Danske Daily - Danske Bank Research

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In focus today

- In the euro area, the ECB will announce its deposit rate. We expect the ECB to raise policy rates by 25bp, bringing the deposit rate to 2.50%, in line with consensus and market pricing. We expect Lagarde to retain full optionality over the future rate path and provide no firm guidance, which should limit the market reaction. Read more in ECB Preview - Hiking, not guiding, 4 September.
- In the US, August PPI is due for release. In recent months, y/y growth in both headline and core PPI has trended down. Headline PPI inflation is likely to have increased, as oil prices rose again. Unusually, PPI is released before CPI, which is due tomorrow. As a result, PPI could carry more weight than usual for markets.
- In Norway, we expect core inflation (CPI-ATE) to rise from 2.7% y/y to 3.1% y/y in August (cons: 3.0% y/y). The main driver is that kindergarten prices were cut sharply in August last year, and this base effect will lift annual growth by about 0.3 pp. Apart from this, we expect only minor changes, although somewhat higher price growth for food and imported goods than last year should add about 0.1 pp to annual growth. As usual, the biggest risk is prices for airline tickets and ICT equipment. If we are correct, core inflation will still be well below Norges Bank's estimate of 3.3% y/y in the June Monetary Policy Report.
- In Sweden, July GDP figures will be released, alongside production data (PVI). Consensus points to a modest m/m decline of 0.1% in July, following a 0.2% drop in June and a strong second quarter overall, when GDP rose 1.6% q/q. The monthly indicator is volatile, so a small decline would not be surprising. A strong print, however, would reinforce the view that the domestic economy is gaining momentum and add pressure on the Riksbank to raise rates in the near term.
- In Denmark, August CPI data is due for release. We expect CPI inflation to increase to 2.2% y/y from 1.7% y/y in July on the back of significantly higher electricity prices. The inflation level remains elevated from a much higher weight on holiday centres and camping sites, which adds significantly to inflation during the summer months. This is counterweighed by the large cut in the electricity fee in January. Underlying price pressures remain muted in Denmark.

Economic and market news

What happened overnight

In commodities, Brent rose above USD 100/bbl yesterday and held above that level overnight, as the largest wave of US-Iran attacks on shipping since the war began intensified supply concerns. Oil flows through the Strait of Hormuz remain far below pre-war levels and pressure on Red Sea routes is rising. President Trump said the conflict may not end until after the midterms, while the *WSJ reported* that top White House advisers see a risk it could last through the end of his term, pointing to limited prospects for near-term de-escalation.

In Japan, expectations for another BoJ rate hike next week were reinforced after board member Masu warned that still-loose financial conditions could require rapid rate hikes if inflation accelerates. He said real rates should be moved out of negative territory as soon as possible, citing higher producer, fuel, chemical and food prices, a weaker yen and greater corporate cost pass-through as price risks. Markets have now almost fully priced in a 25bp hike for the September meeting, and a total of 3-4 hikes by next summer.

In the US, at the opening night of the Republican Party's first-ever midterm convention in Dallas, President Trump promised a USD 5,000 payout to adult citizens if Republicans retain control of Congress. The proposal is a direct financial appeal to voters but would risk adding to inflation pressure and fiscal concerns. The proposal could cost up to USD1.3 trillion in total, and increase the budget deficit by some 4%, making it nearly impossible to get through even a republican-controlled congress.

What happened yesterday

In the US, the Treasury announced that today's first expanded long-end bond buyback operation will be up to USD 6bn. This is probably close to the bare minimum needed after the August guidance pointed to more than a doubling of the previous USD 2bn amount, and some investors had seemingly hoped for a larger first step. The announcement applies to today's operation only and does not set the size for later ones. Long-end US Treasury yields rose following the announcement, although the move was contained.

In Poland, the National Bank of Poland kept its key rate unchanged at 3.75%. The decision came despite CPI inflation being just below the upper end of the central bank's target band, mainly due to higher fuel price inflation, while softer wage growth and falling enterprise-sector employment supported a wait-and-see approach.

