



Sunrise

Wednesday, 21 October 2015

Core bonds hit the skids: simple profit taking

No specific reason behind the day-long slide of core bonds. Profit taking as the upside seemed blocked is the best explanation, as equities had also a weaker season (limited losses) and FX trading was uneventful. Today, the calendar is nearly empty and with the ECB meeting ahead, we expect sideways trading. Will Portugal underperform?

Dollar shows mixed picture

Yesterday, there was no clear trend in the major USD cross rates. The dollar lost ground slightly against the euro, but remained well bid against the yen even as equities fell prey to profit taking. Today, more technical trading can be expected ahead of the ECB policy meeting. Sterling traders will keep an eye at a speech of BoE's Carney later today.

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	↗

- **European equities** closed yesterday's trading session with small losses, despite opening in the green for the fourth day in a row. **US equities** wrapped up with small losses after an uneventful trading day. Overnight, **Asian equities** are trading in the green, with the Japanese indices outperforming.
- **Japan reported another trade deficit in September**, with export up 0.6% and imports down 11.1%. A trade surplus of ¥87.0b was expected, but was undershot once again with a trade deficit of -¥114.5b..
- **Portugal socialists opposition leader, Antonio Costa**, said he **secured the backing** of two smaller leftist parties **to form a government** with majority support in the newly elected parliament.
- The commodities moves were limited yesterday, with **Brent Crude** sliding further down to **48.5\$/Barrel**, **but no significant movement regarding metals**, Gold up 0.5%, Platinum up 0.9% and Copper down -0.6%.
- Today the **market-calendar is nearly empty, with only the Bank of Canada deciding on its benchmark rate**. Later today, **BoE's Carney will speak** at an event. On the corporate calendar, **Boeing, Coca-Cola and General Motors** are releasing their **Q3 earnings**.

Rates

Core bonds hit the skids: simply profit taking?

Core bonds slump without a good cause. Profit taking ahead of ECB? Technical resistance holds (US/German bonds?)

Peripheral yield spreads stabilize

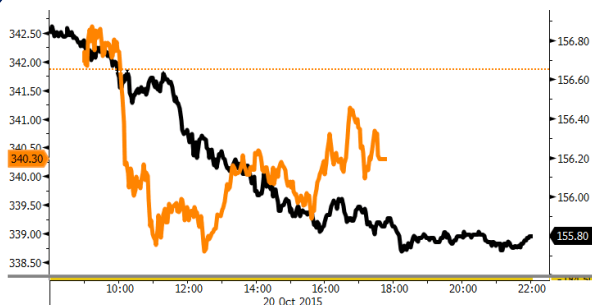
	US yield	-1d
2	0,6371	0,0445
5	1,3914	0,0541
10	2,0688	0,0513
30	2,9174	0,0433

Portuguese Socialists near forming government

	DE yield	-1d
2	-0,2270	0,0390
5	0,0170	0,0520
10	0,6370	0,0780
30	1,4090	0,0840

Yesterday, global core bonds were hard hit the whole day long, despite weaker European equities and a nearly empty calendar. We didn't find fundamental reasons for the sharp losses throughout the session. **The ECB lending survey was positive and thus Bund negative, but the decline started in earnest well after the release of the report. The selling continued also after mixed US starts & permits figures, but stopped around 4 pm CET.** We suspect that failure to test/take out important resistance (Bund/US Note future) and support (US 10-yr yield 2%), convinced some longs to take profit. Once the ball got rolling, more sellers jumped the bandwagon. The price action wasn't supported by equities either, which declined in Europe and treaded water in the US session. **Volumes were high in the Bund market and average in the US Treasury market.** In a daily perspective, US yields rose 4.2 bps (2-yr) to 5.5 bps (7-yr), the belly slightly underperforming. Changes on the German yield curve varied between +2.4 bps (2 yr) and +6 bps (8-yr and beyond). On intra-EMU bond markets, 10-yr yield spreads changes versus Germany were negligible.

Portuguese Socialist leader Costa said he has the backing of two smaller parties, the Left Bloc and the Communists, to form a minority government with sufficient support in the parliament. He asked the president to name him PM. It would put the centre-right alliance of outgoing PM Passos Coelho in the opposition. The Left Bloc leader confirmed the support of her party for a Socialist government, but the Communists didn't react yet. **Policy will thus become more centre-left instead of centre-right previously.** The Left parties dropped their insistence on seeking a debt restructuring, but apparently secured tax cuts and higher public sector salaries. The budget deficit would be trimmed at a slower pace. **From a market point of view,** such a government is less desirable, as there are many doubts on the solidity of the left alliance. New snap elections aren't excluded. **We will look closely to the Portuguese yield spread to see how markets assess such a constellation.** Of course, there are still hurdles to take before Mr. Costa will eventually be nominated Prime Minister.



