



## Sunrise

Friday, 23 September 2016

### Rates: Ebullient Bund rally on CB decisions

Big day for core bonds yesterday, registering strong gains driving the curve flatter. Today, only the EMU PMI is a main driver with central bank speakers a wildcard. The context is positive for bonds as we see downside risks to PMI's. However, after the recent rally, bonds may be a bit exhausted, making more strong gains today unlikely.

### Currencies: Post-Fed dollar correction already slows

The dollar lost initially ground post-Fed, but the decline already slowed during the US session. The global picture for EUR/USD trading didn't change. USD/JPY remains in the defensive. Today, a soft EMU PMI might be slightly euro negative. Sterling entered calmer waters as the recent decline slows.

### 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 rose for a second straight session yesterday.** The S&P ended up by 0.65%, led by the real estate sector. This morning, **sentiment weakened in Asia** with both Chinese and Japanese equities trading in negative territory.
- **The ECB needs to have a flexible approach to the time needed to reach its inflation objective,** ECB's Knot said, to make sure its policies are aligned with financial stability objectives.
- **For the first time in seven months, the Japanese manufacturing PMI expanded in September,** rising from 49.5 to 50.3 led by a strong rebound in orders, an encouraging sign that economic growth might be picking up.
- **German unemployment is expected to drop further in 2017,** the research arm of Germany's Federal Employment agency said, despite the influx of nearly a million migrants last year.
- **The Japanese government must not rely solely on the Bank of Japan to boost economic growth and defeat deflation,** Finance Minister Aso said this morning, adding that the government would tackle head on issues such as labour reform. A government spokesman said this morning **Japanese authorities are ready to act against excessive yen rises.**
- Today, the **eco calendar** contains only the first estimate of the euro zone PMI's for September and the US Markit manufacturing PMI. ECB's Weidmann and Constancio & Fed's Kaplan, Harker, Mester and Lockhart are scheduled to speak.

# Rates

**BOJ and FOMC trigger bond rally from which EMU bonds profit the most**

**Curves bull flatten**

**Portugal lags other peripherals that keep up with German bonds**

	US yield	-1d
2	0,7744	-0,0040
5	1,1691	-0,0196
10	1,6201	-0,0345
30	2,3338	-0,0445

	DE yield	-1d
2	-0,6630	0,0010
5	-0,5430	-0,0260
10	-0,0830	-0,0870
30	0,4851	-0,1040

**Downside risks EMU PMI**

**ECB Constancio & Weidmann at risk conference on low rates & fin. Stability**

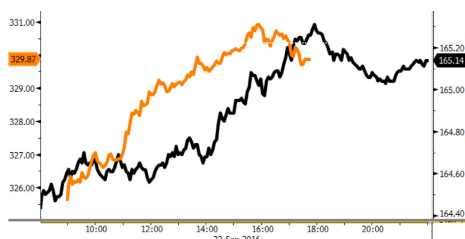
## Sharp flattening of the curve following CB action

Yesterday, core bonds (and equities & commodities) profited fully from the soft FOMC decisions to postpone a rate hike, but especially to lower the rate path and the neutral rate. The hawkish hint on a December rate hike was put aside. In combination with the BOJ decision to cap the 10-yr yield, it triggered a broad-based follow through rally. Interestingly, German long bonds outperformed the US ones, even taking into account Thursday's evening's decline of US yields, driving the 10-yr yield spread back to 171 bps, a 4 month high. Markets appreciate the FOMC bonus of a few months more of cheap money and it remains the case that markets can always count of the Fed when the going becomes a bit more difficult. It puts the hunt for yield back in vogue and lifts all boats, at least for now. We are a bit cautious on the ebullient run of the Bunds, which might have been more linked to the desperate and probably futile move of the BOJ. The curves bull flattened with German yields 1.4 bps (2-yr) to 11.8 bps (30-yr) lower, while US yields were a more modest 0.4 bps (2-yr) to 3.9 bps (30-yr) ,lower. The bond rally was clearly led by European bonds, with the Bund future now near the contract high. Peripheral bonds matched the pace of German bonds with only Portugal lagging (+6 bps 10yr-yield spread).

