Sunrise

Wednesday, 03 February 2016

Rates: Sentiment remains positive for core bonds

The US 10-yr yield fell below 1.9% and tested final (minor) support (1.82%) ahead of last year's low (1.64%). While short-term profit taking moves in overbought markets (both Bund and US Note future) are not excluded, sentiment remains positive for core bonds. Oil prices, risk sentiment and US eco data are key for trading today.

Currencies: USD/JPY returns below 120

Yesterday, the global risk-off trade and the decline in the oil price weighed on the dollar. USD/JPY was hit the most. The losses of the dollar against the euro were gain more modest. Today, the focus for USD trading will remain on global market sentiment. US data (ISM ADP) and oil inventories are a wildcard for USD trading.

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	→

- **Strong Google earnings failed to support US Equities** yesterday with both the S&P and Dow ending almost 2% lower. Energy shares were hit the hardest with the WTI oil price falling below $30/barrel. This morning, **the sell-off in Asia intensified with the Nikkei losing more than 3%.** Chinese stocks reversed their losses.
- **Activity in China's services sector expanded last month at its fastest pace in six months**, the Caixin services PMI showed this morning, rebounding from 50.2 to 52.4. The details show that employment rose at its fastest pace in six months and also new business edged up.
- **ECB's Mersch cautioned that investors shouldn't assume the bank will aggressively beef up its stimulus next month**, saying that no decision had been made and all options are on the table. The central banker added that it is not their communication which is flawed, but the hype that is being provoked by people with vested interests.
- **Oil prices dropped for a second straight session yesterday** with the WTI closing below the $30/barrel level after data showed that crude oil stocks surged to more than half a billion barrels.
- **Spain's King Filipe tapped Socialist leader Pedro Sanchez yesterday to try to form a government** following the inconclusive December election in which the conservative Popular Party came in first, but failed to drum up enough support for a coalition or minority government.
- Today, the **eco calendar is well-filled** with the euro zone (final) and UK services PMI, the euro zone retail sales, US **ADP employment report** and **US non-manufacturing ISM**. The European Commission releases its **Winter Economic Forecasts.**

Rates

Core bond rally extended

Core bonds rally on the back of weakness in stock and oil markets

US 10-yr yield below 1.9%

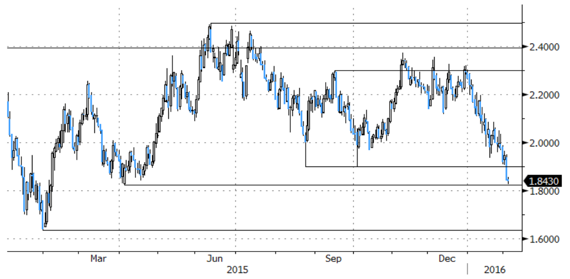
	US yield	-1d
2	0,7381	-0,0515
5	1,2664	-0,0842
10	1,8482	-0,0847
30	2,6589	-0,0879

	DE yield	-1d
2	-0,4840	-0,0190
5	-0,3141	-0,0230
10	0,3030	-0,0420
30	1,0364	-0,0452

Weakness in equity markets and declining oil prices took over command in bond markets yesterday. Monday's profit taking move proved to be a one-off. US Treasuries outperformed German Bunds. At the end of the day, the German yield curve shifted 0.9 bps (2-yr) to 4.4 bps (10-yr) lower. The US yield curve bull flattened with yields 7.9 bps (2-yr) to 10.5 bps (30-yr) lower. **The US 10-yr yield fell below the 1.9% support and tested a final (minor) hurdle (1.82%) before last year's low at 1.64% comes on the radar.** Hawkish comments by Fed George (voter) didn't weigh on US Treasuries. She said that *"the recent bout of volatility is not all that unexpected, nor necessarily worrisome, given that the Fed's low interest rate and bond-buying policies focused on boosting asset prices as a means of stimulating the real economy."* Therefore, it's no reason to further delay more rate hikes. *"If we wait for the data to provide complete confirmation before making a policy decision, we may well have waited too long."*

On intra-EMU bond markets, 10-yr yield spread changes versus Germany widened up to 2 bps with the periphery underperforming. The Spanish/Italian spread added 6 bps, the Portuguese one 10 bps and the Greek one 19 bps. In Spain, Socialist leader Pedro Sanchez was given a mandate to try to form a government. He will try to negotiate a potential government coalition in order to avoid new elections. The current political deadlock suggests that his chances are rather slim.

