



Sunrise

Thursday, 15 October 2015

Weak US retail sales and soft producer prices push expectations lift-off further out

Dismal figures make a Fed lift-off ever more unlikely. How and when will Fed take a turn towards the markets' view? Core bond curves shifted sharply lower with US short end doing best. US and German 10-year yields are at or near key yield support at 2%/0.50%. Equities held up rather well till now. Need core bonds a sharp decline of equities to give them more upside?

Dollar hammered as Fed rate hike hopes evaporate on poor US data

Yesterday, the dollar fought an uphill battle as US eco data disappointed. USD/JPY dropped below the 119 big figure. EUR/USD broke through the 1.1460 resistance. Today, US regional confidence and the US CPI are key for USD trading. Sterling rebounded off the recent lows after a decent UK labour market report.

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	↓

- **European equities** closed yesterday's trading session again with losses after a weak open. **US equities** closed off in the red yesterday, also due to Wal-Mart disappointing guidance. Overnight, the **Asian equities** are surprisingly trading nicely in the green for the first time in three days.
- **Australia's jobs outlook has become slightly negative** after 5.1K jobs were lost in September, whereas economists had expected a job creation of 9.6K jobs. The weakest point was the loss of 13.9k full-time employees, the most since April.
- **The Bank of Korea has cut its economic and inflation outlook for 2015 and 2016.** Now expecting 2015 GDP to grow 2.7% (from 2.8%) and 2016 GDP to grow 3.1% (from 3.2%). 2015 inflation is expected to increase 0.7% (from 0.9%) and 2016 inflation to increase 1.7% (from 1.8%).
- The key data on **the corporate agenda** are Q3 earnings for Goldman Sachs Group and **Citigroup** (before market opening).
- Today the **eco-calendar** is dominated by US data, with the **US jobless claims**, the **empire manufacturing** survey, the **Philly fed business outlook** and the **CPI data**. Also speeches of **Fed Bullard, Dudley and Mester will be very interesting**.

Rates

Weak retail sales and soft PPI push core bonds higher

Core bonds profit from soft US eco data

	US yield	-1d
2	0,5647	-0,0523
5	1,295	-0,0571
10	1,9999	-0,0405
30	2,8546	-0,0234

	DE yield	-1d
2	-0,2540	-0,0100
5	-0,0370	-0,0240
10	0,5480	-0,0390
30	1,3160	-0,0390

Global core bonds strongly profited from weak US eco data and some equity weakness. The combination of dismal retail sales and a downshift in producer prices set the core bond market on fire. The front end of the curve outperformed as Fed rate hike expectations were once more downgraded. The market now expects a 27% chance on a December rate lift-off and a 48% chance for a March 2016 lift-off. Equities initially recouped from the post-data decline, but later on lost ground on grim guidance of Wal-Mart. In a daily perspective, the US curve shifted sharply lower. Yields dropped 6.8 bps (2-yr) to 8.5 bps in the 2-to-5-yr sector, but also 10- and 30-yr yields fell 7.2 and 5 bps respectively. German yields fell by 0.8 bps (2-yr) to 4.6 bps (10-yr). For EMU, the prospect of a delay in the Fed lift-off puts pressure on the ECB (via higher euro) to ease policy further. This should be favourable for EMU bonds. However, yesterday, peripheral bonds underperformed with yield spreads (10-yr) widening 1 to 11 bps³. Greece and Portugal underperformed. The Fed Beige Book was slightly weaker than previous ones (see our KBC app).

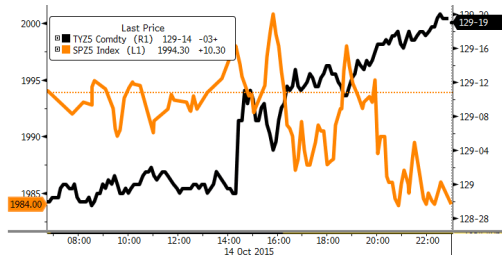
US CPI and regional business sentiment key today

US Initial claims and CPI expected near consensus

NY Fed survey: some slight upward risks, while we side with consensus on Philly Fed.

