Sunrise

Thursday, 29 October 2015

More hawkish FOMC puts December lift-off on the table

The US yield curve bear flattened with yields up to 10 bps higher. Additionally to the FOMC message, oil jump higher creating a risk-on sentiment. Finally, the US 5-year Note auction went badly. Collateral damage for German bonds will likely be limited after the ECB pre-announced more easing. Stronger US eco data may keep pressure on Treasuries.

Fed policy statement sends EUR/USD below 1.10 level

The dollar rebounded after the FOMC policy statement as the Fed kept the door open for a lift-off at the December meeting. The dollar received unexpected interest rate support and gained across the board. EUR/USD dropped below the psychological barrier off 1.10. Decent US eco data might keep the US currency well bid.

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 strong gains, indices up more than 1%. **US equities** also thrived yesterday, with the S&P up 1.3%, after having already gained more than 10% in October. Overnight, **Asian equities** are trading mixed, not really inspired by the European/US rally.
- **Last night , the FOMC opened the door for an eventual Dec. rate hike,** as they downplayed the impact of the global developments and were not concerned about the US economy and explicitly mentioned the December meeting.
- **The New Zealand Central Bank decided to hold their interest rates at 2.75%**, resisting to cut for the fourth time this year as the drop in dairy prices weigh on the terms of trade.
- Japan's **industrial production September surprised on the upside in September g**rowing 1.0% M/M (-0.9% Y/Y), beating the consensus expectations.
- **On the corporate agenda there are the quarterly earnings from MasterCard, Bayer, Total, Deutsche Bank and Royal Dutch Shell.**
- Today, the **eco-calendar in the US contains the Q3 GDP growth & core PCE inflation** and **the weekly jobless claims**. In the **euro zone**, the October EC **confidence indicators** are published and **Germany releases HICP inflation.**

Rates

FOMC keeps door open for lift-off in December

US curve bear flattens on hawkish FOMC

Peripheral yield spreads tighten with Portugal outperforming

	US yield	-1d
2	0,707	0,0739
5	1,4645	0,0929
10	2,0867	0,0497
30	2,8631	0,0070

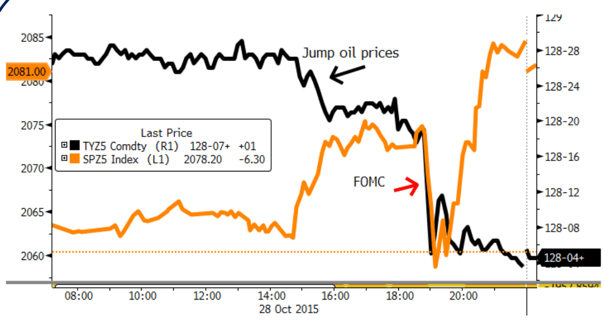
Global core bonds were hit by a sudden jump higher in oil prices. That triggered a risk-on reaction in equity markets with negative repercussions for core bonds. However, the main bearish driver came from a more hawkish than expected FOMC statement (see below). It pulled US Treasuries lower and the curve bear flattened, a typical reaction on changing Fed rate expectations. The move of US Treasuries was magnified by a somewhat surprising post-FOMC equity rally. The US 5-yr T-Note auction didn't go well either. In a daily perspective 2-to 5-yr yields went up 8 to 10 bps, the 10-yr yield added 6.3 bps and the 30-yr only 1.9 bps. In the German cash market, which closed ahead of the FOMC decision, yield changes were limited between -0.4 and -0.9 bps. The Bund traded 40 ticks lower after the FOMC decision. Of course, the German bond market is to a certain extent ring-fenced by the dovish ECB.

FOMC is not overly concerned about weaker US data

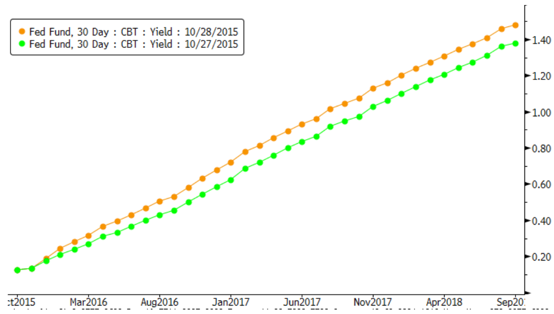
FOMC explicitly cites the Dec meeting as key meeting.

