Sunrise

Tuesday, 09 February 2016

Rates: Risk aversion lifts core bonds to new highs

Overnight, risk sentiment in Asia remains negative with lower US rates, a stronger yen and weak equities. Risk sentiment and technical factors will continue to drive trading. Both the Bund and the US Note future are heavily overbought, making them vulnerable for bouts of short term profit taking if risk sentiment improves. At this stage, that's not the case.

Currencies: yen strengthens below key USD/JPY 115.98

The yen continues to strengthen as global risk sentiment deteriorates further. The euro and the dollar are more or less in balance. The jury is still out which one might be the second best after the yen. Financial stability issues and a widening of peripheral spreads might be negative for the euro. Sterling set a new short-term correction low against the euro.

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** showed broad-based losses yesterday with S&P closing at its lowest level in nearly two years. Materials and financials were hit the hardest. The sell-off spreads to **Asia** this morning with Japanese shares hit the hardest (-5%), while Chinese markets remain closed for the Lunar New Year holidays.
- **Crude oil prices remain under pressure** with both the Brent and WTI trading lower for a fourth consecutive session this morning. The WTI oil price fell back below $30/barrel as oversupply continues to weigh. **Gold prices**, on the contrary, extended their rally showing the biggest one-day gains in more than a year to close at its highest level in almost eight months.
- ECB's Coeure said yesterday the **euro zone's economic recovery is primarily driven by ECB action and low oil prices** and added that they are thinking about which assets and how much they can buy. Coeure also warned that emerging market economies risk further depreciation of their currencies and will be addressed in a coordinated manner.
- **Japan's benchmark 10-year government bond yield dropped below zero this morning** as Japanese shares dropped more than 5% and the yen rose sharply. The move comes less than two weeks after the central bank introduced negative interest rates.
- **Growth in British retail spending hit a four-month high in January** as consumers splashed out on big-ticket items like furniture, the BRC said today. BRC like for like retail sales accelerated to 2.6% Y/Y in January from 0.1% Y/Y in December, while only a marginal pick-up was expected.
- Today, the **eco calendar** contains the **US NFIB small business confidence indicator**, **US JOLTS job openings** and **UK visible trade balance. In the US, New Hampshire holds Presidential Primary elections.**

Rates

Core bonds are king in horror land

Savage liquidation of riskier assets

Core bonds gain

Central bank rate expectations pushed out far in the future

At last also peripheral bonds came under pressure

Technical picture equities deteriorates

	US yield	-1d
2	0,6542	-0,0878
5	1,1175	-0,1518
10	1,6988	-0,1644
30	2,5294	-0,1616

	DE yield	-1d
2	-0,5310	-0,0430
5	-0,2850	0,0273
10	0,2160	-0,0720
30	0,8949	-0,1051

Accumulation of multiple risks

Immigration in Europe besides Brexit, Spain, Portugal and Greece

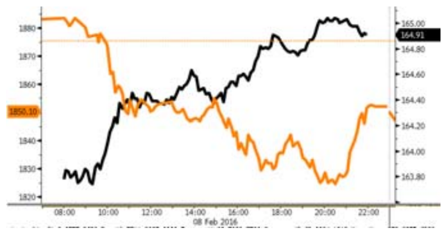
China the big black hole

EM dollar debt

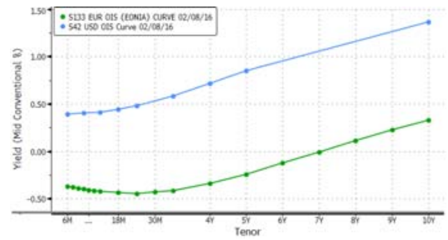
Global core bonds had another very strong run as panic in riskier markets spread rapidly and might turn into crisis anytime, or did we witness an exhaustion move? We didn't find a serious trigger to explain the moves. The eco calendar was empty and events were few. Yes, there was some bad news on Greece again, but that shouldn't cause panic worldwide. Yes, there were rumours about a big German bank running out of cash (going forward) and the NY Fed inflation survey showed slightly declining inflation expectations, albeit at still rather high level. **It is more simply general confidence that is flowing away at high speed. The realisation that asset prices are once again out of line with the economic environment that reasonably can be expected in the next few years.** Moreover, there is the feeling that central bankers, who were also the loyal servant of markets are out of bullets and ideas. **The ECB experiments with negative rates, as if it is doing an innocent chemical experiment somewhere in the backyard during a BBQ. The Fed's dot plot with 4 rate hikes in 2016 looks comical.** In the meantime, political and geopolitical risks are rising. In Europe, migration is fast unravelling the fundament of open frontiers. In the UK, Brexit may well end up with the country leaving the EU. Portugal is reversing its economic policy, Italy has to cope with its banks, Spain has no government and Catalonia is ever closer to independence. **Not to mention Greece…**