Bund future (black) & EuroStoxx (orange): Bund hit whole day long in solid volume, regardless equity moves, suggesting profit taking was at work



US 10-year yield: 2% yield resistance too strong. Trigger for selling? .

Nearly empty calendar

BoC to stay put

R2	160,62	-1d
R1	157,67	
BUND	155,8	-0,9300
S1	155,21	
S2	153,5	

Today, the **market-calendar** remains thin, with only the **Bank of Canada's** policy decision. Consensus expects an unchanged policy rate (0.5%). We expect no rate change either, also because the new government is only just installed and has no firm programme yet (only policy intentions like an easier fiscal policy, which isn't immediately associated with a policy loosening). However, 1 out of 27 analysts estimates expects a cut.

More "strength" in Schatz auction?

The German Finanzagentur concludes this week's scheduled EMU bond supply by tapping the on the run 2-yr Schatz (€4B 0% Sep2017). Total bids averaged €6.47B at the previous 5 Schatz auctions. These short-term German auctions are the only ones who manage to get a decent bid (unlike Bobl and Bund auctions). Overall, we expect the auction to go well especially given the relatively low amount on offer for a Schatz auction.

Today: Waiting game continues

Overnight, most Asian stock markets trade positive with Japan outperforming despite weaker eco data (easing expectations in the run-up to key policy meeting at the end of the month?). The US Note future trades sideways, suggesting a neutral opening for the Bund.

Today's eco calendar remains thin with only the Schatz auction so it won't influence bond markets. **We keep a close eye at main US and EMU equity indices which are near (hard-to-break?!) resistance levels.** Profit taking in stock markets could trigger some safe haven flows. Yesterday's repositioning move on bond markets suggests that the Bund market is more neutrally positioned going into the ECB meeting. We continue to expect a very dovish tone from ECB Draghi, which should be supportive for the Bund. **Ahead of the outcome of the ECB meeting, we remain neutral for core bonds.**



German Bund: more neutrally positioned into ECB meeting. We still expect a very dovish tone from Draghi.



US Note future: Second test of August high also rejected

Currencies

USD trading still in wait-and-see modus

Dollar shows a mixed picture

R2	1,1714	-1d
R1	1,1495	
EUR/USD	1,13555	0,0024
S1	1,1306	
S2	1,1087	

Disappointing Japanese export data weaken the yen.

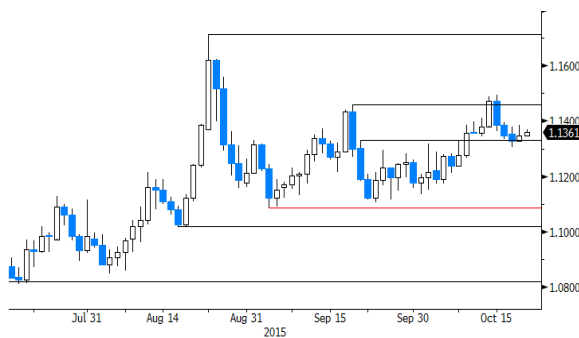
Yesterday, the risk-on rally ran into resistance. The losses on the equity markets were modest, but enough to halt the recent rebound of the dollar against the euro. The euro received also some support from an improvement in lending according to the ECB lending survey. EUR/USD ended the session slightly higher on a daily basis (1.1346 vs 1.1327 on Monday). Trading in USD/JPY was primarily order driven. The pair performed relatively well given the loss of momentum on the equity markets. It closed the session at 119.84 (from 119.50)

Overnight, the Japanese September trade balance showed a larger than expected deficit. Weaker than expected exports suggest rather poor global demand. This context might reinforce calls for more policy stimulation by the BOJ (and from other central banks). Asian equities mostly show modest gains with Japan outperforming and China underperforming. The yen is weakening with USD/JPY nearing the 120 level. EUR/USD is gaining a few ticks compared to yesterday's close and trades currently in the 1.1360 area.

