



Sunrise

Wednesday, 17 February 2016

Rates: Core bonds remain resilient

Yesterday, core bonds lost modest, but technically insignificant ground in a sideways oriented session. Overnight risk sentiment turned slightly negative. Oil prices remain under pressure, stocks are weak and some Fed governors talked soft. So, we might see core bonds trading pretty solid, but start of a new up-leg is unlikely.

Currencies: Dollar rebound running into resistance

The dollar showed a mixed picture yesterday. USD/JPY struggled as sentiment on risk deteriorated. At the same time, the US currency remained well bid against the euro. Today, the focus is on the Fed minutes. A soft tone might hamper further USD gains. Uncertainty on the EU/UK negotiations continues to weigh on sterling.

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 extended their gains yesterday** to close the session with gains of up to 2%, despite a decline in the oil price, as US equities caught up with European equities (after Monday's close on Wall Street). This morning, **most Asian shares trade lower** led by Japanese ones, as the yen strengthened again.
- The WTI oil price fell back below \$30/barrel** yesterday, while the Brent is losing further ground this morning, nearing the \$32/barrel level after major oil producers decided to freeze oil production. **OPEC members will travel to Iran today to persuade the country to participate in the deal.**
- Rating agency **Standard & Poor's** warned that **the increase in China's debt relative to GDP could pressure the country's credit rating**, adding that it could be downgraded if weak economic or financial sector trends materially increase the government's contingent fiscal liabilities, or if policy makers try to boost growth by expanding credit to fund investment spending. **S&P currently rates China at AA-**.
- ECB's **Nowotny** said in an interview that **financial market turbulence in recent weeks has been largely driven by emerging markets**. Nowotny added that preserving liquidity remains paramount for lenders, underscoring why the ECB's measures in this pace are so important.
- China has positioned surface-to-air missiles on a disputed island in the South China Sea**, US and Taiwan officials said, after US President Barack Obama met with leaders of Southeast Asian nations and called for a peaceful resolution of territorial disputes.
- Today, the **eco calendar** contains the UK labour market data, US housing starts and building permits, US PPI inflation and the US production data. The Fed will release the **Minutes from its January 26-27 FOMC meeting**.

Rates

	US yield	-1d
2	0,7055	-0,0243
5	1,1924	-0,0423
10	1,7465	-0,0344
30	2,6132	-0,0192

Core bonds lose ground, steepening the curve, despite weaker US and EMU eco data and declining oil

Curves bear steepen outperforms

Peripheral bonds calm down

	DE yield	-1d
2	-0,5030	0,0030
5	-0,2950	0,0160
10	0,2620	0,0230
30	0,9687	0,0223

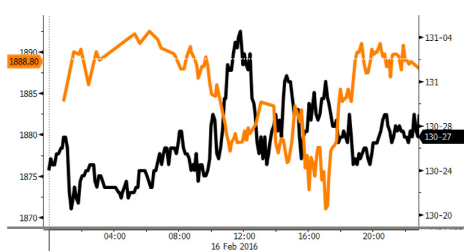
Fed Harker and Rosengren plead for delay in tightening cycle

