



## Sunrise

**Monday, 03 October 2016**

### Rates: Stronger ISM negative for US Treasuries, but more to come

The US manufacturing ISM is the first of this week's important US economic data releases (ISM's, ADP, payrolls). Risks are on the upside of expectations which could weigh on US Treasuries. Developments on the Spanish political scene raised the odds of avoiding a third general election, though several hurdles still need to be cleared. Spanish bonds could outperform.

### Currencies: Positive risk sentiment and constructive ISM to be mildly USD supportive

On Friday, USD/JPY profited as financial tensions eased. EUR/USD finished the session little changed. Today, the focus is on manufacturing sentiment. A good US ISM might be slightly USD supportive, but we don't expect EUR/USD to break out of the established ranges. Sterling is again in the defensive as UK PM May signals to start the exit in Q1 2017.

### 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** gained about 0.80%, as risk sentiment improved, amongst others on financials. **Asian equities** replicate WS's performance overnight in follow through buying, as DB woes are deflated.
- **UK PM May said she'll begin the UK's process of withdrawal from the EU in Q1 of 2017** in her clearest announcement yet about her Brexit strategy. The pull-out will occur in 2019. It may suggest Ms May is looking for a hard Brexit. Sterling is under pressure
- **Japan manufacturing confidence (Tankan) was stabilised in Q3**, but marginally below consensus, while non-manufacturing sentiment was a tad weaker, but close to expectations. It had little lasting impact on Japanese markets. **Chinese official PMI's** were little changed at 50.4 (manufacturing) and 53.7 (services).
- **Deutsche Bank was dealt a fresh blow** as an Italian court charged the company for colluding with Banca Monte dei Paschi to falsify their 2008 to 2012 accounts. On Friday, the stock surged on expectations the firm's fine will be much smaller than initially expected. It also may announce a 1 000 job cut.
- **Spain's Socialist leader Sanchez resigned** after the rejection of his call for an emergency leadership election. His resignation **may open the way for outgoing PM Rajoy to install a minority government**, that is not voted away by Socialists.
- **Italian PM Renzi** and his government won't resign whatever the outcome of the Dec 4 referendum on constitutional reforms, retreating from his earlier threat to resign if the people vote against the proposals.
- **Hungarian PM Orban failed to convince at least 50% of his people to vote in the referendum**, making it invalid, but of the 39.7% who turned up, 98% supported a "no" vote.
- **Today**, attention goes to the various business sentiment's indicators. The plight of DB may still have impact too

# Rates

*Risk sentiment took a turn for the better, as markets expect the DB fine to be much lower than \$14B*

*US curve bear steepen.*

*German curve little changed as some catching up had to be done*

*Widening peripheral spreads reversed*

	US yield	-1d
2	0,7778	0,0515
5	1,1606	0,0598
10	1,6065	0,0637
30	2,3301	0,0635

	DE yield	-1d
2	-0,6880	0,0100
5	-0,5710	0,0230
10	-0,1210	-0,0040
30	0,4552	0,0111

*Upside risks US ISM*

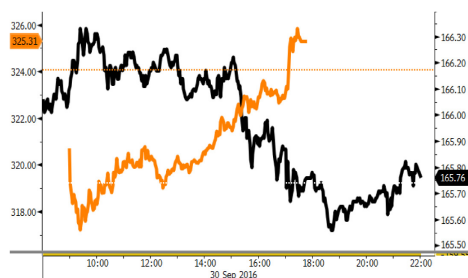
*Chinese and German markets closed*

## Bonds sold off once risk sentiment turned positive

On Friday, European bonds started strong, catching up with US Treasuries. However, sentiment on risk improved fast, allowing equities to gradually erase early losses. German bonds initially slid into a sideways trading mode, but more strength in US equities was the straw that broke the camel's back, triggering outright bond selling. It pushed US Treasuries well into the red and eliminated early German bond gains. The trigger for the turn in the sentiment on risk was reports that the terms for the Deutsche Bank settlement would be much better than the \$14B earlier spoken about. The decline in oil prices in the morning session may still have restraint core bonds losses, but the recovery in the afternoon session helped equities to rebound further even it occurred largely ahead of the core bond selling. In a daily perspective, the US yield curve bear steepened with yields 2.8 bps (2 yr) to 3.9 bps (30-yr) higher. The German yield curve, which had to play still catching up with the US Treasuries ended narrowly mixed with yields up 0.2 (2-5-yr) and down 0.3-0.4 bps at the 10-yr tenor and beyond. On intra-EMU bond markets, the initial sharp spread widening attracted bargain hunters once the risk sentiment improved. Spanish and Italian 10-yr yield spreads fell still 4 and 2 bps, while Greece and Portugal were 2 bps wider.

