



Sunrise

Thursday, 02 February 2017

Rates: Fed keeps it simple; US Treasuries rebound

US Treasuries rebounded as the Fed kept its monetary policy unchanged without giving a hint about when the tightening cycle will continue. Its policy statement was nearly a copy for the December one. Today's eco calendar is thin with only US weekly jobless claims. Speeches by ECB governors and the BoE policy meeting are wildcards.

Currencies: Fed doesn't help the dollar

Yesterday, the USD returned gains eked out after strong eco data as the Fed stayed muted on the timing of further rate increases. Today, a cautious risk-off sentiment may continue to weigh on the dollar. Sterling traders keep a close eye on the BoE policy decision. A positive BoE assessment might be (moderately) supportive for sterling.

Calendar

Headlines

S&P	↗
Eurostoxx 50	↘
Nikkei	↘
Oil	↗
CRB	↗
Gold	↘
2 yr US	↘
10 yr US	↘
2yr DE	↘
10 yr DE	↘
EUR/USD	↘
USD/JPY	↘
EUR/GBP	↘

- **US stock markets ended close to unchanged** with Nasdaq outperforming (+0.5%). **Overnight, most Asian stock markets lose ground** with Japan underperforming on the back of a stronger yen.
- **The Federal Reserve kept its monetary policy unchanged** and said it remains on track to gradually raise short-term interest rates this year **without giving a hint about when the next increase might come**.
- **Facebook's revenue and earnings soared in the fourth quarter** despite investors' concerns sales will slow as it hits the limit on how many advertisements it puts in its news feed.
- **Australia boasted its biggest trade surplus on record** in December as surging commodity prices showered the resource-rich nation in cash, a windfall that could lessen the risk of a downgrade to its triple A credit ratings.
- **Theresa May won lawmakers' OK to trigger EU separation talks by the end of March**, though lawmakers warned not to mistake that for unconditional support to negotiate freely. The government outlines its strategy today.
- **Italy has pledged to meet the EU's demands for extra cuts to its budget deficits** by ramping up its tax evasion efforts and introducing new spending cuts, though the timing and precise scale of the move remain uncertain.
- **President Trump urged Republicans in the Senate to make a major change to the chamber's voting rules** if Judge Gorsuch can't attract the necessary Democratic support to win confirmation for the Supreme Court.
- **Today it's Carney's first "Super Thursday" of 2017**, with the BOE chief presiding over a policy decision, new inflation forecasts and a press conference. **ECB Draghi, Praet and Coeure speak** and US weekly jobless claims will be published.

Rates

Bund loses ground on better risk sentiment and strong US data

US Treasuries erases most losses after dovish FOMC

	US yield	-1d
2	1,21	-0,01
5	1,92	-0,02
10	2,46	-0,01
30	3,07	0,00

	DE yield	-1d
2	-0,71	-0,02
5	-0,29	0,11
10	0,47	0,03
30	1,20	0,05

BoE to stand put, but surprises may affect overall sentiment

ECB speakers to confirm APP stays on track

Eco data second tier today

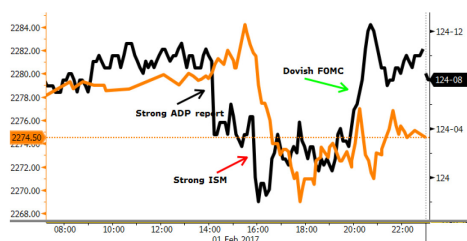
US Treasuries' losses largely erased after dovish FOMC

Yesterday, global core bonds lost ground intraday, but recouped most of the losses after the FOMC statement. The Bund opened weaker on the back of improving risk sentiment in Asian trading. Gradually rising European equity and oil prices weighed on Bunds throughout the session. **A stunning US ADP employment report and a very strong manufacturing ISM (with a skyrocketing price index), added another blow to US Treasuries and Bunds. Finally, the FOMC published a dull statement (see flash report).**

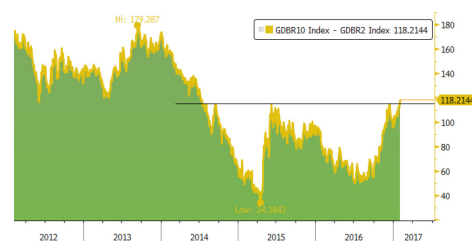
As markets expected something slightly more hawkish, US Treasuries reacted in a dovish way, erasing a large part of the intraday losses. In a daily perspective, US yields ended between 0.8 bps (2-yr) and 1.7 bps (5-10-yr) higher. The German yield curve (cash market closed ahead of FOMC meeting) bear steepened with yields up to 5.7 bps (30-yr) higher. Please note that the 3-to-5-yr German yield changes (+7 to +10.9 bps) were partly due to benchmark changes. The German 2-10-yr yield spread reached 118 bps, the highest level since July 2014. The improving economic EMU environment and rising inflation expectations play a major role in the steepening. **On intra-EMU bond markets, 10-yr yield spread changes versus Germany widened up to 2 bps with Spain (5 bps) underperforming on upcoming supply.**

