



Sunrise

Tuesday, 23 May 2017

Rates: More range-trading?

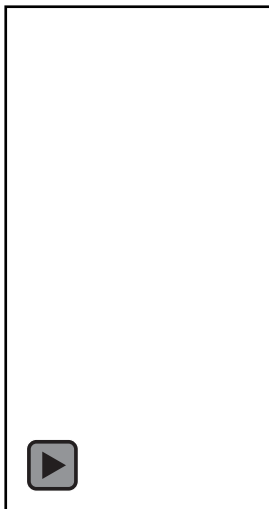
After yesterday's data-poor session, data are plentiful today. In addition, several central bankers will speak. The Manchester attack might help core bonds to a good start. Data are expected to be narrowly mixed, while Fed speakers probably won't reveal much new info. That makes us think that range-trading may continue, but today maybe with upward bias.

Currencies: Euro extends rebound. Dollar still fighting an uphill battle

Yesterday, euro strength dominated. This morning sentiment on risk turns slightly less positive. Uncertainty on Trump and investor caution slow the risk-on trade, but doesn't help the dollar. The eco data might be mixed for USD trading. The dollar correction has been substantial, but for now there is no trigger for a ST reversal.

Calendar

Headlines



- **Wall Street is getting its swagger back.** The S&P, up 0.6% yesterday, is close to its pre-selloff levels as investors shrugged off ongoing political controversies in Washington to focus on the bounce-back in oil and on the arms and investment deals struck between the US and Gulf states over the weekend. **Asian equities trade mixed overnight.**
- **Manchester Police said they were treating the explosion that rocked Arena as a terrorist incident** until proved otherwise. Market reaction was minimal with US Treasuries marginally up and sterling slightly lower.
- **Oil prices were pulling back in Asia after almost a fortnight of solid gains.** Prices were buoyed last week after Russia and Saudi Arabia announced they planned to push for the extension of production cuts.
- **Japanese manufacturing growth slipped to a six-month low in May** as output and job creation fell to multi-month lows. The headline PMI reading dipped to 52 from 52.7 in April, but remained above the 50-point threshold.
- **Greece's creditors failed to reach a deal on debt relief** during seven hours of talks on Monday, leaving the eurozone locked in a race to finish negotiations before Athens faces crippling debt repayments in July. Germany and the IMF clashed over how to ease the debt burden after 2018.
- **MSCI will on June 20 announce whether it would include China's domestic A-shares in its global indices.** The US index provider already delayed for three straight years the A-shares' inclusion into its benchmark \$1.5tn EM stock index.

Rates

Modest downward pressure on bonds continues

In a thinly traded, data-poor Monday session, German bonds came under modest selling pressure mid-morning, which accelerated around noon. The Merkel saying that the euro was too cheap bolstered the single currency, but at the same time triggered more Bund selling. There was also lots of talk of Weidmann replacing Draghi as ECB chief.... in October 2019 when Draghi's term ends, but that looks to be loose talk without much immediate effect. **US Treasuries fell slightly in the overnight session to stabilize further out, with a small steepening bias.** European equities traded mixed (stronger euro?) with Italy underperforming. US equities did again very well, while oil was slightly up around \$54/barrel. It all had only a small impact in a still thinly traded market. **Therefore, we shouldn't draw too many conclusions from Yesterday's price action. In a daily perspective,** US yields rose a small 1.2 bps (2-yr) to 1.9 bps (10-yr). The German yields rose 0.7 to 3.1 bps, steepening the curve a tad.

PMI business sentiment in focus

Attention will focus on **US & EMU PMI business sentiment.** EMU PMI business sentiment is expected to be marginally lower (in fact to stabilize) in May at 56.7 from 56.8 in April. This is a high level, suggesting healthy growth. **We wouldn't be surprised to see a somewhat bigger decline, that would nevertheless still point to strong activity.** We acknowledge that the ZEW and the Sentix sentiment surveys improved in April, but they measure investors' sentiment and are strongly linked to the equity markets. Last month's forward looking PMI orders sub-indices were lower for a number of big countries, which points to a decline of the headline index in France and Italy this month. It doesn't concern Germany. Therefore, we see the **German IFO go higher again. US service and manufacturing PMI business sentiment** declined since the peak in January at 55.6 and 55 respectively. Service sentiment went up slightly last month. We see a modest rebound in both indices.