## Manufacturing confidence in focus today

In August, the US ISM manufacturing confidence index fell unexpectedly to 49.4 from 52.6 in July. It was the first month below the 50 boom/bust level since February 2016. For September, an improvement to 50.2 is expected. The regional surveys were mixed, but mostly slightly better than expected. Our projection is for a rise to 50.6, slightly above the consensus. The EMU manufacturing PMI rose unexpectedly in September (52.6) while the Caixin and National PMI's stabilized just above 50. So, we see risks for an above consensus outcome, but the index should only slightly exceed the 50 threshold, suggesting the manufacturing sector continues to struggle as the global economic motor shows little signs of an acceleration. The final EMU manufacturing PMI is expected to have remained unchanged compared to the preliminary one (52.6). Of course also the UK, Canadian and many other, smaller countries publish their PMI's, which might affect the local markets. Later this week, the US payrolls on Friday will as ever be the eye-catcher.



Bund future (black) and EuroStoxx (orange) intraday: risk-off turns to risk-on, allowing equities to recoup losses and pushing Bund lower



S&P: tries again to re-enter small sideways range near the highs.

R2	167	-1d
R1	166,36	
<b>BUND</b>	<b>165,76</b>	0,3000
S1	164,29	
S2	163	

## Germany, France and Spain tap market

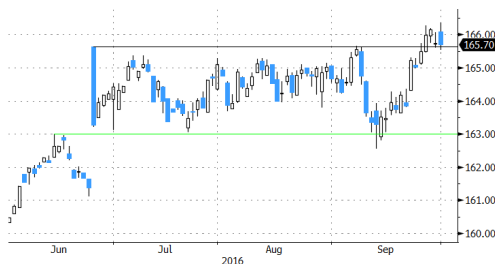
**This week's scheduled EMU bond supply is rather low, with only Germany, France and Spain tapping the market.** On Wednesday, the German Finanzagentur auctions the 10-yr on the run Bund (€4B 0% Aug2026). On Thursday, the French debt agency sells the on the run 10-yr OAT (0.25% Nov2026), 15-yr OAT (1.5% Mar2031) and 50-yr OAT (1.75% May2066) for a combined €6.5-7.5B. The Spanish Treasury taps the on the run 5-yr Bono (0.75% Jul2021), 10-yr Obligacion (1.3% Oct2026) and the off the run 30-yr Obligacion (4.2% Jan2037). The amount on offer still needs to be announced. This week's auctions won't be supported by bond redemptions.

## Stronger ISM negative for Treasuries, but more to come?

**Overnight,** Asian stock markets gain ground in line with Deutsche Bank's and WS's revival on Friday. China and South Korea are closed for holidays. The US Note future and Brent crude trade stable, suggesting a neutral opening for the Bund.

**The main item on today's eco calendar is the US manufacturing ISM.** Risks are on the upside of expectations, which is slightly negative for US Treasuries especially if dust settles on last week's financial sector concerns. **They could influence Fed rate hike expectations. Currently, the market implied probability of a Fed rate hike is 17% in November and 59% in December.** Some investors might remain side-lined with other major eco releases (US non-manufacturing ISM, ADP, payrolls) ahead this week. **On intra-EMU bond markets, Spanish bonds could outperform following the resignation of Socialist party leader Sanchez.** This raises chances that some socialist MP's abstain if PM Rajoy makes another bid with his proposed minority government ahead of the Oct. 31 deadline.

**Technically, the Bund broke above the upper bound of the post-Brexit trading range (163-165.63).** The break wasn't confirmed by a move of the German 10-yr yield below -0.20%, making it less relevant. **The trading range for the US Note future is expected to be 130-01+ to 132-05.** Depending on the outcome of this week's eco data, a test of one of these boundaries could occur.



German Bund: Break above upper bound sideways trend channel needs to be confirmed by drop below -0.20% German 10yr yield



US Note future: Key week with main US eco releases (ISM's, ADP, payrolls)

# Currencies

## Decent ISM and risk-on sentiment mildly USD positive?

On Friday, the euro opened weak as financial uncertainty weighed on European markets. However, tensions eased fast. USD/JPY and EUR/USD rebounded off the intra-day lows set early in Europe. The US eco data were mostly slightly better than expected, but with no big impact on the dollar. EUR/USD (1.1235 vs 1.1222) finished the day little changed. USD/JPY extended its cautious uptrend to close the session at 101.35 (From 101.03).