In the US, there is the tail risk that the presidential elections will go between two outsiders with ideas that don't bode well for the role of the US and stability in the world. The oil war may become another war in the Middle East between Iran and Saudi. Finally, China faces a transition of its economy that few countries have succeeded in the past while EM firms drown in dollar debt. **All this occurs in a context where the BIS admits that the regulation of the banking sector has inevitably affected the available liquidity in many markets. Examples are plenty. Corporate credit spreads are rapidly moving higher and so are peripheral spreads. Dollar liquidity is becomes expensive (45 bps between Euribor and US libor). The technical picture of major equity markets is rapidly deteriorating. All these recent movements smell like crisis.** ECB Coeuré said that the G-20 will address the weakness of EM which risk triggering further depreciation of their currencies. **Let's see whether the selling wave of riskier assets like equities, very prominent this morning in Japan, continues. The Japanese 10-yr yield fell below zero for the first time ever. Market technically, we might have witnessed an exhaustion move yesterday which could be followed by an uneasy calm for some time to come. Volumes were very high in equity and core bond future markets for a Monday.**

In a daily perspective, the German yield curve bull flattened with yields 1.8 bps (2-yr: -0.51% new low) to10 bps (30-yr: 0.90%) lower. Changes on the US yield curve ranged between -5.6 and -9.2 bps. Markets only discount another Fed rate hike in 2-years' time and further out see the rate at 1.43% in 5-years' time. On intra-EMU bond markets, peripheral yield spreads widened significantly after staying remarkably stable during the volatile start of the year. The Greek spread increased by 69 bps. The Portuguese spread widened by 33 bps and Italian/Spanish spreads added 19/20 bps. Semi-core spreads added 4-5 bps.



Bund future (black) and S&P future (orange):Bund surges as investors liquidate riskier assets and seek shelter in "safe haven" Bunds



Eonia and US OIS curves: Very low expectations on central bank rates going forward: Next US tightening expected by end …2017. First really positive overnight rate mid 2019

Today: Risk sentiment on stock markets key

R2	166	-1d
R1	165,06	
BUND	**164,91**	0,9700
S1	160,38	
S2	156,4	

Overnight, most Asian equity markets remain closed (including China). Other indices trade up to 2% lower with Japan significantly underperforming on the back of JPY strength. The Nikkei loses more than 5%. The US Note future continues his march higher, suggesting a stronger opening for the Bund as well.

Today's eco calendar remains rather unexciting with only US NFIB small business optimism and JOLTS Job openings. Apart from tomorrow's Yellen testimony and Friday's retail sales, the calendar isn't that enticing later this week either. **This means that risk sentiment and technical factors will continue drive trading.** European equity markets lost another important support level, suggesting more downside (risk aversion, positive core bonds). The S&P 500 is still testing crucial support. The recovery of oil prices remains tough going and no immediate treat for the Bund. So longer term sentiment remains positive for core bonds (also taking into account the technical picture; see below), but both the Bund and the US Note future are heavily overbought, which make them vulnerable for **bouts of short term profit taking is risk sentiment improves**.

Technically, the German 10-yr yield fell below final support (0.42%). Weakness in equity market/oil prices and the dovish turn of global central banks (ECB, BoE, BoJ and Fed) pulled yields lower since the start of the year. **The break lower opens the way for a complete retracement towards the all-time low at 0.05%. The US 10-yr yield dropped below 1.9%. From a technical point of view, this also suggests more downside towards 1.64%.**

German Bund: Technically overbought. Vulnerable to profit taking?

US Note future: Also overbought. Too dovish ahead of Yellen speech?

Currencies

Dollar and euro in balance as risk-off trade intensifies

Currency trading shifts into crisis modus. The yen remains the preferred safe haven .

The jury is still out whether the dollar or the euro will take the role of second best

On Monday, global markets slipped again in outright risk-off modus even as Chinese markets were closed. On the currency market, the yen obviously remained the preferred safe haven currency. USD/JPY dropped below the key 115.98 support and closed the session at 115.85 (from 116.87 on Friday). Initially, the dollar rather than the euro was the preferred second best. EUR/USD dropped temporary below 1.11 but rebounded later as the US equity sell-off accelerated. EUR/USD closed the session at 1.1193 (from 1.1158 on Friday). So, the jury is still out on which currency will be the second best among the majors to take up a safe haven role. The trade-weighted dollar reversed an earlier rebound and closed the session in the red.

Japanese equity markets suggest a continuation of the risk-off trade

USD/JPY extends decline below 115.98 support.

