Sunrise

Thursday, 27 October 2016

Rates: Core bonds arrive at key technical levels. Break in soured sentiment?

Overnight, most Asian stock markets lose ground while oil prices remain under downward pressure. However, in line with yesterday, the US Note future also declines and even tests 129-26 support suggesting that negative sentiment on core bond markets could continue today with the Bund also testing the 163-162.56 support area.

Currencies: USD rally takes a breather

Yesterday, the dollar rally ran into resistance even as core bond yields rose further, but the correction was limited. EUR/USD rebounded north of 1.09. USD/JPY held near the recent highs even as equities drifted south. Today, the data will probably be of sector tier importance for USD trading. Sterling traders keep an eye on the UK Q3 GDP estimate.

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% lower yesterday. **Overnight** Asian stock markets face a similar faith with South Korea outperforming.
- **UK banks and insurers are probably going to lose their EU passporting rights after Brexit**, the Trade Minister said. Nor is an alternative known as equivalence likely to work, he said. The government is working on a hybrid model to allow banks’ access to Europe and stave off a possible exodus of business.
- **Tesla** posted a surprise $22 million profit in its latest period, buoyed by record sales of its pricey electric cars. **Samsung** said its net profit fell 16.8% because of a disastrous recall of its premium Galaxy Note 7 smartphone.
- **Greece’s ruling Syriza party suffered a major embarrassment** when judges struck down its plan to revamp Greece’s media sector, after a weeklong power struggle that produced allegations of blackmail and “fascist” methods.
- **Chinese industrial profit growth slowed sharply** as some key manufacturing sectors stumbled on weak activity and rising debt, suggesting the Chinese economy remains underpowered despite emerging signs of stability.
- **US crude stockpiles unexpectedly fell** last week as refinery activity picked up pace. Brent crude temporary surged back above $50.6, but failed to cling on to gains, falling back towards $50/barrel.
- **The ECB** is nearly certain to **continue buying bonds beyond its March target** and to **relax its constraints on the purchases** to ensure it finds enough paper to buy, central bank sources have told Reuters.
- **Today, the eco calendar** contains UK Q3 GDP, EMU M3 Money supply, US Durable goods orders and weekly jobless claims. The Swedish Riksbank and Norwegian Norges Bank decide on monetary policy.

Rates

Bear steepening despite lower oil and equities

Sharp bear steepening German curve

Milder shift up for US yield curve

	US yield	-1d
2	0,8764	0,0119
5	1,3115	0,0405
10	1,8021	0,0549
30	2,5475	0,0582

	DE yield	-1d
2	-0,6370	0,0110
5	-0,4280	0,0440
10	0,0920	0,0580
30	0,7307	0,0727

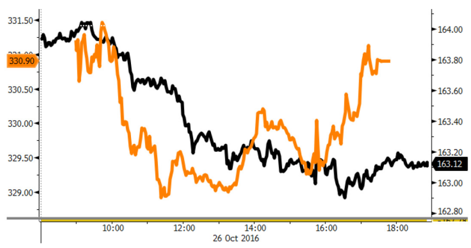
Global core bonds defied traditional trading wisdom yesterday by declining in lockstep with oil prices (Brent crude <$50/barrel) and stock markets. The move occurred amid a thin eco calendar and in absence of headline news. EMU and US supply was negative at the margin. Key support levels in the Bund (163 area) and US Note future (129-26) were tested (Bund) or again within reach (T-Note). **We think that rate markets become enthralled by the recent change of tone of central bankers and rising inflation expectations.** The market implied probability of a December Fed rate increased above 70%, **ECB president Draghi** laid the foundation of QE tapering and the **BoE changed its intentions** about additional easing this year. The **US Markit services PMI** surprised on the upside and the US **trade deficit** was much smaller than expected in September, suggesting that GDP may be a bit higher than expected. **These data were bond-unfriendly, but published when the intraday sell-off was mostly done. US New Home sales** rose by 3.1% in September, but after sizeable downward revisions in the previous two months.

In a daily perspective, the German yield curve bear steepened with yields 1 bps (2-yr) to 7 bps (30-yr) higher. The US yield curve shifted similarly, but with yields only 1.6 bps (2-yr) to 4.3 bps (30-yr) higher. On the UK curve, the 2 and 5-yr yield were 2.1 and 4.7 bps higher on Carney's inflation comments. **On intra-EMU bond markets,** 10-yr yield spread changes versus Germany ranged between -4 bps (Portugal) and +2 bps (Italy) with Greece outperforming (-14 bps).

