Sunrise

Friday, 07 April 2017

Rates: Risk off after US attack; focus on payrolls now

US Treasuries spiked higher overnight after the US conducted missile strikes against Syria, retaliating the gas attack earlier this week. The US 10-yr yield tested key 2.3% support, but a break didn't occur. Today's attention turns to the US payrolls report. With risks slightly on the upside of expectations, 2.3% should become even stronger support.

Currencies: Will payrolls be strong enough to restore a better USD bid?

The dollar stabilized yesterday after Wednesday's post-Minutes correction. Overnight, USD/JPY revisited the recent lows on headlines of the US strike against Syria, but no break occurred. Later today, the focus for USD trading will be on the US payrolls. Of late, the dollar gradually lost interest rate support. Will the payrolls be strong enough to reverse this trend?

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	→

- **US equities** ended a dull trading session with small gains. **Risk sentiment deteriorated** after the US conducted missile strikes against Syria. Most Asian equity indices lose around 0.3% with Japan and China outperforming.
- **The US military launched nearly 60 Tomahawk cruise missiles against a Syrian air base** this morning, responding to mounting calls for a display of force in the wake of this week's suspected chemical-weapons attack in Syria.
- Under rules passed by the US Senate, **lawmakers in the minority party will no longer be able to block presidential appointments to the Supreme Court** a move so extreme it had been known as "the nuclear option".
- Overtime pay in Japan, a barometer of strength in corporate activity, edged up in February for the first time in nine months, **while real wages remained flat,** government data showed on Friday
- The ECB has proposed that **large branches of foreign banks in the EU be subject to tighter regulation and capital requirements,** a move that would increase US and Asian lenders' costs and also hit British banks after Brexit.
- **ECB President Draghi** yesterday looked to dull speculation that the ECB will halt its negative rate experiment later this year. In a press conference later in the day, **ECB VP Constâncio said that Draghi has "a lot of support" for his stance**
- **Today's eco calendar** contains US payrolls and UK industrial production data. Euro-area finance ministers will try to break a months-long deadlock over Greece's bailout in Malta. BoE Carney is scheduled to speak.

Rates

Core bonds resilient as investors await US payrolls

Core bonds resilient despite higher oil and decent equities

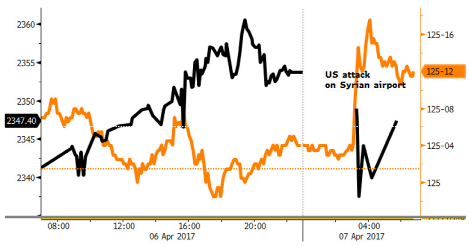
Yield changes limited though

	US yield	-1d
2	1,22	-0,01
5	1,83	-0,02
10	2,31	-0,02
30	2,96	-0,02

	DE yield	-1d
2	-0,78	0,02
5	-0,45	0,01
10	0,26	0,01
30	1,04	-0,01

Yesterday, global core bonds moved according to script until European noon. Equity and oil prices gradually rose, pulling Bunds and US Treasuries somewhat lower. ECB's Draghi urged that it's too early to speculate on an ECB exit as the central bank needs sufficient confidence that inflation converges to the ECB objective. Apart from some minor losses for the euro, markets ignored his comments. **During US trading, core bonds again showed their recent resilience. They changed direction, even if intraday trends higher on stock and commodity markets were extended.** On top, US weekly jobless claims unexpectedly declined towards the cycle low and **ECB Minutes showed that divergence inside the ECB is larger than president Draghi indicated in the morning.** They eventually decided to keep forward guidance unchanged as changing it could backfire on markets. **SF Fed governors Williams** confirmed that the Fed could start winding down its balance sheet towards the end of the year, something which was revealed when the Minutes were published Wednesday eve.

In a daily perspective, the German yield curve marginally bull flattened with yield changes ranging between +1.7 bps (2-yr) and -0.9 bps (30-yr). Changes on the US yield curve varied between 1.2 bps (2-yr) to 2.3 bps (30-yr). **On intra-EMU bond markets,** 10-yr yield spread changes versus Germany moved between -5 bps (Ireland/Portugal) and +1/2 bps (Spain/Greece). **The French debt agency successfully launched a new 10-yr OAT, while the Spanish auction was plain vanilla. French bonds slightly outperformed their Belgian peer (10y).**



US T-Note future (orange) and S&P future (black): Treasuries resistance rebound in equities. Overnight up on US missile attack.

US 10yr yield at key yield support after US attack on Syrian airport and ahead of payrolls. Testing times!!!

