



Sunrise

Friday, 12 February 2016

Rates: A downward correction today?

Core bonds still thrived very well yesterday, but closed well off the intra-day highs. In Asia, the sentiment on risk seems to have improved with oil higher and a stable yen. The eco data may surprise positively. Combined this could give riskier markets some respite and help trigger a correction of core bonds which became heavily overbought.

Currencies: Intervention speculation blocks downside in USD/JPY

Yesterday, a new risk-off selling wave hit the dollar hard. USD/JPY dropped to the 111 area. From there, speculation on BOJ interventions capped the rise of the yen. The losses of the dollar against the euro remained modest. Today, the eco calendar heats up. Will decent US eco data help to ease global tensions and help to build a base for the dollar?

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	↗

- **US Equities lost further ground** yesterday with the S&P ending 1.2% lower led by financials. The Nasdaq reversed part of its losses to end 0.4% down. This morning, **most Asian shares trade lower but losses are generally contained**. After being closed yesterday, Japanese shares closed 5% lower.
- **Japanese policymakers said they would seek a global policy response from G20 nations to world market turbulence** when they meet later this month in Shanghai. BOJ Governor Kuroda dismissed suggestions that the rout was caused by the bank's new negative interest rate policy.
- **World powers agreed this morning to a cessation of hostilities in Syria set to begin in one week** and provide rapid humanitarian access to besieged Syrian towns, but failed to secure a complete ceasefire or an end to Russian bombing as the agreement did not apply to Islamic State and other defined terrorists by the UN.
- In the final three months of the year, the **German economy grew by 0.3% Q/Q** in line with market expectations. **The Stats office added that impulses came from domestic demand, higher state spending and a slight increase in private consumption**, while net exports were a drag on growth.
- **The WTI oil price rebounds almost 5%** this morning after having dropped to a 12-year low yesterday, supported by comments of the United Arab Emirates energy minister who said OPEC was ready to cooperate on production cuts. **The Brent oil price rebounded too**, hovering currently around \$31.50/barrel.
- **Today the eco calendar heats up** with the **first estimate of euro zone Q4 GDP**, EMU industrial production, the **US retail sales** and US University of Michigan consumer confidence. **EU Finance Ministers meet in Brussels**.

Rates

Core bonds extend rally

German curve continues to bull flatten.

Peripheral spreads continue to blow out, especially Portuguese and Greek ones.

	US yield	-1d
2	0,6574	-0,0366
5	1,1441	0,0187
10	1,6881	0,0149
30	2,5306	0,0385

	DE yield	-1d
2	-0,5190	-0,0130
5	-0,3320	-0,0440
10	0,1970	-0,0480
30	0,9020	-0,0448

Yellen slightly more dovish than on Thursday

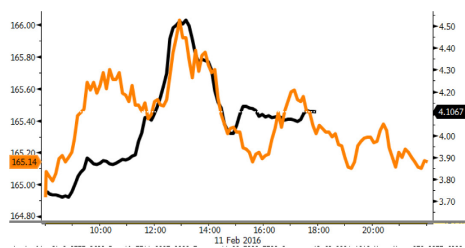
Too early to know whether turmoil will alter Fed rate policy

Fed examine negative rates as tool if the US economy would falter.

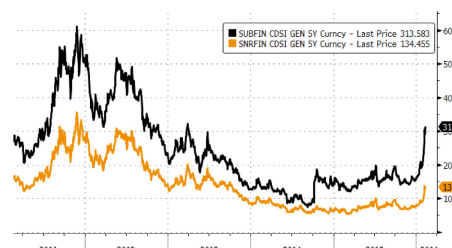
Ugly markets support core bonds, as stress mounts fast

Yesterday, global core bonds profited once more from safe haven flows. European equity weakness, amid an ongoing sell-off of financials, rising credit spreads and in particular a significant Portuguese spread widening pushed the Bund (and US Note future) higher. As Portuguese tensions eased (central bank buying?), core bonds lost part of the intraday gains. In a daily perspective, the German yield curve bull flattened with yields 2.8 bps (2-yr) to 8.6 bps (30-yr) lower. Changes on the US yield curve vary between -5.2 bps (2-yr) and -1.2 bps (30-yr). The US 10-yr yield dropped below 1.64% support (1.626%), to the lowest level since 2012 (1.52%). The all-time low stands at 1.38%. **Other bond positive factors** were a risk warning of SG that negatively affected equities, a Swedish 15 bps rate cut to -0.50%, a sharp rise in Portuguese bonds and credit spreads in general and a new low in WTI oil (\$26.05). US initial jobless claims on the contrary were better than expected, but ignored. **On intra-EMU bond markets**, 10-yr yield spreads versus Germany increased up to 4 bps for the (semi-)core, 11/13 bps for Spain/Italy, 45/70 bps for Portugal and Greece.