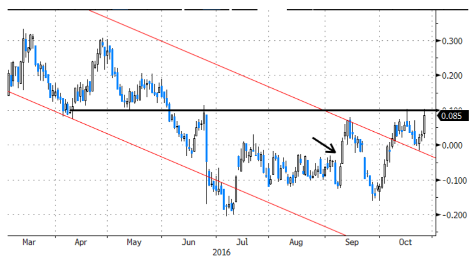
Eco calendar thin

Durables to remain weak, but claims may be lower again

In **EMU**, the releases are limited to the **September M3 money supply** figures. The markets expect a stabilization at 5.1% Y/Y. Already for 18 months M3 supply hovers between 4.5 and 5.1% Y/Y, a level accetable for the ECB. Markets will look to the lending data, but usually don't react to the report **In the UK , the advance Q3 GDP** will be released (0.3% Q/Q), which may cause ripples in euro markets too in case of surprises. **In the US, the durable goods orders and the initial claims** will get attention. **Claims** are expected to have dropped to 255K from 260K in the previous week when claims jumped 13K albeit from record low levels, probably due to huricane Matthew. **Durable goods orders** are expected flat for September following a 0.1% M/M increase in August. It is a volatile series, but overall orders remain tepid. Capital goods shipments (nondefence), a source for GDP business investment is expected up 0.4% M/M following 4 monthly declines.



Bund future (black) and EuroStoxx (orange) intraday: Both down in European morning trading. While equities fought back, Bunds couldn't react.



German 10-yr yield retests the 10 bps yield resistance after breaking above downtrendline. In case resistance is broken, bottoming out could become reality

R2	166,36	-1d
R1	164,29	
BUND	**163,04**	-0,7800
S1	163	
S2	162,56	

Average demand for US supply

The US Treasury continued its end-of-month refinancing operation with an **uneventful $15B 2-yr FRN auction** and an **average $34B 5-yr Note auction.** The 5-yr auction stopped right on the 1:00 PM bid side with a just above average bid cover (2.49). Bidding details were run-of-the-mill. Today, the US Treasury ends its operation with **a $28B 7-yr Note auction.** Currently, the WI trades around 1.61%.

Sentiment on bond markets soured

Overnight, most Asian stock markets lose ground while oil prices remain under downward pressure. However, in line with yesterday, the US Note future also declines and even tests 129-26 support suggesting that negative sentiment on core bond markets could continue today with the Bund also testing the 163-162.56 support area.

Today's calendar contains amongst others UK Q3 GDP data and US durable goods orders. Exceptionally, core bond markets could pay more attention to Scandinavian central bankers with policy meetings in Norway and Sweden. Both countries have an extraordinary easy monetary policy despite strong underlying growth and even picking up inflation. If also the Riksbank and Norges Bank signal a shift in policy ahead (in line with similar messages from ECB, BoE and Fed; see above) it could intensify the sell off on core bond markets, preparing for a normalization of yields.

Technically, the US 10-yr and 30-yr yields held above key resistance levels at 1.75% and 2.5%, suggesting that the US Note future could break key support levels in the run-up to next week's FOMC meeting, anticipating a clear hint on a December rate hike. The German 10-yr yield tested the 0.10% resistance a second time yesterday. A break higher would be very relevant from a technical point of view and unlock a new trading range (0.10%-0.30%). Rising inflation expectations and an expected ECB QE tapering announcement in December could do the trick.

German Bund: Testing very important support

US Note future: Extensively tested the downside, but break didn't occur so far

Currencies

USD rally takes a breather

Dollar rally takes a breather, but correction remains limited

R2	1,1366	-1d
R1	1,1123	
EUR/USD	**1,0911**	0,0023
S1	1,0826	
S2	1,0711	

On Wednesday, the dollar lost slightly ground after the recent rally. A risk-off correction on global equity markets was a good reason to lock in some USD profits. Core bond yields rose further. This is often USD positive, but this time interest rate differentials moved slightly in favour of the euro. EUR/USD rebounded well above 1.09, but closed the session off the intraday highs at 1.0908 (from 1.0889 on Tuesday). USD/JPY held within reach of the recent top as the rise in core yields 'neutralised' the correction in equities. USD/JPY closed the session at 104.47 (from 104.22).

Further modest correction on Asian equity markets

Dollar tries to resume uptrend

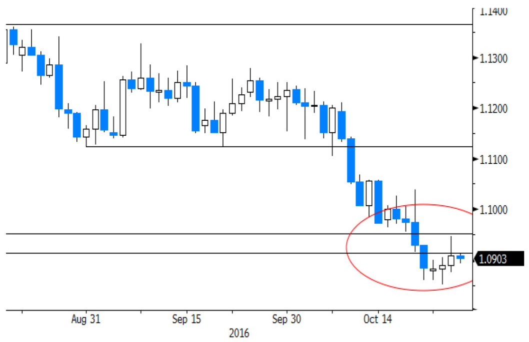
USD/JPY trades within reach of recent top

Overnight, Asian equities correct a bit furhter, but the losses remain modest. The rise in global yields and the strong dollar are mixed developments for Asian/emerging markets. The trade-weighted dollar holds within reach of the seven month top. USD/JPY trades in the mid 104.50 area. So, the dollar (and the euro) outpefrom the yen on higher core yields. EUR/USD changes hands in the 1.0900 area, off yesterday's intraday top around 1.0945. So, it looks that yesterday's USD correction might have been short-lived.