The **US jobless claims** are expected to have increased from 263k to 270k last week, and the continuing claims are expected to decrease marginally. We see no reason to expect otherwise. The key figure is the **September US CPI inflation**. The headline CPI is expected to drop into deflation territory, at -0.1% Y/Y, coming from +0.2% Y/Y in August. Inflation is expected to remain underpinned by services prices, while commodities prices stay weak. The core CPI is expected to remain stable at 1.8% Y/Y. We side with the consensus. Regarding the **US Empire Manufacturing survey**, the market expects an increase to -8.00 in October, coming from -14.67 in September. So, manufacturing activity continues to weaken, albeit at a slower pace. While we are downbeat on manufacturing, given the steep drop in August, some stronger rise shouldn't been surprising. We expect new orders to remain soft. We see upward risk to the number. Lastly, the **Philly fed business outlook** for is expected to increase from -6.0 last month to -2.0 for October, according to the consensus.

Today, Fed Bullard, Dudley and Mester speak. Their comments will be interesting after the weak recent eco data. Their latest opinions: Bullard is firmly in favour for a 2015 lift-off, Dudley is a "guarded yes" to a December lift-off, while also Mester is in the 2015 lift-off camp. Have they changed positions?



T-Note future (black) & S&P future (orange): Weak data push Treasuries higher. Reaction of equities more mixed, but Wal-Mart guidance push equities back down



US 10-yr yield tests 2% barrier for third time. One more downward surprise needed to push it through?

R2	160,62	-1d
R1	157,67	
BUND	156,83	0,0000
S1	155,77	
S2	153,5	

France and Spain tap market

The French debt agency taps the on the run 5-yr OAT (0.25% Nov2020) and two off the runs (4% Apr2018 & 3% Apr2022) for a combined €7-8B. The bonds traded sideways going into this auction. On the French curve, the Nov2020 OAT is slightly cheap. Overall, we expect a plain vanilla auction. Currently, France already completed almost 90% of this year's funding need. **The Spanish treasury taps the on the run 3-yr Bono (0.25% Apr2018), 10-yr Obligacion (2.15% Oct2025) and 15-yr Obligacion (1.95% Jul2030) for up to €4B.** In the run-up to the auction, the bonds cheapened around 3 bps in ASW spread terms. On the Spanish curve, the Oct2025 and Jul2030 Obligacions are rich. This could hamper demand though the pick-up over Italian BTP's remains interesting. Other factors like economic strength and lower 2015 net issuance are supportive as well.

Today: T-Note up for a test of contract high?

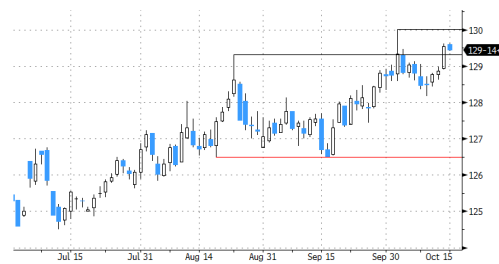
Overnight, the US Note future trades with a downward bias. Risk sentiment on Asian stock markets is positive with China outperforming (+2%).

Today's trading focus remains on the US with inflation data, claims, empire manufacturing and Philly Fed Business outlook together with Fed speak. Following horrible payrolls, weak retails sales and disappointing PPI data, markets are wary of more negative numbers. That would trigger a test of the contract high in the US Note future (130-00+). The US 10-yr yield is also back at the psychological 2% mark with key support at 1.96% (62% retracement Feb to June rally). **Fed speakers are wildcards (Bullard, Mester and especially Dudley).** Is their thinking on a 2015 lift-off already influenced by recent downbeat events? **A dovish shift won't go unnoticed though a 2016 lift-off scenario seems already discounted for a large extent.** Finally, risk sentiment on equity markets and evolutions on commodity markets play a role as well. Both asset classes show signs of topping off following the rebound since early October.

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/commodity prices further fuels core bonds at this stage. **We become 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: Weak US eco data and new decline in commodities/equities supports US Note future.

