Sunrise

Friday, 09 February 2018

Rates: Core bonds hardly profit as US stocks take another dive

Core bonds made an intraday U-turn yesterday as US stock markets suffered another huge blow (-4%), but gains remained rather limited. It confirms underlying bearish sentiment. Spill-over effects to other markets are in general muted. Today's eco calendar is empty, so all eyes will be again on bourses.

Currencies: Dollar struggles to extend gains as global market volatility remains high

Yesterday, EUR/USD tried to extend its decline after Wednesday's break, but the move had no strong momentum. The dollar still has difficulties to play its save have role even as US yields remain elevated. Sterling jumped as the BoE signaled a steeper rate hike path, but the gains could not be sustained. EUR/GBP 0.8690 remains a very solid support.

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	↘

- **A late-afternoon rout sent S&P (-3.75%) to its lowest close since November.** That leaves the S&P 500 benchmark 10% below its Jan. 26 record high. **Volatility roared back with the VIX surging more than 20%.** Asian stock markets lose up to 2.5% with China underperforming (up to -5%).
- **US Congress missed a midnight deadline, failing to fund the government for a second time this year** as a two-year bipartisan budget deal encountered delays in the Senate. A new vote is scheduled later today.
- **A fast-growing mutual fund** has told investors that it will not charge them to redeem what is left of their money, after **losing more than 80% of its value in the wake of this week's turbulence.** It's the biggest one-week drop for a mutual fund recorded in 20 years.
- **China's producer and consumer inflation eased as expected in January.** The PPI rose 4.3% Y/Y in January, the smallest rise in 14 months. CPI rose by 1.5% Y/Y.
- **Australia's central bank** said the economy is some way off full employment and inflation returning to the midpoint of its target, signalling policy will stay on hold.
- **Moody's,** the last of the major credit rating agencies to keep **Portugal's** debt in "junk" territory, **considers it on the verge of regaining investment grade** thanks to the country's economic and fiscal improvements.
- **Today's eco calendar** is thin with only UK industrial production data and UK trade balance.

Rates

Bonds hardly support from hemorrhage in US stocks

US yield		-1d
2	2,10	-0,02
5	2,56	-0,02
10	2,82	-0,01
30	3,14	0,02

DE yield		-1d
2	-0,55	-0,01
5	0,11	0,01
10	0,76	0,02
30	1,39	0,01

Global core bonds traded with a downward bias during yesterday's European trading session. US Congress' bipartisan agreement on a 2-yr funding bill (not approved yet) weighed on core bond sentiment in the first hours of trading. **The sell-off accelerated around noon via the UK Gilt market after an hawkish inflation report by the Bank of England.** Core bonds made U-turn during US dealings as sentiment on US stock markets soured again, eventually resulting in losses to the tune of 4%. **The core bond rebound was disappointing given this slaughter on bourses, underpinning negative underlying bond sentiment.** Changes on the German yield curve ranged between -0.6 bps (2-yr) and +1.7 bps (30-yr). US yields added 0.5 bps (10-yr) to 1 bp (5-yr) on a daily basis. On intra-EMU bond markets, 10-yr yield spread changes versus Germany range between -1 bp and +3 bps. Greece underperformed (+11 bps). **The country launched a new 7-yr syndicated bond yesterday (€3bn 3.375% Feb2025).**

The US Note future stabilizes overnight even if the sell-off persist in Asia (up to -5% for China). The US Senate vote on the 2-y funding bill was delayed to today, resulting in a new partial government shutdown. We expect the bill to pass, but it's a wildcard. We expect a neutral to slightly positive opening for the Bund.