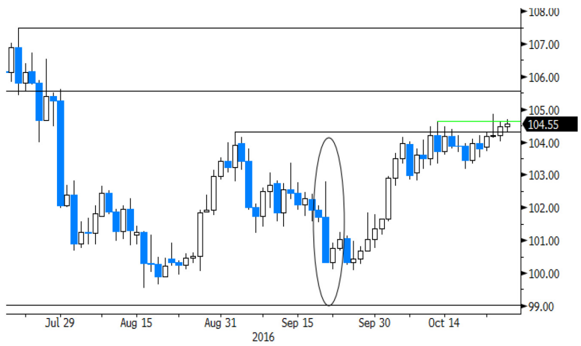
Eco calendar probably no big driver for USD trading

Some more USD consolidation might be on the cards short-term

Today, the EMU M3 money supply data will be published. The market expects a stabilization at 5.1% Y/Y. Markets will also look to the lending data, but usually don't react to the report. **In the UK , the advance Q3 GDP** will be released (0.3% Q/Q is expected), which may cause ripples in euro markets in case of a surprise. **In the US, the durable goods orders and the jobless claims** will get attention. **Weekly jobless claims** are expected to have dropped to 255K from 260K. September **durable goods orders** are expected flat following a 0.1% M/M increase in August. It is a volatile series, but orders remain tepid. Capital goods shipments (nondefence), a source for GDP business investment are expected up 0.4% M/M following 4 monthly declines. **As was the case yesterday, the data will probably only be of sector tier imprtance for currency trading.** Markets consider a Fed rate hike more or less a done thing, unless unexpected economic or other event risk spoils the game. **Yesterday, long term bond yields rose more in Europe than in the US. This interrupted the gradaul rise of the dollar.** Some further USD consolidation might be on the cards as markets already discount a high probablity of a Decmeber Fed rate hike. The dollar probably needs addiontal postive news (data or otherwise) to extend its recent rebound.



EUR/USD: modest USD correction, but trend remains intact



USD/JPY: holding near the recent highs even as equities struggle

A risk-off corection, for whatever reason might also slow the USD uptrend. At the same time, the Fed rate hike expecations put a solid floor under the US currency. So, **in a day-to-day perspective, we remain a bit more neutral on the USD, even as the MT trend remains USD-positive.**

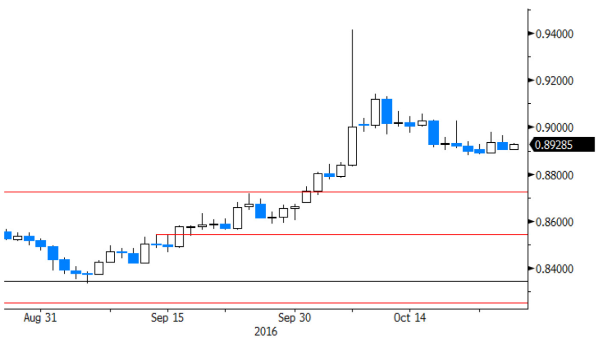
From a technical point of view, EUR/USD dropped below 1.0952/13 support. The break is an extra USD positive and opens the way to next intermediate support (1.0822/1.0711). USD/JPY struggles to break north of 104.32/64. A sustained break would paint a double bottom formation on the charts with targets in the 108/109 area. The rise in US/core bond yields provided solid downside protection for the dollar recently. Even so, we stay cautious on a sustained USD/JPY upleg as global volatility might come back in play.

Sterling succeeds cautious rebound

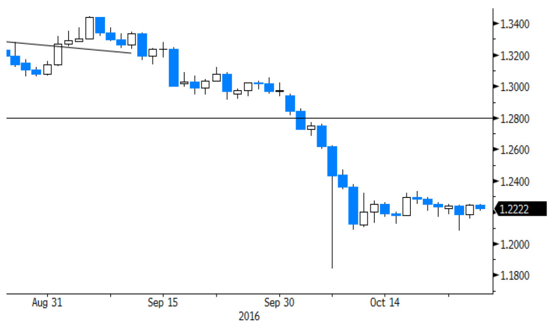
R2	0,9142	-1d
R1	0,9027	
EUR/GBP	**0,8927**	-0,0020
S1	0,8725	
S2	0,8589	

On Wednesday, sterling took a breather after Tuesday's roller-coaster rise. **EUR/GBP held a tight sideways range in the mid 0.89 area.** The BBA loans for home purchases were slightly stronger than expected after a protracted decline earlier this year, but the report had no big impact on sterling. On Tuesday, BoE's Carney indicated that the BoE couldn't ignore the substantial decline of sterling. A November BoE policy easing has become unlikely. This was probably a temporary supportive for sterling. Cable rebounded north of 1.22, compared with an intraday low below 1.21 yesterday. However, this move was at least partially due to USD weakness. EUR/GBP closed the session at 0.8907 (from 0.8934).