Equities: Equities were markedly lower on Wednesday as higher energy prices, rising bond yields and a disappointing Treasury buyback announcement weighed on sentiment. The S&P 500 fell 0.5%, while the Stoxx 600 dropped a notable 1.4%. Tech continued to outperform, explaining why US held up better than most regions. Semis finished modestly higher and Meta surged 7% following the release of its Muse consumer AI agent, providing another example of the industry's shift towards increasingly autonomous AI applications.

More complex models require greater computing power, which helps explain why semiconductor stocks have remained resilient despite rising yields.

Market breadth was nevertheless weak, with 405 of the 500 S&P constituents closing lower. Cyclical sectors such as industrials and consumer discretionary led the declines, falling roughly ~1.5%. However, this was not a classic risk-off session. Defensive sectors like utilities, consumer staples and real estate also underperformed heavily, explained by the yield sensitivity. As a result, yesterday's sector performance was more consistent with a stagflationary shift than outright growth concerns.

FI and FX: Yields rose yesterday as energy prices pushed higher, with EUR swaps rising around 8bp higher in the 2Y to 10Y segments of the curve. The US announcement of the size of the buyback announcement was slightly less than market anticipated, and we saw the EUR/USD edge slightly higher in tandem with longer Treasury yields. Today, focus turns to the ECB meeting, where a hike is widely expected. We do not expect Lagarde to rock the boat materially, but keeping all options open, which should limit the market reaction in our view. We expect Danmarks Nationalbank to follow the ECB with a 25bp hike. In Norway, this morning's inflation print will be hugely important for Norges Bank's decision later this month. While EUR/NOK made new YTD lows yesterday, the SEK has been a relative underperformer this week.

Fixed income and FX markets

Majors FI

Yields moved higher during yesterday's session as headlines related to the war in the Middle East pushed energy prices higher. The Brent oil futures contract broke above USD 101 per bbl, and European gas prices continued higher as well, with the front-month futures contract at its highest level since 2022. The EUR swap curve rose by 8bp across the 2Y to 10Y segments of the curve. 10Y France and Italy widened against Germany, by around 3bp.

Today, focus turns to the ECB meeting. A 25bp hike is widely anticipated so attention will turn to Lagarde and her comments during the press conference. We expect Lagarde to retain full optionality over the future rate path and provide no firm guidance, limiting the market reaction. See more in our ECB Preview - Hiking, not guiding, 4 September. Given the increase in energy prices and inflation pricing, it is worth highlighting that the cut-off date for ECB forecasts was 18 August. Since then, Brent oil is around 10% higher and the TTF gas price is around 20% higher.

US yields also rose yesterday, but to a lesser extent with the swaps 4-5bp higher. The US Treasury announced yesterday that the buyback sizes will be increased to USD 6bn, with the first operation using the new size is scheduled for today. US 10Y rose around 3bp when the size was announced, suggesting that markets had anticipated a larger amount. Tonight, the US will auction USD 22bn of 30-year bonds, which will be a further test of the long end. At 5.30%, the 30Y UST yield is at its highest levels since 2007.

Italy will supply the market with 3Y and 7Y bonds for up to EUR3.5bn each, and, at the very long end with up to EUR 750m in the 2.15% 2072 bond.

Majors FX

EUR/USD ultimately edged only cautiously higher after some back-and-forth trading through yesterday's session. The US Treasury announced that the size of the first increased long-end buyback operation conducted today will be USD6bn. This was on the lower end of expectations, as it just barely fulfils the guidance for "more than doubling" the earlier amount of USD2bn. Furthermore, the Treasury did not provide guidance for later long-end operations that are conducted roughly every 1-2 weeks. Long-end UST yields ticked modestly higher, US swap spreads tightened and EUR/USD declined, but the moves were relatively contained compared to the August announcement. Brent oil price rose back above USD100/barrel, and other energy prices remain on the rise as well. European TTF natural gas price temporarily broke through EUR80/MWh for the first time since late 2022, and electricity futures prices in Northern Europe have also risen notably in September. Overall, euro area's commodity terms-of-trade have reached their weakest level since early 2023, and over the medium-term, we see further rise in energy prices as a relatively larger downside risk to EA growth outlook (vs. the US), and a negative driver for EUR/USD. Today, we expect Lagarde will not rock the boat materially, but looking further ahead, our EUR strategists continue to see downside risks to current ECB pricing. Our forecasts for upcoming US inflation releases are also in line with consensus, but we will keep a close eye on the PPI data released already today, unusually ahead of the CPI tomorrow.