All attention for the March US payrolls

Slight upward risks payrolls

Payrolls started 2017 on a strong note with employment gains of 238K and 235K in January and February, which signalled an acceleration from Q4 2016 average of about 150K. We expect that the labour market remained healthy in March, but somewhat less buoyant. Indeed, the increases in January/February might have been partly helped by unusual mild seasonal weather conditions. So, construction and manufacturing may be sources of some moderation. The ISM and the Markit manufacturing PMI employment sub-indices though gave contradictory signals. **The market expects a 180K net job gains.** We got some divergent signals with a bumper ADP private employment report, but an easing of the Non-manufacturing ISM employment sub-index and some increase in the relevant initial claims statistics (even if these might have been distorted on the upside given the sharp drop in the last week's claims).

Regional labour market indications remained strong. So, **we would nevertheless put the risk somewhat to the upside of expectations** with the 6m and 12m average of 195K as our guesstimate. The unemployment rate might have stabilized at 4.7%, while we hope to see earnings to have stabilized at 2.8% Y/Y (consensus 2.7% Y/Y).

Important test of bond sentiment with US payrolls

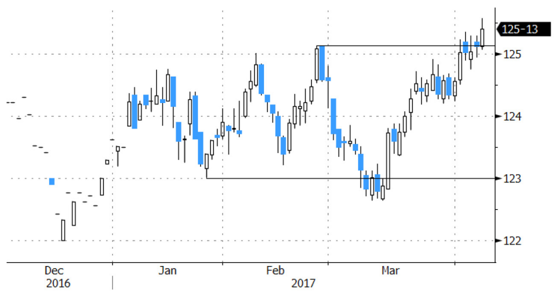
R2	164,40	-1d
R1	163,12	
BUND	162,77	0,20
S1	158,28	
S2	157,28	

Overnight, risk sentiment deteriorated after the US launched a missile attack against Syria. The US Note future spiked higher with the US 5-yr (1.8%) and 10-yr (2.3%) yields testing key support. A break didn't occur. Rising oil prices partly dampened the gains. We still expect a higher opening for the Bund though.

The missile attack will grab the headlines at the onset of dealings, but we don't expect risk aversion to go far. **Later, focus turns to US payrolls. Risks are on the upside with expectations.** The unemployment rate and average hourly earnings will also be closely monitored. **We expect the overall report to be strong enough to reinforce the lower boundary (in yield terms) of sideways trading ranges for the 5-yr yield (1.8%-2.14%) and 10-yr yield (2.3%-2.64%). The test of these bottom levels could be used to offload bonds or position for higher rates.** Markets still have to align with the Fed's tightening scenario and didn't take into account effects of the start of the run-off the balance sheet ahead of the year-end. **Our hypothesis will be tested in case of a disappointing outcome.** Nevertheless, even in that scenario, we expect the Fed to proceed with monetary normalisation as planned with eventually higher US yields as a result.

The German 10-yr yield is declining in a similar sideways range (0.2%-0.5%). We take a same approach as for US Treasuries and don't anticipate a decline below 0.2%.

German Bund: More upside as German 10-yr yield slides towards 0.2% support



US Note future: new contract high as US 10-yr yield tests 2.3%. We don't expect technical breaks.

Currencies

USD going nowhere ahead of the payrolls

Dollar regained marginally ground, counting down to the US payrolls report

The dollar regained slightly ground against the euro and the yen yesterday after Wednesday's soft market reaction to the March Fed Minutes. EUR/USD dropped briefly on soft Draghi comments early in Europe, but the pair soon returned to wait-and-see modus ahead of today's US payrolls. The pair closed the session at 1.0644 (from 1.0663). USD/JPY reversed early losses to finish the session at 110.81 (from 110.70).

Asian markets hit by risk-off reaction on US strike against Syria

Yen attracts safe have bid, but reaction in major USD cross rates remains modest.

Overnight, Asian markets were hit by a (temporary?) risk-off reaction as the US executed a missile strike against Syria in response to the use of chemical weapons. Markets followed the 'standard risk-off procedure'. Equities and US bond yields declined. The yen rebounded. The oil price jumped also higher as markets feared more instability in the region. **However, the reaction was limited and an important part of the moves is already reversed at the time of writing.** Several Asian equity markets including Japan returned already in positive territory. USD/JPY dropped close to the recent low in the low 110 area, but the test was again rejected (currently 110.60). The moves in EUR/USD were very limited. The pair is holding a narrow range in the mid 1.06 area.

US payrolls the eye-catcher for USD trading today.

Impact of Syria to be limited?

