



Sunrise

Monday, 19 October 2015

Rates: Risk sentiment key

Overnight, Chinese eco data were mixed but close to consensus. Chinese stock markets initially profited but risk sentiment deteriorates going into European trading. Main EMU and US stock indices are close to important resistance levels. Profit taking might occur, which could trigger a safe haven bid for core bonds.

Currencies: More USD gains ahead of the ECB meeting?

Friday's session should be rapidly forgotten, as FX crosses traded sideways without momentum. Looking forward, the eco calendar is thin and Fed speakers won't treat the economy or monetary policy. However, the ECB meeting is the highlight. A dovish outcome is expected, which should be euro negative. However, can EUR/USD 1.11 support be broken?

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 | → |

- **EU equities** closed off Friday's trading session with modest gains. Overnight, **Asian equities** started the week fairly weak, with most indices trading with losses, mainly driven by weaker Chinese data.
- **The Chinese Q3 GDP growth decelerated to 6.9%**, coming from 7.0% the previous quarter. Making it the slowest growing quarter since Q1 2009. **Retail Sales grew 10.9% Y/Y in September**, slightly better than the expected 10.8% Y/Y. **Industrial production's growth declined to 5.7% Y/Y**, below the expected 6.0% Y/Y and so did investment (10.3% Y/Y versus 10.9% Y/Y previously).
- **S&P held Russia's credit rating unchanged at BB+**. Since the drop of oil prices, Russia's creditworthiness has been in the spotlight. **However, the S&P outlook for Russia's debt remains negative.**
- **Commodities** did not move a lot since Friday afternoon, **Brent Crude** remains slightly **above the 50\$/barrel** mark. Metals are declining, with **Copper** being **down 1.5%** and **Gold down 0.8%** since Friday's open.
- Today the **eco-calendar** is thin with only the US NAHB housing market survey. Q3 earnings of Morgan Stanley (pre-opening) will get attention too.

Rates

Uneventful Friday trading session

Core bonds end mixed in dull, range-bound session

| | US yield | -1d |
|----|----------|--------|
| 2 | 0,6048 | 0,0080 |
| 5 | 1,352 | 0,0244 |
| 10 | 2,0298 | 0,0176 |
| 30 | 2,8796 | 0,0235 |

| | DE yield | -1d |
|----|----------|---------|
| 2 | -0,2640 | -0,0030 |
| 5 | -0,0380 | -0,0080 |
| 10 | 0,5510 | -0,0080 |
| 30 | 1,3130 | -0,0240 |

US eco data second tier

Focus on ECB and PMI's

On Friday, global core bonds ended mixed : the US Note future slightly lower and the Bund somewhat higher. Intraday trading ranges were very narrow though and moves technically irrelevant. Eco data included a confirmed final EMU CPI, in line with expectations US industrial production data and an above consensus University of Michigan consumer sentiment. **At the end of the day,** changes on the German yield curve ranged between -0.8 bps (2-yr) and -0.2 bps (10-yr). The US yield curve shifted 1.2 bps (2-yr) to 2 bps (5-yr) higher.

On **intra-EMU bond markets,** 10-yr yield spreads versus Germany narrowed up to 5 bps (Portugal). The Portuguese political deadlock remains. PM and Social Democrat leader Passos Coelho reiterated that his coalition remains available to negotiate an agreement for "government and stability" with the opposition Socialists. He invited them to provide a counter-proposal. Socialist Leader Costa said that the dialogue with (extreme) left-wing parties, an alternative to form a government, isn't easy but talks are going well. **Lingering uncertainty remains a negative for Portuguese OT's.**

