



Sunrise

Wednesday, 07 December 2016

Rates: Uneventful trading ahead of ECB

Today's eco calendar remains uninspiring for core bond trading which means that investors will continue counting down to tomorrow's ECB meeting. We expect sideways trading. The Bund is close to 160.72 support (March contract!), but we don't expect a break ahead of the ECB.

Currencies: Euro short squeeze short-lived?

Yesterday, the euro short squeeze after the Italian referendum petered out. Today the eco calendar is thin. Markets look forward to tomorrow's ECB policy decision. An ongoing constructive risk on sentiment might be slightly USD supportive. Sterling declines even as the government suggests more Parliamentary involvement in the Brexit process.

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 equities** ended up to 0.5% higher in uneventful trading. **Overnight**, Asian stock markets record similar gains with Japan marginally outperforming.
- **Australia's economy shrank for the first time in more than five years** in the third quarter amid steep falls in business investment, housing construction and public spending. AUD/USD declined from 0.7475 to 0.7425.
- **Allies of outgoing Italian PM Renzi have joined opposition calls for fresh elections**, making it more likely that the country will go to the polls next year. However, Italy's President **Mattarella wants parliament to draft a new electoral law before any ballot is held**, a source close to the president said.
- **The British government** has accepted that it **should set out its plans for Brexit** in the face of a nascent rebellion among backbench Tories. MPs will vote today on a Labour motion that calls on Theresa May to set out her plans.
- **Moody's has shifted its outlook for the global asset management industry to negative** as the growth of passive investment strategies continues to threaten fees in the industry. Increased regulation and underwhelming performance compared with cheaper passive investment funds have disrupted the industry.
- **BoJ Deputy Governor Iwata** said the BoJ has **not shifted its focus away from the pace of money printing**, contradicting the governor's view and exposing a rift in the board on how best to break the country's deflation shackles.
- **President-elect Donald Trump laid out a U.S. military policy that would avoid interventions in foreign conflicts** and instead focus heavily on defeating the Islamic State militancy.
- **Today's eco calendar is uneventful** with only UK industrial production data and a German Schatz auction. The Bank of Canada decides on monetary policy.

Rates

Bund underperforms listless US Treasuries

Listless US Treasury trading

German bonds underperform US ones

Investors pick up peripheral bonds and equities as risk sentiment improved

	US yield	-1d
2	1,1241	0,0001
5	1,8423	0,0016
10	2,3924	0,0055
30	3,0772	0,0189

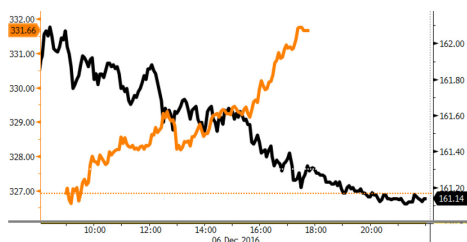
	DE yield	-1d
2	-0,6950	0,0160
5	-0,3420	0,0490
10	0,3770	0,0560
30	1,0462	0,0656

Second tier US eco data

Yesterday, US Treasuries traded listless in the absence of new drivers. Nevertheless, German Bunds underperformed US Treasuries. Two possible but not completely coherent stories might explain the price action. Fears about a tapering or less dovish ECB talk at tomorrow's meeting haunted Bunds. However, renewed interest for peripherals, also in the equity markets, may have in the disadvantage of Bunds as well (European risk-on). Whatever, the Bund future is now near the sell-off lows, the level of two and three days ago. The eco calendar was empty apart from very strong German factory orders and the final revision of Q3 EMU GDP growth (confirmed at 0.3%) which didn't impact trading. **In a daily perspective**, the German yield curve shifted 1.6 bps (2-yr) to 4 bps (10-yr) higher. Changes on the US yield curve varied between -0.6 bps (2-yr) and +1.4 bps (30-yr), with yields up only at the very long end. **On intra-EMU bond markets**, 10-yr yield spreads versus Germany narrowed up to 4 bps in (semi-)core countries with Italy (-8 bps), Portugal (-11 bps) and Spain (-10 bps) outperforming. **As the Italian referendum didn't cause market turmoil, investors used the recent spread widening to buy again into peripheral bonds.** The uncertain fate of BMPS seems no issue.