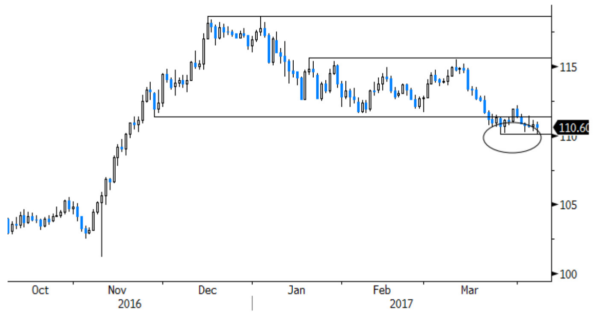
Will payrolls be strong enough to support US yields and the dollar?

Today, there are plenty of second tier eco data. However, except for the fall-out from the Syria strike, focus of (FX) trading will be on the US payrolls. Payrolls started 2017 on a strong footing (238K and 235K in January and February). We expect an ongoing healthy labour market in March, but somewhat less buoyant. **The market expects a 180K net job gains.** Other labour market indicators gave some mixed signals of late. Still, we **put the risk somewhat to the upside of expectations** with the 6m and 12m average of 195K as our guesstimate. The unemployment rate might have stabilized at 4.7%, while we hope to see earnings to have stabilized at 2.8% Y/Y (consensus 2.7% Y/Y).

R2	1,1145	-1d
R1	1,0906	
EUR/USD	1,0653	-0,0018
S1	1,0341	
S2	1,0000	

Of late, US bond yields drifted back to key support levels and this also weighed on the dollar. Our base scenario of in-line to slightly better than expected payrolls, should be good enough to prevent a sustained break lower of US yields and of the dollar. USD/JPY remains vulnerable to a downside test in case of a weak payrolls report. However, **as we don't expect a sustained decline of US yields beyond key support levels(10-j < 2.30%), a real USD sell-off is unlikely.** EUR/USD didn't show clear dynamics this week. We expect the topside to be rather well protected, even in case of a soft payrolls report.

EUR/USD: perfectly calm going into the US payrolls release



USD/JPY struggles not the fall below the key 110 area.

Last week, the dollar decline slowed, but the subsequent rebound had no strong legs as US yields remain relatively low near key support levels. The Fed Minutes didn't help the dollar even as the Fed confirmed its **intention to continue policy normalization.** The (FX) market apparently anticipates that reducing the balance sheet might slow the pace of Fed rate hikes. Both measures could go hand in hand if the US economy remains on track. **In any case, further down the road, US monetary policy conditions will most likely be tightened which should be USD supportive.**

From a technical point of view, USD/JPY last week failed to regain the 111.36/60 previous range bottom. A decline below 110 would signal more trouble ahead. We remain cautious on USD/JPY ST and first want a clear sign that a solid bottom is in place. **EUR/USD extensively tested the topside of the MT range, but the test was rejected last week. The 1.0874/1.0906 area now looks a solid resistance. EUR/USD might return lower in the previous 1.0875/1.05 trading range.**

Sterling stays in consolidation modus

R2	0,8881	-1d
R1	0,8854	
EUR/GBP	0,8540	-0,0008
S1	0,8403	
S2	0,8304	

Yesterday, sterling was driven by non-UK factors and technical considerations. EUR/GBP spiked briefly lower to the 0.8510/15 area on the Draghi headlines early in the European trading. As was the case for EUR/USD, the decline was almost immediately reversed. EUR/GBP hold a tight range in the mid 0.85 area further out (close at 0.8537 from 0.08542). Cable finished sideways at 1.2470.

Today, the UK calendar is well filled with The Halifax House prices, the production and the trade balance data. The production is expected to rebound after a poor reading in January. The trade deficit is expected more or less stable after a tentative better performance of the previous months. A further narrowing of the trade deficit might be slightly sterling supportive. BoE governor Carney will speak in London. If he says anything on the economy or on monetary policy we expect him to stress the uncertainty of the Brexit process and avoid any signal about policy tightening. **Mid-March, sterling found a better bid after** higher than expected UK inflation and a more hawkish tone from the BoE. **We changed our short-term bias on EUR/GBP from positive to neutral. The EUR/GBP 0.88/0.84 range should guide trading for now. Since late last week, the sterling rally/short-squeeze shows tentative signs of running into resistance, but we see no trigger for a real change in sentiment yet. Longer term,** Brexit-complications remain a potential negative for sterling. We are not convinced that the BoE will raise rates anytime soon, even not after recent higher inflation data.