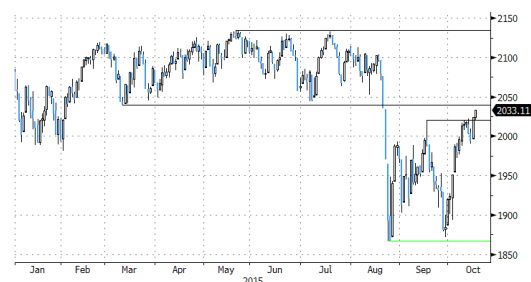
ECB meeting and EMU PMI's key this week

Today, the eco-calendar is rather thin with only the **US NAHB housing market index.** Central bank speakers include Fed Brainard, Fed Lacker (both not on monetary policy) and ECB Nowotny (spoke last week very dovish). The NAHB index is expected to remain stable at 62 in October. This reading would point to the fact that the housing market remains very sound in the US. We see no real risks towards this number. **Later this week we get more housing data** with starts & permits (Tuesday) and Existing Home sales (Thursday). These are quite volatile data and are unlikely to drive trading. Other US eco data are also second tier with initial claims (Thursday) and the Markit manufacturing PMI (Friday). The **US earnings season** is in full swing, but markets seem in good mood, also as the bar to meet the consensus is low. Nevertheless risk sentiment remains a potential market driver.

The **EMU calendar** is more enticing this week with especially the **ECB meeting (Thursday).** We don't expect the ECB to take yet additional measures, but **Mr. Draghi may lay the groundwork for additional easing at the December meeting.** (see KBC flash on Tuesday). That could keep EMU rates under pressure. The other main event are the **PMI business confidence surveys (Friday).** A very modest deterioration is expected.



T-Note future (black) & S&P future (orange): choppy sideways trading



US S&P 500: approaching key resistance around 2040.

| | | |
|-------------|---------------|--------|
| R2 | 160,62 | -1d |
| R1 | 157,67 | |
| BUND | 156,84 | 0,0000 |
| S1 | 155,77 | |
| S2 | 153,5 | |

OLO auction: no problems expected

The Belgian debt agency kicks off this week's scheduled EMU bond supply by tapping OLO 65 (4.25% Sep2022), OLO 74 (0.8% Jun2025) and OLO 71 (3.75% Jun2045). The treasury aims to raise €2.3-2.8B. The OLO's on offer traded stable in ASW spread terms last week and are normal on the Belgian curve. Both OLO 74 and OLO 71 still offer around 3 bps pick-up in ASW spread terms compared to French OAT's with similar maturities. Overall, we expect plain vanilla demand. Year-to-date, Belgium already completed around 90% of this year's expected funding need. Later this week, supply is thin with only a German Schatz auction. This week's auctions are supported by a €26.8B French redemption.

Today: Risk sentiment key

Overnight, markets focused on the Chinese eco data release with Q3 GDP, retail sales and industrial production. Q3 GDP growth slowed from 7% Y/Y in Q2 to 6.9% Y/Y in Q3, but was a tad above expectations (6.8% Y/Y). Industrial production data slightly disappointed while retail sales were somewhat stronger. Overall, a mixed, very close to consensus outcome. Sentiment on Chinese stock markets was initially positive but stocks are sliding going into the start of European trading. The US Note future initially lost ground but is recovering these losses.

Today's eco calendar is thin with only the second tier NAHB Housing index in the US. Topics of Fed speakers (Brainard & Lacker) suggest that they won't comment on monetary policy. ECB Nowotny warned already last week that the ECB is clearly missing its inflation target and that the CB should act. Over the weekend, he tempered his comments by saying that it's too early to talk about extending QE beyond September 2016. So overall, we don't expect today's calendar to influence bond markets. **Risk sentiment on equity markets is key with main US and EMU indices approaching important (hard-to-break?!) resistance levels.** Profit taking in stock markets could trigger some safe haven flows. Thursday's ECB meeting will likely hold EMU rates under downward pressure (dovish bias).

After the dovish September FOMC meeting, we eyed a return to the contract high for the US Note future, but we didn't anticipate a break higher. That last assumption is under new pressure as markets push a Fed lift-off well into 2016, while also anticipating additional QE by the ECB. A new decline in equity prices could further fuel core bonds at this stage. **We are neutral for core bonds. A test of the contract highs is very likely.**



German Bund: test upper bound failed and back in ST range. Longer term uptrend still intact.