US Note future (black) and S&P future (orange): weakness on stock markets lifts bonds



US 10-yr yield: test of final hurdle (1.82%) before retracing towards 1.64%

Modest profit taking on overbought conditions

Upside risks for final EMU services PMI, US non-manufacturing ISM

Downside risks ADP employment

The eco calendar is interesting today with the final reading of **the EMU services PMI**, the **EMU retail sales,** US **ADP employment report** and **US non-manufacturing ISM.** According to the 1st estimate, the **EMU services PMI** dropped from 54.2 to 53.6 in January, while a stabilization was expected. Data from Germany and France were mixed with the German services PMI weakening significantly, while the French one rebounded. The final reading is expected to confirm the first outcome. Although revisions will probably be limited, we see risks for an upward surprise. **EMU retail sales** are expected to have rebounded slightly in December, rising by 0.3% M/M following three consecutive monthly declines. We continue to see downside risks following poor data from Germany, Portugal and Spain. Only French consumer spending picked up in December, following the Paris attacks in November.

In the **US, the non-manufacturing ISM** is expected to have declined slightly further in January, from 55.8 to 55.1. In December, the details were quite strong and the initial figure was also slightly upwardly revised. We believe therefore that the consensus might be too pessimistic. Finally, **ADP employment** will be interesting too ahead of Friday's payrolls. The consensus is looking for an increase in private sector employment by 193 000 from 257 000 in December. After strong hiring in the fourth quarter of last year, we believe it might slow somewhat early 2016. We see downside risks. Finally, the **EC's Winter Economic Forecasts** will be interesting too. We don't expect major changes in the GDP forecasts (respectively at 1.8% for 2016 and 1.9% for 2017), but inflation forecasts (currently at 1.0% for this year and 1.6% next) will probably be revised lower, especially for this year.

Ohn de German Bobl auction

Today, the German Finanzagentur launches a new 5-yr Bobl (€5B 0% Apr2021). On the grey market, the new Bobl trades with a 0.4 bps pick-up in ASW spread terms compared with the previous benchmark (0.25% Oct2020). That corresponds with a 5 bps pick-up in yield terms. Overall, we expect more weakness at this German auction given record low negative yields (even below ECB deposit rate!).

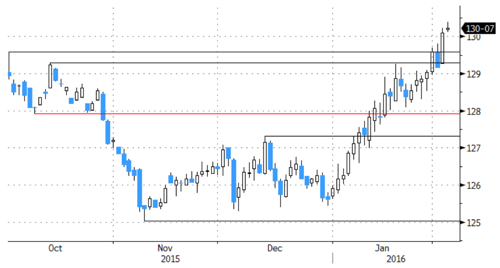
R2	165	-1d
R1	163,78	
BUND	**163,76**	0,6900
S1	160,38	
S2	156,4	

Bund remains in overbought conditions

Overnight, Asian equity indices lose ground like Europe and the US yesterday. Japanese stocks underperform on the back of a stronger yen. A strong Chinese services PMI couldn't turn the tide. The oil price trades stable around yesterday's low. The US Note future reached a minor new contract high.

Today's eco calendar heats up with final EMU services PMI, EMU retail sales, US ADP employment and US non-manufacturing ISM. Especially the US eco data could be relevant for markets. The outcome might be mixed, but in current sentiment especially negative surprises could leave traces on markets. **While short-term profit taking moves in overbought markets (both Bund and US Note future) are not excluded, sentiment remains positive for core bonds.** Weakness in equity market/oil prices and the dovish turn of global central banks (ECB, BoE, BoJ and Fed) pulled yields lower. **Technically, the German 10-yr yield fell below final support (0.42%). That opens the way for a complete retracement towards the all-time low at 0.05%. The US 10-yr yield dropped fell below 1.9%. From a technical point of view, this also suggests more downside towards 1.64%**

German Bund: dovish central banks give Bund another boost



US Note future: new high on the back of weakness on stock markets and a new slide of the oil price

Currencies

USD/JPY returns below 120 as oil declines

Dollar under pressure against the yen and the euro as oil and equities decline

R2	1,106	-1d
R1	1,0985	
EUR/USD	**1,0922**	0,0022
S1	1,0778	
S2	1,065	

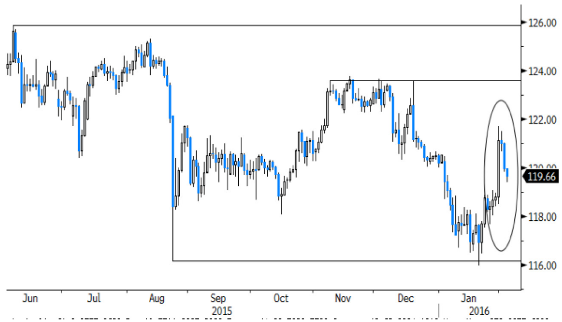
A new down-leg of the oil price was the dominant factor for global trading yesterday. There were hardly any in the US or in Europe. The oil-rout affected in the first place equities. However there was also a modest negative fall-out on the dollar. Especially USD/JPY was affected. Deepening losses on the US equity markets pushed the pair back to the 120 area. The pair closed the session 119.97 (from 120.99 on Monday). The losses of the USD against the euro were more modest. EUR/USD closed the session at 1.0919 (from 1.0888).