Today's eco calendar is empty. **Risk sentiment on stock markets is the only thing that matters.** The rise in global yields since December last year proved that stock markets aren't untouchable. A correction from record levels was overdue. Volatility surged to levels not seen in the past 5 years and caused liquidations of short vol ETP's which exaggerated the stock market sell-off. **Risk aversion could temporary revive the safe haven argument for core bonds, but for now the spillover effects are very limited. At this stage, any upward correction in bonds could be short-lived.**

Strong growth momentum, rising inflation (expectations) and the global turn towards monetary policy normalization are structurally negative factors for core bonds medium term. US and German yields cleared resistance levels earlier this year and moved at high-speed towards next targets. The trading band for the US 10-yr yield is 2.64%-3.05%. Correction towards the lower bound could be used to put up short positions in the Note future. The German 10-yr yield's trading band is 0.62%-1.06% trading band.

S&P 500: sell-off accelerates

US Note future (intraday, this week): limited rebound yesterday despite huge equity sell-off

Currencies

R2	1,2643	-1d
R1	1,2537	
EUR/USD	1,2247	-0,0017
S1	1,1713	
S2	1,1554	

R2	0,9307	-1d
R1	0,9033	
EUR/GBP	0,8803	-0,0034
S1	0,8690	
S2	0,8657	

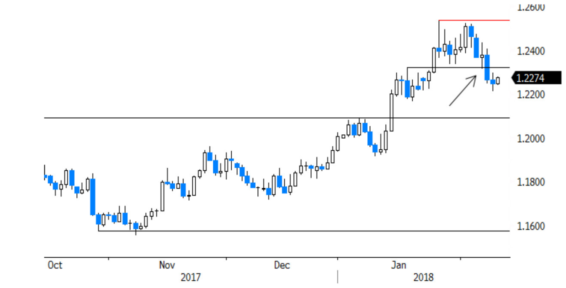
EUR/USD decline slows even as volatility persists

The dollar maintained a positive momentum yesterday morning, but dynamics eased during the day. Some EUR/USD follow-trough selling occurred after the break below 1.2323. EUR/GBP selling after the BoE pushed EUR/USD to an intraday low in the 1.2215 area. From there, the euro decline/USD rally stalled, despite risk aversion. EUR/USD returned higher in the 1.22 big figure and closed the day at 1.2247. The return of volatility finally also triggered yen buying. USD/JPY dropped below 109. EUR/JPY tested 133 support, but a sustained break didn't occur. The moves in the FX majors stay modest given the swings on other markets.

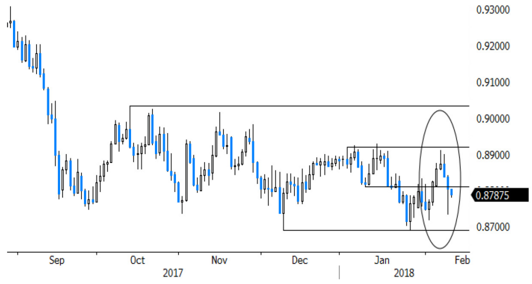
Risk aversion still dominates Asian trading. Regional indices are losing up to 5%. Japan slightly outperforms. USD/JPY dropped temporary to the 108.50 area, but aggressive BOJ bund buying reinforces the Bank's will to maintain an easy policy, slowing the rise of the yen. USD/JPY trades again around 109. EUR/USD is going nowhere in the 1.2250 area. The yuan stabilizes after yesterday's correction against the dollar.

There are no important data in the US and Europe today. So, global factors will continue to dominate FX trading. Of late, the swings in the major USD cross rates were modest given the turmoil on other markets. **The combination of higher core yields and an aggressive risk-off finally turned out USD positive.** That said, **the safe haven appeal of the dollar was far from impressive.** It more looked like some cautious by default USD buying. We assume that this pattern can continue as long as the current global repositioning continues. **Technical picture:** the dollar decline slowed of late and EUR/USD finally dropped below 1.2323/35 support. A break below 1.2165 would call off the ST downside alert (for USD). We continue to monitor the EUR/JPY price action. A further risk-off correction in EUR/JPY might also put downward pressure on EUR/USD. However, in this respect, yesterday's price action was inclusive. The EUR/JPY decline was blocked at the key 133 support area.