In the second leg of her semi-annual testimony, **Fed chairwoman Yellen** refuted the idea the Fed's rate hike in December was the reason behind the turmoil in markets since the start of January. She blamed the yuan depreciation and a dive in oil prices as the drivers behind the turmoil. **Yellen sounded a bit more dovish than on Wednesday when she said the Fed was assessing the impact of the swings in markets on the economy, but she doubted that would prompt it to reverse course and cut rates.** "It's not what I think the most likely scenario". It is too soon she added to know whether those risks are severe enough to alter Fed's rate policy. Yellen admitted that the Fed was taking another look at **negative rates** as a potential policy tool if the US economy faltered. In 2010, the Fed had decided that they would not work well, but the experience of European countries has convinced the Fed to take another look. Legal issues still need to be cleared out.



Bund future (orange) and Portuguese 10-yr yield (black): Part of Bund gains due to Portuguese bond sell-off. Buying from CB to help it lower again? Spread widening rapidly becomes ECB concern



Itraxx CDS banks subordinate (black) senior (orange): Stress in bank credit should fast become next concern ECB. Negative yields are contra-productive, but is Draghi ready to admit?

Upside risks for EMU GDP and US retail sales

Fed Dudley to speak

Busy eco calendar

Several EMU countries already published their **GDP** figures, showing continued strong growth in Spain (0.8% Q/Q), a limited slowdown in French growth (0.2% Q/Q from 0.3% Q/Q), while Belgian GDP picked up slightly (to 0.3% Q/Q from 0.2% Q/Q). This morning, German GDP came out in line with expectations, increasing by 0.3% Q/Q, the same pace of growth as in Q3. For **the euro area**

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reading, the consensus is looking for an increase in GDP by 0.3% Q/Q, also the same pace of growth as in Q3. We see limited upside risks to the consensus. **In the US**, following disappointing end of year sales, **retail sales** are forecast to have increased slightly in January, by 0.1% M/M. The headline figure will probably remain depressed by lower gasoline prices. As a result, the control group is expected to show a somewhat stronger 0.3% M/M increase. Although personal consumption growth slowed in Q4, a further improvement in labour market conditions, increasing wages and lower oil prices should continue to support spending. We believe therefore that **the risks are for an upward surprise**, while also more normal weather (less warm) conditions might have supported sales of seasonal goods. The **University of Michigan consumer confidence** is expected to show a slight uptick in February after a limited decline in January. Overall favourable economic conditions might however be overshadowed by turmoil on financial markets and therefore we see risks for a **downward surprise**.

R2	167	-1d
R1	166,16	
BUND	165,59	0,8100
S1	160,38	
S2	156,4	

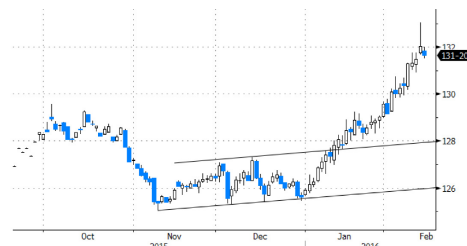
Today: at last again some eco data of importance

Overnight, Japanese equities are sharply lower, but this is still mainly catching up after closure. Other open Asian bourses modestly lose ground, not more than WS yesterday. Yen is stable, albeit helped by verbal support of FM Aso (abrupt market moves are undesirable according to G7-20; watch FX with sense of urgency and respond if necessary) and BOJ Kuroda (watching markets closely). US Treasuries trade lower and European equities should open higher. Oil trades higher after setting new low yesterday (WTI). This suggests a weaker opening for the Bund as well and maybe some further correction after the breathtaking rally.

Today's eco calendar is busy and eventful. We see **upward risk for the EMU Q4 GDP and for US retail sales**. Economic data have been overshadowed in past month by market turmoil. EMU Q4 GDP is a bit outdated, but a market reaction on a stronger outcome is possible as we have the feeling the upside of the Bund (and US Treasuries) may have become a bit exhausted for now. US retail sales are timelier and a stronger report may be welcomed in riskier markets and embraced as a sign the sell-off is overdone. However, markets may be cautious ahead of the US closed markets on Monday (President's day) and the return of the Chinese, which are intrinsically bond positives. After weighing all factors, we think that some core bond correction is likely, but it is too early to call it a change in direction. It should be more technical inspired. US T-Note graph (see below) shows a tentative reversal sign. However, **longer term sentiment remains positive for core bonds, but heavily overbought, it makes them vulnerable for bouts of short term profit taking**.



German Bund: Technically overbought. Vulnerable to profit taking?



US Note future: Also overbought and yesterday tentative sign of ST reversal

Currencies

USD/JPY decline blocked on intervention speculation

Down down-leg on global equities weighs on the dollar.

