Sunrise

Wednesday, 27 July 2016

Rates: FOMC to jolt markets awake?

Uneventful trading yesterday, but the FOMC has the opportunity to give markets something to chew on. They might be more optimistic on growth and less worried about the impact of Brexit. Nevertheless, they'll choose to postpone a rate decision to later this year. Risks for markets are asymmetric though, as they are positioned for a rate hike in mid-2017.

Currencies: Fed to support the dollar?

Today, the focus for USD trading is on the FOMC statement. If the Fed acknowledges recent good US eco data and the constructive post-Brexit market reaction, it might be modestly supportive for the dollar. USD/JPY trades volatile as markets are still uncertain on the BOJ's contribution to the fiscal stimulus package.

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 equity markets ended unchanged, as better than expected eco data failed to boost sentiment. Overnight,** Asian shares trade mixed. Japan outperforms as Abe announced plans more than 28 trillion yen in economic stimulus. China underperforms on regulatory concerns.
- **Japan is considering issuing 50-yr bonds for the 1st time**, the longest maturity of Japanese government debt in the postwar era, to take advantage of the ultralow rates resulting from the BoJ's monetary easing, sources told the WSJ.
- **Apple assured investors that demand for the iPhone was getting stronger** and the worst of the decline in sales of its flagship device was behind it, as it reported third-quarter results just ahead of Wall Street expectations.
- **Industrial profit growth in China accelerated last month to 5.1% Y/Y** with the statistics bureau citing better returns on invested capital and a fall in financial fees, less downward pressure on prices from stocks and finished goods and a moderate decline in the industrial debt ratio.
- **Hillary Clinton became the first female presidential nominee of any major party**, a historic milestone that sets the stage for a battle to prove to voters that she is someone they can trust in the White House.
- **Italy was last night racing to secure a privately backed bailout of Monte dei Paschi di Siena**, the most exposed of Italy's troubled lenders, including a plan to raise €5B of further capital to avert nationalisation, according to bankers and EU officials.
- **Today's eco calendar contains EMU M3 money data, UK Q2 GDP data and US Durable goods orders, but all attention will go to tonight's FOMC meeting.** Germany and the US tap the market.

Rates

Summer trading session yesterday

Sideways bond trading dominated

US eco data unable to give direction

Yesterday, global core bonds had an uneventful trading session amid a thin eco calendar and ahead of today's FOMC decision. Traded volumes remained low. US eco data included weaker than expected US Markit services PMI which nears the 50 boom/bust level. **US Consumer confidence, Richmond Fed manufacturing and New Home sales** were all better than expected. The impact on US Treasuries was small and temporary. The US $34B 5-yr Note auction was very bad (see below), but the "negative" reaction rapidly reversed. Oil prices drifted initially towards the $44/barrel area, before rebounding in US dealings and closing unchanged. US equities traded up and down in narrow range to close virtually unchanged. **In a daily perspective,** the US yield curve barely changed with yields flat (2-yr) to 1.2 bps lower (10-yr), while the German yield curve shifted 0.3 (2-yr) to 1.4 bps (10-yr) higher. On intra-EMU bond markets, 10-yr yield spreads chances versus Germany narrowed up to 2 bps.

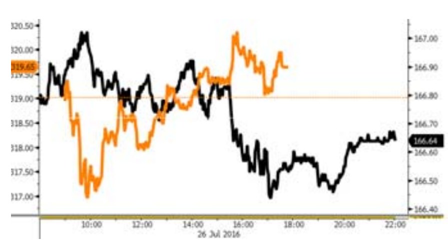
	US yield	-1d
2	0,7539	-0,0040
5	1,1556	0,0323
10	1,5662	0,0120
30	2,2879	0,0190

	DE yield	-1d
2	-0,6050	0,0050
5	-0,4870	-0,0010
10	-0,0310	0,0090
30	0,4699	0,0076