This morning, a lot of Asian markets are still closed for the Lunar New Year holidays. Japanese markets are again in very rough weather. Japanese equity indices show losses of about 5%. The 10-year government bond yield dropped below 0%. The yen strengthens further after yesterday's break below the USD/JPY 115.96 support. The pair trades currency at 114. 75. Brent oil hovers near $ 33 p/b but the losses are moderate given the wild swings on markets. The same conclusions applies for commodity currencies like the Aussie dollar (AUD/USD currently 0.7035) and Canadian dollar (CAD/USD at 1.3950). EUR/USD trades marginally higher at 1.1205.

There are again few eco data with market moving potential on the agenda today

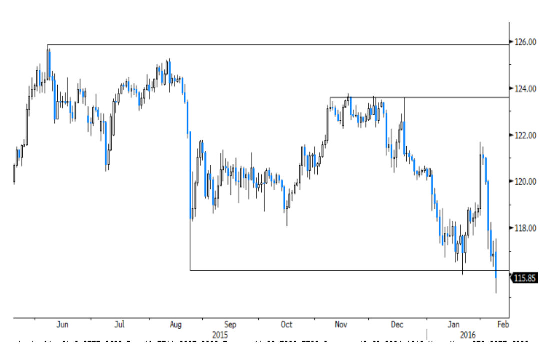
Risk-off sentiment will probably continue to dominate trading

Today, the calendar is thin. In the US, NFIB small business confidence, JOLTS job report and wholesale inventories will be released. A big negative surprise can reinforce the negative ST momentum, but we don't see a lasting impact on USD trading. Global factors will again set the tone for currency trading.

Global sentiment on risk will probably be driven by headlines on the stress in the financial sector. Over the previous days, intra-EMU government bond spreads also widened in a substantial way. On the other hand, interest rate differentials between the dollar and the euro might narrow further as markets price out the chances of more Fed tightening. **It's difficult to assess the relative weight of both factors for the EUR/USD balance. However, with important pockets of rising financial stress coming to the surface, we don't see a big case for the euro to be a better safe haven than the dollar**. Ever deeper negative interest rates are also no help for the euro. The jury is still out and currency markets made some wild, chaotic swings of late. However, we don't see a big case for big sustained euro gains.

R2	1,1495	-1d
R1	1,1246	
EUR/USD	**1,1202**	0,0066
S1	1,106	
S2	1,081	

EUR/USD: no clear trend as global risk-off trade intensifies



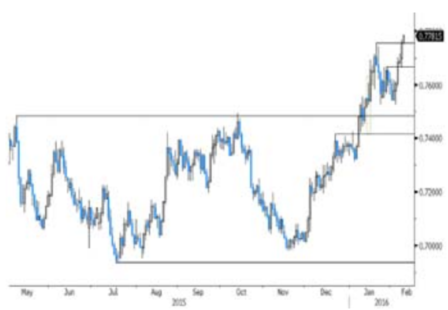
USD/JPY drops below key support

From a technical point of view, EUR/USD broke above the 1.1060/1.1124 resistance area (15 Dec top: 62% retracement). This is a dollar negative. The short-term correction high stands at 1.1246. Next important resistance kicks in at 1.1495.The jury is still out, but we have think that the EUR/USD rebound might be topping out. **The picture for USD/JPY improved temporarily as the pair rebounded above 120 after the BoJ easing two weeks ago. However, the gains evaporated very soon. The pair yesterday even dropped below the key 115.98 pre-BOJ correction low. This a high profile warning signal. We expect the BOJ to send warning signals. However, for now there is no good reason to fight current yen strength as long as global uncertainty persists.**

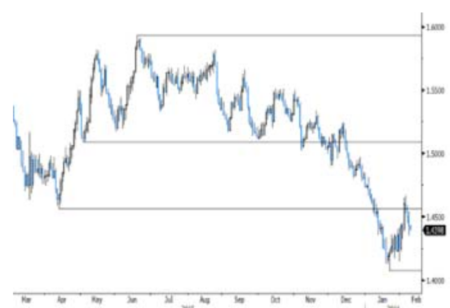
Global sell-off continues to weigh on sterling

R2	0,8066	-1d
R1	0,7854	
EUR/GBP	**0,7771**	0,0096
S1	0,7525	
S2	0,7313	

There were no important UK eco data yesterday. **Global risk-off sentiment weighed again heavily on the UK currency.** This was in the first place visible in cable. The pair traded in the 1.4545 area just before the open of the European markets, but at some point lost almost 2 big figures. In volatile trading, the pair closed the session at 1.4433 (from 1.4503). In the global risk-off trade, cable again underperformed EUR/USD (even as EUR/USD dropped temporary around noon). EUR/GBP rebounded to the key 0.7756 resistance and closed the session at 0.7767 (from 0.7670). Uncertainty on Brexit apparently still makes sterling an easy victim when risk sentiment plummets.