BoE meeting and ECB speakers

The BoE meets today, but no change of the policy stance is expected. Rather subdued headline inflation gives them leeway to stay soft. Nevertheless we don't expect the asset purchases to be prolonged beyond the original amount which is almost reached. **This should be no surprise either, but it is another central bank that stops buying assets and thus may have some impact on sentiment.** Markets will closely look to the revision of growth and inflation projections. If there would be a surprise, it could also affect sentiment on the other European bond markets. **ECB Draghi, Praet and Coeuré will speak today.** We suspect that after the strong eco data, the unexpected sharp rise of headline inflation and criticism of various governors, **the Executive board might feel the need to confirm that their APP programme remains on track. They will point to subdued core inflation. In the past, when headline inflation was too high and core within the objective, the ECB often raised rates arguing that headline inflation influences with a time lag core inflation. Of course, those were different times...**



T-Note future (black) and S&P future (orange) (intraday): Initial decline on strong US data, but dovish Fed brought salvation



German 2-to-10-yr yield spread reaches 2.5 year high as ECB keeps short end in check and better eco data/inflation push longer end up.

R2	164,90	-1d
R1	164,45	
BUND	161,89	0,05
S1	160,72	
S2	159,91	

France and Spain supply markets

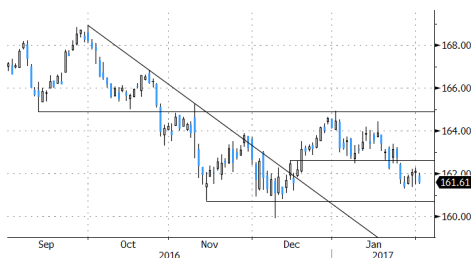
The French treasury taps the on the run 10-yr OAT (0.25% Nov2026) and 15-yr OAT (1.5% May2031) for a combined €6-7B. Both bonds cheapened in the run-up to the auction is ASW-spread terms. The May2031 OAT is rather expensive on the French curve. We think that investors will use the recent politics-related French underperformance to snap up some bonds, suggesting a good auction. **The Spanish Tesoro taps the on the run 3-yr Bono (0.25% Jan2019), 15-yr Obligacion (1.95% Jul2030) and off the run Obligacion (4.2% Jan2037) for €3-4B.** These bonds also cheapened in the run-up to the auction. The Jan2019 & Jan2037 SPGB's look good on the Spanish curve while the Jul2030 Obligacion is expensive. We expect a plain vanilla auction.

Dovish ECB vs neutral/hawkish BoE?

Overnight, most Asian stock markets lose ground with Japan underperforming on the back of a stronger yen. The US Note future ekes out some additional gains following yesterday's rebound on an unchanged Fed decision (see above). We expect the Bund to open higher as well.

Today's EMU/US eco calendar is uninspiring with only EMU PPI data and US weekly jobless claims. **Central bank speeches (ECB Draghi, Praet, Coeuré) are wildcards for trading.** We expect them to downplay the surge in headline inflation (1.8% Y/Y) because of subdued underlying price pressure (0.9% Y/Y). **The BoE's policy decision could also impact Bunds and US Treasuries via the UK Gilt markets** as the BoE probably hit the end of its monetary easing cycle (see FX). The new inflation report might point to higher future inflation, suggesting that the BoE will eventually need to follow in the Fed's footsteps more rapidly than expected. **So in balance: core bonds could be caught between dovish ECB talk and neutral/hawkish BoE talk. In that case, and with recent German critic on the ECB's policy in mind, we think that markets will be more sensitive to the BoE's message.**

From a technical point of view, the Bund's break below the neckline of a double top (162.62) is negative. We expect the Bund to go for a test of the bottom/cycle low. The US Note future trades in the 122-14+ - 125-09 sideways range. We expect also a move towards the lower bound of the range. We hold our negative views on both German Bund and US Note future on the back of accelerating growth and inflation. US investors still have to adapt to the Fed's 2017 rate hike scenario (3 hikes) while European investors might face another "recalibration" of the ECB's APP-programme in H2 2017.



German Bund: break below neckline double top paves way to range bottom?



US Note future: 125-09 resistance 'unbreakable'. Heading towards December low?

