uncertainty but, looking at the price action of the previous days, the impact on the dollar is not that evident.** Negative

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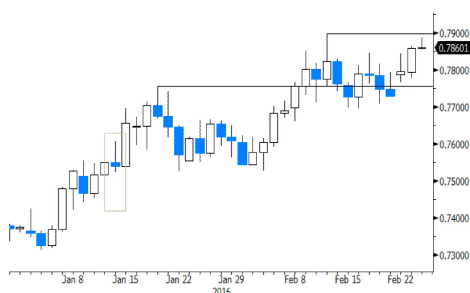
global/US sentiment recently was negative for USD/JPY. However, the 110.98 correction low is coming on the radar. It is likely that the BOJ will come out to warn markets if the yen strengthens too fast. It is unlikely for the yen to weaken in a sustainable way as long as sentiment on risk remains negative, but the pace of the recent decline might slow. **The euro recently didn't profit from negative news and the technical picture of EUR/USD deteriorated. For now, there is no reason to row against the EUR/USD negative tide.**

**From a technical point of view**, the correction high stands at 1.1376. Next important resistance kicks in at 1.1495. Recently, the dollar slowly fought back, but this move had no strong momentum. Monday's decline below 1.1060 is a ST negative for EUR/USD and might open the way to the 1.0810/1.0711 support area, but confirmation is needed. **USD/JPY dropped below the key 115.98 pre-BOJ low.** Japanese officials warned on potential action, putting a short-term floor under the pair. Even so, it remains vulnerable and is nearing again USD/JPY ST lows at 110.99. **Any rally might soon run into resistance (1.1487 recent high) The 115.98 January low is a next resistance.**

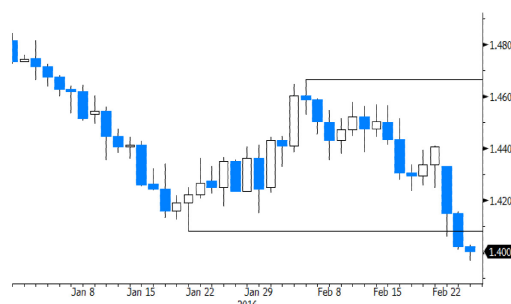
|         |               |        |
|---------|---------------|--------|
| R2      | 0,8066        | -1d    |
| R1      | 0,7898        |        |
| EUR/GBP | <b>0,7873</b> | 0,0051 |
| S1      | 0,7695        |        |
| S2      | 0,7526        |        |

## Cable falling to 1.40

**On Tuesday, there were no UK eco data but several BoE members including governor Carney testified to parliament.** Individual members put their own accents (Vlieghe was soft). Carney reiterated he still thinks the next move will be a rate hike, but the Bank has room to support the economy if needed. He also acknowledged the sterling decline due to uncertainty on Brexit. The BoE will handle this issue as any other political event risk. Carney was very reluctant to negative interest rates. Sterling initially traded with a slight negative bias, but the decline accelerated later in the session as oil declined and sentiment on risk deteriorated. Cable set a new multi-year low and closed the session at 1.4022. EUR/GBP finished the day at 0.7859 (from 0.7795 on Monday).



EUR/GBP: uncertainty for sterling remains high even after EU/UK deal



GBP/USD: testing the psychological barrier of 1.40

Today, the **BBA loans for Home purchases** and the **CBI distributive trades report** will be published in the UK. For the loans, a modest rebound is expected after last month's setback. For the distributive trades, a limited decline from 15 to 12 is expected. **UK retail sales have been very volatile of late, but the underlying trend remains constructive.** However, last week, sterling hardly reacted to very strong official retail sales data. We doubt that today's data will be able to support sterling. The negative global context will probably remain the dominant factor. After the recent decline, quite some bad news should already be discounted for sterling. However, we see no trigger for a reversal especially as oil/the global context remain negative. **The medium term technical picture of sterling against the euro remains negative as EUR/GBP broke above the 0.7493 Oct top. First resistance stands at EUR/GBP 0.7898. A return below EUR/GBP 0.74 would be a first indication that sterling enters calmer waters.**

