



## Sunrise

Thursday, 25 February 2016

### Rates: Oil and equity movements remain key driver core bonds

Moves on equity markets and the oil price triggered more volatility on bond markets yesterday. Overnight, Chinese stocks lose more than 5%, but risk aversion didn't spill over to other Asian markets. The German 10-yr yield is only 10 bps away from the all-time low (0.05%). Testing times ahead? Or can overbought conditions trigger some profit taking on the bond rally?

### Currencies: Dollar still shows diffuse picture

Yesterday, risk-off sentiment and a poor US Services PMI initially weighed on USD/JPY. At the same time, the dollar held up reasonably well against the euro. However, a late session decline of oil reversed the earlier moves. Today, the eco data might be slightly USD supportive. Sterling continues its Brexit-driven decline.

### 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 reversed their losses yesterday**, supported by a rebound in the oil price, to end the session 0.5% higher. This morning, **Asian shares trade mixed**. Chinese stocks underperform, losing up to 7% as money-market rates increased and the offshore yuan declined.
- Yesterday, the **IMF** called on **the world's leading economies to join forces and take bold action in a bid to boost growth** at tomorrow's G20 gathering in Shanghai, adding that weakness in global demand is a problem that cannot be solved by just looking at the United States.
- Although US inventory data showed that crude stockpiles rose to another record high last week, **crude oil prices rebounded sharply yesterday evening**, reversing earlier losses. The Brent closed at \$34.41/barrel and the WTI at \$32.15/barrel.
- **Bank of Japan board member Kiuchi** said this morning that economic and price conditions had not deteriorated enough to justify easing last month and warned **that negative rates could potentially reduce financial system stability** by causing further harm to financial institutions' revenues.
- Yesterday, **Hungary's Prime Minister Orban said the Hungarian government had decided to call a referendum on whether the country should be forced to resettle refugees**. Austria met nine other countries to discuss ways of curbing the flow of people heading to Europe.
- The **eco calendar heats up today** with the final reading of euro zone HICP inflation for February, the EMU M3 money supply and credit growth data, the second estimate of UK Q4 GDP, US jobless claims and US durable goods orders.

# Rates

*Volatile oil/equity prices dominate the bond market that showed two faces yesterday*

*German yields still lower, US ones slightly higher at end of the session*

|    | US yield | -1d     |
|----|----------|---------|
| 2  | 0,75     | -0,0039 |
| 5  | 1,1944   | -0,0087 |
| 10 | 1,7295   | 0,0035  |
| 30 | 2,5918   | 0,0083  |

*Dovish Bullard hesitates and admits he might be wrong on inflation. Is he becoming more hawkish?*

*Kaplan pleads for wait and see approach*

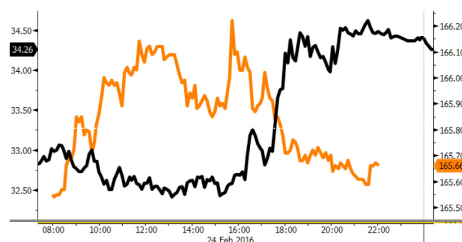
*Lacker (non-voter) in favour of tightening.*

|    | DE yield | -1d     |
|----|----------|---------|
| 2  | -0,5190  | 0,0060  |
| 5  | -0,3340  | -0,0060 |
| 10 | 0,1770   | -0,0040 |
| 30 | 0,8379   | -0,0131 |

## Bund sets new high, but cannot hold onto gains

Yesterday, global core bonds initially gained additional ground in an old-fashioned risk-off session that was devoid of key European eco releases, but included a disconcerting weak Markit service PMI. The Bund set a new high (166.25) and the US T-Note future showed good gains. However, going into the European close, oil rebounded on lower inventory statistics followed swiftly by surging US equities. It went downhill for bond futures which erased all (US) to large part (Bund) of earlier gains. For the German Bund, it was nevertheless the fifth consecutive winning session. In a daily perspective, **German yields went up to 4.5 bps lower at the 30-yr (testing ST lows), flattening the curve. US yields on the contrary ended 2 to 2.6 bps higher across the curve.**