	DE yield	-1d
2	-0,3200	0,0100
5	-0,1160	0,0110
10	0,4460	0,0010
30	1,1970	0,0070

The FOMC press release *(see flash for extensive review)* **was definitely more hawkish than expected. It specifically opened the door for a December lift-off. First,** the description of the economic situation was not materially changed despite two months of weaker economic data. **Second**, the Fed surprisingly **downplayed the impact of global economic and financial developments**. **Third it mentioned explicitly the next meeting** as a moment to assess whether the conditions for the lift-off are fulfilled. **By emphasizing December, the Fed probably wants to warn markets that they still may go in 2015**. According to market pricing, chances for rate hike are now about 50% (from 38%). **Of course, the lift-off remains conditional on some further improvement in the labour market and reasonable confidence that inflation will move back to its 2% objective over the medium term.** So, while the FOMC may start tightening, there is **no firm commitment** to do so in December. The hurdle to do so is lower though. It might be enough that eco/labour data don't really disappoint.



T-note future (black) & S&P future (orange) (intraday): Jump in oil prices and more hawkish Fed drive markets. Remarkable recovery of equities in face of higher yields and stronger dollar.



Fed Fund strip curve (yesterday-day before): shifts higher on FOMC statement (to same level as one month ago). About 50% chance on Dec. lift-off is discounted.

Today, the US eco-calendar contains the Q3 GDP growth, core PCE inflation and the weekly jobless claims. October. The **US GDP** is expected to have grown 1.6% Q/Q in Q3, down from 3.9% Q/Q in Q2. The decline should be due to inventory build-down and lower net export. The FOMC statement suggested strong domestic demand. So, one should not only look to the headline figure but also to the final sales, which will be strong. Nevertheless, **we see some upward risks**

R yield

to consensus. If yesterday's trade figures are already included in the number, the GDP figure might be stronger. If it is not included, markets will know that an upward revision will follow. The **Core PCE** is expected to have increased 1.4% Q/Q in Q3, coming from a 1.9% Q/Q in Q2. We side with consensus. The **weekly jobless claims** for last week are estimated at 265k, coming from a low 259k previously. We see **potential downside risks**. In EMU, **October economic confidence** indicator is expected to decline slightly, from 105.6 to 105.1. In **Germany**, **October HICP inflation** is expected to move back to positive territory (0.0% Y/Y from -0.2% Y/Y previously).

R2	160,62	-1d
R1	158,6	
BUND	**157,95**	0,0000
S1	155,71	
S2	155,41	

Auctions in Italy and the US

Today, the Italian treasury launches a new 5-yr BTP (€3.5-4B 0.65% Nov2020) and taps the on the run 10-yr BTP (€1.75-2.25B 2% Dec2025). On the grey market, the new BTP trades with a 3.6 bps pick-up in ASW spread terms compared with the previous 5-yr benchmark (0.7% May2020). That corresponds with a 10 bps pick-up in yield terms. The 10-yr BTP richened in the run-up to the meeting in ASW-spread terms and is rather rich on that part of the Italian yield curve. Apart from these micro-evaluations, the strongest driver for peripheral auctions remains the ECB's very loose monetary policy. Therefore, we expect these Italian auctions to go well.

Today: Hawkish repositioning

Overnight, Asian stock markets couldn't build on yesterday's US equity strength. WS performed strong despite the hawkish FOMC statement. The US Note future trades stable around the post-FOMC lows. The Bund could be under modest downward pressure at the European opening though.

Today's eco calendar heats up with US Q3 GDP, weekly claims, EMU EC confidence and German inflation data. We see risks for GDP on the upside of expectations, which is a negative for US Treasuries. US eco data remain key for markets. **The Fed bought an option for a December lift-off, but remains data-dependent. The ECB's additional easing in December on the other hand, is carved in stone.** This clear divide between the Fed and the ECB suggests a further US/EU spread widening. On the US yield curve, we expect the front end to underperform especially in case of solid eco data. Technically, the US Note future tested first support at 128-05+ after the Fed. We believe that there is more downside with next support at 126-16. **The evolution on commodity and equity markets remains a wildcard for intraday trading.** Atlanta Fed Lockhart is scheduled to speak but he most likely won't comment on the Fed's policy.