The **Richmond Fed manufacturing index** is expected at a still healthy 15 in April from 20 in March, which was close to the cycle highs. We have no strong view on the outcome as two pointers for the Richmond survey differed sharply. The NY Fed survey was surprisingly weak, but the Philly Fed survey surprised on the strong side. **US new home sales** rose strongly in past months and are a whisker away from cycle highs. After two strong increases, some modest decline wouldn't surprise, but no reason to worry.



Calm sentiment driver session....

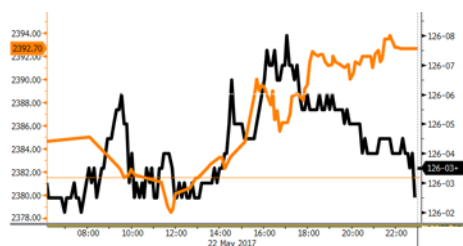
Small losses for core bonds as Merkel, equities and upcoming supply played some role

Spain underperforms peers as new socialist leader may threaten minority government

EMU PMI's to flatten out?

US PMI's to rebound

US New Home sales modestly lower?



T-Note future (black) and S&P future (orange) intraday: Core bonds end slightly lower after trading in a tight range. Equities climb higher and are again approaching the highs.



US-German 10-year yield spread continues to narrow, as investors have doubts on Fed, Trump and core inflation, while fearing ECB exit policy

US and Germany tap the market.



The Belgian government announced a new launch of a syndicated June 2037 OLO (OLO 84). We expect the issue to be priced later today. Germany will launch the **Schatz June 2019** for an amount of €5B. The US Treasury starts its monthly financing operation with a **\$26B 2-yr Note auction**. In the When Issued market, the 2-year is trading at 1.285%.

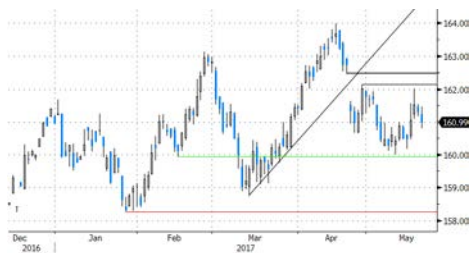
More range trading?

Overnight, the risk sentiment is marginally negative. The Manchester terror attack had only a very modest effect on markets. The Japanese PMI fell slightly lower. Asian equities trade mixed ignoring WS good run yesterday. The T-Note is slightly higher, USD/JPY is down, while oil pulls back following an 8 day rally (\$53.56/barrel). This suggests the Bund may open fairly well.

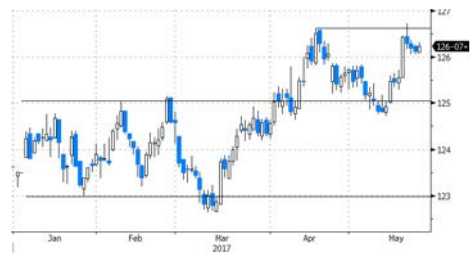
Today's market calendar is busy. The EMU PMI's will remain promising, but a slight weakening from high levels is possible. However, a stronger IFO may offset an eventual disappointment. The US eco data may be on the positive side with stronger PMI's, strong New Home sales, even as it may show a slight erosion. The **Greek deal wasn't concluded** due to ongoing differences between IMF and Germany on debt relief. **This is a positive for core bonds.** The time slot to find an agreement before Greece has to pay about €7B of maturing bonds is becoming tight. We expect Greece to underperform.

Even as the data and fresh supply may on the margin be bond unfriendly, we think that core bonds may do better than in recent days on a softer risk sentiment. However, it is expected to remain essentially a range-trading session. We expect the Bund to stay in a range we define between 160 (recent sell-off low) and 162.15/49 (recent highs/gap) with risks for a test of the downside.