**Fed Bullard** said that it is too early to speculate on what might happen. He was though concerned about the IMF's growth downgrade. **On inflation, Bullard starts to hesitate his view that inflation expectations will have a big impact on actual inflation, after a hot January CPI reading (2.2% Y/Y).** The Phillips curve effects will could be stronger than anticipated. Bullard flip-flops from time to time on his policy expectations. Lately he was dovish, but inflation developments may make him change his views. So, if the debate inside the FOMC turns to higher rates, he probably wouldn't dissent. **Richmond Fed Lacker (non-voter) is more steadfastly in his (hawkish) views.** There is no strong evidence to shift the rate outlook. So, he remains in favour of increasing rates (like Fed George) as policy is still very accommodative. **Fed Kaplan** says that it is better to wait before raising rates and look what happens in the economy and markets. **We don't expect a rate hike in March, as the Fed doesn't hike rates during market turmoil, but the case may be different in June as various key Fed governors seem anxious about the low unemployment rate and its potential (upward) effect on inflation.**



Bund (black) and oil (orange) (intraday): Initial gains evaporate as oil/equities rally



German 10-yr yield approaches all time low amid overbought condition. Only 10 bps away from all-time low. Test or profit taking?

## Eco calendar heats up today

*EMU HICP to be confirmed at 0.4% Y/Y*

*Improvement in EMU lending data?*

*Stronger US durable orders and lower initial claims?*

**Euro zone HICP inflation** picked up from 0.2% Y/Y to 0.4% Y/Y in January. Core inflation picked up unexpectedly, from 0.9% Y/Y to 1.0% Y/Y. The final reading is expected to confirm this outcome. **Growth in EMU M3 money supply** is expected stable at 4.7% Y/Y in January after having slowed in the previous two months. Following very poor Dec. lending data, we look for signs of improvement. In the **US, durable goods orders** are forecast to have rebounded by 2.7% M/M in January following a 5.0% M/M decline in December. Aircraft

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orders are forecast to have rebounded. Also excluding transportation, durables are expected to have increased by 0.3% M/M. **Following poor data previously, we see risks for an upward surprise.** Finally, **US initial jobless claims** are expected to have picked up slightly in the past week. The President's Day holiday might have distorted the figures. We see **risks are for a lower outcome.**

## US Treasury ends refinancing operation

|             |               |               |
|-------------|---------------|---------------|
| R2          | 167           | -1d           |
| R1          | 166,25        |               |
| <b>BUND</b> | <b>165,66</b> | <b>0,1300</b> |
| S1          | 163,25        |               |
| S2          | 162,86        |               |

**The US Treasury continued its end-of-month refinancing operation yesterday with a solid \$34B 5-yr Note auction.** The auction stopped sharply through the 1:00 PM bid side with an average bid cover. Bidding details showed strong buy-side support while the dealer bid was extremely small. The **\$13B 2-yr FRN auction was decent as well** with strong direct bids, but weak indirect bids. **Today, the US Treasury ends its refinancing operation with a \$28B 7-yr Note auction.** Currently, the **WI trades around 1.51%.**

## Today: More volatility ahead?

**Overnight,** Asian markets trade marginally higher with Japan outperforming (+2%) and **China underperforming (-5%).** The Chinese move is rather strange as there were no specific headlines by policy makers. The eco calendar was empty and the PBOC kept CNY stable. Sentiment didn't spill to other Asian markets either. Oil prices are stable overnight, but the US Note future trades with a small upward bias, suggesting a slightly stronger opening for the Bund as well.