Newcomer Kashkari wants to break up big banks

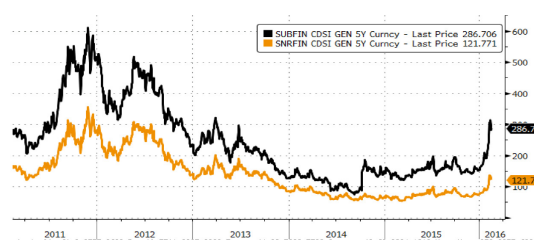
Core bonds remain resilient

Yesterday, following a weaker opening, global core bonds traded sideways in a 50 tick range (Bund) to close near the lows, registering modest losses. Banking shares and oil prices triggered intraday volatility. European equities closed with modest losses, but US equities eked out solid gains of 1.5% (S&P), catching up with European equities. Oil fell sharply lower, as the Saudi-Russia production freeze deal was unable to turn the tide for the commodity. The Bund initially gained on the drop in oil, but couldn't hold on to the gains despite oil sliding further down. EMU ZEW showed a further weakening in investors' sentiment in February, while the NY Fed manufacturing survey remained weak and NAHB housing sentiment fell albeit from high levels. In a daily perspective, the German yield curve bear steepened with yields 0.4 bps (2-yr) to 4.7 bps (30-yr) higher. Changes on the US yield curve were slightly lower between 0.6 bps (2-yr) and +3.5 bps (30-yr). On **intra-EMU bond markets**, 10-yr yield spread changes versus Germany range between -2 bps (Portugal) and +2 bps (Spain) with Greece outperforming (-25 bps).

Philly Fed Harker said he'd be in favour of **delaying further rate increases** until inflation recovers from oil-induced weakness. That would be prudent. He declined to say how many rate hikes he expects in 2016, but said he wasn't thinking about a rate cut and believes that negative rates are a high hurdle to take. He sees downside risks, but remains upbeat on the outlook. **Boston Fed Rosengren unsurprisingly pleaded for a delay in tightening too**, as inflation will move slower to target. He suggested slower tightening as he is afraid that lower oil prices might have second round effects and lead to permanent lower inflation. **Minneapolis Kashkari** floated the idea of **breaking up the big banks** or alternatively obliging them to raise sharply the required capital.



T-Note (black) and S&P future (orange) (intraday): Sideways trading after strong opening equities (catching up) and weaker opening Treasuries



intraxx CDS subordinate (black) & senior (orange) banks: Tensions hardly eased during the past two risk-on sessions

Full US calendar including FOMC Minutes

In December, both **US housing starts and permits** fell back following strong November data. Housing data are usually volatile, especially during the winter months. For January, consensus expects a 2.3% M/M rebound in starts, while permits are forecast to have dropped slightly further (-0.3% M/M). We see **upside risks** as weather conditions remained generally favourable. **Industrial production** is expected to have rebounded by 0.4% M/M in January, which if confirmed would be the first increase in five months.

Upside risks US housing starts and permits

Upside risks US production and PPI

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Manufacturing production should be the main driver as aggregate hours worked in the sector picked up too and utilities are forecast strong due to less warm winter weather. **As a result, we see risks for an upward surprise**, although mining will remain a drag on activity. Finally **PPI inflation** is expected to have dropped by 0.2% M/M, but positive base effects will support the annual rating, which is expected to pick up from -1.0% Y/Y to -0.6% Y/Y. Core PPI is expected to have edged slightly higher too, from 0.3% Y/Y to 0.4% Y/Y. We believe that, especially for the core reading, **a higher outcome is not excluded. The FOMC Minutes** will be scrutinized for hints about the timing of future rate hikes, but following the semi-annual testimony of Yellen, **our expectations to read hot new news are pretty low.**

The German Finanzagentur taps the on the run 10-yr Bund (€5B 0.5% Feb2026). Earlier this week, the bond cheapened around 3 bps in ASW spread terms. On the German curve, the bond trades rather cheap as well. However, we fear that this won't be enough to compensate for the low yield in absolute terms. Another unsubscribed auction is not excluded. This week's auctions will be supported by small Belgian (€3B) and Portuguese (€2B) redemptions.

R2	167	-1d
R1	166,16	
BUND	164,36	-0,3700
S1	163,25	
S2	162,86	

Today: Sentiment on core bond markets remains strong

Overnight, Asian markets initially tried to build on yesterday's WS gains. However, risk sentiment made a turn for the worse after the **PBOC fixed the CNY again weaker**. Most Asian equity indices trade up to 0.5% lower with Japan underperforming (-1%; stronger yen) and China outperforming (+0.5%). **Oil prices remain under downward pressure** while the **US Note future profits** from weak stocks, weak oil and soft Fed speak (see above). The German Bund is expected to open stronger.