Today, the focus is on the first estimate of the UK Q3 GDP. A rise of 0.3% Q/Q and 2.1% Y/Y is expected. So, the data are expected to confirm that the UK economy held up well immediately after the Brexit vote. A better than expected report might further reduce the case for a BoE rate cut near term. In this scenario, the sterling rebound might have some further to go. The CBI reported sales are expected to improve from -8 to -2, but the release will probably have no big impact on sterling trading. Over the previous days, sterling traded on a more solid footing. Some further consolidation or even a slight further rebound might be on the cards short-term. **However, we don't expect this sterling rebound to go far and look to sell sterling on more pronounced up-ticks. EUR/GBP 0.8725 remains a key reference. Political event risk remains a lasting source of sterling uncertainty.**



EUR/GBP: holding below the 0.90 barrier, for now



GBP/USD: consolidation, but no sustained rebound yet

Calendar

Thursday, 27 October		Consensus	Previous
US			
14:30	**Durable Goods Orders (Sep P)**	**0%**	**0.1%**
14:30	Durables Ex Transportation (Sep P)	0.2%	-0.2%
14:30	Cap Goods Orders Nondef Ex Air (Sep P)	-0.1%	0.9%
14:30	**Cap Goods Ship Nondef Ex Air (Sep P)**	**0.4%**	**-0.1%**
14:30	**Initial Jobless Claims**	**255k**	**260k**
14:30	Continuing Claims	2052K	2057k
16:00	Pending Home Sales MoM / NSA YoY (Sep)	1.1%/4%--	-2.4%/4.0%
UK			
10:30	**GDP QoQ / YoY (3Q A)**	**0.3%/2.1%**	**0.7%/2.1%**
10:30	Index of Services MoM // 3M/3M (Aug)	0.1%/0.8%	0.4%/0.6%
12:00	CBI Retailing Reported Sales (Oct)	-2	-8
12:00	CBI Total Dist. Reported Sales (Oct)	--	17
EMU			
10:00	**M3 Money Supply YoY (Sep)**	**5.1%**	**5.1%**
Norway			
08:00	Unemployment Rate AKU (Aug)	4.9%	5.0%
10:00	**Deposit Rates**	**0.50%**	**0.50%**
Sweden			
09:30	**Riksbank Interest Rate**	**-0.50%**	**-0.50%**
Events			
Q3 earnings	Samsung (01:32), Dow Chemical (Bef-mkt), Amazon.com (22:01), Alphabet (Aft-mkt)		
14:00	Austrian Central Banker Ewald Nowotny Speaks in Cyprus		
19:00	ECB's Mersch Speaks in Hachenburg, Germany		
19:00	US to sell $28B 7-yr Notes		

10-year	td	-1d	2-year	td	-1d	STOCKS		-1d	
US	1,80	0,05	US	0,88	0,01	DOW	18199	18199,33	
DE	0,09	0,06	DE	-0,64	0,01	NASDAQ	for Exch - NQI	#VALUE!	
BE	0,33	0,08	BE	-0,65	0,00	NIKKEI	17320	17320,32	
UK	1,16	0,05	UK	0,25	0,01	DAX	10709,68	10709,68	
JP	-0,06	0,01	JP	-0,24	0,00	DJ euro-50	3081	3080,98	
						USD	td	-1d	
IRS	EUR	USD (3M)	GBP	EUR	-1d	-2d	Eonia EUR	-0,351	0,001
3y	-0,141	1,169	0,677	Euribor-1	-0,37	0,00	Libor-1 USD	0,26	0,26
5y	-0,019	1,322	0,794	Euribor-3	-0,31	0,00	Libor-3 USD	0,40	0,40
10y	0,455	1,634	1,106	Euribor-6	-0,21	0,00	Libor-6 USD	0,56	0,56

Currencies		-1d	Currencies		-1d	Commoditie	CRB	GOLD	BRENT
EUR/USD	1,0911	0,0023	EUR/JPY	114,03	0,51		188,7198	1268,41	50,14
USD/JPY	104,525	0,23	EUR/GBP	0,8927	-0,0020	-1d	-0,72	-4,94	0,00
GBP/USD	1,2219	0,0057	EUR/CHF	1,0836	0,0003				
AUD/USD	0,7633	-0,0061	EUR/SEK	9,719	0,00				
USD/CAD	1,3376	0,0025	EUR/NOK	9,0199	0,02				

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