German Bund: Dovish Draghi underpins Bund

US Note future: More downside after hawkish Fed

Currencies

Dollar propelled by hawkish Fed statement

USD jumps higher as Fed keeps door open for December rate hike

R2	1,114	-1d
R1	1,1087	
EUR/USD	**1,0938**	-0,0102
S1	1,0848	
S2	1,0715	

Yesterday, investors initially were apparently covering positions against a potentially soft Fed statement. USD/JPY didn't go anywhere even as European and US equities traded with a positive bias. EUR/USD was squeezed higher away from the recent lows and traded the 1.1080 area just before the Fed policy announcement. The Fed policy statement was more hawkish than expected. The Fed kept the door open for a December lift-off and wasn't too worried about recent softer US eco data. US bond yields jumped higher and so did the dollar. USD/JPY rebounded to the 121.25 area and closed the session at 121.09 (from 120.46). EUR/USD dropped to the low 1.09 area and closed the session at 1.0923 (from 1.1051 on Tuesday).

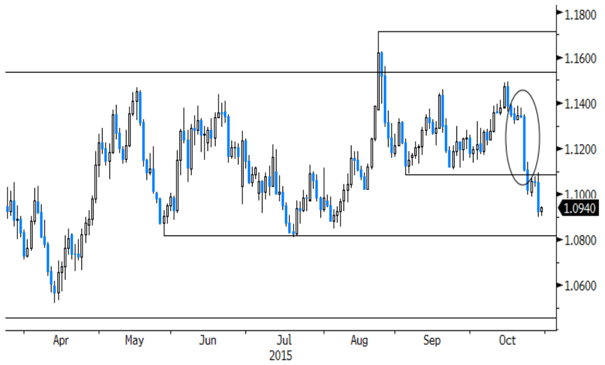
Asian markets reaction cautious to the Fed policy statement. Dollar rally slows

Overnight, most Asian equity indices trade mixed (Japan about flat, mainland China in positive territory, most other Asian indices in negative territory). This contrasts with the Post FOMC US equity rally. The trade-weighted dollar is trending higher and trades currently at 97.55 (the cycle high stands at 100.39, first key resistance at 98.36). USD/JPY is drifting off yesterday's highs and trades currently in the 120.75 area. EUR/USD is trading in the 1.0930/35 area, marginally higher from the post-FOMC low.

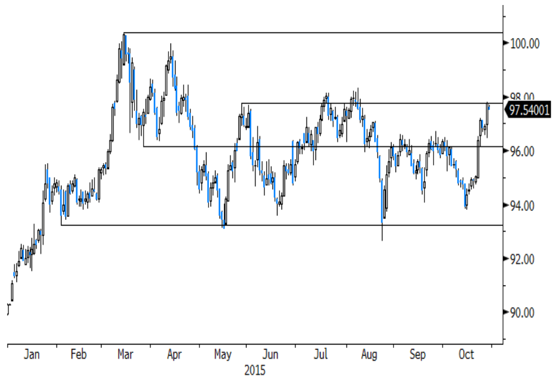
Plenty of eco data on the agenda.

Will a decent US Q3 GDP report support more USD gains?

Today, the eco calendar is again very well filled. In Europe, it contains the German CPI data & labour data and the EC confidence indicators. For the German HICP a rebound from -0.2% Y/Y to 0.0% Y/Y is expected. We side with consensus. A softer than expected CPI would highlight the policy divergence between the ECB and the Fed and weigh on the euro. In the US, the initial jobless claims and the advance reading of the US Q3 GDP will be published. Jobless claims are expected to stay low at 265.000, while US Q3 GDP is expected to have increased by an annualised 1.6% Q/Q. Private consumption is expected solid. Inventories and net export will probably weigh on growth. The risks are for an above consensus outcome. If so, it supports the case for a December Fed rate hike and support the dollar. **In a day-to day perspective, we expect the dollar to stay strong in the wake of the FOMC policy statement, especially against the euro. The picture for USD/JPY might be less buoyant if the equity rally slows.**



EUR/USD: from euro weakness to USD strength



USD (trade-weighted) trending north on 'hawkish Fed take).