Today's eco calendar contains only US eco data. Risks are on the upside of expectations, but the second tier releases are unlikely to leave a lasting stamp on trading. The FOMC Minutes of the January statement could somewhat more dovish on the outlook, but Fed president Yellen pointed that out at last week's testimony. **So overall, risk sentiment and technical factors will continue to drive trading. The past two session, core bonds held up quite well, suggesting that the downside is limited, at least for now.**



German Bund: no longer overbought. Short-term end to rally? More sideways action ahead?



US Note future: similar technical signal as Bund. 2016 uptrend still in place, but changing into more sideways action?

Currencies

Dollar rebound slows

Dollar rebound slows

R2	1,1495	-1d
R1	1,1376	
EUR/USD	1,11655	0,0009
S1	1,106	
S2	1,081	

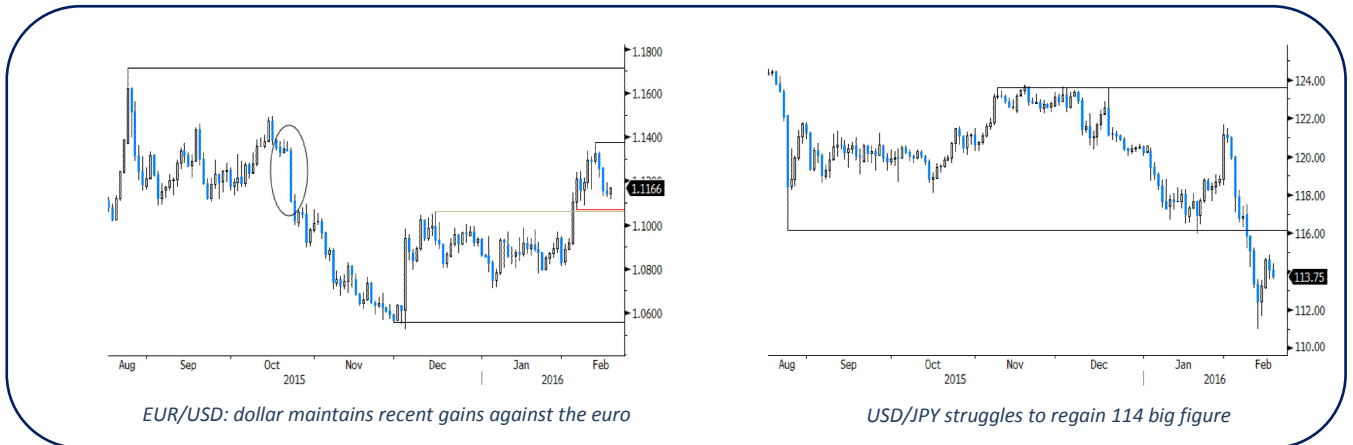
On Tuesday, global market sentiment remained constructive early in the session, but was dampened by the deal to freeze oil production later. European shares reversed their gains, but the impact on global core bonds was limited. The dollar came under pressure. Especially USD/JPY fell prey to profit taking. The losses of the dollar against the euro were much more limited. In technical trading, the dollar even found a better bid later in the session. EUR/USD closed the session at 1.1144 (from 1.1156 on Monday). USD/JPY closed the day at 114.07 (from 114.60).

Asian risk-on rally running into resistance

PBOC guides the yuan lower

Dollar trading with a slight negative bias this morning

This morning, most Asian equities are in correction modus after the gains of the previous days. Chinese equity markets outperform with slight gains as the PBOC fixed the yuan weaker at 6.5237. Both the CNY and the CNH trade slightly weaker this morning at 6.5245 and 6.5248 respectively. Elsewhere in the region, the South Korean Won trades at a five year low against the dollar on market speculation of potential further easing. USD/JPY is holding south of the 114 barrier as global sentiment turned slightly risk-off in Asia, despite a good equity performance in the US yesterday evening. EUR/USD trades little changed in the 1.1165 area. Oil remains under pressure with Brent currently testing the \$32 p/b.