The US Note future tested the contract high (126-20) last week (2.16% support for US 10-yr yield), but a break higher didn't occur. Once the dust settles, we would use those levels to enter new short position, given that we're on the brink of another Fed rate hike and sentiment is again on the mend.



German Bund: Range-trading in 160-to-162.15/49 band, but with downward risks



US Note future: Failed test of 126-20 resistance, suggests some space to decline with first support area at 125/124-23 Time to enter new short positions?

Currencies

Euro jumps to new ST high as Merkel says it is too weak

Dollar extends slide

Overnight risk sentiment eased slightly on new Trump headlines and the Manchester terrorist attack

The business confidence data in the US and Europe might have a limited impact on FX trading

Global sentiment in risk will continue to dominate. Will the USD rout continue?

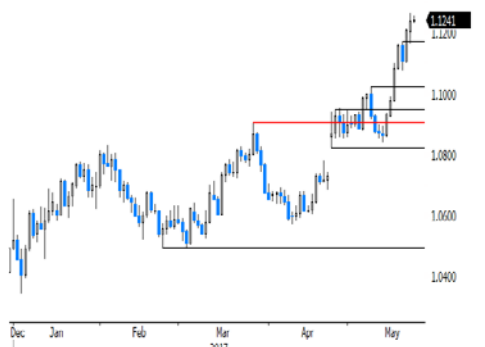


Euro strength and USD softness persist

On Monday, the euro dropped temporarily early in Europe, but the dip was short-lived. **The euro even set new highs after German Chancellor Merkel said that the euro is too weak.** EUR/USD touched a correction top in the 1.1264 area and closed the day at 1.1237. The dollar also continued a mediocre performance against the majors including the yen even as US equities extended the rebound. USD/JPY closed at 111.30.

Overnight, the terrorist attack in Manchester and articles in the Washington Post on Trump trying to influence the communication of the intelligence services on the links of its campaign with Russia, are dominating the headlines of the financial press. However, the impact on the markets is modest. Asian equities are trading mixed. The yen is trading marginally stronger (USD/JPY 111.00). EUR/USD (1.1250 area) is holding near the recent highs even as negotiations on a solution for the Greek debt involving the IMF, broke down.

Today, the eco calendar heats up with the US & EMU PMI business sentiment and Ifo business survey. EMU business sentiment is expected marginally lower in May (56.7). We see slight downside risks for the PMI's. At the same time, the **German IFO might go higher again.** The **US service and manufacturing PMI's** might modestly rebound. **US new home sales** growth might ease after two strong months. **We don't expect today's data to be game changers for euro or USD trading.** The dollar might remain vulnerable to negative surprises. **We also keep an eye on US equities. Will the rally continue or will some Trump uncertainty resurface.** If the equity rebound slows, USD/JPY might drift below the 111 barrier. The impact of the less positive risk sentiment on the euro is a bit ambiguous. A decline in core yields recently weighed more on the dollar than on the euro, but this might change especially if European equities would continue to underperform. So, we look out whether/when the euro rally has run its course. For now, there is no such signal. We keep a close eye on the EUR/JPY performance.



EUR/USD: continues on euro strength and USD weakness



USD/JPY struggles not to lose further ground

At the end of last week, we assumed that an easing of the Trump-crisis could slow the decline of the dollar. **For now, core yields and the dollar hardly profited from the rebound of equities.** The euro (EUR/USD) remains strong going into the June 08

ECB meeting. However, the mediocre performance of USD/JPY also suggests USD softness. **We think that the EUR/USD rebound has gone far enough, but it remains dangerous to row against the EUR/USD rally as long as interest rate differentials move (slightly) in favour of the euro.** Investors are also cautious to be short euro going into the ECB meeting. For now we don't row against the euro positive tight

Technical picture.

The USD/JPY rebound ran into **resistance** two weeks ago. Wednesday's sell-off/re-break below the 112.20 previous top aborted the uptrend and made the short-term picture negative. Return action lower in the 108.13/114.37 range is possible.