Currencies

Dollar ceding further ground on poor US data

Dollar pressure by disappointed US data

R2	1,1714	-1d
R1	1,1534	
EUR/USD	1,1488	0,0094
S1	1,133	
S2	1,1087	

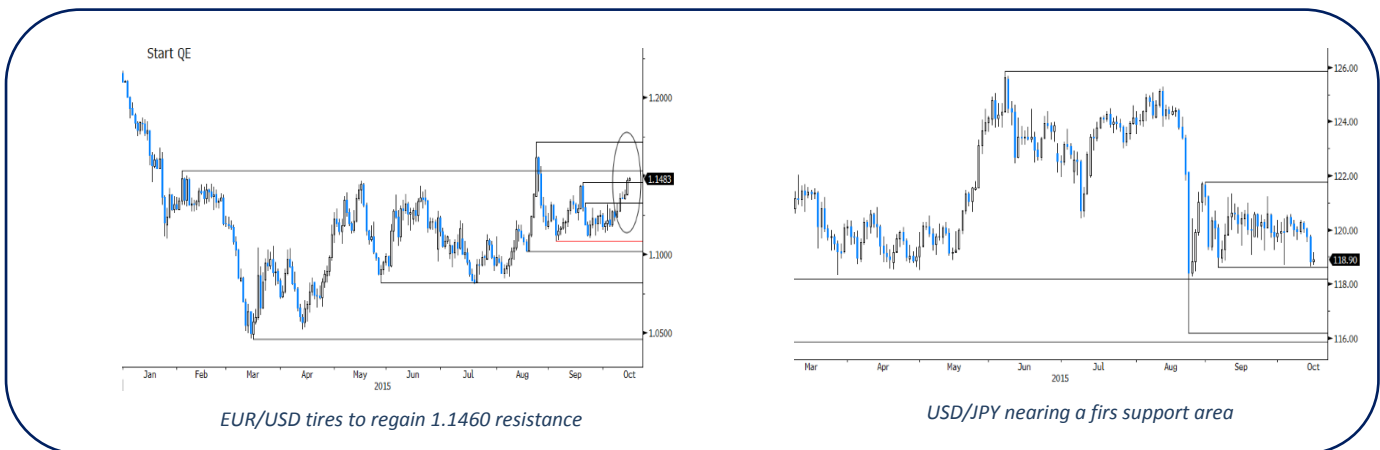
Sentiment on risk improves in Asia but doesn't help the dollar, for now.

US CPI and regional sentiment indicators in focus for USD trading

On Wednesday, the dollar stayed under pressure. Global sentiment on risk softened and the US data (retail sales and PPI) disappointed, making a 2015 Fed rate hike less likely. The dollar paid the price. USD/JPY closed the session at 118.83 (from 119.75). EUR/USD ended the session at 1.1474 (from 1.1379). So, the 1.1460 resistance is under heavy strain. The Fed Beige book had a slightly soft bias, putting additional pressure on the US currency.

Overnight, Asian equities opened mixed, but sentiment on risk improved gradually later in the session. Markets apparently adjust positions for a scenario of the Fed keeping interest rates lower for longer. This scenario will keep global monetary conditions easy too, supporting a risk-on trade, at least short-term. USD/JPY tries to regain the 119 level. This time, the risk on rally doesn't help the dollar against the euro as the focus is on an easier than expected Fed policy going forward. EUR/USD trades in the 1.1480 area. The dollar is also losing ground against the likes of the Kiwi dollar and the Aussie dollar. The Australian September labour data were slightly softer than expected, but didn't really hurt the Aussie dollar. USD weakness prevailed. AUD/USD is holding north of 0.73.

Today, there are no important data in Europe. We look out for comments from ECB members attending a conference in Warsaw. Will they pick up recent developments? Nowotny is not really a dove. So, if he turns more dovish on ECB policy, that would be an interesting signal. In the US, the calendar is very interesting with the jobless claims, the Empire manufacturing survey and the Philly Business outlook and, last but not least the CPI. Regarding the activity indicators, the Empire survey and the Philly Fed survey are expected to improve after a recent setback. The headline CPI is expected to fall back into negative territory from 0.2% Y/Y to -0.1% Y/Y. Core inflation is expected stable at 1.8% Y/Y. We don't have strong arguments to take a different view from the consensus for the CPI, but if US data would again surprise on the downside, there will be additional damage for the dollar as it would further diminish the chances for a Fed rate hike in the near future. Later in the session, several Fed members including Bullard, Dudley and Mester will speak.