US Note future: New test of high likely

Currencies

| | | |
|----------------|---------------|---------|
| R2 | 1,1714 | -1d |
| R1 | 1,1495 | |
| EUR/USD | 1,1376 | -0,0006 |
| S1 | 1,133 | |
| S2 | 1,1087 | |

EUR/USD drifts slightly lower

On Friday, the main FX crosses had a quiet, unspectacular sideways oriented session in which the dollar ultimately closed with some minor gains against euro, yen and sterling. Risk sentiment wasn't too bad and at times supported the dollar. The US eco data were mixed. The JOLT labour data disappointed a bit, while the production and especially Michigan consumer confidence were stronger. EUR/USD traded in the 1.14 to 1.1340 range. As the last move of US equities was sharply up, EUR/USD ended the session near the lower boundary of the intra-day range at 1.1349, down from 1.1384 on Thursday. USD/JPY held initially close to the 119 level, but got some momentum in the US afternoon trading, closing at 119.44 (up from 118.90 previous close).

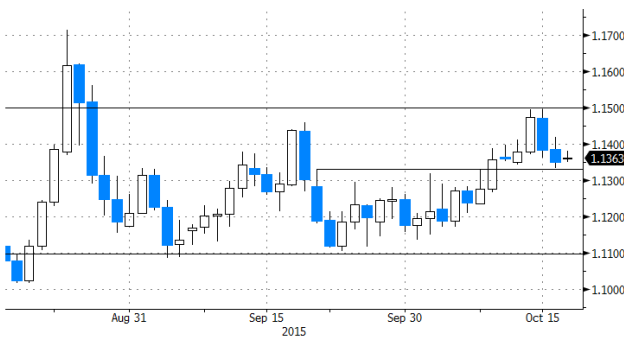
EUR/USD and USD/JPY stabilize

Chinese figures can't charm investors, reflected by mild risk off

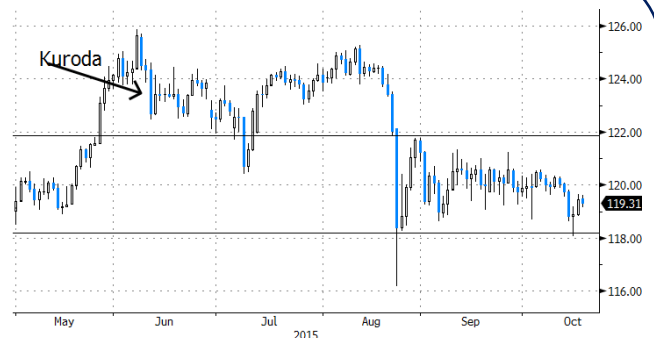
Overnight, the dollar trades slightly weaker against euro (1.1368) and against yen (119.29). Risk sentiment turned slightly negative overnight and most equity indices now show modest to moderate losses. The Chinese figures were mixed. Chinese Sept. retail sales were marginally stronger while industrial production and investment were a lot weaker than expected. Q3 GDP was a tad higher than expected at 6.9% Y/Y (but Q/Q stable and as expected at 1.8%; still the slowest growth rate since Q1 2009). GDP details showed weakness in exports and manufacturing and strength in consumption and services. These figures are widely contested. European and US equity markets are at or near key resistance, which suggests that some profit taking may occur after a test.

Light eco calendars this week, but ECB meeting highlight, as is the earnings season and equity reaction.

Regarding trading, the US calendar is light today and in fact the whole week. Today, the NAHB homebuilders' sentiment is expected to have stabilized at a high level (62). More house data include starts & permits on Tuesday and Existing Home sales on Thursday. These are quite volatile on a month-to-month basis and unlikely to give the dollar firm guidance. For the sake of completeness, the initial claims will be released on Thursday and the Markit manufacturing PMI on Friday. So, eco data are nothing to get excited about. Similarly, there are 5 public appearances by Fed members scheduled, but none deals monetary policy or the economy and thus it doesn't look promising in terms of FX market movements. The US earnings season is now in full swing, but markets seem in good mood, also as the bar to meet the consensus is low. Nevertheless risk sentiment may be a key driver for the dollar ahead of the ECB meeting.