Sterling jumped higher as the BoE indicated that rates will probably have to be raised faster than anticipated. Most of the rebound was reversed later as a new wave of risk-off repositioning weighed on sterling. Markets probably also realized that the Brexit-cliff isn't out of the way. EUR/GBP closed the session only marginally lower at 0.8803. UK production and trade balance data will be published today. Yesterday's price action confirmed our working hypothesis that the 0.8690 support probably won't be easy to break without big progress on Brexit.



EUR/USD: few follow-through gains despite Wednesday's break lower.



EUR/GBP: sterling succeeds only modest gains despite the BoE signalling more policy tightening.

Calendar

Friday, 9 February		Consensus	Previous
Canada			
14:30	Net Change in Employment (Jan)	10.0k	64.8k
14:30	Unemployment Rate (Jan)	5.8%	5.8%
Japan			
00:50	Money Stock M3 YoY (Jan)	A: 2.9%	3.1%
China			
02:30	**PPI YoY (Jan)**	**A: 4.3%**	**4.9%**
02:30	CPI YoY (Jan)	A: 1.5%	1.8%
UK			
10:30	**Industrial Production MoM / YoY (Dec)**	**-0.9%/0.3%**	**0.4%/2.5%**
10:30	Manufacturing Production MoM / YoY (Dec)	0.3%/1.2%	0.4%/3.5%
10:30	Construction Output SA MoM / YoY (Dec)	-0.1%/-1.9%	0.4%/0.4%
10:30	Visible Trade Balance GBP/Mn (Dec)	-£11550	-£12231
13:00	NIESR GDP Estimate (Jan)	0.5%	0.6%
France			
08:45	Industrial Production MoM / YoY (Dec)	0.1%/3.5%	-0.5%/2.5%
08:45	Manufacturing Production MoM / YoY (Dec)	-0.5%/3.4%	-1.0%/3.0%
Italy			
10:00	Industrial Production MoM / WDA YoY (Dec)	0.8%/1.9%	0.0%/2.2%
Norway			
08:00	CPI MoM / YoY (Jan)	0.1%/1.6%	0.0%/1.6%
08:00	CPI Underlying MoM / YoY (Jan)	-0.2%/1.5%	0.1%/1.4%
08:00	GDP Mainland QoQ (4Q)	0.6%	0.6%
Events			
03:00	Fed's George Speaks on the Economy		

10-year	Close	-1d		2-year	Close	-1d	Stocks	Close	-1d
US	2,82	-0,01		US	2,10	-0,02	DOW	23860,46	-1032,89
DE	0,76	0,02		DE	-0,55	-0,01	NASDAQ	6777,159	-274,82
BE	1,01	0,01		BE	-0,47	0,00	NIKKEI	21382,62	-508,24
UK	1,62	0,07		UK	0,68	0,05	DAX	12260,29	-330,14
JP	0,07	-0,02		JP	-0,15	0,00	DJ euro-50	3377,3	-77,22
IRS	EUR	USD	GBP	EUR	-1d	-2d	USD	-1d	-2d
3y	0,07	2,48	1,15	Eonia	-0,3630	0,0020			
5y	0,48	2,63	1,38	Euribor-1	-0,3690	0,0000	Libor-1	1,5793	0,0000
10y	1,12	2,84	1,67	Euribor-3	-0,3290	0,0000	Libor-3	1,7999	0,0000
				Euribor-6	-0,2780	0,0000	Libor-6	2,0044	0,0000
Currencies	Close	-1d		Currencies	Close	-1d	Commodities	Close	-1d
EUR/USD	1,2247	-0,0017		EUR/JPY	133,19	-0,90	CRB	191,77	-0,57
USD/JPY	108,74	-0,59		EUR/GBP	0,8803	-0,0034	Gold	1319,00	4,40
GBP/USD	1,3913	0,0032		EUR/CHF	1,1468	-0,0111	Brent	64,81	-0,70
AUD/USD	0,7781	-0,0042		EUR/SEK	9,9419	0,0269			
USD/CAD	1,2603	0,0035		EUR/NOK	9,7077	0,0102			

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