Eco calendar is modestly interesting

Fed minutes might be in focus

Today, there are no data with market moving potential in Europe. In the US, housing starts, building permits, PPI and industrial production will be published. On average, we expect the US data to be inline or even slightly better than expected. Later in the session, the Fed will publish the Minutes of the January policy meeting. The interdenal debate and the tone off the minutes might be a bit softer than the official communiqué as published after the meeting. Of course, a lot of the interpretation work is already done by Yellen at the hearing before Congress. Even so, if several Fed member are openly inclined to move toward a slow-down of the rate hike path, it might be a negative for the dollar. Aside from the data and the Fed minutes, global market sentiment will play its role for USD trading as well. Given the intraday price action in Asia and the decline of the oil price, we assume that the dollar won't get much support from the global market context this morning. We started the week with a cautiously USD positive bias.

There is no obvious reason to really make a U-turn, but further sustained USD gains against the euro might become more difficult. 1.1060/70 support area is the first target.

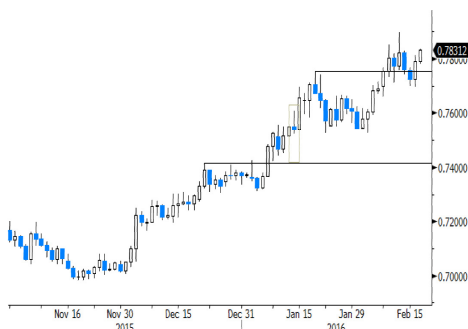
From a technical point of view, EUR/USD broke above the 1.1060/1.1124 resistance area (15 Dec top: 62% retracement). This was USD negative. The short-term correction high stands at 1.1376. Next important resistance kicks in at 1.1495. We see some short-term topping out process in EUR/USD. **USD/JPY dropped below the key 115.98 pre-BOJ low**. Japanese officials warned on potential action and this put a short-term floor. Even so, the pair remains vulnerable if global tensions resurface. **We doubt that the time is ripe for a sustained USD/JPY rebound. Any rally might run into resistance quite soon. The 115.98 previous low is a first technical reference.**

R2	0,8066	-1d
R1	0,7898	
EUR/GBP	0,7821	0,0081
S1	0,7661	
S2	0,7526	

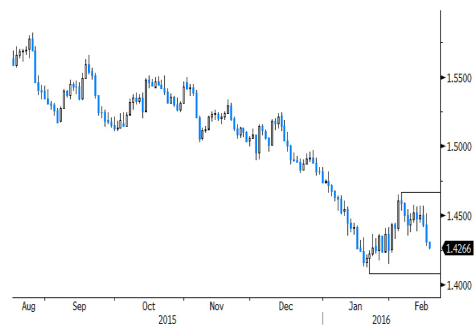
Sterling stays on the defensive ahead of EU summit

On Tuesday, sterling trading was in a wait-and-see modus. Investors were looking for more concrete signals on the outcome of the EU/UK negotiations. Currency traders were apparently a bit afraid being wrong-footed by a higher than expected UK CPI. **Sterling gained against the euro and the dollar in the run-up to the UK CPI report**. Headline CPI was close to expectations (0.3% Y/Y) but core inflation was marginally softer at 1.2% Y/Y. So, the report didn't provide any trigger for sterling shorts to feel uncomfortable going into the EU summit. Sterling reversed the earlier gains. Later in the session, sterling came again under pressure as also the oil price dropped further. **Ahead of the EU/UK Summit, sterling remains vulnerable to negative news**. EUR/GBP closed the session at 0.7798 (from 0.7726 on Monday). Cable closed the session at 1.4306 (from 1.4435)

Today, the UK labour market **report is expected to confirm a rather healthy state of the UK labour market with the unemployment rate declining to 5.0% and decent employment growth**. At the same time, the **weekly earnings** are expected slightly softer compared to the previous month. Usually the labour market report is one of the most important data series for sterling trading. Currently, the market focus is on the Brexit debate and on the negotiations between the UK and the EU. In this context we see an asymmetric risk. A poor figure might reinforce the sterling negative momentum. A good report might have much less impact. **We stay cautious on sterling gains until there is more clarity on the EU/UK negotiations. Pressure on sterling might ease once a deal is reach, but it's too early to preposition for such a scenario. There is too much binary risk.**