*USD/JPY better bid as financial tensions ease.*

*EUR/USD little changed*

*EUR/USD holds a tight range*

*USD/JPY stays above 101 as regional data are not too bad*

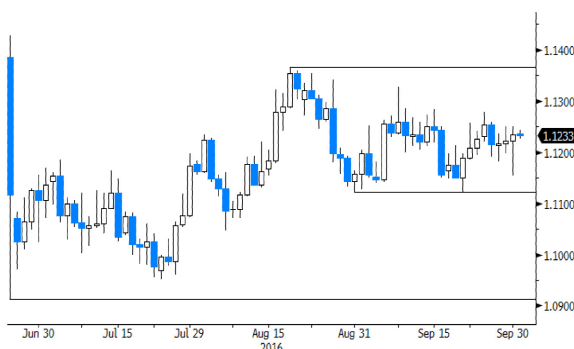
R2	1,1366	-1d
R1	1,1327	
EUR/USD	<b>1,123</b>	0,0011
S1	1,1123	
S2	1,1046	

*The manufacturing confidence in focus today*

**Overnight**, several Asian markets including China are closed. In Japan, the Tankan business sentiment was close to expectations limiting its impact on markets. During the weekend, a similar as expected outcome was registered for Chinese business Global sentiment on risk remains positive after positive news on Deutsche bank, mainly last Friday. Easing financial tensions and decent Japan/Chinese data are mildly supportive for USD/JPY. The pair trades in the 101.40 area. EUR/USD is again holding a tight sideways range near 1.1235

**Today**, the manufacturing confidence will be in focus on both sides of the Atlantic. In August, the **US manufacturing ISM** fell unexpectedly to 49.4 from 52.6. For September, an improvement to 50.2 is expected. The regional surveys were mostly slightly better than expected. Our ISM Nowcast projection is for a rise to 50.6, slightly above the consensus. So, **we see risks on an above consensus outcome**, but the index should only slightly exceed the 50 threshold, suggesting the manufacturing activity remains sluggish. The final EMU manufacturing PMI is expected unchanged compared to the preliminary one (52.6). **Of course also the UK, Canadian and many other, smaller countries publish their PMI's, which might affect the local markets.** Later this week, the US payrolls on Friday will as ever be the eye-catcher.

Of late, EUR/USD was little affected by data or headline news. A better than expected US ISM might be slightly USD supportive. However, we don't expect EUR/USD to break out of the recent range. USD/JPY might also maintain last week's gains due to the combination of a constructive sentiment on risk and a decent US ISM. However, also for this cross rate it won't be easy to extend gains beyond first technical resistance (e.g. 102.79, 21 sept top).



EUR/USD holding tight ranges



USD/JPY: gradually rebound, but technical picture hasn't improved, yet.

EUR/USD tested the 1.1123 support before the Fed, but the test was rejected as the Fed stayed in wait-and-see modus. **The Fed decision hasn't changed the broader picture for EUR/USD.** Markets look out whether the data support the case for a December rate hike. **Swings in December rate hike expectations will probably remain the main driver for USD trading.** The downside of the dollar looks well protected as long as the market implied probability of a Fed rate hike remains at current levels, We prefer more range trading in the 1.1123/1.1366 band and a sell-on-upticks approach. **USD/JPY remains in the defensive after the BOJ meeting.** 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 99.89/104.32 range to hold, but downside risks have grown post BOJ/Fed.

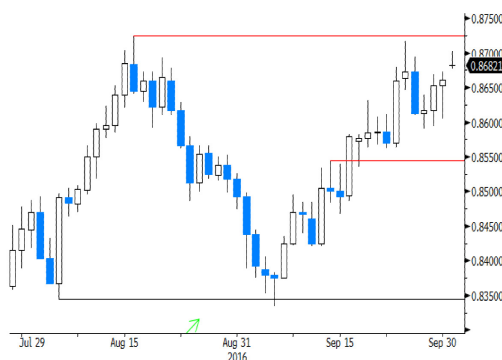
### Sterling again in the defensive

Sterling trading on Friday was again driven by technical considerations, like end of quarter repositioning. Uncertainty on the German banking sector initially weighed on the euro. EUR/GBP dropped to the 0.8620 area. **The UK eco data (Q2 GDP revision and Q2 current account) were marginally better than expected,** but we doubt they had any impact on GBP trading. Still, EUR/GBP declined to the low 0.86 area. Later on, EUR/USD rebounded, pushing both EUR/GBP and cable off the intraday lows. EUR/GBP finished marginally higher (0.8661 vs 0.8653). Cable finished the day nearly unchanged at 1.2972.

