17 December 2015

Danske Daily

Market Movers

- We expect Norges Bank (NB) to leave rates at 0.75% but it has admittedly become a very close call – in our view close to even odds – amid the renewed collapse in the oil price, which could trigger another 25bp ‘insurance cut’ as it did in December 2014 and September 2015. We expect NB to indicate a very dovish stance by lowering the rate path, signalling a close to 100% probability of a rate cut in March. Markets are pricing in a roughly 50% probability of a 25bp December rate cut, a full 25bp rate cut for the March meeting and an accumulated 40-45bp worth of cuts on a 9-12M horizon (the period where the most easing is priced in). For more details see our *Norges Bank Preview – Unchanged and very dovish bias - but unusually close call*, 14 December.
- In terms of data releases, we expect the German IFO expectations to improve slightly and point to steady growth in line with the signals from yesterday’s Euro flash PMI.
- We expect UK retail sales (ex fuels) to increase 0.3% m/m in November, which is more or less in line with the consensus estimate of 0.4% m/m.
- In Sweden, unemployment figures will be released at 9:30 CET.
- Finally, note that the Bank of Japan (BoJ) early Friday morning announces its monetary policy decision. We expect BoJ to keep its target for the annual rise in monetary base unchanged at JPY80trl. Anything but an unchanged target would be a surprise to the market.

Selected Market News

Last night was all about the long-awaited FOMC meeting and as widely expected by both analysts and financial market participants, the FOMC increased the Federal Funds rate target by 25bp. It was the first US interest rate increase in more than nine years. The median ‘dots’ now signal four hikes in both 2016 and 2017, i.e. a total of eight hikes until year-end 2017 (down from nine). On the surface, the unchanged median ‘dot’ in 2016 might be interpreted as a hawkish signal but it hides that most individual ‘dots’ next year have in fact been lowered. For more details see FOMC Review that we will publish this morning.

The rate hike was relatively well-received in the market and risk sentiment was boosted in a relief rally as the Fed managed to take away at lot of uncertainty by hiking rates. We think it is fair to say that FOMC and not least Yellen during her press conference found a sound balance between neither being too dovish nor too hawkish and US equity markets rallied with the SP500 index closing 1.45% higher. Asian equity markets also trade higher this morning. In the FX market, the USD gained versus the G10 currencies – most notably against the EUR that has dropped to 1.0850 this morning – while many EM currencies gained from the relief rally. The 2Y10Y US yield curve flattened slightly with a 2bp increase in yields on 2Y US government, while yields on 10Y treasuries dropped 4bp. Despite the unchanged 2016 dots we stick to our view that Fed will hike three times in 2016 and four times in 2017. The market is pricing in only two full hikes in 2016 and an additional two are priced for 2017. This is too soft in our view and we expect US yields to continue to trend higher.

Market overview

		07:30		1 day +/-,%
S&P500 (close)		2073.1	↑	1.45
S&P500 fut (chng from close)		2058.3	↓	-0.26
Nikkei		19343.8	↑	1.54
Hang Seng		21832.5	↑	0.60
	17:00	07:30		+/-, bp
US 2y gov	1.00	1.00	↑	0.6
US 10y gov	2.30	2.27	↓	-3.7
iTraxx Europe (IG)	79	79	↑	0.0
iTraxx Xover (Non IG)	329	330	↑	1.0
				+/-, %
EUR/USD	1.095	1.086	↓	-0.82
USD/JPY	121.820	122.410	↑	0.48
EUR/CHF	1.08	1.08	↑	0.05
EUR/GBP	0.729	0.726	↓	-0.41
EUR/SEK	9.315	9.282	↓	-0.36
EUR/NOK	9.56	9.57	↑	0.11
				USD
Oil Brent, USD	37.3	37.1	↓	-0.46
Gold, USD	1074.6	1067.2	↓	-0.70

Note:
** The iTraxx Europe Index shows the spread development for the most liquid investment grade CDS contracts in the euro credit market.*

***The iTraxx Europe Crossover show the spread development of the most liquid non-investment grade CDS contracts in the euro credit market.*

****The Markit CDX North America Investment Grade Index shows the spread development for the most liquid investment grade CDS contracts in the US credit market.*