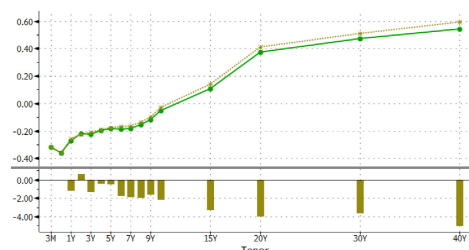
## EMU data and Fed speakers in focus

Last month, the euro area composite PMI dropped to its lowest level since early September, the consensus is looking for a limited further drop from 52.9 to 52.8. Last month, weakness was mainly based in the manufacturing sector, while the services PMI dropped only slightly. For September, a further drop in the manufacturing PMI from 51.7 to 51.5 is expected, but we believe that the risks are for a weaker outcome as sentiment seems to have soured after the initial Brexit optimism. For the services PMI, a stabilisation at 52.8 is forecast. Also here, we see risks for a weaker outcome as sentiment seems to have soured recently, as was also indicated by the latest German IFO business climate indicator and European Commission's consumer confidence.

Regarding ECB governors, we will look for their opinions on the impact of low rates on stability. Weidmann will certainly be concerned but what about Constancio. If he sees financial stability risks it might signal that the ECB won't cut rates further below zero easily. Currently, markets still discount 10 bps of rate cut.



Bund future (black) and EuroStoxx (orange) intraday: Strong follow through rally on FOMC/BOJ decisions.



Japanese yield curve (overnight): Flattening of the curve, not exactly what the BOJ needs. No confidence in new inflation target and operational toolbox

## Upward intraday bias core bonds

R2	166	-1d
R1	165,67	
<b>BUND</b>	<b>165,13</b>	0,6100
S1	164,29	
S2	163	

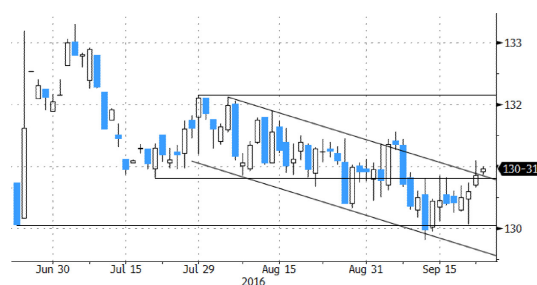
**Overnight**, Asian equities trade mixed to marginally weaker. The US Note future trades stable and Brent crude slightly lower. We expect a neutral opening for the Bund. The Japanese yield curve, suggesting markets don't really buy the latest QQE modification by the BoJ (long term interest rate control aiming for a steeper yield curve).

**Today's** eco calendar heats up in EMU with PMI data. We see **risks on the downside of expectations** which could support core bonds today given the change of sentiment after the Fed meeting. We expect that the downside in the Bund (163) and US Note future (130-01+) is better protected. Fed speakers include Harker, Mester, Lockhart and Kaplan. However, the topics of the events where they feature are non-monetary policy related (Fed's role in communities & Energy Forum). **Overall, core bonds could again trade with an upward bias, but we suspect that recent rally and the approaching resistances keep eventual gains limited.**

**Overall, we favour more range trading for the Bund within the post-Brexit range between 163-165.63. The trading range for the US Note future is expected to be 130-01+ to 132-05, at least until the first week of October (ISM's/payrolls) or until Washington-based Fed governors change the tone of their public comments (Oct 14, Yellen speech).**



German Bund: Range trading between 163 and 165.63



US Note future: Downside better protected short term after dovish FOMC

# Currencies

## Post-Fed dollar losses remain limited

*Dollar trading slightly softer post-Fed, but stays in well-known-territory*

*USD/JPY rebounds (temporary?) on equity strength*

R2	1,1366	-1d
R1	1,1252	
EUR/USD	1,1202	-0,0004
S1	1,1123	
S2	1,1046	

*Dollar extends yesterday's late session rebound*

*USD/JPY struggles to regain 101 barrier*

*Poor European PMI a negative for the euro*

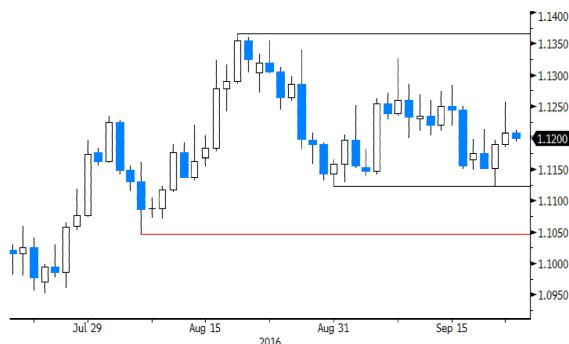
*Global picture for the dollar (EUR/USD) little changed*