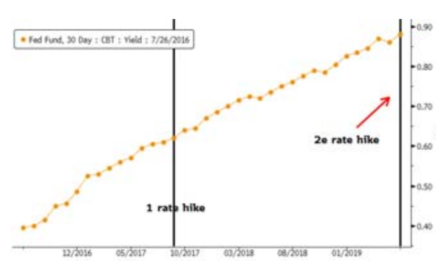
Calendar remains thin, but FOMC meeting key

The **June EMU M3 money supply** figures are expected to be little changed (5% Y/Y) from June (4.9% Y/Y). The **UK Q2 GDP** is expected to be fairly good at 0.5% Q/Q and 2.1% Y/Y, slightly up from Q1. Given the Brexit at the end of June, we expect markets to react subdued to eventually upward surprises. In the US, **June durable orders and pending home sales will be ignored**. Regarding the **FOMC**, markets see a 10% chance on a rate hike today and respectively a 28% and 49% chance for a move in September and December. The June FOMC median rate projections still showed 2 rate hikes in 2016, but 6 governors indicated they expect only one. Since the June meeting, **economic data surprised on the positive side** with Q2 GDP growth estimated at 2.6% (consensus). Our Nowcast model sees growth slightly above 3%. The **June labour market report** was strong, following 2 weaker reports, which were one of the reasons why the Fed stood put at the June meeting. Retail sales were strong too. The other Fed concern, Brexit, did happen, but its negative effects on markets (outside the UK) have been reversed since, making financial conditions looser than before. The recent inflation data certainly don't show that the Fed is already behind the curve. **Therefore, the markets and we think the Fed will keep its wait and see stance.** In September, they will have more info including new eco and rate projections and Yellen will give a press conference. So, today's statement should be a bit more positive on activity, but still mention the too low inflation (expectations) and the geopolitical risks. **With the door open for eventual rate hike in September, there might be some asymmetrical risk/reward opportunities (see lower).**

Fed more optimistic on economy and more hawkish than markets expect?



Bund future (black) & EuroStoxx (orange)(intraday): Sideways trading dominates in narrow range



Fed Fund strip curve: Markets fully discount rate hike in July 2017 and a second one by the end of 2019

Wednesday, 27 July 2016

R2	170	-1d
R1	168,86	
BUND	**166,64**	-0,1600
S1	165,61	
S2	163,61	

Ugly 5-yr Note auction: fear of the Fed?

The US Treasury continued its end-of-month refinancing operation with an ugly $34B 5-yr Note auction. The auction stopped notably above the 1:00 PM bid side and it had the smallest bid cover (2.27) in seven years. Bidding details were also disappointing with especially weak indirect demand. The auction comes on the heels of a very lousy 2-yr Note auction yesterday and suggests that investors fear a hawkish Fed tonight. Tonight, the US Treasury continues its refinancing operation with a **$15B 2-yr Floating Rate Note auction.**

The German Finanzagentur taps the on the run 30-yr Bund (€1B 2.5% Aug2046). The Bund cheapened marginally in ASW spread terms going into the auction. Total bids averaged €1.24B at this year's previous 4 Bund auctions, suggesting that the Finanzagentur will this time reach the (low) auction threshold. However, the auction yield is set to become the lowest ever (<0.5%) and markets are thinning. Therefore, we have low expectations for this auction.

Today: US Treasuries vulnerable for hawkish Fed

Overnight, Asian stock markets trade mixed with Japan outperforming on stimulus hopes (>28T yen according to Kyodo) and China underperforming amid concern that regulators are moving to limit equity investments by some wealth-management products. The US Note future trades slightly lower, but we expect a neutral opening for the Bund.

Today's eco calendar contains EMU M3 money data and US durables, but they will be dwarfed by tonight's **FOMC meeting.** After the British EU-referendum, rate markets completely priced out Fed rate hike expectations even if markets till now relatively easy dealt with this political blow. Additionally, US eco data printed at decent levels. Therefore, we think that the Fed could be more optimistic on the economy while hinting at a rate hike later this year. **Given current market pricing, this could trigger some repositioning lower in US Treasuries, with the front end of the curve underperforming and (limited) spill-over effects to Europe tomorrow.**

The **technical picture** of the US Note future became more neutral following the decline below first support (132-14). Next support stands at 131-07+. The Bund closed in on similar support at 165.68, but the test failed.