EUR/GBP: Brexit uncertainty weighs on sterling



GBP/USD: drifting back lower on Brexit uncertainty

Calendar

Wednesday, 17 February		Consensus	Previous
US			
13:00	MBA Mortgage Applications	--	9.3%
14:30	Housing Starts MoM / Total (Jan)	2.3%/1175K	-2.5%/1149K
14:30	Building Permits MoM / Total (Jan)	-0.3%/1200K	-3.9%/1204K
14:30	PPI Final Demand MoM/YoY (Jan)	-0.2%/-0.6%	-0.2%/-1.0%
14:30	PPI Ex Food and Energy MoM/YoY (Jan)	0.1%/0.4%	0.1%/0.3%
15:15	Industrial Production MoM (Jan)	0.4%	-0.4%
15:15	Capacity Utilization (Jan)	76.7%	76.5%
15:15	Manufacturing (SIC) Production (Jan)	0.3%	-0.1%
Japan			
00:50	Machine Orders MoM/YoY (Dec)	A: 4.2%/-3.6%	-14.4%/1.2%
07:00	Machine Tool Orders YoY (Jan F)	A: -17.2%	-17.2%
UK			
10:30	Jobless Claims Change (Jan)	-3.0k	-4.3k
10:30	Average Weekly Earnings 3M/YoY (Dec)	1.9%	2.0%
10:30	Weekly Earnings ex Bonus 3M/YoY (Dec)	1.8%	1.9%
10:30	ILO Unemployment Rate 3Mths (Dec)	5.0%	5.1%
10:30	Employment Change 3M/3M (Dec)	225k	267k
EMU			
11:00	Construction Output MoM/YoY (Dec)	--/--	0.8%/2.1%
Events			
01:00	Fed's Rosengren Speaks at Colby College		
20:00	U.S. Fed Releases Minutes from Jan. 26-27 FOMC Meeting		
Sweden	Bond Auction (Sek 3.5B 2.5% May 2025, Sek 0.5B 2.25% Jun 2032) (11:03)		
Norway	Bond auction (NOK6B 1.5% Feb2026) (11:05)		
Germany	Bund Auction (Eur 5B 0.5% Feb 2026) (11:30)		
UK	New Gilt Auction (GBP 2.75B 1.5% Jul 2026) (11:30)		

10-year	td	-1d	2-year	td	-1d	STOCKS	-1d
US	1,75	-0,03	US	0,71	-0,02	DOW	16196 16196,41
DE	0,26	0,02	DE	-0,50	0,00	NASDAQ	for Exch -NQI #VALUE!
BE	0,63	0,01	BE	-0,38	0,03	NIKKEI	15836 15836,36
UK	1,43	0,00	UK	0,35	-0,01	DAX	9135,11 9135,11
JP	0,05	0,01	JP	-0,17	0,00	DJ euro-50	2821 2821,26

						USD	td	-1d
IRS	EUR	USD (3M)	GBP	EUR	-1d	-2d	Eonia EUR	-0,242 0,001
3y	-0,105	0,852	0,818	Euribor-1	-0,24	0,00	Libor-1 USD	0,51 0,51
5y	0,065	1,098	0,991	Euribor-3	-0,18	0,00	Libor-3 USD	0,59 0,59
10y	0,640	1,577	1,431	Euribor-6	-0,12	0,00	Libor-6 USD	0,74 0,74

Currencies	-1d	Currencies	-1d	Commodity	CRB	GOLD	BRENT
EUR/USD	1,11655 0,0009	EUR/JPY	126,97 -0,78		160,3628	1205,4	32,19
USD/JPY	113,73 -0,81	EUR/GBP	0,7821 0,0081	-1d	0,00	7,90	-2,55
GBP/USD	1,4273 -0,0135	EUR/CHF	1,1017 -0,0005				
AUD/USD	0,7091 -0,0061	EUR/SEK	9,4747 0,01				
USD/CAD	1,3883 0,0109	EUR/NOK	9,6299 0,03				

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