Global markets struggle to assess the health of the global economy and its impact on monetary policy. In a short-term perspective, markets are focused on the impact of weaker US data on the Fed rate hike path. This makes the dollar vulnerable short term even as the ECB might also ease policy further if economic conditions deteriorate further. However, potential ECB action is probably some way off. So, the short-term context is USD negative; EUR/USD is currently breaking above the 1.1460 resistance. Technically this is a further USD negative. Both in bonds and in the dollar quite some bad news should already be discounted. Even so, we don't row against the tide until there is a clear sign that EUR/USD rebound has run its course (e.g; the ECB stepping up its easing rhetoric). Delayed Fed rate hike expectations also weigh on USD/JPY even as equities hold up well.

In a long term perspective, EUR/USD and USD/JPY might see more range trading. A Fed rate hike will likely be delayed, but such a scenario also raises the chances for more ECB or BOJ easing. In this context, one doesn't expect a protracted downtrend of the dollar against the euro. If the policy divergence between the Fed and the ECB becomes less obvious, EUR/USD may return toward the August correction high at 1.1719.

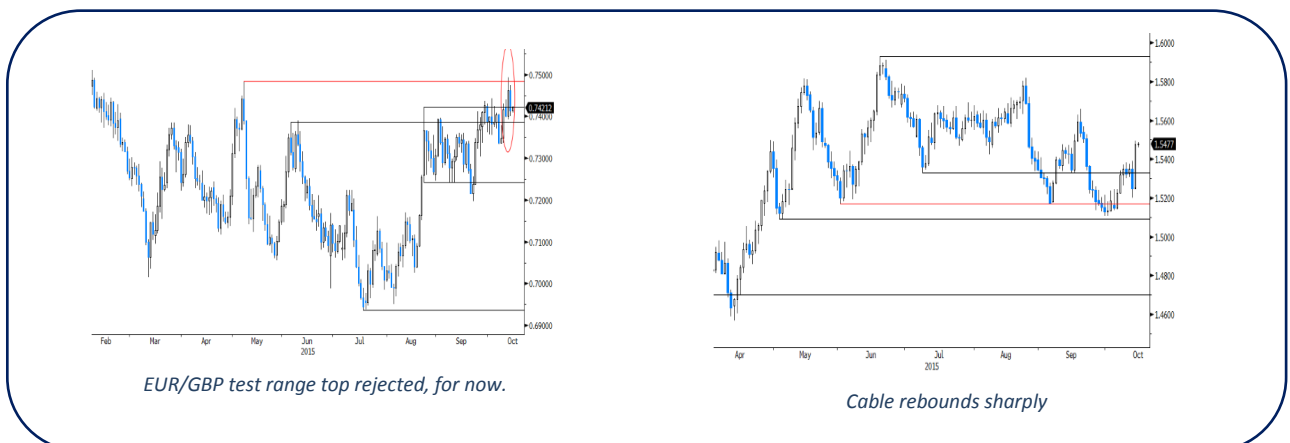
R2	0,7692	-1d
R1	0,7493	
EUR/GBP	0,7421	-0,0036
S1	0,7333	
S2	0,7196	

Test of EUR/GBP 0.7383 resistance rejected

On Wednesday, the UK labour report painted a mixed picture. The unemployment rate declined from 5.5% to 5.4 % and the number of new people employed rose by 140.000. On the other hand, wage growth rose at a slower than expected pace. **Sterling regained some ground against the euro and the dollar. The move was probably also a reversal in the wake of Tuesday's post-CPI losses.** EUR/GBP dropped from the 0.7460 area to the low 0.74 area. Cable was already trending higher in the run-up to the labour data due to overall USD weakness. The rebound accelerated after the labour report and was reinforced by poor US data. Cable closed the session at 1.5477 (from 1.5248!). EUR/GBP closed the session at 0.7413 from 0.7462.

Today, there are no important eco data in the UK. So we look out whether sterling will be able to maintain yesterday's gains. If so, it might be an indication that the recent correction has run its course. Yesterday's price action also indicated that the 0.7483/93 area is a strong resistance.