Source: Bloomberg

Selected readings from Danske Bank

- *Research Denmark: Set for another year of low inflation*
- *Research Finland: Some growth is better than none*
- *UK: Mixed labour market report as Carney takes Q1 BoE hike off the table*

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Scandi Markets

Norway. We expect Norges Bank to stay on hold today. Domestic growth, inflation and global growth have been in line with expectations. Yields abroad have been somewhat lower and money market rates slightly higher than anticipated, pulling down the rate outlook. On the other hand, fiscal policy looks set to be somewhat more expansionary next year and the NOK is more than 4% weaker than expected. This is pulling in the other direction and the net effect on the rate path is actually positive. However, the oil price has dipped below USD40/bl, increasing the downside risk to the Norwegian economy – and so also the chances of Norges Bank cutting rates on a pre-emptive basis to guard against this downside risk as it did in December last year and September this year. The decline in the oil price since September has, however, been substantially smaller than that from June to September, and may not therefore be enough to spur the central bank into action. There is also a risk that fiscal policy will be even more expansionary than expected. We very tentatively predict that Norges Bank will hold fire this time around but indicate a very high probability of a reduction at its meeting in March. As we say, though, there is a more or less even chance of a cut here and now. For more details see our *Norges Bank Preview – Unchanged and very dovish bias - but unusually close call*, 14 December.

Sweden. We expect the unemployment rate to remain unchanged at 7.6% in November but also continued decent growth in employment.

Fixed Income Markets

Despite the unchanged 2016 dots we stick to our view that Fed will hike three times in 2016 and four times in 2017. The distribution of the 2016 dots shows that there is a fine balance between members expecting three and four hikes in 2016 and we assess that the 'centre' for the voting FOMC members will remain to have a dovish-to-neutral view and we expect the next hike to happen in April (i.e. three meetings from now).

In light of this we view the current market pricing as too soft. June FOMC is around 58bp and is thus 25bp above the expected Fed Funds rate starting from tomorrow followed by 85bp priced for December FOMC. This leaves only two full hikes being priced for 2016 with an additional two priced for 2017. Although the coming month’s market rate outlook is likely to be characterised by range trading on the back of soft US data and the Fed speakers not wanting to rock the boat too much, we should expect US yields to continue to trend higher, most significantly at the shorter end of the curve. Therefore, our forecasts for US rates remain above the forward market but we expect most of the increase to happen in the spring of 2016.

A potential spill-over to EUR fixed income should be dominant in longer segments with the easy ECB policy having a firm grip on the front and belly of the curve (out to 5Y area). In our view, the spill-over from the US will be felt mainly in the 10Y segment as the ECB keeps 2Y and 5Y yields in check with QE purchases and a deposit rate at -0.3%. Looking six and 12 months ahead, the spill-over from US yields should result in slight upward pressure and we expect a steepening of the EUR curve driven from higher 10Y yields.

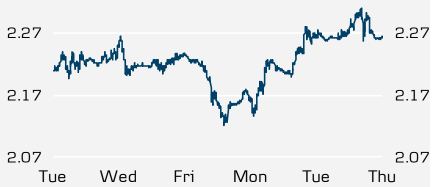
FX Markets

After a volatile session during last night’s FOMC rate announcement and the following press conference, EUR/USD has dropped to 1.0850 this morning. Near term, the removal of uncertainty regarding whether the Fed could back-track on rate lift-off as in September coupled with the potential for markets to price more ECB easing during spring, could drag EUR/USD a few figures lower still on a 3M horizon.