Scandies

SEK has been a relative underperformer this week, with EUR/SEK rising to 11.15 and USD/SEK to 9.58. The move reflects weaker risk sentiment, as oil prices have climbed above 100 USD/bbl, alongside neutralized expectations of a Riksbank hike in September, after the soft CPI print. The ECB is widely expected to deliver a 25bp hike today, which would widen the policy rate gap to 75bp versus the Riksbank. Looking at our rate models, there is still upside in both EUR/SEK and USD/SEK, in line with our forecasts, driven by rate differentials and the broader risk sentiment. NOK/SEK continues to trend higher as elevated oil prices support the Norwegian krone. With the Riksbank remaining dovish and volatility in NOK/SEK staying relatively low, the carry trade is becoming increasingly attractive, weighing on SEK. The policy rate gap already stands at 250bp and could widen further if Bank of Norway delivers another rate hike.

EUR/NOK made new YTD lows in yesterday's session, with the NOK continuing to benefit from rising oil prices, which topped USD 100/bbl for the first time since late July. The catalyst is the escalating tensions in the Middle East, where any near-term de-escalation increasingly looks elusive. The Iran-Oman deal that was described as "imminent" last week has effectively collapsed in the face of renewed military escalation. While the NOK is currently more or less solely in the hands of the global environment - and not least energy prices - this morning's Norway August CPI print will be hugely important for Norges Bank's decision later this month. We expect core inflation to rise from 2.7% to 3.1% y/y, partly reflecting base effects from last year's sharp cut in kindergarten prices. Even so, this would remain below Norges Bank's June forecast of 3.3%. We maintain our call for a 25bp hike to 4.50% on 24 September. That said, a downside inflation surprise this morning and/or a weaker Regional Network Survey - due on 17 September - could see Norges Bank stay on hold. We remain constructive on the NOK in the near term, although we also highlight that the move higher increasingly looks exhausted unless oil consolidates above USD 100/bbl.

Given the recent rise in the global government bond yields including Denmark, then we are very close to opening the 10Y interest only version of 5% 30Y callable (5% 2059IO). The price spread to 4'59IO is expected to be around 4.5-5pts and with a cash price of 94-94.25 for 4'59IO, then the mortgage banks should open a 5% 2059IO.

The initial reaction to opening a 5% 30Y callable is a bit risky in this environment. However, with 5% 2056IO closed for issuance, then the mortgage banks must open a new series such as the 5% 2059IO. We expect that the opening of 5% 2059 will put some pressure on 5'56IO and 5'53O

Tactical views

FX

EUR/USD - On a structurally declining trend, target 1.12 in 12M

EUR/NOK - Tactically neutral to slightly bearish. Strategically bullish.

EUR/SEK - Dovish Riksbank skews risks to the topside in EUR/SEK

EUR/GBP - Tactically neutral and strategically bullish

USD/JPY - Looking for strategic selling opportunities

EUR/DKK - DN to cap EUR/DKK around the 7.4758 peak from June

USD/CNY - Tactically sell on rallies, strategically bearish

Fixed Income

Europe - Bund ASW-spreads to tighten

US - 10Y US Treasury yields to hit 5% over the coming year

Sweden - Look for SEK underperformance vs EUR

Norway - Look to enter steepeners in the coming month

Denmark - Long high-coupon callables versus DGBs and swaps

Commodities

Oil - remains in the hands of developments in the Middle East.

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