**During the weekend, UK PM May said she will start the Brexit process in the first quarter of 2017.** However, most questions on what the UK institutional framework will look like after-Brexit remain of course open. Sterling is in the defensive this morning. Cable filled bids just north of 1.29. **Later today, the UK manufacturing PMI will be published.** The index rebounded sharply to 53.3 last month. For September, a decline to 52.1 is expected. **Sterling is probably more sensitive to a negative surprise rather than to a stronger one as fear on a hard Brexit weighs.**

Last week, there was a pause in the Brexit-related decline of sterling. However, a real rebound didn't occur, partially because a fragile global sentiment. **Both EUR/GBP and cable came close to important technical barriers at respectively 0.8725 and 1.2866/1.2798.** These levels might provide support for sterling short-term. However, the fear for a hard Brexit still looms. In this context any GBP rebound shouldn't to go far. **A sell sterling on upticks approach remains preferred.**

R2	0,8815	-1d
R1	0,8725	
EUR/GBP	<b>0,868</b>	0,0026
S1	0,8344	
S2	0,8251	



EUR/GBP: test of 0.8725 post-Brexit top rejected, but no sustained sterling rebound.



GBP/USD: consolidation, but cable fails to sustain north of 1.30

# Calendar

Monday, 3 October		Consensus	Previous
<b>US</b>			
	Wards Domestic Vehicle Sales (Sep)	13.33 m	13.13m
	Wards Total Vehicle Sales (Sep)	17.42m	16.91m
15:45	Markit US Manufacturing PMI (Sep F)	51.4	51.4
16:00	Construction Spending MoM (Aug)	0.3%	0.0%
16:00	ISM Manufacturing (Sep)	50.3	49.4
<b>Canada</b>			
15:30	RBC Manufacturing PMI (Sep)	--	51.1
<b>Japan</b>			
01:50	Loans & Discounts Corp YoY (Aug)	A 2.11%	2.25%
01:50	Tankan Large Mfg Index / Outlook(3Q)	A 6/6	6 / 6
01:50	Tankan Large Non-Mfg Index (3Q)	A 18 / 16	19 / 17
02:30	Nikkei Japan PMI Mfg (Sep F)	A 50.4	50.3
07:00	Vehicle Sales YoY (Sep)	A 3.7%	5.7%
<b>UK</b>			
10:30	Markit PMI Manufacturing SA (Sep)	52.1	53.3
<b>EMU</b>			
10:00	Markit Manufacturing PMI (Sep F)	52.6	52.6
<b>Germany</b>			
09:55	Markit/BME Manufacturing PMI (Sep F)	54.3	54.3
<b>France</b>			
09:50	Markit Manufacturing PMI (Sep F)	49.5	49.5
<b>Italy</b>			
09:45	Markit/ADACI Manufacturing PMI (Sep)	50.3	49.8
10:00	Deficit to GDP YTD (2Q)	--	4.7%
<b>Norway</b>			
09:00	Manufacturing PMI (Sep)	52.3	50.8
<b>Spain</b>			
09:15	Markit Manufacturing PMI (Sep)	51.5	51.0
<b>Sweden</b>			
08:30	Swedbank/Silf PMI Manufacturing (Sep)	52	50.7
<b>Events</b>			
	German, Chinese Markets are Closed		
10:00	Bank of Portugal Governor, Finance Minister Speak in Lisbon		
15:50	Bank of England Bond-Buying Operation Results		
18:00	ECB Mersch speaks in Luxemburg		



# Contacts

10-year	td	-1d	2-year	td	-1d	STOCKS	-1d
US	1,61	0,06	US	0,78	0,05	DOW	18308 18308,15
DE	-0,12	0,00	DE	-0,69	0,01	NASDAQ	for Exch - NQI #VALUE!
BE	0,15	0,03	BE	-0,64	0,00	NIKKEI	16598 16597,97
UK	0,76	0,04	UK	0,09	0,05	DAX	10511,02 10511,02
JP	-0,07	0,01	JP	-0,28	0,01	DJ euro-50	3002 3002,24

						USD	td	-1d
IRS	EUR	USD (3M)	GBP	EUR	-1d	-2d	Eonia EUR	-0,329 0,014
3y	-0,217	1,060	0,440	Euribor-1	-0,37	0,00	Libor-1 USD	0,27 0,27
5y	-0,148	1,174	0,502	Euribor-3	-0,30	0,00	Libor-3 USD	0,38 0,38
10y	0,275	1,449	0,781	Euribor-6	-0,20	0,00	Libor-6 USD	0,53 0,53

Currencies	-1d	Currencies	-1d	Commoditie	CRB	GOLD	BRENT
EUR/USD	1,123 0,0011	EUR/JPY	113,95 0,59		185,8277	1314,89	49,97
USD/JPY	101,5 0,42	EUR/GBP	0,868 0,0026	-1d	0,00	-9,11	1,11
GBP/USD	1,2935 -0,0021	EUR/CHF	1,0918 0,0086				
AUD/USD	0,7649 0,0023	EUR/SEK	9,6399 0,02				
USD/CAD	1,3118 -0,0033	EUR/NOK	8,9619 -0,07				

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