German Bund: failed test of first support at 165.68.

US Note future: below first support (132-14, neckline double top). Headling to 131-07+ after Fed?

Currencies

Will USD receive support from Fed-statement?

EUR/USD holding near 1.10 ahead of the Fed

USD/JPY drops on stimulus uncertainty

On Tuesday, currency trading developed in calm summer holiday conditions. The yen rebounded in Asia as markets questioned Japanese authorities' readiness to add aggressive stimulus. However, the move petered out soon. USD/JPY settled in the lower half of the 104 big figure. The dollar gained slightly ground after the publication of the US mid-morning eco figures. EUR/USD closed at 1.0986 (from 1.0995). USD./JPY finished the day at 104.66 (from 105.81).

Yen declines in volatile trade as Japanese government signals JPY 28 trillion of fiscal stimulus

EUR/USD still paralyzed near 1.10

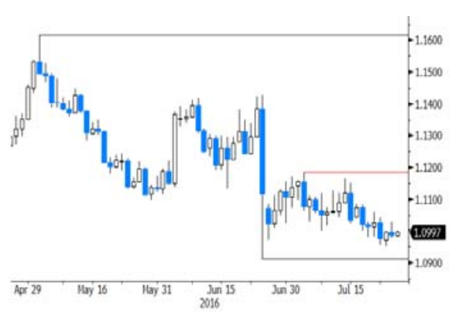
This morning, Asian equities show again a diffuse picture. Most regional indices trade mixed, even as US equity futures show decent gains after the results of Apple published after-closure. Chinese equities show losses of more than 2%. Industrial profits (+5.1% Y/Y) were ok, but equities decline on a report that wealth managers might face stricter rules to invest in equities. Japanese markets gain more than 1% in volatile trading. USD/JPY jumped north of 106 on speculation (report) that Japanese PM Abe would announce a fiscal stimulus package. USD/JPY jumps up and down in the 105 big figure as Abe is now quoted that the stimulus will be more than JPY 28 trillion. However, the details of the plan and its financing are not available yet. EUR/USD is again little affected by the global market developments. The pair holds very close to 1.10.

R2	**1,1428**	-1d
R1	1,1189	
EUR/USD	**1,09965**	-0,0014
S1	1,0913	
S2	1,0822	

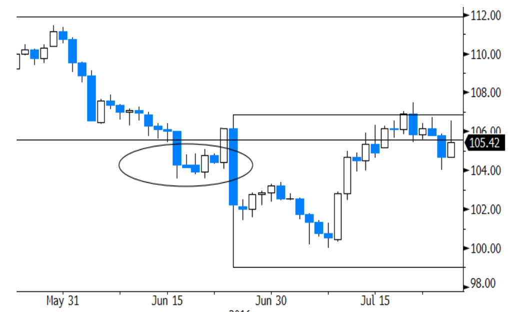
Focus will be on the FOMC statement

The dollar might gain ground if the Fed becomes more positive on economy

Today, the US durable orders and pending home sales will be released. Durable orders are again expected soft. **However, the impact of the report will be very limited as investors await the FOMC statement.** At the previous meeting, a Fed rate hike was put on hold 'sine die' after disappointing payrolls and as the Fed was afraid of Brexit uncertainty and market volatility. **Will the Fed will amend its assessment after better US eco data? The uncertainty on Brexit isn't over yet, but the constructive market reaction caused a de facto loosening of monetary conditions**. We don't expect the Fed to make a U-turn preparing markets for a rate hike in the near future. However, markets are currently positioned for a very soft Fed. If the Fed elaborates on the recent positive developments, US bond yields and the dollar might go moderately higher. **So, we keep a positive intraday bias on the dollar going into the Fed meeting. This applies in the first place to USD/EUR, but we expect the key support at EUR/USD 1.0913 to hold. USD/JPY traders will continue to look out to what extent the fiscal stimulus will be matched a further easing of the BOJ.**



EUR/USD: holding near 1.10 ahead of the Fed decision ?



