



Sunrise

Wednesday, 25 May 2016

Rates: Greece secures funding

The Eurogroup agreed to disburse the next aid tranche to Greece which should cover the country's funding need over the next 12 months. Additionally, they agreed on a package of debt measures which will be phased in progressively depending on necessity and conditionality. The outperformance of Greek bonds could continue today.

Currencies: Risk-on rally propels USD

Yesterday, the dollar profited from an outright risk-on sentiment even as the US currency received little additional interest rate support. EUR/USD extensively tested the 1.1144 support. Today, the eco calendar is again thin. Can the dollar maintain its momentum without hard news? Sterling rebounded as polls showed a further lead for 'remain' at the EU referendum.

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 gained up to 2% yesterday** supported by higher oil prices and strong housing data, ignoring a stronger US dollar. This morning, **Asian shares show broad-based gains too**. Japanese shares outperform on a weaker yen.
- **Greece's international creditors agreed on broad but inexact principles to ease the country's debt mountain** when its €68 billion bailout package ends in 2018. **A full agreement was also reached on the package of reforms Greece had committed to last summer**, allowing the country to get €10.3 in rescue loans, beginning with a €7.5 billion cash release next month.
- **Japanese Finance Minister Aso said he told his G7 counterparts last week that his country will proceed with the scheduled sales tax hike next year** as it is an important factor in maintaining trust in Japan's finances.
- **The People's Bank of China set this morning the trading band for the renminbi at its weakest level against the US dollar since March 2011**, 0.34% weaker than the day before due to a stronger dollar. The market rate is however still 0.5% stronger than its nadir in January, when there was panic about the economy.
- **Crude oil prices jumped higher yesterday after API data showed US crude stocks dropped 5.1 million barrels last week**, double the expected amount. Both the Brent and WTI are nearing the \$50/barrel level, ignoring a stronger US dollar.
- Today, the **eco calendar** contains the **German IFO indicator** and US house price data. The **Bank of Canada will decide on rates** and a whole range of ECB and Fed speakers will take the stage.

Rates

	US yield	-1d
2	0,9264	0,0293
5	1,4112	0,0478
10	1,8664	0,0401
30	2,6464	0,0278

Hawkish Fed talk continues to affect short end US curve

Longer end US and German curves again little changed

Peripheral spread narrowing on risk-on sentiment

	DE yield	-1d
2	-0,5050	-0,0010
5	-0,3530	0,0040
10	0,1790	0,0130
30	0,9053	0,0106

Upward surprise IFO sentiment

Greece gets €10.3B in new loans

Complicated and conditional debt relief

Treasuries under pressure as bets on Summer hike rises

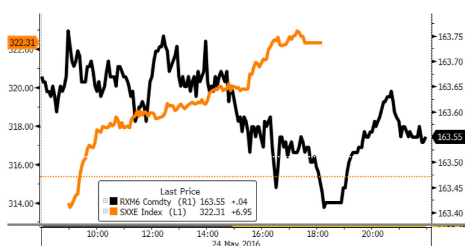
Global core bonds parted ways today. German Bunds traded sideways while US Treasuries lost some modest ground, especially at the 2-to-5-yr sector. Implied probabilities of a Summer rate hike by the Fed increased further after comments of Fed Harker, who confirmed earlier comments that the Fed could go as early as in Summer. A strong 2-yr US Note auction pushed 2-yr yields somewhat lower, but not enough to erase the earlier increase. Very strong New Home sales nurtured the idea the Fed could hike rates soon. German Bunds actually held up quite well against the background of surging European equity markets and a recovering oil price. In a daily perspective, German yields were virtually unchanged across the curve, while the US yield curve shifted 1.3 bps (2-yr) to 3.6 bps (5-yr) higher, the shorter end underperforming the longer end. **On intra-EMU bond markets**, peripheral 10-yr yield spread changes versus Germany narrowed up to 4 bps in the risk-on context. **Greek bonds didn't specifically outperform ahead of the Euro group meeting.**

German IFO and central bankers in focus today

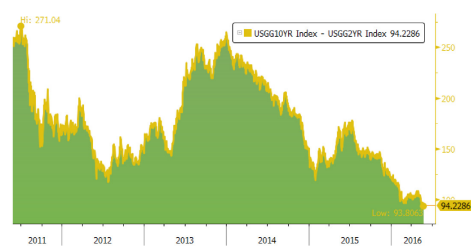
After a marginal drop in April, the **German IFO business climate indicator** is expected to have picked up slightly in May from 106.6 to 106.8. We believe however that the **risks for the IFO are on the upside of expectations** following remarkably strong German PMI's earlier this week. **US house prices and Markit services PMI** are usually no market movers. ECB governors Linde, Villeroy, Knot, Constancio and Praet speak throughout the day. We will listen careful, but don't expect new info with market implications. Fed Kashkari, Harker and Kaplan speak too, but have already spoken recently.