Earlier this month, it looked that EUR/USD could revisit the 1.0821/1.0778 support (gap). However, poor US data and political upheaval finally propelled EUR/USD north the 1.1023 range top. **The correction tops at 1.1300/1.1366 is the next resistance. We think that USD sentiment will have to be extremely negative to clear this hurdle short-term. Further ST EUR/USD gains might become tougher. A return below 1.1023 would indicate that the upside momentum has eased.**

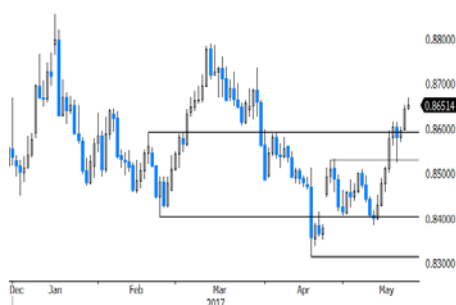
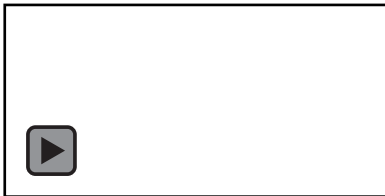
EUR/GBP uptrend continues

Yesterday, **euro strength was also the dominant factor for EUR/GBP trading.** The Merkel comments on a weak euro pushed EUR/GBP further beyond the 0.86 big figure. The pair closed the session at 0.8643. At the same time, sterling also tried to regain ground against an overall weak dollar. The pair returned to the 1.30 area, but Friday's top (1.3040/50 area) just wasn't reached. **Some factors weighed also on sterling .** The lead of the conservative party over labour in the polls for the Parliamentary election is still big, but declining. The EU rubberstamped its Brexit negotiation position and still wants an agreement on the UK financial commitments first. **At least for now, this uncertainty weighs more on the sterling than on the euro**

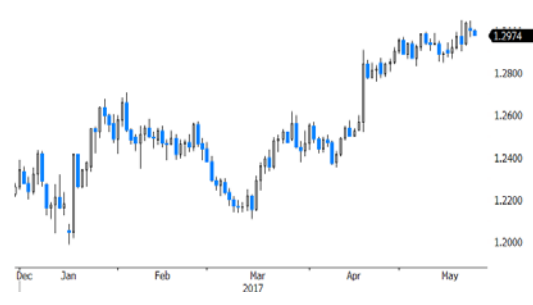
Overnight, the headlines of the Manchester terrorist attack weighed slightly on sterling, but the impact remains modest. Later today, the UK public finance data and the CBI retail sales data will be published. The **CBI data** are interesting, especially as retail activity was under pressure in the first quarter. However, the market reaction is often limited. An easing (10 from 38) after strong April data is expected.

Uncertainty in the wake of the Manchester attack and an easing in retail sentiment might keep a soft sterling sentiment in place.

Of late, the positive sterling sentiment faded and euro strength prevailed in EUR/GBP trading. The pair bottomed out with 0.84/0.8330 as a solid bottom. The breach of 0.8509/31 (previous ST tops) improved the technical picture. For now, we stick to the EUR/GBP uptrend **even as the euro rebound might slow short-term.** Longer term, Brexit remains potentially negative for sterling.