EUR/USD: Test of 1.1460/1.15 area rejected. Now a test of the downside this week?



USD/JPY: 118-122 range stays intact, but risk on test downside still present

The **EMU calendar** is more enticing with the **ECB meeting on Thursday**. We don't expect the ECB to take yet additional measures, but **Mr. Draghi may lay the groundwork for such extra loosening**. (KBC flash follows on Tuesday). **So, any upside for EUR/USD should be limited this week**. The other main event is the release on Friday of the **PMI business confidence surveys**. A very modest deterioration is expected.

Some come-back of the dollar this week?

Global markets struggle to assess the health of the global economy and its impact on monetary policy. Of late (currency) markets were focused on the impact of weaker US data on the Fed rate hike path. This made the dollar vulnerable short term, but in absence of US eco data this week, attention may turn to the ECB which may send a dovish message at its meeting on Thursday. The 1.1460/95 resistance was extensively tested, but the test was rejected. For today, we see mainly sideways trading, driven by the eventual gyrations of the equity markets, even if the relationship between equities and EUR/USD loosened. The jury is still out, but the topside in EUR/USD is better protected. The dollar may try to make some come-back ahead of the ECB meeting. In this respect EUR/USD support stands at 1.11. In a longer term perspective, **if the policy divergence between the Fed and the ECB becomes less outspoken, EUR/USD may return toward the August correction high at 1.1719. USD/JPY looks more vulnerable to a delay in the Fed risk-off and/o**

Will sterling dip below 0.733 resistance on ECB?

Uneventful sterling trading on Friday.

On Friday, Sterling traders endured an uninspiring trading session that ended mixed for sterling. Slight gains versus euro and minor losses versus dollar.

| | | |
|----------------|---------------|--------|
| R2 | 0,7592 | -1d |
| R1 | 0,7493 | |
| EUR/GBP | 0,7363 | 0,0007 |
| S1 | 0,7333 | |
| S2 | 0,7196 | |

Trading in EUR/GBP and cable was at the mercy of global market moves in the dollar and the euro. The euro felt some slightly follow-through selling in the wake of Thursday's setback. EUR/GBP traded with a slight negative bias in the morning, but soon settled close to the 0.7350 level, where it closed, down from 0.7363 on Thursday. Cable hovered also in a tight range near 1.5450 and closed at 1.5438, down from 1.5460 on Thursday. Both cross rates didn't go anywhere.

UK retail sales on Friday main eco release

Regarding the market calendar this week, only the **retail sales** on Thursday have market moving potential. Important might be a testimony and a speech of **BoE Carney** on Tuesday/Wednesday. According to the FT, the government mandated former MPC member Branchflower to lead a review of the BoE mandate. Are other objectives than inflation needed to include? Should the target be higher or lower? Very important questions that may in time move UK yields and sterling.

Many MPC speakers incl. Carney twice

BoE mandate to be reviewed.

Earlier tonight, Rightmove house prices were up 0.6% M/M and 5.6% Y/Y, down from 6.4% Y/Y in September. It won't have a lasting impact though. This emptied today's UK eco calendar. Sterling temporarily weakened but EUR/GBP (0.7358), trades again close to Friday's levels. So sterling trading will again be driven by **technical considerations and by the price swings in the major dollar cross rates**. The downside in sterling (EUR/GBP 0.7483/0.75 strong resistance) looks better protected, but will a dovish ECB help to extend the recent sterling rebound? **From a technical point of view**, EUR/GBP still trades in the upper part of the sideways range capped by 0.7483/0.7333. The former (resistance) was extensively tested last week. Sustained trading north of 0.7483 would deteriorate the ST sterling picture, but a drop below 0.7333 paints a sterling bullish double top on the charts, which may see EUR/GBP extend towards 0.72 (tough resistance for sterling). Will a soft ECB meeting help sterling regain ground? That's our bias at the start of the week.