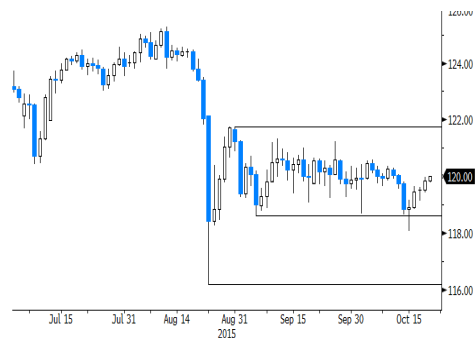
Eco calendar is empty

Sentiment on risk and prospect of ECB meeting to guide USD trading today

Today, the eco-calendar is again almost empty both in Europe and in the US. So, trading in major USD cross rates will again be at the mercy of global markets developments. Sentiment on risk is rather constructive this morning, supported by the hope that global stimulus will remain in place for longer. This is a mixed picture for the dollar. It should be fairly neutral for EUR/USD. Sentiment on USD/JPY might improve a bit further. However, we don't expect both cross rates to break out of the well-established ranges. With no high profile news on the agenda, markets will look forward to tomorrow's ECB policy meeting and press conference. Of late, several members indicated that it is too early to take action now. More sideways trading might be on the cards going into the ECB policy decision. We don't expect the ECB to take additional measures yet. Even so, the upside of EUR/USD might be rather well capped as ECB's Draghi will sound soft and lay the groundwork for more easing, maybe in December.



EUR/USD: correction halts



USD/JPY returning to the 120 area

In a longer term perspective, global markets struggle to assess the health of the global economy and its impact on monetary policy. Of late (currency) markets were focused on the impact of weaker US data on the Fed rate hike

path. This made the dollar vulnerable. However, in absence of key US eco data this week, attention turns to the ECB which may send a dovish message at its Thursday's meeting. The 1.1460/95 resistance was extensively tested, but the test was rejected. The jury is still out, but the topside in EUR/USD is better protected.. First support for EUR/USD stands at 1.11. In a longer term perspective, **if the policy divergence between the Fed and the ECB becomes less outspoken, EUR/USD may return toward the August correction high at 1.1719. USD/JPY looks more vulnerable to a delay in the Fed rate hike cycle in case of risk-off and/or rising volatility. However, for now global sentiment on risk remains quite constructive.**

R2	0,7493	-1d
R1	0,7373	
EUR/GBP	0,7354	0,0034
S1	0,7302	
S2	0,7196	

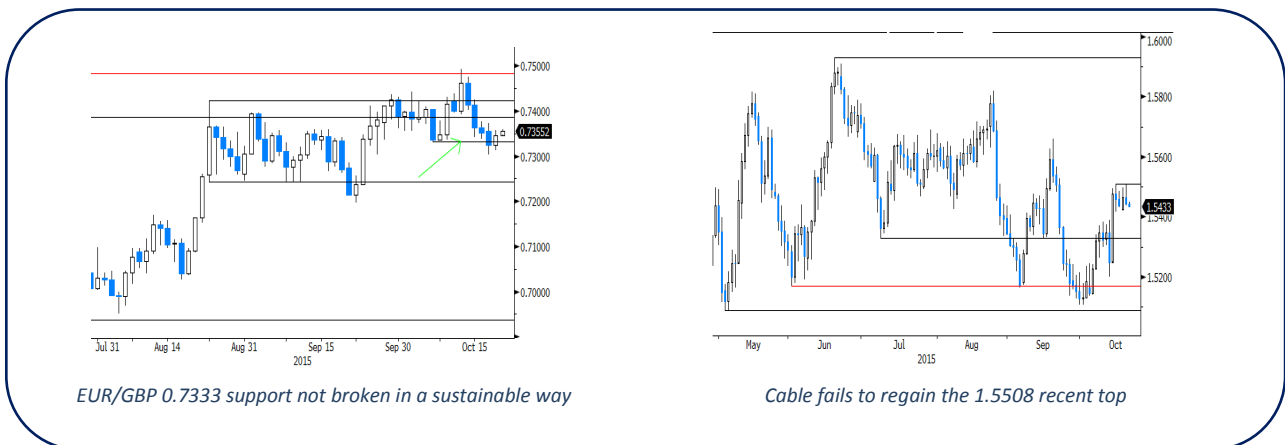
Sterling rebound slows

Sterling extends cautious rebound

Yesterday, Cable spiked higher early in European dealings. The pair approached the recent highs in the 1.5508 area. However, with no hard news to support the move, sterling strength evaporated soon. Cable dropped back below the 1.55 mark. EUR/GBP trended gradually higher, reversing part of Monday's decline. The move was in the first place technical in nature. BoE McCafferty maintained his hawkish tone as he said the BoE needs to avoid being behind the curve. However, the impact on sterling trading was limited. Cable couldn't sustain north of 1.55. EUR/GBP followed to a large extent the gyrations in EUR/USD. The pair rebounded to the 0.7350/55 area around noon. Early in US dealings, sterling trading remained erratic and confined to tight ranges. EUR/GBP closed the session at 0.7346 (from 0.7324). Cable ended the session little changed at 1.5444 (from 1.5447).