In a longer term perspective, global markets recently focused on the impact of weaker US data on the Fed rate hike path. That made the dollar vulnerable. **Last week, markets were positioned for soft ECB speak, but at the press conference, ECB Draghi went much further towards additional easing than markets anticipated**. The topside in EUR/USD (1.1460/95 resistance) became better protected. The ECB prepared markets for a new round of monetary easing which pushed EUR/USD below the key 1.1087/1.1105 support. Yesterday's Fed policy statement 'confirmed' a potential policy divergence between the Fed and ECB, **pushing EUR/USD further south in the LT consolidation pattern**. 1.0819 is a first important support area. The targets of the multiple top with neckline in the 1.1087/1.1105 are in the low 1.07 area. **For now, there is no reason to fight the euro negative/USD positive tide.**

EUR/GBP extends decline

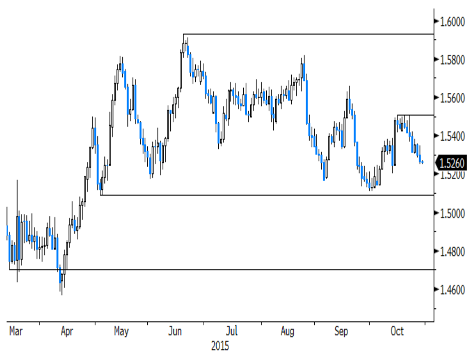
R2	0,7374	-1d
R1	0,725	
EUR/GBP	**0,7168**	-0,0042
S1	0,7144	
S2	0,7026	

With no UK eco data on the calendar, sterling trading was at the mercy of the global market repositioning ahead of the Fed policy decision yesterday. Cable hovered directionless in a tight range slightly below the 1.53 big figure. The pair jumped higher ahead of the FOMC decision, but dropped back to the mid 1.5250 area on global post-Fed USD strength. EUR/GBP was initially squeezed higher by the overall rebound of the euro (EUR/USD), but the pair also returned back below 0.72, in the wake of the Fed policy decision.

This morning, the UK Nationwide House prices were close to expectations at 0.6% M/M and 3.9% Y/Y. Later today, the September money supply and lending data will be published. Later the CBI will also publish the October reported sales. Lending data are expected to improve further. For CBI sales, a moderate easing from 49 to 35 is expected. We see slight downside risks to today's UK data. If so, it might be a slightly negative for sterling, especially against the dollar.

Looking at the broader picture, the soft tone at the ECB press conference pushed EUR/GBP back lower in the longstanding sideways range. The pair tested the 0.7196 support, but the level was 'really' broken after yesterday's FOMC announcement. Euro weakness still prevails. We maintain a sell-on-upticks approach for EUR/GBP.