From a technical point of view, EUR/GBP still trades in the upper part of the sideways range capped by 0.748/933. The latter was extensively tested earlier this week. Sustained trading north of 0.7483 would deteriorate the short-term picture of sterling. This is not our preferred scenario. Even so, partial stop-loss protection on EUR/GBP shorts is warranted.



Calendar

Thursday, 15 October		Consensus	Previous
US			
14:30	Initial Jobless Claims (Oct 8)	270k	263k
14:30	Continuing Claims (Oct 1)	2200k	2204k
14:30	Empire Manufacturing (Oct)	-8.00	-14.67
14:30	CPI MoM/YoY (Sep)	-0.2%/-0.1%	-0.1%/0.2%
14:30	CPI Ex Food and Energy MoM/YoY (Sep)	0.1%/1.8%	0.1%/1.8%
14:30	Real Avg Weekly Earnings YoY (Sep)	--	2.3%
15:45	Bloomberg Consumer Comfort (Oct 11)	--	44.8
16:00	Philadelphia Fed Business Outlook (Oct)	-2.0	-6.0
Canada			
15:00	Existing Home Sales MoM (Sep)	--	0.3%
Japan			
06:30	Industrial Production MoM/YoY (Aug F)	A: -1.2%/-0.4%	-0.5%/0.2%
06:30	Capacity Utilization MoM (Aug)	A: -0.9%	-0.2%
06:30	Tertiary Industry Index MoM (Aug)	A: 0.1%	0.2%
Norway			
10:00	Trade Balance NOK (Sep)	--	20.8b
Sweden			
09:30	Unemployment Rate SA (Sep)	--	7.0%
Events			
03:15	EMU - ECB's Constancio Speaks in Hong Kong		
09:00	EMU - ECB's Nowotny Speaks at Conference in Warsaw		
10:30	Spain - Auctions Bonos/Obligaciones		
11:30	UK - Gbp 1.5bn 0.125% Mar 2026 I/L Gilt		
11:50	France - Auctions BTANs & Auctions OATI		
11:30	EMU - ECB's Hansson Speaks at Conference in Warsaw		
13:30	US - Goldman Sachs Group Q3 earnings release		
14:00	US - Citigroup Q3 earnings release		
19:00	EMU - ECB's Nowotny Speaks at Conference in Warsaw		
16:30	US - Fed's Bullard Makes Opening Remarks at Policy Conference		
16:30	US - Fed's Dudley Speaks at Brookings Institution		
22:30	US - Cleveland Fed's Mester Delivers Remarks at Event in New York		

10-year	td	-1d	2-year	td	-1d	STOCKS	-1d
US	2,00	-0,04	US	0,56	-0,05	DOW	16925 16924,75
DE	0,55	-0,04	DE	-0,25	-0,01	NASDAQ	for Exch - NQI #VALUE!
BE	0,87	-0,03	BE	-0,20	-0,01	NIKKEI	18097 18096,90
UK	1,76	-0,06	UK	0,48	-0,04	DAX	9915,85 9915,85
JP	0,32	0,01	JP	0,02	0,00	DJ euro-50	3192 3191,57

						USD	td	-1d
IRS	EUR	USD (3M)	GBP	EUR	-1d	-2d	Eonia EUR	-0,135 0,001
3y	0,109	0,903	1,070	Euribor-1	-0,11	0,00	Libor-1 USD	0,51 0,51
5y	0,325	1,298	1,366	Euribor-3	-0,05	0,00	Libor-3 USD	0,58 0,58
10y	0,934	1,918	1,797	Euribor-6	0,03	0,00	Libor-6 USD	0,75 0,75

Currencies		-1d	Currencies		-1d	Commoditie	CRB	GOLD	BRENT
EUR/USD	1,1488	0,0094	EUR/JPY	136,47	0,16		199,8289	1185,2	49,33
USD/JPY	118,83	-0,82	EUR/GBP	0,7421	-0,0036	-1d	0,10	12,30	-0,04
GBP/USD	1,5473	0,0197	EUR/CHF	1,0902	-0,0011				
AUD/USD	0,7321	0,0091	EUR/SEK	9,311	0,05				
USD/CAD	1,2912	-0,0094	EUR/NOK	9,2435	-0,02				

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