No clear technical signal yet

Today, the monthly UK public finance data will be published. The usually have only a limited impact on sterling trading, unless there is a big deviation from consensus. Later (7 pm CET), BoE governor Carney gives a speech in Oxford. At the same time, the BoE might release a report on how EU membership affects the central bank's policy framework. Comments from BoE governor Carney on this politically sensitive issue will probably be guarded. The debate on Brexit as such is a negative for sterling.



EUR/GBP 0.7333 support not broken in a sustainable way

Cable fails to regain the 1.5508 recent top

Looking at the broader picture, the downside in sterling (EUR/GBP 0.7483/0.75 strong resistance) looks better protected. At the same time, a dovish ECB might help to extend the recent decline in EUR/GBP short-term. **From a technical point of view,** EUR/GBP tries to sustain south of the 0.7333 short-term support. A drop below 0.7333 paints a sterling bullish double top on the charts, which could extend the decline in EUR/GBP towards 0.72 (tough resistance for sterling). Some further sterling gains against the euro might be on the cards short-term, but we expect the pair to maintain the established ranges.

Calendar

Wednesday, 21 October		Consensus	Previous
US			
13:00	MBA Mortgage Applications	--	-27.6%
Canada			
16:00	Bank of Canada Rate Decision	0.50%	0.50%
Japan			
01:50	Trade Balance (Sep)	A: -¥114.5b	-¥569.7b
01:50	Trade Balance Adjusted (Sep)	A: -¥355.7b	-¥358.8b
01:50	Exports YoY (Sep)	A: 0.6	3.1
01:50	Imports YoY (Sep)	A: -11.1	-3.1
06:30	All Industry Activity Index MoM (Aug)	A: -0.2%	0.2%
07:00	Supermarket Sales YoY (Sep)	A: 2.9%	2.0%
UK			
10:30	Public Finances (PSNCR) (Sep)	--	-0.2b
10:30	Central Government NCR (Sep)	--	0.2b
10:30	Public Sector Net Borrowing (Sep)	9.6b	11.3b
10:30	PSNB ex Banking Groups (Sep)	10.1b	12.1b
EMU			
11:00	Govt Debt/GDP Ratio (2014)	--	91.9%
Events			
11:30	Germany - German Schatz auction (€4B 0% Sep2017)		
14:00	Norway - Norway's Schanke speaks in Qatar		
19:00	UK – BoE Governor Carney speaks at event in Oxford, England		
19:30	US - Fed's Powell Moderates Panel on Markey Liquidity in New York		
Before market opening	The Boeing co. Q3 earnings release		
Before market opening	The Coca-Cola co. Q3 earnings release		
Before market opening	General Motors co. Q3 earnings release		

10-year	td	-1d	2-year	td	-1d	STOCKS	-1d
US	2,07	0,05	US	0,64	0,04	DOW	17217 17217,11
DE	0,64	0,08	DE	-0,23	0,04	NASDAQ	for Exch - NQJ #VALUE!
BE	0,95	0,07	BE	-0,18	0,02	NIKKEI	18593 18592,82
UK	1,86	0,03	UK	0,53	0,00	DAX	10147,68 10147,68
JP	0,32	0,00	JP	0,02	0,00	DJ euro-50	3256 3255,72

						USD	td	-1d	
IRS	EUR	USD (3M)	GBP	EUR	-1d	-2d	Eonia EUR	-0,139	0,003
3y	0,119	0,981	1,128	Euribor-1	-0,12	0,00	Libor-1 USD	0,51	0,51
5y	0,361	1,397	1,448	Euribor-3	-0,05	0,00	Libor-3 USD	0,58	0,58
10y	1,000	2,012	1,896	Euribor-6	0,02	0,00	Libor-6 USD	0,75	0,75

Currencies	-1d		Currencies	-1d		Commoditie	CRB	GOLD	BRENT
EUR/USD	1,13555	0,0024	EUR/JPY	136,25	0,90		196,7286	1175,7	48,56
USD/JPY	120,03	0,56	EUR/GBP	0,7354	0,0034	-1d	-2,72	6,19	-0,22
GBP/USD	1,5436	-0,0039	EUR/CHF	1,0851	0,0020				
AUD/USD	0,7262	-0,0005	EUR/SEK	9,4258	0,02				
USD/CAD	1,2975	-0,0061	EUR/NOK	9,2278	0,02				

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