*Downside of USD/JPY remains vulnerable*

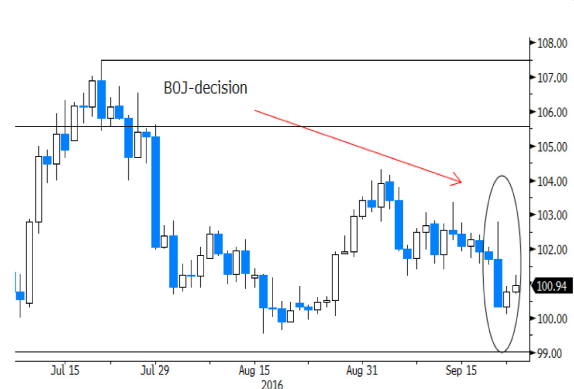
On Thursday, the post-Fed global momentum drove USD trading. Dollar softness was the name of the game in Europe and early in the US as monetary conditions were expected to remain soft for long. EUR/USD set an intraday top in the 1.1257 area. Later in the session, the dollar correction eased. A modest rise in US/German interest rate differentials intraday might have helped to put a floor for the dollar. EUR/USD closed the session at 1.1208 from 1.1189. The price pattern of USD/JPY was slightly different. The pair touched a correction low just north of 100 in Asia, but regained gradually ground later on the global equity rebound. USD/JPY closed the session at 100.76 (from 100.32).

**Overnight**, Asian equities trade narrowly mixed, talking a breather after recent gains. Japanese/Asian markets try to find out how to the new post-BOJ policy framework works. At least for now, the BOJ-pledge to steepen the yield curve doesn't work yet as 10-y yields decline below the 0% target. Overnight, the dollar is stronger across the board, further reversing yesterday's initial post-Fed softness. In this move USD/JPY tries to regain the 101 barrier, but the move is not really convincing even as Japanese government officials signal that Japan is ready to act if excessive FX sensitivity continues. The dollar trades also slightly stronger against the euro with EUR/USD changing hands just below 1.12.

**Today**, the focus turns to the **euro area** with **the first estimate of the PMI's for September**, while in the US the Markit manufacturing PMI will be released. ECB's Constancio & Weidmann and Fed's Harker, Mester, Lockhart and Kaplan are scheduled to speak. Last month, the **euro area composite PMI** dropped to its lowest level since early 2015, from 53.2 to 52.9. For September, the consensus expects a limited further drop to 52.8. Last month, weakness was mainly based in the manufacturing sector. For September, a further drop in **the manufacturing PMI from 51.7 to 51.5** is expected. We see risks for a weaker outcome as sentiment seems to have soared after the initial Brexit optimism. For the **services PMI**, a stabilisation at 52.8 is forecast. Also here, we see risks for a weaker outcome. Central bankers speeches are a wildcard. **We look out for the reaction of European yields in case of a weak PMI**. If yields decline further, it could be a slightly negative for the euro. Of course, European yields declined already substantially yesterday. So, a further drop is not that evident.



EUR/USD: Post-Fed dollar decline slows



USD/JPY: Yen holding strong post BOJ-FFC

EUR/USD tested the 1.1123 support before the Fed, but the test was rejected as the dollar couldn't maintain its post-BoJ gains. Later, the USD lost some further ground after the Fed decision. **We assume that the Fed decision hasn't changed the broader picture for EUR/USD.** Markets will be sensitive whether the data support the case for a December rate hike. **Swings in December rate hike expectations will probably be the driver for USD trading going forward.** The dollar might lose slightly further ground short-term, but as long as the market implied probability of a Fed rate hike remains at current levels, the downside of the dollar looks well protected. For now, we prefer more range trading in the 1.1123/1.1366 range and a sell-on-upticks approach. **USD/JPY** was in the defensive of late. Markets were reluctant to hold big yen shorts going into the BOJ policy decision. The post-BOJ decline of the yen was very short-lived and reversed. We stay cautious on USD/JPY long exposure. However, the **99.54/99.02 area will remain a strong support. 104.32 is the first main resistance.** We expect the established 99.89/104.32 range to hold, but downside risks have grown post BOJ/FED.

### Sterling consolidation continues, for now

**Dollar softness after the Fed policy decision drove initially the the intraday moves in cable and EUR/GBP.** The dollar traded softer against most other majors, including sterling. Cable rebounded to the 1.31 area, compared to levels in the 1.2960 area pre FOMC. In the dollar decline, EUR/USD initially slightly outperformed cable, sending EUR/GBP marginally higher. However, in the afternoon sterling was supported by hawkish comments from BoE's Forbes, questioning the need for further easing. Cable set an intraday top in the 1.3120 area, but closed the session at 1.3078 as the dollar rebounded later in the session. The EUR/USD rally initially pushed EUR/GBP north of 0.86, but the pair declined later on an EUR/USD setback and sterling strength (Forbes). EUR/GBP closed the session at 0.8570 (from 0.8587).