Currencies

Dollar in the defensive as Fed stays muted

Dollar rebounded on strong US data

However, gains were reversed after release Fed statement

On Wednesday, risk sentiment improved. Initially, dollar gains remained very limited. A very strong ADP report and a solid US manufacturing ISM propelled the dollar, even as investors remained cautious ahead of the FOMC meeting. The Fed policy statement didn't give any hint on the timing of a next rate hike. Investors expected something more sending USD bond yields a few basis points lower. The dollar lost most of its intraday gains. USD/JPY closed the session at 113.25. EUR/USD finished the day at 1.0769.

Overnight, Asian equities open mixed, but are drifting well into negative territory. **The dollar remains in the defensive in the wake of yesterday's dull Fed statement.** This is often a positive for Asian equities (ex-Japan), but not today. USD/JPY declines and is changing hands in the 112.65 area. So, the correction low (112.08) is on the radar. EUR/USD is returning to the 1.08 barrier.

Today, there are no key eco releases. US. So the focus for USD trading will be **on global issues**. Investors will also look forward to tomorrow's US payrolls. There is no direct link between the **BoE policy decision** and the timing of any further steps of the Fed. However, the BoE completing its asset purchases and raising its growth forecasts might be another sign that global monetary conditions are gradually turning to tighter. If so, there might be some positive spill-over effects on the dollar. **On the other hand, the Fed clearly doesn't want to anticipate on the expected pro-growth policy of the Trump administration.** This is a **short-term dollar negative**. At the same time, the risk momentum is apparently again turning risk-off today, as investors are growing nervous on the unconventional policy style and the protectionist approach of the Trump administration. **So, Trump-driven uncertainty might weigh on the USD.** However, **the losses of the dollar might remain limited ahead of tomorrow's US payrolls.** Yesterday's price reaction showed that, despite rising global uncertainty, the dollar is still sensitive to strong US eco data. So, a break of the EUR/USD 1.0874 is unlikely today.

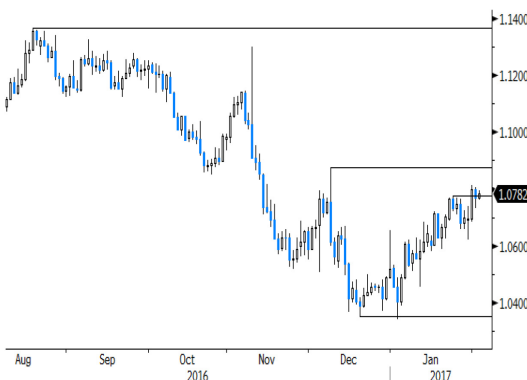
The dollar stays in the defensive in Asian trading

Thin eco calendar today

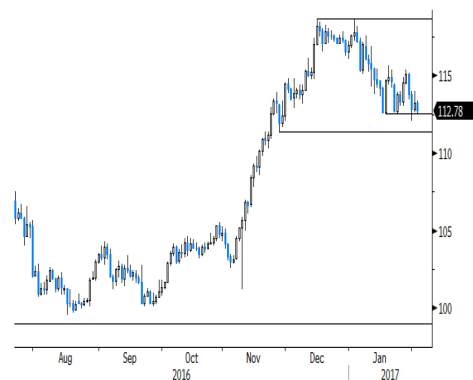
Cautious Fed statement might remain a slight dollar negative

USD traders look forward to tomorrow's payrolls

R2	1,1145	-1d
R1	1,0874	
EUR/USD	1,0783	0,0004
S1	1,0341	
S2	1,0000	



EUR/USD dollar remains in the defensive as Fed remains cautious on further rate hike



USD/JPY is again nearing the bottom of the recent trading range on US currency rhetoric

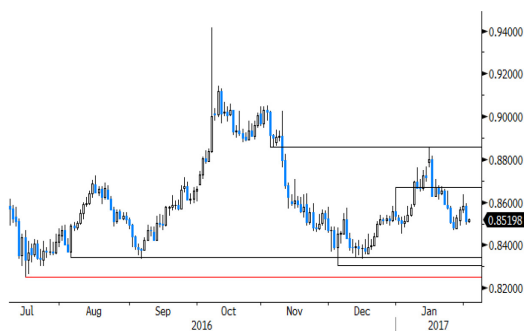
Global context. Of late, the USD rally due to the Trump reflation trade petered out. Even more, **the Trump politics/communication is becoming a sources of global uncertainty that weighs on the dollar.** EUR/USD cleared a next minor resistance at 1.0775. Next resistance is coming in at 1.0874. The day-to-day USD momentum has become more fragile. A return above EUR/USD 1.0874 would question the short-term USD positive outlook. **At some point, the absolute interest rate support should provide a USD floor, but we are not in a hurry to play this card.** We wait for technical signals that the USD correction has run its course. **Tomorrow's payrolls, if strong, might provide such a signal.** USD/JPY is trading well off the post-Trump highs (118.60/66). The rebound off the lows (112.08) isn't convincing. USD/JPY 111.16 (38% retracement of the 99.02/118.66 rally) is the next key support.