Greece reaches breakthrough deal with creditors

Greece, the EU and the IMF reached a quite complicated deal. First and foremost, **Greece will get €10.3B in fresh loans** starting with a €7.5B instalment in the second half of June. It will allow Greece to satisfy its ST debt service obligations (to IMF and ECB) and start the clearance of part of the arrears as support for the real economy. A complicated compromise had been reached with the IMF (and especially Germany) on some debt relief. It consist of ST, MT and LT measures that however all still need to be negotiated and agreed in due time. Germany accepted the principle of debt relief while the IMF accepted that the most important debt-relief measures wouldn't be enacted until at least 2018, when the Greek bailout ends. So, it's a compromise. The debt relief package should keep Greek debt financing costs below 15% of GDP until 2030 and 20% after that. Before 2018, the ESM will rearrange its loan book with the aim of smoothing its payment profile and reducing interest risk.



Bund future (black) & EuroStoxx (orange) (intraday): Bund holds up well in face of strong equities and higher oil prices.



US 2-to-10-yr yield spread at lowest level in 5-years as rate expectations increase and longer end reacts subdued.

R2	165	-1d
R1	164,6	
BUND	163,51	-0,1500
S1	161,46	
S2	160,81	

Very strong US 2-yr Note auction

The German Finanzagentur taps the off the run 30-yr Bund (€1B 2.5% Jul2044). Tapping off the run Bunds (only 30-yr) is a new feature in this year's German funding strategy. The Bund on offer didn't cheapen in ASW-spread terms in the run-up to the auction, but trades normal at the very long end of the German yield curve. Total bids at the previous 6 30-yr Bund auctions averaged €1.27B and we don't expect much improvement today. **The US treasury started its end-of-month refinancing operation** with a very strong \$26B 2-yr Note auction. The auction stopped more than 2 bps below the 1:00 PM bid side and the bid cover was high (3.00). The backup in yields appeared to outweigh short-term Fed rate hike concerns. Bidding details showed an especially large and aggressive dealer bid. Today, the Treasury holds a \$34B 5yr Note auction and a \$13B 2-yr FRN auction. Currently, the WI of the former trades around 1.41%.

Trading driven by risk sentiment

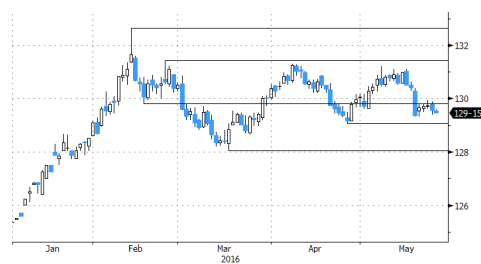
Overnight, Asian stock markets build on strong risk sentiment in Europe and the US yesterday. Main indices gain more than 1% with China underperforming and recording smaller advances. Brent crude holds on to yesterday's gains and hovers above \$49/barrel. The US Note future trades more or less stable, suggesting a neutral opening for the Bund.

Today's eco calendar contains German Ifo. Risks are on the upside of expectations, but European eco data can't leave a trace on markets at this stage. Several ECB members speak, but their message is well-known. Fed Harker, Kashkari and Kaplan already shed their views. Overall, we have no strong view for today's trading. If yesterday's rally on equity/commodity markets persists, it could further weigh on core bonds. On peripheral markets, Greek bonds should continue to outperform following the Eurogroup's approval to disburse the next aid tranche.

Longer term, the Bund remains in the sideways channel between 160.81 and 164.60. **We would sell on upticks near the resistance for a move back deeper in the range. In yield terms, 0.07% is key support for the German 10-yr yield.** The US Note future trades in the middle of the 128-01+ to 131-14 sideways range. A June rate hike is a plausible scenario, which is far from completely discounted by markets. Therefore, we expect more price action towards the downside of the range. Short-term (2y/5y) spread differentials between the US and Europe could widen further on the hawkish repositions of US bond markets. The front-end of European yield curve is locked by the ECB's easy monetary policy.



German Bund (160.81 to 164.60): New sell-on-upticks around the upper bound



US Note future: Heading towards 128-01+ on hawkish Fed?

Currencies

USD propelled by risk-on rally

Dollar rebounds as equities rally

R2	1,1616	-1d
R1	1,1349	
EUR/USD	1,1152	-0,0063
S1	11,1058	
S2	1,1012	

Today, the focus is on the IFO business climate and central bank speak

Will the dollar and equities extend gains without new high profile news?