Of late, the global risk-on and decent US eco data (payrolls, retail sales) had only a limited impact on EUR/USD. The pair traded with a slightly negative bias, but held within the 1.1189/1.0913 post-Brexit range. For now, there is no trigger to break this pattern. In case of ongoing good US data, the Fed might come again in the picture. **After Brexit, we assumed that EUR/USD entered a sell-on-upticks market. We hold on to that view. The post-Brexit intraday top (1.1189) is a first resistance. First support comes in at 1.0913 (June 24 low).** USD/JPY was well bid recently on the hope for more fiscal stimulus and ongoing easy monetary conditions in Japan. The pair broke the 106.84 resistance on speculation of "Helicopter Money". The move was aborted as BOJ Kuroda dismissed the idea. The debate is ongoing (also this morning). **The prospect of more stimulus is yen negative. However, the 107.49 correction top is a strong resistance that may hold unless the BOJ eases really aggressive (on Friday).**

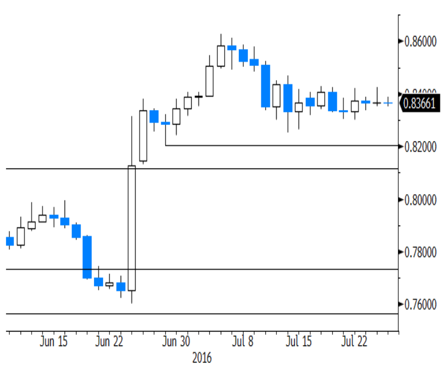
Sterling little changed despite soft BoE comments

R2	0,8627	-1d
R1	0,847	
EUR/GBP	**0,8371**	-0,0024
S1	0,8251	
S2	0,8206	

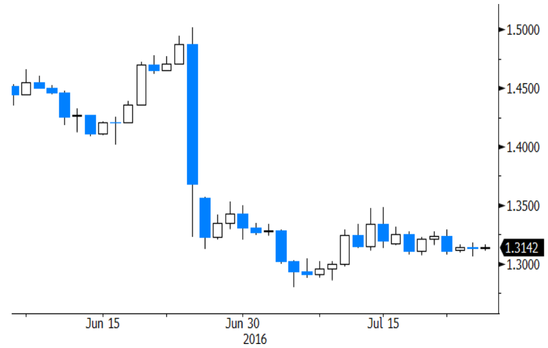
On Tuesday, sterling was initially under pressure as BoE's hawk Weale left its reluctance on further monetary easing based on soft PMI's. EUR/GBP rose to the 0.8425 area early in European dealings. Cable filled **bids** in the 1.3060 area. **However, sterling recouped a big part of the initial losses later in the session.** Markets are apparently not yet convinced on the magnitude and the nature of potential BoE easing at next week's meeting. EUR/GBP closed the session unchanged at 0.8367. Cable finished the day at 1.3130 (from 1.3140).

Today, the first estimate of the UK Q2 GDP and the CBI distributive trades will be published. UK Q2 growth is expected at a decent 0.5% Q/Q and 2.1% Y/Y. Consumer spending is expected to have been strong, but only the details of the supply side will be published. A good figure might be mildly positive for sterling but we expect any reaction to be modest as this report applies to the pre-Brexit era. In this respect, the **July CBI reported sales might be more interesting even as the market reaction to this release is mostly limited.** A modest decline is expected. A negative surprise is negative for sterling, but sterling held up reasonably well of late. Currency markets don't feel inclined to trigger a clear directional move ahead of next week's BoE meeting.

Longer term picture. Over the previous two weeks, sterling initially held strong as the BoE left its policy unchanged, even as the BoE indicated that stimulus was likely at the August meeting. This prospect should cap further sterling gains. We consider the post BoE highs of sterling against the euro (EUR/GBP 0.8250) and against the dollar (Cable 1.3480 area) as strong resistances. We prefer to sell sterling on upticks.