BoE to support sterling?

Yesterday, **the UK currency found its composure after a setback on Tuesday.** The UK January manufacturing PMI printed in line with expectations at 55.9, but prices rose sharply, questioning the appropriateness of an ongoing ultra-easy BoE policy. **EUR/GBP started a gradual but protracted intraday downtrend. The positive risk sentiment also supported sterling, in particular against the euro.** Investors were also looking forward to today's BoE policy meeting. EUR/GBP closed the session at 0.8509. Cable also profited from a softer dollar post-Fed and finished the session at 1.2659, testing the recent highs.

Today, the focus for sterling trading will be on the BoE's policy decision. The BoE will probably acknowledge the resilience of the UK economy post Brexit and raise its growth forecasts. The inflation forecast will probably be little changed. The BoE already expected an overshoot of the target due to the decline of sterling. Until now, the BoE maintained a relatively soft policy bias related to the uncertainty/potential negative impact of the Brexit-process. We expect that this will remain the case. The BoE is also expected to finish its bond buying plan this month, as planned. Carney probably will try to avoid further market rate hike speculation. **However, individual members might stress upside risks. We expect a balanced approach, but the market/sterling is probably more sensitive to positive signals/deviations rather than to warnings of downside risks. In this context, a retest of the 0.8450 support is possible.**

R2	0,9047	-1d
R1	0,8881	
EUR/GBP	0,8514	-0,0071
S1	0,8450	
S2	0,8304	



EUR/GBP: 0.8450 support still within reach going into the BoE policy decision"



GBP/USD holds strong on USD weakness

Calendar

Thursday, 2 February		Consensus	Previous
US			
14:30	Nonfarm Productivity (4Q P)	1%	3.1%
14:30	Unit Labor Costs (4Q P)	1.9%	0.7%
14:30	Initial Jobless Claims	250K	259k
14:30	Continuing Claims	2063K--	2100k
Japan			
06:00	Consumer Confidence Index (Jan)	A 43.2--	43.1
UK			
10:30	Markit/CIPS UK Construction PMI (Jan)	53.8	54.2
13:00	Bank of England Bank Rate	0.250%	0.250%
13:00	BOE Asset Purchase Target (Feb)	435b	435b
13:00	BOE Corporate Bond Target (Feb)	10b	10b
EMU			
11:00	PPI MoM / YoY (Dec)	0.5%/1.2%	0.3%/0.1%
Norway			
10:00	Unemployment rate (Jan)	3.2%	2.8%
Events			
	Chinese markets closed for Lunar New Year		
Q4 earnings	Royal Dutch Shell (08:00), Merck (12:45), Amazon (22:01), Deutsche Bank, ...		
10:00	ECB Publishes Economic Bulletin		
10:30	Spain to Sell Bonds		
10:50	France to Sell Bonds		
13:00	Bank of England Inflation Report & Press Conference Carney (13:30)		
13:15	ECB Draghi speaks in Ljubljana)		
18:00	ECB Praet speaks in Berlin		
13:15	ECB Coeure participate in Paris debate		

10-year	td	-1d		2-year	td	-1d		Stocks	td	-1d
US	2,46	-0,01		US	1,21	-0,01		DOW	19890,94	26,85
DE	0,47	0,03		DE	-0,71	-0,02		NASDAQ	5642,65	27,86
BE	1,01	0,02		BE	-0,45	0,00		NIKKEI	18914,58	-233,50
UK	1,45	0,03		UK	0,14	0,01		DAX	11659,5	124,19
JP	0,11	0,02		JP	-0,21	0,01		DJ euro-50	3258,92	28,24
IRS	EUR	USD	GBP	EUR	-1d	-2d		USD	td	-1d
3y	-0,04	1,71	0,84	Eonia	-0,3470	-0,0020		Libor-1	0,7794	-0,0006
5y	0,20	2,00	1,07	Euribor-1	-0,3720	0,0000		Libor-3	1,0346	0,0006
10y	0,82	2,38	1,48	Euribor-3	-0,3280	-0,0010		Libor-6	1,3474	-0,0092
				Euribor-6	-0,2440	-0,0010				
Currencies	td	-1d		Currencies	td	-1d		Commodities	td	-1d
EUR/USD	1,0783	0,0004		EUR/JPY	121,6	-0,53		CRB	194,34	2,30
USD/JPY	112,76	-0,54		EUR/GBP	0,8514	-0,0071		Gold	1216,10	7,20
GBP/USD	1,2666	0,0109		EUR/CHF	1,0692	0,0008		Brent	56,54	1,10
AUD/USD	0,7636	0,0066		EUR/SEK	9,4182	-0,0284				
USD/CAD	1,3019	-0,0071		EUR/NOK	8,858	-0,0495				

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