Nearly empty calendar

The **Euro area calendar** contains only Italian unemployment and Spanish house prices, no market movers. Some more attention may go to the **UK industrial production** data, but these are only for UK markets of some importance. In the US, only the **JOLTS job openings report** and consumer credit are released, but these are also no market movers. The **Canadian central bank** meets, but analysts don't expect a rate change.



Bund future (black) and EuroStoxx (orange) (intraday): Bunds down and equities up with the driver open for discussion



EuroStoxx: still in sideways pattern, but now threatening to breakout on the upside.

R2	163,19	-1d
R1	162,08	
BUND	161,2	-0,8500
S1	159,14	
S2	158,67	

Small German Schatz auction

The German Finanzagentur holds its final Schatz auction of the year by tapping the 0% Dec2018 bond for a relatively small €3B. Total bids averaged €5.66B at the previous 4 Schatz auction, suggesting that the auction will pass smoothly even if the upcoming ECB meeting might keep some investors sidelined. The bond cheapened slightly in ASW spread terms going into the auction.

Counting down to ECB meeting

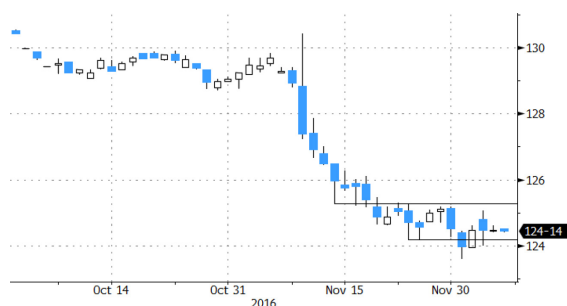
Overnight, most Asian equity markets trade positive, eking out gains of up to 0.5% with Japan slightly outperforming. Brent crude and the US Note future trade stable, suggesting a neutral opening for the Bund.

Today's eco calendar remains uninspiring for core bond trading which means that investors will continue counting down to tomorrow's ECB meeting. We expect sideways trading. Latest press articles suggested that the central bank will be less soft than generally expected. **The Bund is close to 160.72 support (March contract!), but we don't expect a break ahead of the ECB. Oil prices and inflation expectations remain wildcards for intraday trading.**

Technically, the US 2-yr yield broke above 1.1% resistance. The US 5-yr yield tries to break above the 1.85% area, while a first test of 2.5% resistance in the US 10-yr yield failed. The US 30-yr yield remains below a similar 3.25% mark. We wait for specific news (e.g. a hawkish Fed next week) before anticipating a break higher (5yr & 10 yr). We hold our sell-on-upticks approach in US Treasuries.



German Bund: Downtrend remains intact despite adverse Italian referendum outcome. Up next: ECB meeting



US Note future (March contract): sell-on-upticks

Currencies

EUR/USD short squeeze ran into resistance

Some dollar strength returned later in the session

R2	1,0851	-1d
R1	1,0809	
EUR/USD	1,07175	-0,0027
S1	1,0506	
S2	1,0458	

Dollar holds near yesterday's intraday high

Aussie dollar declines on soft Q3 GDP data

Eco calendar is thin today

Currency traders will look out for tomorrow's ECB meeting.