EUR/GBP: set new ST high above 0.7756



GBP/USD: risk-off weighs more on sterling than on the dollar

This morning, the BRC sales (like-for-like) were reported at 2.6.% Y/Y in January, much strong than expected (consensus 0.3% Y/Y). However, the report didn't help sterling much. EUR/GBP still trades in the 0.7775 area. **Later today**, the UK foreign trade data will be published. The December trade deficit is expected little changed from November. We don't have a strong reasons to take a different view from the consensus. A weaker figure might be a slight additional negative for sterling. We don't expect sentiment on sterling to improve in a sustained way even not in case of better than expected trade data. Global factors will continue to set the tone for sterling trading. For now, it looks that the context remains sterling negative. We maintain the view that a sustained comeback of sterling will be difficult as long as there is no clear sign how the Brexit debate will turn out. **The medium term technical picture of sterling against the euro remains negative as EUR/GBP broke above the 0.7493 Oct top. Next big resistance stands at 0.7854/75.** A return below EUR/GBP 0.74 would be a first indication that sterling enters calmer waters.

Calendar

Tuesday, 9 February		Consensus	Previous
US			
12:00	**NFIB Small Business Optimism (Jan)**	**94.5**	**95.2**
16:00	**JOLTS Job Openings (Dec)**	**5350**	**5431**
16:00	Wholesale Inventories MoM (Dec)	-0.1%	-0.3%
Japan			
00:50	Money Stock M2 YoY (Jan)	A: 3.2%	3.0%
00:50	Money Stock M3 YoY (Jan)	A: 2.5%	2.5%
07:00	Machine Tool Orders YoY (Jan P)	A: -17.2%	-25.7%
UK			
01:01	BRC Sales Like-For-Like YoY (Jan)	A: 2.6%	0.1%
10:30	**Visible Trade Balance (Dec)**	**-£10400**	**-£10642**
10:30	Trade Balance (Dec)	-£3000	-£3170
Germany			
08:00	**Industrial Production SA MoM/WDA YoY (Dec)**	**A: -1.2%/-2.2%**	**-0.3%/0.1%**
08:00	Trade Balance (Dec)	A: 18.8b	20.6b
08:00	Exports SA MoM (Dec)	A: -1.6%	0.4%
08:00	Imports SA MoM (Dec)	A: -1.6%	1.6%
Events			
10:30	BoE's Cunliffe Speaks at Conference in London		
Austria	**Bond Auction (€1.1B 1.2% Oct2025, 3.15% Jun2044) (11:00)**		
Germany	**I/L Bund Auction (€0.5B 0.1% Apr2046) (11:30)**		
UK	Gilt Linker auction (£1.3B 0.125% Mar2026) (11:30)		
US	**3Yr Note Auction ($23B) (19:00)**		
	Quarterly earnings release from Coca-Cola (Bef-Mkt), Walt Disney (22:15), UniCredit		

10-year	td	- 1d	2 -year	td	- 1d	STOCKS		- 1d
US	1,70	-0,16	US	0,65	-0,09	DOW	16027	16027,05
DE	0,22	-0,07	DE	-0,53	-0,04	NASDAQ	or Exch - NQI	#VALUE!
BE	0,56	-0,04	BE	-0,41	-0,02	NIKKEI	16085	16085,44
UK	1,42	-0,14	UK	0,26	-0,09	DAX	8979,36	8979,36
JP	-0,01	-0,06	JP	-0,27	-0,06	DJ euro-50	2785	2785,17

							USD	td	-1d
IRS	EUR	USD (3M)	GBP	EUR	-1d	-2d	Eonia EUR	-0,242	-0,006
3y	-0,130	0,843	0,814	Euribor-1	-0,23	0,00	Libor-1 USD	0,51	0,51
5y	0,050	1,089	0,987	Euribor-3	-0,17	0,00	Libor-3 USD	0,59	0,59
10y	0,600	1,600	1,432	Euribor-6	-0,10	0,00	Libor-6 USD	0,74	0,74

Currencies		- 1d	Currencies		- 1d	Commoditie	CRB	GOLD	BRENT
EUR/USD	1,1202	0,0066	EUR/JPY	128,62	-2,09		161,9322	1191,1	32,81
USD/JPY	114,83	-2,57	EUR/GBP	0,7771	0,0096	- 1d	-1,52	26,50	-1,54
GBP/USD	1,441	-0,0095	EUR/CHF	1,1031	-0,0037				
AUD/USD	0,7039	-0,0054	EUR/SEK	9,4645	0,04				
USD/CAD	1,3940	0,0064	EUR/NOK	9,6122	0,07				

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