EUR/GBP sterling short-squeeze is easing, but no sustained sterling correction yet

GBP/USD: sterling rally slows even as USD is also losing momentum

Calendar

Friday, 7 April		Consensus	Previous
US			
14:30	**Change in Nonfarm Payrolls (Mar)**	**180**	**235k**
14:30	Change in Private Payrolls (Mar)	170k	227k
14:30	Change in Manufact. Payrolls (Mar)	17k	28k
14:30	**Unemployment Rate (Mar)**	**4.7%**	**4.7%**
14:30	**Average Hourly Earnings MoM / YoY (Mar)**	**0.2%/2.7%**	**0.2%/2.8%**
14:30	Average Weekly Hours All Employees (Mar)	34.4	34.4
Canada			
14:30	Unemployment Rate (Mar)	6.7%	6.6%
14:30	Net Change in Employment (Mar)	5.7k	15.3k
China			
	Foreign Reserves (Mar)	$3007.5b	$3005.1b
UK			
09:30	Halifax House Price M/M 3Mths/Year (Mar)	0.4%/4.0%	0.1%/5.1%
10:30	**Industrial Production MoM / YoY (Feb)**	**0.2%/3.7%**	**-0.4%/3.2%**
10:30	Manufacturing Production MoM / YoY (Feb)	0.3%/3.9%	-0.9%/2.7%
10:30	Construction Output SA MoM / YoY (Feb)	0.1%/1.9%	-0.4%/2.0%
10:30	Visible Trade Balance GBP/Mn (Feb)	-£10900	-£10833
14:00	NIESR GDP Estimate (Mar)	0.6%	0.6%
Germany			
08:00	Industrial Production SA MoM / WDA YoY (Feb)	-0.2%/0.5%	2.8%/0.0%
08:00	Trade Balance (Feb)	17.7b	14.8b
08:00	Current Account Balance (Feb)	19.1B	12.8b
08:00	Exports SA MoM (Feb)	-0.5%	2.7%
08:00	Imports SA MoM (Feb)	0.2%	3.0%
France			
08:45	Trade Balance (Feb)	-4900m	-7940m
08:45	Industrial Production MoM / YoY (Feb)	0.5%/1.4%	-0.3%/-0.4%
08:45	Manufacturing Production MoM / YoY (Feb)	0.9%/0.9%	-1.0%/-1.3%
Italy			
10:00	Retail Sales MoM YoY (Feb)	-0.2%/0.5%	1.4%/-0.1%
Norway			
08:00	Industrial Production manufacturing MoM / WDA YoY (Feb)	0%/--	0.2%/-0.9%
Events			
10:00	Riksbank's Olsson Gives Speech		
11:00	BoE Carney speaks in London		
18:15	Fed Dudley speaks on financial regulation in NY		

10-year	td	-1d		2-year	td	-1d	Stocks	td	-1d
US	2,31	-0,02		US	1,22	-0,01	DOW	20662,95	14,80
DE	0,26	0,01		DE	-0,78	0,02	NASDAQ	5878,95	14,47
BE	0,77	-0,01		BE	-0,56	0,00	NIKKEI	18664,63	67,57
UK	1,10	0,01		UK	0,13	0,01	DAX	12230,89	13,35
JP	0,05	-0,01		JP	-0,21	-0,01	DJ euro-50	3489,57	16,99
IRS	**EUR**	**USD**	**GBP**	**EUR**	**-1d**	**-2d**	**USD**	**td**	**-1d**
3y	-0,05	1,72	0,67	Eonia	-0,3530	-0,0010			
5y	0,15	1,94	0,81	Euribor-1	-0,3720	0,0010	Libor-1	0,9856	-0,0006
10y	0,71	2,29	1,14	Euribor-3	-0,3300	-0,0010	Libor-3	1,1504	0,0006
				Euribor-6	-0,2420	-0,0010	Libor-6	1,4229	-0,0028
Currencies	**td**	**-1d**		**Currencies**	**td**	**-1d**	**Commodities**	**td**	**-1d**
EUR/USD	1,0653	-0,0018		EUR/JPY	117,68	-0,15	CRB	186,78	0,63
USD/JPY	110,47	0,05		EUR/GBP	0,8540	-0,0008	Gold	1266,50	10,50
GBP/USD	1,2475	-0,0009		EUR/CHF	1,0697	-0,0013	Brent	55,60	1,53
AUD/USD	0,7524	-0,0018		EUR/SEK	9,6013	0,0123			
USD/CAD	1,3403	-0,0038		EUR/NOK	9,1656	-0,0195			

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