Asian markets stay in risk-off modus even as China services PMI improves

The dollar is losing further ground

The global equity sell-off continues on Asian markets this morning. The Caixin **China services PMI** succeeded a nice rebound from 50.2 to 52.4, but doesn't stop the bleeding. The PBOC set the CNY fixing marginally weaker against a relatively strong dollar. Still, the off-shore CNH weakens to USD/CNH 6.6420 currently, suggesting rising tensions. Brent oil is holding near yesterday's low. For now there are no additional losses. Even so, commodity currencies like the Aussie dollar are trending south. AUD/USD is nearing the 0.70 barrier. The yen profits from the risk-off context. USD/JPY is drifting further below 120 (currently in the 119.60 area). BOJ's Kuroda said that the BOJ can cut rates beyond minus 0.1% and that the Bank has ample room to expand stimulus. For now, the impact is limited. The loss of the dollar against the euro stays modest, even as interest rate differentials narrow. EUR/USD trades in the 1.0925 area.

EUR/USD gains a few ticks within a very tight sideways range



USD/JPY drops back below 120

The US data might give a mixed signal for USD trading
Tion

A disappointing ADP report might be an additional negative for the dollar.

Today, the eco calendar contains the final EMU services PMI's. In the US, the nonmanufacturing ISM and the ADP labour market report will be published. **The non-manufacturing ISM** is expected to have declined slightly further in January, from 55.8 to 55.1. We believe that the consensus might be too pessimistic. The **ADP employment** will also be interesting ahead of Friday's payrolls. The consensus is looking for private sector employment growth of 193 000, down from a strong 257 000 in December. After strong hiring in the fourth quarter of last year, we believe it might slow early 2016. So we see downside risks. **A poor labour market report might cause additional nervousness**. Also keep an eye at the interest rate differentials. Until now, declining interest rate differentials between the dollar and the euro had only a limited impact. However, if this narrowing continues, the euro might gradually come under further upward pressure. Last but not least, the US oil inventories might also be a wildcard for USD trading. So, looking at the developments in Asia this morning, we can only start the day with a cautious bias on the dollar. Will the 1.0985 resistance come under test? Or will global sentiment improve later today?

From a technical point of view, EUR/USD tried to break below the 1.08 barrier several times, but a sustained down-move didn't occur, leaving the pair in a very tight sideways consolidation pattern. Next support is at 1.0711/1.0650 (correction low, 76% retracement off 1.0524/1.1060) and at 1.0524. On the topside, 1.0985/1.1004 (reaction top) is a first reference. This level was left intact even as sentiment was outright risk-off before the ECB meeting. Next resistance comes in at 1.1060/1.1124 (15 Dec top: 62% retracement). We expect this resistance to be difficult to break. We look to sell EUR/USD on upticks for return action lower in the range. **The picture for USD/JPY improved temporarily as the pair rebounded above 120 after Friday's BOJ policy decision. However, the gains could not be sustained. We stay reluctant to position for further sustained USD/JPY gains as long as global uncertainty persists.**

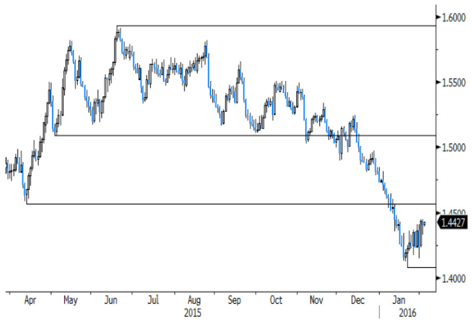
Sterling holding stable despite risk-off

R2	0,7755	-1d
R1	0,7666	
EUR/GBP	**0,7572**	0,0000
S1	0,7525	
S2	0,7313	

Yesterday, sterling hovered again up and down driven by conflicting signals. Early in the session, the British currency was pressured by lower oil and equities. The UK construction PMI was also weaker than expected at 55.0 (from 57.8). Sterling made a temporary comeback later, probably supported by headlines on a draft proposal from EU president Tusk on the new role of the UK within the EMU. During the US session, the focus turned again to the oil-driven risk-off correction, hampering the sterling rebound. EUR/GBP closed the session at 0.7577 (from 0.7544 on Monday). Cable closed the day at 1.4410 (from 1.4433).