USD/JPY decline blocked on intervention speculation

R2	1,1495	-1d
R1	1,1376	
EUR/USD	1,13095	0,0013
S1	1,106	
S2	1,081	

Today, a busy calendar

Upside risks for EMU GDP & US retail sales

Dwnside risks Michigan consumer confidence.

Will they ease the global market sell-off?

Wednesday was again an outright risk-off session. USD/JPY initially tumbled to the 111 area, but the move stalled on intervention speculation. EUR/USD set a correction top in the 1.1376 area as interest rate differentials between the US and Germany narrowed. Later in the session as tensions eased slightly. It helped the dollar only mildly. EUR/USD closed the session at 1.1323 (from 1.1292 on Wednesday). USD/JPY closed the session at the 112.49 (from 113.35).

This morning, Asian equities lose moderate ground, more or less in line with the US yesterday. Japan underperforms (Topix is losing-4.5%) as Japanese markets had some catching up to do after yesterday's closure. There is plenty of market speculation that Japan might be close to interventions. BOJ's Kuroda and PM Abe met to discuss the economic situation. **Fin Min officials described the currency moves as rough and said they were monitoring the FX market with a sense of urgency.** Fin Min Aso indicated that the MOF would take appropriate action if needed. At the same time he said to seek G20 coordination to address the recent turmoil. In nervous trading, USD/JPY 'stabilizes' in the lower half of the 112 big figure. EUR/USD is holding relatively stable near 1.13.

Today, the first **estimate of EMU Q4 GDP** will be published. The consensus expects 0.3% Q/Q and 1.5% Y/Y. We see slight upward risks for growth. If so, it might be a positive for the euro, but we don't expect it to be a game changer. The focus is on other drivers of market stress, not on European growth. **In the US, the retail sales** are expected at a soft 0.1% M/M (0.3M% for the control group), but with upside risks; Michigan confidence is expected marginally higher at 92.3, but with downside risks. Of late, eco data were only of second tier importance for FX trading. The internal market dynamics (risk-off) was the key driver. Can eco data combined with other factors gradually bring markets to a short-term equilibrium? We think the market nears some kind of exhaustion and consolidation. It is still only a working hypothesis. **The reopening of mainland Chinese markets on Monday might still be a tricky moment.** Such an easing of tensions is also an important factor to put a floor for the dollar.



EUR/USD: hovers up and down in the 1.13 area



USD/JPY: sell-off blocked by intervention fears

Over the previous days, **global markets showed diffuse, instable trading dynamics**. It will take time for all these markets to find a new equilibrium. At the same time, US bond yields remain on a downward trajectory, but this move might slow. **A sustained directional rebound of the dollar remains difficult in this context, even as Fed's Yellen kept the door open for further rate hikes**. USD/JPY was vulnerable in this process, but intervention fears have blocked the downside. EUR/USD is setting minor new short-term highs, but the dollar losses against the euro remain limited. We look out for a topping out in EUR/USD.

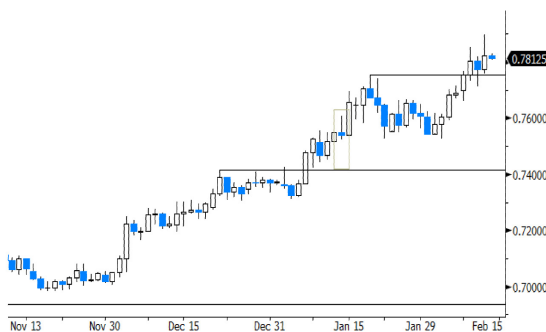
From a technical point of view, EUR/USD broke above the 1.1060/1.1124 resistance area (15 Dec top: 62% retracement). This is a dollar negative. The short-term correction high stands at 1.1378. Next important resistance kicks in at 1.1495. The jury is still out, but we are looking for a topping out in EUR/USD. **USD/JPY dropped below the key 115.98 pre-BOJ correction low. This was high profile warning signal. We expect the BOJ to send further warning signals. This might put a floor for the USD/JPY short term. However, there is no good reason to fight current yen strength as long as global uncertainty persists.**

Sterling declines, but closes off the intraday lows

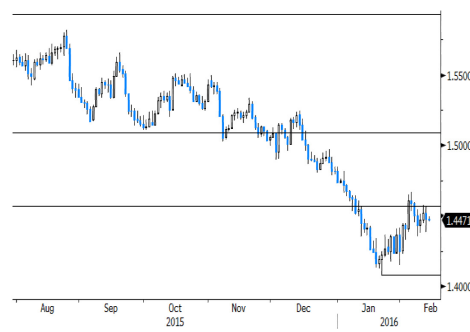
R2	0,8066	-1d
R1	0,7898	
EUR/GBP	0,7813	0,0035
S1	0,7756	
S2	0,7661	

The global risk-off trade weighed again on sterling, in the absence of UK economic news. EUR/GBP set a new correction top just below 0.79, but the pair returned part of the early gains in line with EUR/USD. The pair closed the session at 0.7822 (from 0.7775). Cable lost more than one big figure, but also closed the session off the intraday lows at 1.4477 (from 1.4522).