EUR/GBP extends drop below 0.7196 support



Cable declining on global USD strength

Calendar

Thursday, 29 October		Consensus	Previous
US			
13:30	**Initial Jobless Claims (Oct 24)**	**265k**	**259k**
13:30	**Continuing Claims (Oct 17)**	**2160k**	**2170k**
13:30	**GDP Annualized QoQ (3Q A)**	**1.6%**	**3.9%**
13:30	Personal Consumption (3Q A)	3.3%	3.6%
13:30	GDP Price Index (3Q A)	1.4%	2.1%
13:30	**Core PCE QoQ (3Q A)**	**1.4%**	**1.9%**
15:00	Pending Home Sales MoM/NSA YoY (Sep)	1.0%/7.3%	-1.4%/6.7%
Japan			
00:50	Industrial Production MoM/YoY (Sep P)	A: 1.0 %/-0.9%	-1.2%/-0.4%
UK			
08:00	Nationwide House PX MoM/NSA YoY (Oct)	0.5%/3.8%	0.5%/3.8%
10:30	Net Consumer Credit (Sep)	1.1b	0.9b
10:30	Net Lending Sec. on Dwellings (Sep)	3.3b	3.4b
12:00	CBI Reported Sales (Oct)	35	49
EMU			
11:00	**Economic Confidence (Oct)**	**105.1**	**105.6**
11:00	Business Climate Indicator (Oct)	0.31	0.34
11:00	Industrial Confidence (Oct)	-2.7	-2.2
11:00	Services Confidence (Oct)	12.0	12.4
11:00	Consumer Confidence (Oct F)	-7.7	-7.7
Germany			
	CPI Baden Wuerttemberg MoM/YoY (Oct)	--/--	-0.2%/0.0%
09:00	CPI Saxony MoM/YoY (Oct)	--/--	-0.1%/0.0%
09:55	**Unemployment Change (000's) (Oct)**	**-4k**	**2k**
09:55	**Unemployment Claims Rate SA (Oct)**	**6.4%**	**6.4%**
10:00	CPI Brandenburg MoM/YoY (Oct)	--/--	-0.2%/-0.3%
10:00	CPI Hesse MoM/YoY (Oct)	--/--	-0.3%/0.0%
10:00	CPI Bavaria MoM/YoY (Oct)	--/--	-0.2%/0.0%
10:30	CPI North Rhine Westphalia MoM/YoY (Oct)	--/--	-0.2%/0.0%
14:00	**CPI EU Harmonized MoM/YoY (Oct P)**	**-0.1%/0.0%**	**-0.3%/-0.2%**
Belgium			
	CPI MoM/YoY (Oct)	--/--	0.07%/1.06%
Spain			
09:00	Retail Sales SA YoY (Sep)	3.0%	3.1%
09:00	CPI EU Harmonised MoM/YoY (Oct P)	0.3%/-0.9%	0.4%/-1.1%
Sweden			
09:30	Retail Sales MoM/NSA YoY (Sep)	1.3%/3.0%	-1.7%/1.0%
Events			
11:10	Italy - Auctions BTPs/CCTeus		
14:10	**US - Fed's Lockhart Makes Opening Remarks on Workforce Development ()**		
16:00	**EMU - ECB's Constancio Speaks in London ()**		
17:00	**US - Holds 7-year note auction**		
Before market open	**Corporate earnings releases of Mastercard, Altria, Alcatel-Lucent, Bayer, Sanofi, Total, Deutsche Bank, Royal Dutch Shell**		

10-year	td	-1d	2-year	td	-1d	STOCKS		-1d	
US	2,09	0,05	US	0,70	0,07	DOW	17780	17779,52	
DE	0,47	0,02	DE	-0,32	0,01	NASDAQ	or Exch - NQI	#VALUE!	
BE	0,75	0,01	BE	-0,28	0,00	NIKKEI	18936	18935,71	
UK	1,80	0,04	UK	0,50	0,02	DAX	10831,96	10831,96	
JP	0,30	0,00	JP	0,01	0,00	DJ euro-50	3421	3421,09	
						USD	td	-1d	
IRS	EUR	USD (3M)	GBP	EUR	-1d	-2d	Eonia EUR	-0,145	-0,008
3y	0,020	1,039	1,090	Euribor-1	-0,12	0,00	Libor-1 USD	0,51	0,51
5y	0,240	1,433	1,393	Euribor-3	-0,07	0,00	Libor-3 USD	0,58	0,58
10y	0,844	2,000	1,830	Euribor-6	0,01	0,00	Libor-6 USD	0,74	0,74

Currencies		-1d	Currencies		-1d	Commoditie	CRB	GOLD	BRENT
EUR/USD	1,0937	-0,0103	EUR/JPY	132,1	-0,83		195,0743	1160,11	48,66
USD/JPY	120,8	0,36	EUR/GBP	0,7166	-0,0044	-1d	3,74	-10,29	1,89
GBP/USD	1,5255	-0,0049	EUR/CHF	1,0866	-0,0029				
AUD/USD	0,7112	-0,0012	EUR/SEK	9,3449	-0,04				
USD/CAD	1,3200	-0,0056	EUR/NOK	9,3648	0,02				

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