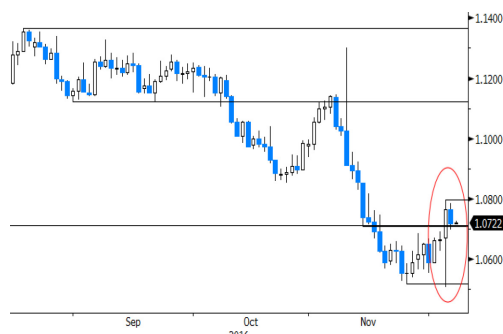
Euro rebound halts as markets await the ECB decision

On Tuesday, global (currency) trading shifted into wait-and-see modus after Monday's impressive euro short squeeze. EUR/USD initially tried to extend its comeback, but failed to take out Monday's top just below 1.08. Data and interest rate differentials failed to give clear guidance. Some cautious dollar strength returned later in the session. EUR/USD closed the day at 1.0718 (from 1.0764 on Monday). USD/JPY finished the session at 114.02 (from 103.85).

Overnight, Asian equities are supported by the yesterday's constructive risk sentiment in Europe and the US. However, the gains are modest. Japanese equities again slightly outperform as the yen stays relatively weak. USD/JPY returned north of the 114 pivot (currently trading near 114.20). The Australian Q3 GDP unexpectedly dropped by -0.5% Q/Q, reducing the Y/Y growth rate to 1.8% (-0.1% Q/Q and 2.2% Y/Y was expected). The RBA expects growth to pick up again in the fourth quarter. Even so, markets see again a higher probability of a rate cut. The Aussie dollar dropped from the 0.7480 area to the 0.7420 area. Core yields show no clear trend overnight. EUR/USD is holding a very tight range in the 1.0720 area.

Later today, the Euro area calendar contains only Italian unemployment and Spanish house prices, no market movers. In the US, only the JOLTS job openings report and consumer credit are released, but these are also no market movers. The Canadian central bank meets, but analysts don't expect a rate change.

Yesterday, **the euro short-squeeze ran into resistance ahead of the EUR/USD 1.08 level and** the euro returned part of Monday's gains. At the same time the dollar holds relatively strong, suggesting that the post-Trump reflation trade puts a solid floor for the US currency. Today, there are few drivers for trading in EUR/USD and USD/JPY. Interest rate differentials and global risk sentiment will have to do the job. **However, US yields are in consolidation modus and European bond investors will probably also take a wait-and-see approach ahead of tomorrow's ECB meeting.** The ongoing positive risk sentiment might be slightly USD supportive, especially for USD/JPY. Basically, we expect more consolidation both for EUR/USD and USD/JPY today.



EUR/USD: short-squeeze stalls ahead of 1.08/1.0809 resistance



USD/JPY tested key resistance just below 115, but test is rejected, for now

From a technical point of view, EUR/USD cleared intermediate support at 1.0851 and 1.0711 (2016 low). The pair set a minor new low below 1.0524/18 support on Monday, but was captured by an impressive short squeeze later. **The 38% retracement from the Trump decline comes in at 1.0809. We look out whether this first important resistance holds going into the ECB meeting.** If the level holds, new EUR/USD shorts can be considered. The technical picture for USD/JPY improved too. The pair took out the key resistance at 111.45/91. Next key resistance at 114.50/115 was tested last week and yesterday, but the test was rejected. **The pair has moved well into overbought territory. The rally might be ripe for a some consolidation/a modest correction.**

R2	0,8708	-1d
R1	0,8578	
EUR/GBP	0,8466	0,0041
S1	0,83	
S2	0,8117	

EUR/GBP stays away from the recent low

On Tuesday, sterling trading also entered calmer waters after Monday's swings in EUR/GBP and **was driven by global price moves**. European politicians again tried to convince the UK not to wait too long to start Brexit negotiations and to give insight in what kind of Brexit the UK government intends to realise. However, the the headlines had no big impact in sterling trading. **EUR/GBP drifted up and down on the various Brexit news items, but finished the session almost unchanged at 0.8453.** Cable was initially captured in a relatively tight sideways range in the mid 1.27 area, but declined later to close the session at 1.2678.