EUR/GBP: euro strength dominates



GBP/USD jumps temporary north of 1.30, but gains prove difficult to sustain

Calendar

Tuesday, 23 May		Consensus	Previous
US			
15:45	Markit US Manufacturing PMI (May P)	53.1	52.8
15:45	Markit US Services PMI (May P)	53.3	53.1
15:45	Markit US Composite PMI (May P)		53.2
16:00	New Home Sales / MoM (Apr)	610k/-1.8%	621k/5.8%
16:00	Richmond Fed Manufact. Index (May)	15	20
Japan			
02:30	Nikkei PMI manufacturing (May)	A 52	52.7
06:30	All Industry Activity Index MoM (Mar)	-0.5%	0.7%
08:00	Nationwide Dept Sales YoY (Apr)	--	-0.9%
UK			
10:30	Public Finances (PSNCR) (Apr)	--	34.3b
12:00	CBI Retailing Reported Sales (May)	--	38
12:00	CBI Total Dist. Reported Sales (May)	--	44
EMU			
10:00	Markit Eurozone Manufacturing PMI (May P)	56.5	56.7
10:00	Markit Eurozone Services PMI (May P)	56.4	56.4
10:00	Markit Eurozone Composite PMI (May P)	56.7	56.8
Germany			
08:00	GDP SA QoQ / WDA YoY (1Q F)	0.6%/1.7%	0.6%/1.7%
09:30	Markit/BME Germany Manufacturing PMI (May P)	58.0	58.2
09:30	Markit Germany Services PMI (May P)	55.5	55.4
09:30	Markit/BME Germany Composite PMI (May P)	56.6	56.7
10:00	IFO Business Climate (May)	113.1	112.9
10:00	IFO Expectations (May)	105.4	105.2
10:00	IFO Current Assessment (May)	121	121.1
France			
08:45	Business Confidence (May)	105	104
08:45	Manufacturing Confidence (May)	108	108
09:00	Markit France Manufacturing PMI (May P)	55.2	55.1
09:00	Markit France Services PMI (May P)	56.7	56.7
09:00	Markit France Composite PMI (May P)	56.6-	56.6
Sweden			
09:30	Unemployment Rate SA (Apr)	6.5%	6.4%
Events			
01:00	Fed's Brainard Speaks on Role of Inclusion in Economy		
03:10	Fed's Evans Speaks in Shanghai at symposium on OTC derivatives (policy management)		
10:30	ECB Coeuré in panel discussion in Paris		
11:30	Germany to Sell €5B 2019 Bonds		
19:00	US to Sell \$26B 2-yr Notes		
21:15	Fed's Kashkari Speaks in Minneapolis (non-policy item) (at 15:00 talk with reporters)		
23:00	Fed's Harker Speaks in New York on economic outlook		

10-year	<u>td</u>	<u>-1d</u>		2-year	<u>td</u>	<u>-1d</u>		Stocks	<u>td</u>	<u>-1d</u>
US	2.23	-0.02		US	1.27	-0.01		DOW	20894.83	89.99
DE	0.38	-0.01		DE	-0.68	0.00		NASDAQ	6133.618	49.92
BE	0.77	0.01		BE	-0.49	0.02		NIKKEI	19613.28	-65.00
UK	1.09	0.00		UK	0.10	-0.01		DAX	12619.46	-19.23
JP	0.05	0.00		JP	-0.16	-0.01		DJ euro-50	3576.53	-10.48
IRS	<u>EUR</u>	<u>USD</u>	<u>GBP</u>	EUR	<u>-1d</u>	<u>-2d</u>		USD	<u>td</u>	<u>-1d</u>
3y	-0.03	1.65	0.63	Eonia	-0.3590	0.0010		Libor-1	1.0171	0.0000
5y	0.20	1.85	0.79	Euribor-1	-0.3740	0.0000		Libor-3	1.1864	0.0000
10y	0.81	2.17	1.16	Euribor-3	-0.3290	0.0020		Libor-6	1.4152	0.0000
				Euribor-6	-0.2510	0.0000				
Currencies	<u>td</u>	<u>-1d</u>		Currencies	<u>td</u>	<u>-1d</u>		Commodities	<u>td</u>	<u>-1d</u>
EUR/USD	1.1231	0.0037		EUR/JPY	124.68	-0.11		CRB	186.07	1.00
USD/JPY	111.02	-0.46		EUR/GBP	0.8649	0.0039		Gold	1262.40	9.10
GBP/USD	1.2985	-0.0017		EUR/CHF	1.0936	0.0025		Brent	53.63	-0.37
AUD/USD	0.7501	0.0057		EUR/SEK	9.7662	-0.0076				
USD/CAD	1.348	-0.0046		EUR/NOK	9.3761	0.0041				

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