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MACRO MARKETS DAILY

Economic data today

- **US 2Q17 Preliminary GDP growth** (last 1.4% QoQa). We estimate that GDP growth could surpass an annualized rate of 2.5% in 2Q17E, thanks mainly to the rebound in personal consumption and the positive contribution from the change in inventories and the external sector.
- **Spain 2Q17 Preliminary GDP growth** (exp. 0.9% QoQ and 3.1% YoY, last 0.8% QoQ and 3.0% YoY). The bulk of the indicators already released point to some acceleration of the Spanish economy in 2Q17, in a context of a strongly positive contribution from domestic spending and a good export performance. Should this prove to be the case, the risks for our GDP forecast for the whole of 2017 (3.1%) would be clearly to the upside.
- **Spain July Preliminary CPI** (exp. 1.5% YoY, last 1.5% YoY). We still believe the risks for core inflation are skewed to the upside, because of the strong internal demand. **Germany July Preliminary CPI** (exp. 1.6% YoY, last 1.6% YoY). For July, we anticipate a yearly rate for both headline and core inflation similar to last month's. **France July Preliminary CPI** (exp. 0.7% YoY, last 0.7% YoY). For core inflation, we see clear upside, supported by the recovery in final domestic spending (above 2.0% YoY) and companies improving their margins.
- **Euro zone July Economic Sentiment** (last 111.1).
- **France June Consumer Spending** (last 1.0% MoM and 1.3% YoY).
- **UK July Economic Sentiment** (last 109.3): We have less upbeat expectations for the UK components of the European Commission's surveys, which have been going sideways rather than accelerating recently. UK manufacturing has been giving relatively strong readings in this survey, as with the PMIs, but this has not translated into the hard data: the ONS currently estimates that the sector contracted by 0.5% during 2Q17.

Rates Strategy

- **EUR rates:** Following a strong opening, with EUR govies catching up with the post-FOMC rally in USTs, the rest of the day saw a much quieter session. The 10y Bund yield touched an intra-day low of 0.51% early in the morning, but finally closed at 0.53% (still 3bp richer on the day). Interestingly and in contrast with the recent price action in the US, where swaps and USTs moved in tandem, the Eurozone swap curve lagged in today's move and swap spreads widened all along the German curve.
- Among EUR issuers, risk premia remain stable-to-tighter despite all the recent volatility, which continues to make us feel **comfortable with our "overweight" periphery call**. As regards changes in the EUR term structure, the belly (5-10 years) led the bullish market yesterday and, as a result, we saw some flattening in 2s5s, but steepening in 10s30s. With 2s5s back at the same levels as a month ago, but 10s30s 5bp steeper, we think that the long end could now outperform if the market remains bullish.

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- **Today**, the release of the first July CPI estimates in Spain, Germany and France should help anticipate possible surprises in the EUR figures on Monday but, barring a huge surprise there, the tone of the session is likely to be determined by the market reaction to the **US GDP figures** – with the risks slightly biased to the bullish side, in our view. Given the Fed's renewed focus on inflation, we believe the market could **underreact to a strong number** (as it would still require inflation to pick up to drive a repricing in monetary policy expectations), **while a weak number would likely add to the bullish sentiment** on USTs, as it would probably push the Fed to become more dovish in the near term.

- Lastly, on the **sovereign ratings** front, the only EUR issuers scheduled for a possible review today are **France** (AA, stable) and **Austria** (AA+, stable), both by Fitch. We expect no changes here, in either case.

- **UK rates** were also playing catch-up with the US rally yesterday, but ended up outperforming them, especially in the long end. That cross-market flattening reflects the coupon/extension/supply factors detailed in our Auction Preview from Monday, in our view, but was still not enough to stop the 10s30s curve from steepening 1bp in the Fed-led rally. 3y gilts were notably strong for a second day, but it was 5y's turn to lead the way, particularly the new 0T 23s (which we still see as too rich versus their neighbours and vulnerable to a correction). Gilts out to 10y once again widened versus swaps in the rally; the 4Q 27s and 6 28s have lagged the surrounding ASW performance, and currently look the most appealing point gilt spreads to buy.

- **UK inflation:** Breakevens were under pressure well beyond that implied by yesterday's nominal rally, and tightened by 3-5bp across the curve to give an outright sell-off in most real yields. The front end held up relatively well, despite the sharper outright rally there and the approaching 10y linker auction on 8 August (perhaps helped by the 10y nominal having one first). Month-end will not necessarily bring any relief for long linkers, as their 0.1y index duration extensions are much smaller than the 0.3y we estimate for nominals. The 10s30s real curve, at 33bp, is near the middle of its 28-40bp range over the last year, so the steepening may have much further to go before finding resistance.

FX Strategy

- The **USD** has dominated the FX market this week, with the currency's post-FOMC weakness on Wednesday night forcing the other G10 currencies higher against the Greenback. The currency reversed most of this decline in European trading yesterday, but still remains somewhat lower, holding below the 94-mark overnight.

- Today, the USD is likely to lead the way once again, as the market prepares for initial Q2-17 GDP data in the US. After a weak Q1-17 print, growth is expected to rise to an annualised 2.5%. Given such a sharp decline in the USD in recent weeks, we think such an outturn should support the currency.

- **EUR/USD** edged a little higher overnight, and is now close to 1.1700, ahead of Eurozone confidence data today. In the UK, while the GdK Consumer Confidence fell back to the same level as that seen a year ago right after the Brexit vote in June, **GBP/USD** has held comfortably above 1.3050, with **EUR/GBP** continuing to sit just below 0.8950. Meanwhile, **USD/JPY** has fallen back to 111.00 despite more weak CPI data in Japan and another set of dovish BoJ minutes.

- **EUR/SEK** rose yesterday, climbing to 9.60 despite a general pick-up in Swedish confidence data and the unemployment rate dropping to 6.4%, a joint eight-year low. Today, the currency will switch its focus to Sweden's GDP data. After quarterly growth of just 0.4% in Q1-17, firmer growth is likely in the second quarter. Indeed, if the quarter-on-quarter print comes in at 0.9%, as expected, it should boost the SEK and pull EUR/SEK lower today.

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