# Calendar

| Wednesday, 24 February  |  | Consensus         | Previous          |
|---|--|-------------------|-------------------|
| <b>US</b>   |  |                   |                   |
| 13:00   | MBA Mortgage Applications                                    | --                | 8.2%              |
| 15:45   | Markit Services PMI (Feb P)                                  | 53.5              | 53.2              |
| 16:00   | <b>New Home Sales Total/MoM (Jan)</b>                        | <b>520k/-4.4%</b> | <b>544k/10.8%</b> |
| <b>Japan</b>  |  |                   |                   |
| 00:50   | PPI Services YoY (Jan)                                       | 0.3%              | 0.4%              |
| 06:00   | Small Business Confidence (Feb)                              | 47.1              | 47.2              |
| 06:00   | Leading Index CI (Dec F)                                     | --                | 102.0             |
| 06:00   | Coincident Index (Dec F)                                     | --                | 111.2             |
| <b>UK</b>   |  |                   |                   |
| 10:30   | BBA Loans for House Purchase (Jan)                           | 44800             | 43975             |
| 12:00   | <b>CBI Distributive Trades Report - Reported Sales (Feb)</b> | <b>12</b>         | <b>16</b>         |
| <b>France</b>   |  |                   |                   |
| 08:45   | Consumer Confidence (Feb)                                    | 97                | 97                |
| 18:00   | Total Jobseekers (Jan)                                       | 3590.0k           | 3590.6k           |
| 18:00   | Jobseekers Net Change (Jan)                                  | -5.3              | 15.8              |
| <b>Italy</b>  |  |                   |                   |
| 10:00   | Industrial Sales MoM YoY (Dec)                               | --                | -1.1%/0.8%        |
| 10:00   | Industrial Orders MoM YoY (Dec)                              | --                | 1.6%/12.1%        |
| <b>Norway</b>   |  |                   |                   |
| 10:00   | Unemployment Rate AKU (Dec)                                  | 4.6%              | 4.6%              |
| <b>Events</b>   |  |                   |                   |
| 02:30   | Fed's Fischer Speaks on Monetary Policy in Houston           |                   |                   |
| 14:00   | Fed's Lacker Speaks on Monetary Policy in Baltimore          |                   |                   |
| 19:10   | BoE's Cunliffe Speaks in London                              |                   |                   |
| 19:15   | Fed's Kaplan Speaks in Dallas                                |                   |                   |
| <b>Italy</b> <b>BTPei Auction (€0.5-1B 1.25% Sep2032) (11:10)</b>               |  |                   |                   |
| <b>Germany</b> <b>Bund Auction (€1B 2.5% 2044) (11:30)</b>                      |  |                   |                   |
| <b>US</b> <b>5Yr Note Auction (\$34B) &amp; 2Yr FRN Auction (\$13B) (19:00)</b> |  |                   |                   |

| 10-year | td    | -1d   | 2-year | td    | -1d   | STOCKS     | -1d                    |
|---------|-------|-------|--------|-------|-------|------------|------------------------|
| US      | 1,73  | -0,02 | US     | 0,75  | 0,00  | DOW        | 16432 16431,78         |
| DE      | 0,18  | 0,00  | DE     | -0,53 | 0,00  | NASDAQ     | for Exch - NQI #VALUE! |
| BE      | 0,51  | -0,01 | BE     | -0,41 | 0,00  | NIKKEI     | 15916 15915,79         |
| UK      | 1,43  | 0,04  | UK     | 0,34  | 0,01  | DAX        | 9416,77 9416,77        |
| JP      | -0,04 | -0,04 | JP     | -0,23 | -0,01 | DJ euro-50 | 2887 2887,38           |

|     |        |          |       |           |       | USD  | td          | -1d           |
|-----|--------|----------|-------|-----------|-------|------|-------------|---------------|
| IRS | EUR    | USD (3M) | GBP   | EUR       | -1d   | -2d  | Eonia EUR   | -0,246 -0,004 |
| 3y  | -0,125 | 0,879    | 0,839 | Euribor-1 | -0,26 | 0,00 | Libor-1 USD | 0,51 0,51     |
| 5y  | 0,029  | 1,104    | 0,996 | Euribor-3 | -0,20 | 0,00 | Libor-3 USD | 0,59 0,59     |
| 10y | 0,547  | 1,557    | 1,414 | Euribor-6 | -0,13 | 0,00 | Libor-6 USD | 0,74 0,74     |

| Currencies |         | -1d     | Currencies |        | -1d     | Commoditie | CRB      | GOLD   | BRENT |
|------------|---------|---------|------------|--------|---------|------------|----------|--------|-------|
| EUR/USD    | 1,10115 | -0,0027 | EUR/JPY    | 123,19 | -0,62   |            | 162,6369 | 1225,6 | 32,95 |
| USD/JPY    | 111,86  | -0,35   | EUR/GBP    | 0,7873 | 0,0051  | -1d        | 3,00     | 9,77   | -1,22 |
| GBP/USD    | 1,398   | -0,0127 | EUR/CHF    | 1,0936 | -0,0048 |            |          |        |       |
| AUD/USD    | 0,7187  | -0,0048 | EUR/SEK    | 9,3471 | -0,03   |            |          |        |       |
| USD/CAD    | 1,3796  | 0,0085  | EUR/NOK    | 9,4715 | -0,03   |            |          |        |       |



# Contacts

| Brussels Research (KBC)    |                  | Global Sales Force |                  |
|----------------------------|------------------|--------------------|------------------|
| Piet Lammens               | +32 2 417 59 41  | <b>Brussels</b>    |                  |
| 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  |
| <b>Dublin Research</b>     |                  | 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 | <b>Prague</b>      | +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 | <b>Bratislava</b>  | +421 2 5966 8820 |
| Budapest Research          |                  |                    |                  |
| David Nemeth               | +36 1 328 9989   | <b>Budapest</b>    | +36 1 328 99 85  |

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