Technicals important, as drop below EUR/GBP 0.7333 paints double top on the charts.

Calendar

| Monday, 19 October | | Consensus | Previous |
|--------------------|--|--------------|-----------|
| US | | | |
| 16:00 | NAHB Housing Market Index (Oct) | 62 | 62 |
| China | | | |
| 04:00 | Retail sales YoY (Sep) | A: 10.9% | 10.8% |
| 04:00 | Industrial Production YoY (Sep) | A: 5.7% | 6.3% |
| 04:00 | GDP SA QoQ/YoY (3Q) | A: 1.8%/6.9% | 1.7%/7.0% |
| UK | | | |
| 01:01 | Rightmove House Prices MoM/YoY (Oct) | A: 0.6%/5.6% | 0.9%/6.4% |
| EMU | | | |
| 11:00 | Construction Output MoM/YoY (Aug) | --/-- | 1.0%/1.8% |
| Events | | | |
| Belgium | OLO auction (OLO 65 4.25% Sep2022, OLO 74 0.8% Jun2025 & OLO 71 3.75% Jun2045) | | |
| 16:00 | Fed's Brainard Speaks on Cutting Regulatory Red Tape | | |
| 17:00 | ECB's Nowotny in Vienna panel discussion | | |
| 18:00 | Fed's Lacker Speaks on Early Childhood Education in Richmond | | |

| 10-year | td | -1d | 2-year | td | -1d | STOCKS | -1d |
|---------|------|-------|--------|-------|-------|------------|------------------------|
| US | 2,03 | 0,02 | US | 0,60 | 0,01 | DOW | 17216 17215,97 |
| DE | 0,55 | -0,01 | DE | -0,26 | 0,00 | NASDAQ | for Exch - NQI #VALUE! |
| BE | 0,87 | -0,02 | BE | -0,21 | -0,02 | NIKKEI | 18131 18131,23 |
| UK | 1,80 | 0,02 | UK | 0,51 | 0,02 | DAX | 10104,43 10104,43 |
| JP | 0,33 | 0,01 | JP | 0,02 | 0,00 | DJ euro-50 | 3265 3264,93 |

| IRS | EUR | USD (3M) | GBP | EUR | -1d | -2d | USD | td | -1d |
|-----|-------|----------|-------|-----------|-------|------|-------------|--------|-------|
| 3y | 0,101 | 0,949 | 1,089 | Euribor-1 | -0,11 | 0,00 | Eonia EUR | -0,142 | 0,001 |
| 5y | 0,327 | 1,363 | 1,395 | Euribor-3 | -0,05 | 0,00 | Libor-1 USD | 0,51 | 0,51 |
| 10y | 0,938 | 1,972 | 1,840 | Euribor-6 | 0,02 | 0,00 | Libor-3 USD | 0,58 | 0,58 |
| | | | | | | | Libor-6 USD | 0,75 | 0,75 |

| Currencies | -1d | Currencies | -1d | Commodity | CRB | GOLD | BRENT |
|------------|----------------|------------|---------------|-----------|----------|--------|-------|
| EUR/USD | 1,1376 -0,0006 | EUR/JPY | 135,65 0,07 | | 199,4474 | 1173,1 | 50,15 |
| USD/JPY | 119,245 0,09 | EUR/GBP | 0,7363 0,0007 | -1d | -0,38 | -3,70 | -0,05 |
| GBP/USD | 1,5447 -0,0017 | EUR/CHF | 1,085 0,0012 | | | | |
| AUD/USD | 0,7275 -0,0009 | EUR/SEK | 9,3633 0,00 | | | | |
| USD/CAD | 1,2923 0,0045 | EUR/NOK | 9,2056 0,00 | | | | |

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