US S&P500 future

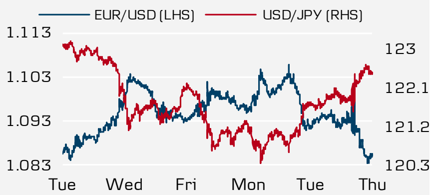
Source: Danske Bank Markets

US 10y gov yield



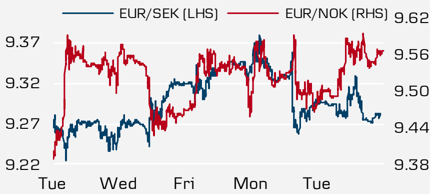
Source: Danske Bank Markets

Global FX



Source: Danske Bank Markets

Scandi FX



Source: Danske Bank Markets

Looking further ahead, our view that risks remain tilted towards three rather than four Fed hikes next year suggests that, while markets are still pricing 'too little' on the Fed compared with both our and the FOMC projections, the potential for upside to US rates next year still exists. However, combined with stretched positioning in the FX market, which arguably reduces the sensitivity to monetary policy, the impetus to further EUR/USD downside from relative rates is still set to fade next year in our view. Thus, we maintain the view that EUR/USD will be range-bound - and notably not reach new cycle lows on a 3M horizon - and then stage a rebound towards 1.16 in 12M as strong euro fundamentals provide support.

Today, focus turns to Norges Bank's (NB) monetary policy meeting. Overall, we see risks skewed to the upside for EUR/NOK in connection with today's meeting. If we are right in our call that NB stays put, current market pricing of roughly 50% probability of a rate cut implies that EUR/NOK should trade lower. However, we think the downside potential is very limited due to (1) 2016 market pricing reflecting our rate path call, (2) the current bearish environment for oil, (3) poor NOK December liquidity as well as 4) general reduction in year-end risk appetite. Meanwhile a cut could send EUR/NOK substantially higher into technically uncharted territory.

Key figures and events

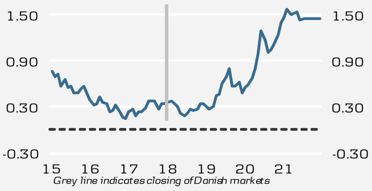
Thursday, December 17, 2015				Period	Danske Bank	*Consensus*	Previous
9:30	SEK	Unemployment (n.s.a.|s.a.)	%	Nov	**6.7%|7.1%**		6.7%|7.2%
10:00	NOK	Norges Banks monetary policy meeting					
10:00	NOK	Norges Banks deposit	%		**0.75%**	*0.50%*	0.75%
10:00	DEM	IFO - business climate	Index	Dec	**109.4**	*108.9*	109.0
10:00	DEM	IFO - current assessment	Index	Dec	**113.8**	*113.4*	113.4
10:00	DEM	IFO - expectations	Index	Dec	**105.1**	*104.8*	104.7
10:00	EUR	ECB Publishes Economic Bulletin					
10:30	GBP	Retail sales	m/m|y/y	Nov	**0.3%|2.8%**	*0.5%|3.0%*	-0.6%|3.8%
10:30	GBP	Retail sales ex fuels	m/m|y/y	Nov	**0.3%|1.8%**	*0.4%|2.2%*	-0.9%|3.0%
11:00	EUR	Labour costs	q/q	3rd quarter			1.6%
14:30	USD	Initial jobless claims	1000				282
14:30	USD	Current account	USD bn	3rd quarter		*-123.0*	-109.7
22:00	FRF	Business confidence	Index	Dec			102.0