On Tuesday, the dollar restarted its recent rebound even as there was little additional news on the chances of a Fed rate hike. Positive risk sentiment and a slight rise in interest rate differentials in favour of the US currency also supported the dollar. EUR/USD tested the 1.1144 support and closed the session at 1.1141. USD/JPY returned to the 110 area (from 109.24 on Monday).

Overnight, Asian equities join yesterday's risk-on rally from Europe and the US. Japan outperforms as USD/JPY rebounded to the 110 area. **The PBOC** fixed the yuan at the lowest level since 2011. The move mostly mirrors USD strength. Despite the weaker fixing, the yuan still trades stronger than the levels in January when the currency was under pressure due to global market tensions. Commodities like copper and oil also trade with a positive bias despite the strong dollar. For now, it is only of limited help for commodity currencies like the Aussie dollar (AUD/USD near 0.72) or the Canadian dollar (USD/CAD 1.31). EUR/USD holds near the recent low in the 1.1150 area. The agreement at the Euro group meeting to pay a next tranche under the Greek rescue plan has no noticeable impact on EUR/USD trading.

Today, the eco calendar is quite thin with only the German IFO business climate indicator, US house price data and advance goods trades balance. Central bankers remain active with a whole range of ECB and Fed governors scheduled to speak. The Bank of Canada will decide on rates.



EUR/USD: testing the 1.1144 support

USD/JPY returns to 110 level

After a marginal drop in April, the **German IFO business climate indicator** is expected to have picked up slightly in May with the consensus looking for an increase from 106.6 to 106.8. We believe however that the risks for the IFO are on the upside of expectations following remarkably strong German PMI's earlier this week. **However, we doubt that today's data will be a key factor for currency trading.** Most Fed speakers already gave their view recently. **So, global market sentiment will probably remain the key factor for USD trading.** Asian equities and US/European equity futures again suggested a positive open. In theory, this might be further supportive for the dollar. However, how long will the risk-on rally continue without further good news from the economy?

Tion

How long will US equities ignore the impact of a stronger dollar? The day-to-day momentum is USD positive. However, as the driver for the risk-on rally is a bit unclear and as the rise in USD bond yields remains limited, we are reluctant to jump on the USD rally at this stage. We look sell/add EUR/USD shorts on upticks.

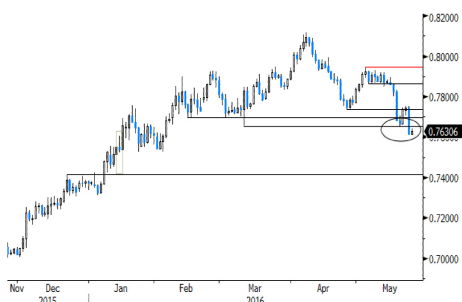
Technically, the March/April USD decline petered out and in May the dollar strengthened, gradually supported by more hawkish Fed comments/Minutes that opened the door for a possible June rate hike. **We maintain our view that the US economy is strong enough to allow the Fed to implement two rate hikes this year.** If the eco data don't disappoint, chances for a June rate hike increase, supporting the dollar. EUR/USD dropped below a first support at 1.1217 and is currently testing the 1.1144 correction low. A break below this level would be USD positive, but we have the impression that it is a bit too early for further sustained USD gains. USD/JPY dropped to new lows early May. **Verbal Japanese interventions and a global, Fed-driven USD rally blocked the downside of USD/JPY. The high 111 area is an important area, where USD/JPY might run into resistance if global risk sentiment would worsen (due to higher US rates or other event risk). The US disapproval for yen interventions is yen supportive if sentiment would turn risk-off.**

Sterling jumps sharply higher across the board

R2	0,8117	-1d
R1	0,7947	
EUR/GBP	0,7631	-0,0109
S1	0,7562	
S2	0,7312	

On Tuesday, sterling was supported by a new poll showing a big lead for the remain camp. Sterling started a rebound against the euro and the dollar at the open of the European markets. EUR/GBP touched a correction low below 0.7650 around noon. The decline continued in the afternoon, but at a slower pace. Cable rebounded north of 1.46. In a hearing before parliament, **BoE governor Carney** defended the BoE approach on the Brexit risk. Carney repeated that, in case of a remain vote, the next BoE rate move will likely be a rate hike.. CBI distributive trades also improved sharply after last month's decline. **So, the news flow was outright sterling positive.** EUR/GBP closed the session at 0.7613. Part of this decline is also due to the overall EUR/USD decline. The gains in cable (close 1.4636) are slightly less due to dollar strength.