EUR/GBP: holding at tight range, awaiting a clear signal from the BoE



GBP/USD ST consolidation persists

Calendar

Wednesday, 27 July		Consensus	Previous
US			
13:00	MBA Mortgage Applications	--	-1.3%
14:30	Durable Goods Orders (Jun P)	-1.1%	-2.3%
14:30	Durables Ex Transportation (Jun P)	0.3%	-0.3%
16:00	Pending Home Sales MoM YoY (Jun)	1.2% / 3.0%	-3.7% / 2.4%
20:00	FOMC Rate Decision (Lower/Upper Bound)	0.25%-0.50%	0.25%-0.50%
Japan			
07:00	Small Business Confidence (Jul)	A: 47.8	46.5
China			
03:30	Industrial Profits YoY (Jun)	A: 5.1%	3.7%
UK			
10:30	GDP QoQ YoY (2Q A)	0.5% / 2.1%	0.4% / 2.0%
12:00	CBI Distributive Trades Report - Reported Sales (Jul)	--	14
EMU			
10:00	M3 Money Supply YoY (Jun)	5.0%	4.9%
Germany			
08:00	GfK Consumer Confidence (Aug)	9.9	10.1
France			
08:45	Consumer Confidence (Jul)	96	97
08:45	PPI MoM YoY (Jun)	--	0.3% / -3.5%
Italy			
10:00	Consumer Confidence Index (Jul)	109.2	110.2
10:00	Manufacturing Confidence (Jul)	102.0	102.8
10:00	Economic Sentiment (Jul)	--	101.2
Spain			
09:00	Retail Sales SA YoY (Jun)	3.6%	2.3%
Sweden			
09:00	Consumer Confidence (Jul)	98.0	98.7
09:00	Manufacturing Confidence s.a. (Jul)	104.4	104.8
09:00	Economic Tendency Survey (Jul)	102.9	103.2
09:30	Trade Balance (Jun)	--	-2.1b
09:30	Household Lending YoY (Jun)	--	7.8%
Events			
	BASF (07:00), Bayer (07:30), Banco Santander (bef mkt), Deutsche Bank, Peugeot, Fiat-Chrysler, Coca Cola (bef mkt), Boeing (13:30), Facebook (22:00)Announce Q2 Earnings		
Germany	Bund Action (€1B 2.5% Aug2046)		
US	2Yr FRN Auction ($15B)		

10-year	td	- 1d	2 -year	td	- 1d	STOCKS		- 1d
US	1,57	0,01	US	0,75	0,00	DOW	18474	18473,75
DE	-0,03	0,01	DE	-0,61	0,01	NASDAQ	or Exch - NQI	#VALUE!
BE	0,22	0,00	BE	-0,55	-0,01	NIKKEI	16682	16681,74
UK	0,83	0,02	UK	0,14	0,02	DAX	10247,76	10247,76
JP	-0,29	-0,04	JP	-0,38	-0,03	DJ euro-50	2979	2978,90

							USD	td	-1d
IRS	EUR	USD (3M)	GBP	EUR	-1d	-2d	Eonia EUR	-0,334	0
3y	-0,200	1,027	0,506	Euribor-1	-0,37	0,00	Libor-1 USD	0,46	0,46
5y	-0,119	1,165	0,581	Euribor-3	-0,30	0,00	Libor-3 USD	0,51	0,51
10y	0,340	1,453	0,900	Euribor-6	-0,19	0,00	Libor-6 USD	0,60	0,60

Currencies		- 1d	Currencies		- 1d	Commoditie	CRB	GOLD	BRENT
EUR/USD	1,09965	-0,0014	EUR/JPY	116,05	1,09		181,3104	1317,6	44,77
USD/JPY	105,55	1,10	EUR/GBP	0,8371	-0,0024	- 1d	-1,59	-1,36	-0,13
GBP/USD	1,313	0,0017	EUR/CHF	1,0903	0,0057				
AUD/USD	0,7480	-0,0044	EUR/SEK	9,5101	0,02				
USD/CAD	1,3181	-0,0006	EUR/NOK	9,4180	-0,01				

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