Source: Bloomberg, Danske Bank Markets

Today's market data: 17 December 2015

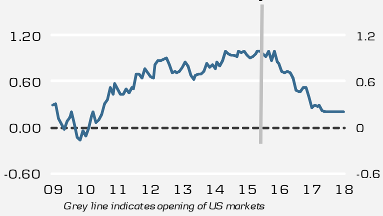
STOCKS

S&P500 Intraday, %



1month	↑	1.1%
Year-to-date	↑	0.7%

Eurostoxx Intraday, %



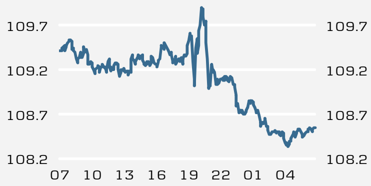
1month	↓	-6.3%
Year-to-date	↑	1.8%

	Close		+/-
DJSTOXX50	3058	↑	0.2%
OMXC20	986	↑	0.5%
OMXS30	1428	↑	0.1%
OSE BX	604	↑	0.3%

	Close		+/-
DOW JONES	17749	↑	1.3%
NASDAQ	5071	↑	1.5%
S&P500	2073	↑	1.5%
NIKKEI (07:30)	19344	↑	0.2%

FX & COMMODITIES

EUR/USD Intraday



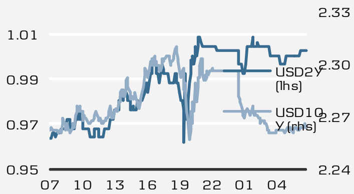
1month	↑	2.14
Year-to-date	↓	-12.42

EUR	*17:00*	*07:30*		*+/-*
USD	109.46	108.56	↓	-0.90
JPY	133.34	132.89	↓	-0.45
GBP	72.92	72.62	↓	-0.30
NOK	955.65	956.70	↑	1.05
SEK	931.52	928.19	↓	-3.33
DKK	746.16	746.16	↑	0.00
PLN	429.75	430.07	↑	0.32
USD	*17:00*	*07:30*		*+/-*
JPY	121.82	122.41	↑	0.59
GBP	150.10	149.49	↓	-0.61
CHF	98.65	99.52	↑	0.87

		Gold, $		**Oil, Brent, $**
07:30		1067.16		37.12
1day	↓	-5.16	↓	-0.27
1month	↓	-3.16	↓	-6.45
Year-t-date	↓	-117.70	↓	-20.21
		CRB 1M future		**CRB, Raw Industrials**
07:30		171.81		400.95
1day	↓	-2.42	↓	-0.16
1month	↓	-11.90	↓	-0.67
Year-t-date	↓	-58.15	↓	-91.16

YIELDS & INTEREST RATES

USD-Yields Intraday

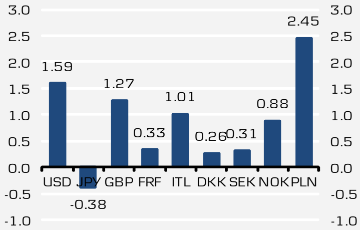


	Policy Rate	**3M**	**Spread, bp**
USD	0.50	0.53	3
EUR	0.05	-0.13	-18
GBP	0.50	0.58	8
DKK	0.05	-0.10	-15
SEK	-0.35	-0.38	-3
NOK	0.75	1.06	31
PLN	1.50	1.62	12

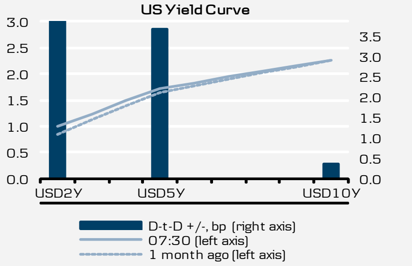
	17:00	*07:30*		*+/-, bp*
USD 10Y	2.30	2.27	↓	-4
USD 30Y	3.02	2.97	↓	-5
JPY 10Y	0.30	0.30	↓	-1
	*07:30(-1)**	*17:00*		*+/-, bp*
DEM 10Y	0.65	0.68	↑	2
DKK 10Y	0.98	0.94	↓	-4
SEK 10Y	0.95	0.99	↑	4
NOK 10Y	1.56	1.56	↑	0
PLN 10Y	3.06	3.13	↑	6

* As of closing previous trading day

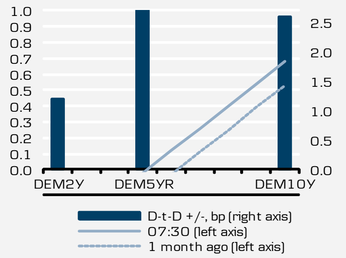
10Y Yield Spread to Germany



US Yield Curve



German Yield Curve



Credit spread, iTraxx s. 11*

	07:30		1day		1month
Europe (IG)	79	↓	0	↑	7
HiVol	101	↑	11	↑	13
Xover (N-IG)	330	↓	-1	↑	26
Finan. Sr.	76	↓	0	↑	4
Finan. Sub.	163	↓	0	↑	6
Non-finan.					

* Ask price

Credit spreads

Swap Spread, bp**

	17:00	*07:30*		*+/-*
USD 10Y				
JPY 10Y	-10	-9	↑	2
	*07:30(-1)**	*17:00*		*+/-*
EUR 10Y	0	14	↑	14
DKK 10Y	34	33	↓	-1
SEK 10Y	43	42	↓	-1
NOK 10Y	59	57	↓	-2

* As of closing previous trading day

** Ask price

Source: Bloomberg, Danske Bank Markets

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First date of publication

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