Overnight, the BRC shop prices declined less than the previous month (-1.8% Y/Y from -2.0% Y/Y). Later today, the UK services PMI is expected to decline marginally to 55.4. A poor figure will fuel market expectations that the BoE will keep a very soft tone at tomorrow's policy meeting. It is an important meeting as the Bank will have a new inflation report available. Over the previous days, sterling showed no clear trend. That said, the UK currency didn't perform that bad given the overall negative context. Is sterling ripe for some ST consolidation if the news flow would become less negative? **In a longer term perspective**, uncertainty on Brexit and global negative risk sentiment remain a negative for sterling. As long as these issues aren't solved, a sustained sterling rebound is unlikely. **The medium term technical picture of sterling against the euro is negative as EUR/GBP broke above 0.7493. Next resistance stands at 0.7875.** A return below 0.74 would be a first indication that sterling enters calmer waters.

EUR/GBP: holding in the 0.76 area



GBP/USD: bottoming out process to continue?

Calendar

Wednesday, 3 February		Consensus	Previous
US			
13:00	MBA Mortgage Applications	--	8.8%
14:15	**ADP Employment Change (Jan)**	**193K**	**257k**
15:45	Markit Services PMI (Jan F)	53.7	53.7
16:00	**ISM Non-Manf. Composite (Jan)**	**55.1**	**55.3**
Japan			
03:00	Nikkei PMI Services (Jan)	A: 52.4	51.5
06:00	Consumer Confidence Index (Jan)	A: 42.5	42.7
China			
02:45	**Caixin PMI Services (Jan)**	**A: 52.4**	**50.2**
UK			
01:01	BRC Shop Price Index YoY (Jan)	A: -1.8%	-2.0%
10:30	Official Reserves Changes (Jan)	--	$527m
10:30	**Markit/CIPS UK Services PMI (Jan)**	**55.4**	**55.5**
EMU			
10:00	**Markit Services PMI (Jan F)**	**53.6**	**53.6**
10:00	**Markit Composite PMI (Jan F)**	**53.5**	**53.5**
11:00	**Retail Sales MoM/YoY (Dec)**	**0.3%/1.5%**	**-0.3%/1.4%**
Germany			
09:55	Markit Services PMI (Jan F)	55.4	55.4
France			
09:50	Markit Services PMI (Jan F)	50.6	50.6
Italy			
11:00	CPI EU Harmonized MoM/YoY (Jan P)	-2.3%/0.3%	-0.1%/0.1%
Spain			
09:15	Markit Services PMI (Jan)	54.3	55.1
Norway			
10:00	Unemployment Rate AKU (Nov)	4.6%	4.6%
Sweden			
08:30	Services PMI (Jan)	57.6	58.0
Events			
03:30	BOJ Governor Kuroda speaks in Tokyo		
09:00	EU Comm. President Juncker Speaks in EU Parliament on UK Renegotiation		
11:00	**European Commission Releases Winter Economic Forecasts**		
Sweden	Bond Auction (SEK2B 5% Dec2020 & SEK2B 2.5% May2025)		
Germany	**Bobl Auction (€5B Apr 2021) (11:30)**		
	Quarterly earnings publication from Merck & Co (Bef-mkt), General Motors Co (Bef-mkt), Mondelez Intl (14:00), Novo Nordisk (Bef-Mkt)		

10-year	td	-1d	2-year	td	-1d	STOCKS		-1d
US	1,85	-0,08	US	0,74	-0,05	DOW	16154	16153,54
DE	0,30	-0,04	DE	-0,48	-0,02	NASDAQ	for Exch - NQI	#VALUE!
BE	0,60	-0,04	BE	-0,38	0,00	NIKKEI	17191	17191,25
UK	1,54	-0,08	UK	0,35	-0,03	DAX	9581,04	9581,04
JP	0,07	-0,02	JP	-0,18	-0,04	DJ euro-50	2952	2951,85

						USD	td	-1d
IRS	EUR	USD (3M)	GBP	EUR	-1d	-2d	Eonia EUR	-0,232	0,005
3y	-0,138	0,937	0,905	Euribor-1	-0,23	0,00	Libor-1 USD	0,51	0,51
5y	0,057	1,210	1,125	Euribor-3	-0,16	0,00	Libor-3 USD	0,59	0,59
10y	0,649	1,709	1,554	Euribor-6	-0,09	-0,01	Libor-6 USD	0,74	0,74

Currencies		-1d	Currencies		-1d	Commoditie	CRB	GOLD	BRENT
EUR/USD	1,0922	0,0022	EUR/JPY	130,67	-0,83		163,4867	1127,66	32,47
USD/JPY	119,65	-1,00	EUR/GBP	0,7572	0,0000	-1d	-3,27	2,53	-1,22
GBP/USD	1,4423	0,0032	EUR/CHF	1,1116	0,0006				
AUD/USD	0,7032	-0,0039	EUR/SEK	9,3682	0,07				
USD/CAD	1,4068	0,0052	EUR/NOK	9,5407	0,05				

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