**Today, the UK calendar is empty.** So, global factors will set the tone for GBP-trading. Some euro softness might weigh slightly on the euro. **The hawkish quotes from BOE Forbes might have created some doubts on the BoE's commitment to ease policy further. However, Forbes is probably in the minor (hawkish) group.** So, we expect some further consolidation in the major sterling cross rates today. **Since mid this week, sterling entered calmer waters. This process might continue, as global sentiment on risk might remain mostly supportive.** However, the fear for a hard Brexit might still resurface. In this context, we don't expect any GBP rebound to go far. A sell sterling on upticks approach remains preferred.

R2	0,8725	-1d
R1	0,8582	
<b>EUR/GBP</b>	<b>0,8587</b>	0,0005
S1	0,8344	
S2	0,8251	



EUR/GBP: sterling decline slows



GBP/USD: rebounds north of 1.30 post Fed

# Calendar

Friday, 23 September		Consensus	Previous
<b>US</b>			
15:45	Markit US Manufacturing PMI (Sep P)	52.0	52.0
<b>Canada</b>			
14:30	Retail Sales MoM (Jul)	0.1%	-0.1%
14:30	Retail Sales Ex Auto MoM (Jul)	0.5%	-0.8%
14:30	CPI MoM YoY (Aug)	0.1% / 1.4%	-0.2% / 1.3%
14:30	CPI Core MoM YoY (Aug)	0.2% / 2.0%	0.0% / 2.1%
<b>Japan</b>			
02:30	Nikkei Japan PMI Mfg (Sep P)	A 50.3	49.5
06:30	All Industry Activity Index MoM (Jul)	A 0.3%	1.0%
<b>EMU</b>			
10:00	Markit Manufacturing PMI (Sep P)	51.5	51.7
10:00	Markit Services PMI (Sep P)	52.8	52.8
10:00	Markit Composite PMI (Sep P)	52.8	52.9
<b>Germany</b>			
09:30	Markit/BME Manufacturing PMI (Sep P)	53.1	53.6
09:30	Markit Services PMI (Sep P)	52.1	51.7
09:30	Markit/BME Composite PMI (Sep P)	53.6	53.3
<b>France</b>			
08:45	GDP QoQ YoY (2Q F)	0.0% / 1.4%	0.0% / 1.4%
09:00	Markit Manufacturing PMI (Sep P)	48.5	48.3
09:00	Markit Services PMI (Sep P)	52.0	52.3
09:00	Markit Composite PMI (Sep P)	51.7	51.9
<b>Belgium</b>			
15:00	Business Confidence (Sep)	-2.4	-3.1
<b>Events</b>			
03:45	China MNI September Business Indicator		
08:10	Riksbank's Ingves Speaks at ESRB Conference in Frankfurt		
08:45	ECB's Constancio Chairs Panel at ESRB Conference in Frankfurt		
16:00	ECB's Weidmann speaks at German-French Finance Event in Berlin		
18:00	Fed's Harker, Mester, Lockhart on Panel at Philly Fed Conf		
18:30	Fed's Kaplan Speaks in Houston in Moderated Q&A		

# Contacts

10-year	td	-1d	2-year	td	-1d	STOCKS	-1d
US	1,62	-0,03	US	0,77	0,00	DOW	18392 18392,46
DE	-0,08	-0,09	DE	-0,66	0,00	NASDAQ	for Exch - NQI #VALUE!
BE	0,14	-0,06	BE	-0,61	-0,01	NIKKEI	16754 16754,02
UK	0,71	-0,09	UK	0,08	-0,02	DAX	10674,18 10674,18
JP	-0,05	-0,02	JP	-0,22	0,00	DJ euro-50	3052 3051,69

						USD	td	-1d
IRS	EUR	USD (3M)	GBP	EUR	-1d	Eonia EUR	-0,342	0,005
3y	-0,215	1,073	0,426	Euribor-1	-0,37	Libor-1 USD	0,27	0,27
5y	-0,148	1,179	0,486	Euribor-3	-0,30	Libor-3 USD	0,38	0,38
10y	0,284	1,446	0,748	Euribor-6	-0,20	Libor-6 USD	0,53	0,53

Currencies		-1d	Currencies		-1d	Commoditie	CRB	GOLD	BRENT
EUR/USD	1,1199	-0,0008	EUR/JPY	112,94	0,51		186,3232	1334,85	47,26
USD/JPY	100,89	0,53	EUR/GBP	0,8588	0,0005	-1d	1,46	2,97	0,04
GBP/USD	1,3037	-0,0013	EUR/CHF	1,0862	-0,0037				
AUD/USD	0,7644	0,0008	EUR/SEK	9,5779	0,00				
USD/CAD	1,3057	-0,0009	EUR/NOK	9,1087	-0,13				

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