Today, only the UK December construction output, not a market mover, will be published. There are some tentative signs that global risk sentiment might be less negative at the start of the European trading session. If confirmed, this should slow the sterling sell-off in a daily perspective. However, we see only limited room for a sustained rebound of sterling. The most recent headlines on the Brexit-negotiations suggest some obstacles in the process. The issue will become even more important next week as the EU summit nears. **The medium term technical picture of sterling against the euro remains negative as EUR/GBP broke above the 0.7493 Oct top. Next big resistance stands at EUR/GBP 0.7854/75.** A return below EUR/GBP 0.74 would be a first indication that sterling enters calmer waters.



EUR/GBP holds near the recent top



GBP/USD: decline to slow (temporary)?

Calendar

Friday, 12 February		Consensus	Previous
US			
14:30	Import Price Index MoM/YoY (Jan)	-1.5%/-6.8%	-1.2%/-8.2%
14:30	Retail Sales Advance MoM (Jan)	0.1%	-0.1%
14:30	Retail Sales Ex Auto and Gas (Jan)	0.3%	0.0%
14:30	Retail Sales Control Group (Jan)	0.3%	-0.3%
16:00	Business Inventories (Dec)	0.2%	-0.2%
16:00	U. of Mich. Sentiment (Feb P)	92.3	92.0
UK			
10:30	Construction Output SA MoM/YoY (Dec)	2.0%/0.8%	-0.5%/-1.1%
EMU			
11:00	Industrial Production SA MoM/WDA YoY (Dec)	0.3%/0.7%	-0.7%/1.1%
11:00	GDP SA QoQ /SA YoY(4Q A)	0.3%/1.5%	0.3%/1.6%
Germany			
08:00	Wholesale Price Index MoM/YoY (Jan)	--/--	-0.8%/-1.0%
08:00	CPI MoM/YoY (Jan F)	-0.8%/0.5%	-0.8%/0.5%
08:00	GDP SA QoQ/YoY (4Q P)	0.3% / 1.4%	0.3% / 1.8%
France			
08:45	Wages QoQ (4Q P)	--	0.2%
08:45	Non-Farm Payrolls QoQ (4Q P)	--	0.0%
Italy			
10:00	GDP QoQ/YoY (4Q P)	0.3%/1.2%	0.2%/0.8%
Spain			
09:00	CPI Core MoM/YoY (Jan)	--/0.7%	0.0%/0.9%
09:00	CPI EU Harmonised MoM/YoY (Jan F)	-2.5%/-0.4%	-2.5%/-0.4%
Events			
EU Finance Ministers Meet in Brussels			
16:00	Fed's Dudley Answers Questions at Press Briefing in New York		
Monday 15 February	US Markets are Closed in Observance of President's Day		

10-year	td	-1d	2-year	td	-1d	STOCKS	-1d
US	1,69	0,01	US	0,66	-0,04	DOW	15660 15660,18
DE	0,20	-0,05	DE	-0,52	-0,01	NASDAQ	for Exch -NQI #VALUE!
BE	0,63	0,02	BE	-0,43	-0,01	NIKKEI	14953 14952,61
UK	1,31	-0,11	UK	0,28	-0,05	DAX	8752,87 8752,87
JP	0,08	0,07	JP	-0,21	0,03	DJ euro-50	2680 2680,35

						USD	td	-1d
IRS	EUR	USD (3M)	GBP	EUR	-1d	-2d	Eonia EUR	-0,239 -0,002
3y	-0,133	0,806	0,736	Euribor-1	-0,24	0,00	Libor-1 USD	0,51 0,51
5y	0,055	1,059	0,883	Euribor-3	-0,18	0,00	Libor-3 USD	0,59 0,59
10y	0,597	1,522	1,307	Euribor-6	-0,11	0,00	Libor-6 USD	0,74 0,74

Currencies		-1d	Currencies		-1d	Commoditie	CRB	GOLD	BRENT
EUR/USD	1,13125	0,0016	EUR/JPY	126,59	-0,36		156,3992	1244	31,47
USD/JPY	111,9	-0,48	EUR/GBP	0,7814	0,0036	-1d	-0,18	35,95	0,80
GBP/USD	1,4473	-0,0050	EUR/CHF	1,1005	0,0031				
AUD/USD	0,7096	0,0001	EUR/SEK	9,4805	0,00				
USD/CAD	1,3909	-0,0051	EUR/NOK	9,6663	0,03				

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