Today, the Halifax House prices, UK production data and the NIESR GDP estimate will be published. UK production data are expected to confirm the scenario of modest growth, but we don't expect it to be of big importance for sterling trading. UK traders will keep an eye at the political debate as the UK government looks prepared to give more insight in its Brexit position ahead of the activation of article 50. **However, the impact of the new approach for the Brexit process is unclear and didn't help sterling yesterday.** Of late sterling mostly profited on headlines of a bigger Parliamentary involvement. Will this change? EUR/GBP extensively tested the 0.8333 support on Monday, but a sustained break didn't occur. The 0.8333/05 area has become an important point of reference. Yesterday's price action was still modestly euro positive/sterling negative and this trend continues morning. **Can this area put a floor under the recent EUR/GBP decline?**



EUR/GBP: tentative signs of a bottoming out process



GBP/USD: running into resistance?

Calendar

Wednesday, 7-Dec		Consensus	Previous
US			
13:00	MBA Mortgage Applications	--	-9.4%
16:00	JOLTS Job Openings (Oct)	5500	5486
21:00	Consumer Credit (Oct)	\$18.3b	\$19.292b
China			
	Foreign reserves Nov	\$3060.7B	\$3120.7B
Canada			
16:00	Bank of Canada Rate Decision	0.50%	0.50%
Japan			
06:00	Leading Index CI (Oct-P)	A-101	100.3
Australia			
01:30	GDP SA QoQ / YoY (3Q)	A-0.5%/1.8%	R0.6%/3.1%
UK			
09:30	Halifax House Prices MoM / 3Mths/Year (Nov)	0.2%/5.9%	1.4%/5.2%
10:30	Industrial Production MoM / YoY (Oct)	0.2%/0.5%	-0.4%/0.3%
10:30	Manufacturing Production MoM / YoY (Oct)	0.2%/0.7%	0.6%/0.2%
16:00	NIESR GDP Estimate (Nov)	0.4%	0.4%
Germany			
08:00	Industrial Production SA MoM / WDA YoY (Oct)	0.8%/1.6%	-1.8%/1.2%
Italy			
10:00	Unemployment Rate Quarterly (3Q)	11.6%	11.5%
Spain			
09:00	INE House Price Index QoQ / YoY (3Q)	--/--	1.8%/3.9%
Norway			
08:00	Industrial Production MoM / WDA YoY (Oct)	--/--	-5.6%/-12.4%
Events			
11:30	Germany to Sell €3B 0% 2018 bonds		

Contacts

10-year	td	-1d	2-year	td	-1d	STOCKS	-1d
US	2,39	0,01	US	1,12	0,00	DOW	19252 19251,78
DE	0,38	0,06	DE	-0,70	0,02		
BE	0,70	0,06	BE	-0,62	-0,01	NIKKEI	18497 18496,69
UK	1,42	0,03	UK	0,12	0,05	DAX	10775,32 10775,32
JP	0,04	-0,01	JP	-0,16	0,00	DJ euro-50	3101 3100,76

						USD	td	-1d
IRS	EUR	USD (3M)	GBP	EUR	-1d	-2d	Eonia EUR	-0,351 -0,004
3y	-0,063	1,534	0,754	Euribor-1	-0,37	0,00	Libor-1 USD	0,26 0,26
5y	0,152	1,827	0,953	Euribor-3	-0,32	0,00	Libor-3 USD	0,38 0,38
10y	0,765	2,226	1,357	Euribor-6	-0,22	0,00	Libor-6 USD	0,54 0,54

Currencies		-1d	Currencies		-1d	Commoditie	CRB	GOLD	BRENT
EUR/USD	1,07175	-0,0027	EUR/JPY	122,48	0,06		192,5257	1168,36	53,76
USD/JPY	114,31	0,33	EUR/GBP	0,8466	0,0041	-1d	-0,95	-2,34	-0,84
GBP/USD	1,2654	-0,0094	EUR/CHF	1,0819	-0,0004				
AUD/USD	0,7436	-0,0012	EUR/SEK	9,7845	-0,03				
USD/CAD	1,3282	0,0007	EUR/NOK	9,0122	0,01				

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