Today, there are no UK eco data on the agenda, meaning that headlines on Brexit and global sentiment will set the tone for sterling trading. The day-to-day momentum of sterling is clearly positive, especially against the euro. However, in line with EUR/USD, we are reluctant to jump in after the recent rally, as we expect some consolation after the recent rally. Of late, the negative sterling momentum eased. Markets adapted positions to a lower probability of a Brexit. EUR/GBP dropped below a first range bottom at 0.7735 and is currently testing the 0.7650 support. A break below this level would further improve sterling sentiment. However, we think that a breather on the recent sterling rally is needed first.



EUR/GBP tests 0.7650 support



GBP/USD: nice rally, but no topside break

Calendar

Wednesday, 25 May		Consensus	Previous
US			
13:00	MBA Mortgage Applications (May 20)	--	-1.6%
14:30	Advance Goods Trade Balance (Apr)	-\$60.0b	-\$56.9b
15:00	House Price Purchase Index QoQ (1Q)	--	1.4%
15:00	FHFA House Price Index MoM (Mar)	0.5%	0.4%
15:45	Markit Services PMI (May P)	53.0	52.8
Canada			
16:00	Bank of Canada Rate Decision	0.50%	0.50%
Germany			
08:00	GfK Consumer Confidence (Jun)	9.7	9.7
10:00	IFO Business Climate (May)	106.8	106.6
10:00	IFO Current Assessment (May)	113.3	113.2
10:00	IFO Expectations (May)	100.8	100.4
France			
18:00	Total Jobseekers (Apr)	3535.5K	3531.0k
18:00	Jobseekers Net Change (Apr)	4.5	-60.0
Italy			
10:00	Industrial Sales MoM YoY (Mar)	--	0.1%/-0.2%
10:00	Industrial Orders MoM YoY (Mar)	--	0.7% / 3.8%
Belgium			
15:00	Business Confidence (May)	-2.4	-2.4
Events			
08:30	ECB's Linde Speaks in Madrid		
09:00	ECB's Villeroy Speaks in Madrid		
09:00	EU Finance Ministers meet in Brussels		
11:00	ECB's Knot Speaks in Madrid		
12:30	ECB Vice President Constancio Speaks in London		
12:30	ECB's Praet Speaks in Madrid		
15:00	Fed's Harker Speaks at Forum in Philadelphia		
17:40	Fed's Kashkari Speaks on Energy and Monetary Policy in ND		
20:00	Fed's Kaplan Speaks at Greater Houston Partnership		
Norway	Bond Auction (NOK3B 1.75% Mar2025)		
Germany	Bund Auction (€1B 2.5% Jul2044)		
Sweden	Bond Auction (SEK1B 3.5% 2022 & SEK3B 1% 2026)		
US	5Yr Notes (\$34B) & 2Yr FRN (\$13B) Auction		

Contacts

10-year	td	-1d	2-year	td	-1d	STOCKS	-1d
US	1,86	0,04	US	0,93	0,03	DOW	17706 17706,05
DE	0,18	0,00	DE	-0,51	0,00	NASDAQ for Exch - NQI	#VALUE!
BE	0,57	0,00	BE	-0,48	-0,01	NIKKEI	16757 16757,35
UK	1,47	0,02	UK	0,47	0,03	DAX	10057,31 10057,31
JP	-0,10	0,00	JP	-0,24	0,00	DJ euro-50	3010 3010,12

						USD	td	-1d
IRS	EUR	USD (3M)	GBP	EUR	-1d	-2d	Eonia EUR	-0,34 -0,002
3y	-0,120	1,172	0,947	Euribor-1	-0,35	0,00	Libor-1 USD	0,51 0,51
5y	0,024	1,355	1,122	Euribor-3	-0,26	0,00	Libor-3 USD	0,59 0,59
10y	0,575	1,703	1,515	Euribor-6	-0,14	0,00	Libor-6 USD	0,73 0,73

Currencies		-1d	Currencies		-1d	Commodity	CRB	GOLD	BRENT
EUR/USD	1,1153	-0,0061	EUR/JPY	122,6	0,10		183,3452	1224,82	49,18
USD/JPY	109,95	0,66	EUR/GBP	0,7629	-0,0111	-1d	-0,86	-19,68	1,11
GBP/USD	1,4612	0,0131	EUR/CHF	1,1059	-0,0048				
AUD/USD	0,7205	0,0015	EUR/SEK	9,2625	-0,10				
USD/CAD	1,3100	-0,0062	EUR/NOK	9,2988	-0,08				

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