**Today's US eco calendar** contains durable goods orders, weekly claims and speeches by Fed Lockhart (cautious wait and see) and Williams (neutral, but compared to expectations hawkish). Risks for the eco data are on the upside of expectations. That's a negative for US Treasuries, but we expect no lasting impact. End-of-month extension buying and the end of the US refinancing operation could protect the downside. In EMU, M3 money data and final January CPI grab attentions. **Core bond trading showed quite some volatility the past sessions. Moves on equity and oil markets remain the most important drivers behind those swings.**

**Technically,** the US Note future's first test to drop firmly below the steep uptrend line failed, suggesting still some momentum. Nevertheless, we expect sideways trading ahead, roughly between 129 and 133. The picture for the Bund is more or less similar. The upper bound of the short-term range (163.25-166.25) was tested yesterday. While the Bund enters overbought conditions, we don't rule out a break higher in coming days. The



German Bund: First test contract high failed



US Note future: high volatility over the past sessions mainly driven by equity markets and oil prices

# Currencies

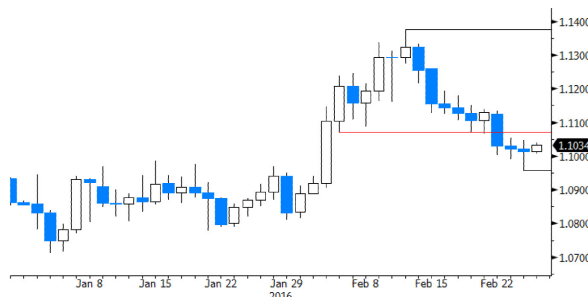
*Dollar shows different intraday dynamics against the euro and the yen*

|         |        |        |
|---------|--------|--------|
| R2      | 1,1376 | -1d    |
| R1      | 1,1139 |        |
| EUR/USD | 1,1031 | 0,0019 |
| S1      | 1,081  |        |
| S2      | 1,0711 |        |

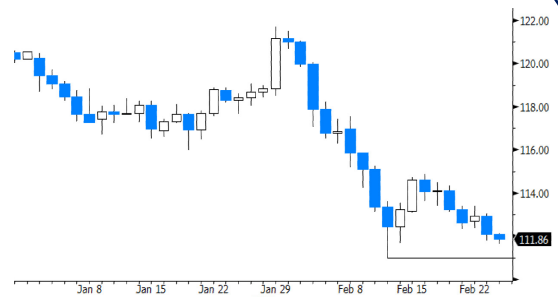
## Dollar still looking for a consistent trading pattern

On Wednesday, the USD showed again no consistent trading pattern. However, at the end of the day the changes were limited. USD/JPY was under pressure due to global risk-off sentiment. A poor US market services PMI sent the pair to the low 111 area. However a real test of the 110.98 low didn't occur as investors feared BOJ action. Later, USD/JPY rebounded as did oil and equities. The trading pattern of the dollar against the euro was different. The euro underperformed even as sentiment was risk-off. The poor US market services PMI was the turning point. The dollar declined and EUR/USD regained the 1.10 barrier to close the session at 1.1013 (from 1.1020). USD/JPY finished the session at 112.18 (from 112.10).

Asian markets show a mixed picture this morning. Most indices show modest gains with Japan outperforming. At the same time Chinese equities underperform showing substantial losses. Japanese equities are supported as the yen shows signs of topping about. USD/JPY trades currently in the 112.20 area. A BOJ official warned on the risks of negative interest rates. At the same time, there are headlines on the Japanese government considering additional fiscal stimulus. In theory, this isn't bad for the yen. The PBOC fixed the yuan little changed. EUR/USD stabilises in the 1.1035 area after the recent decline.



EUR/USD holding below 1.1060/70 support



USD/JPY: nearing the 110.98 correction low

The **eco calendar heats up** with final EMU CPI inflation data, EMU M3 money supply, the US jobless claims and durable goods orders. According to the preliminary estimate, **euro zone HICP inflation** picked up to 0.4% Y/Y. Core inflation rose unexpectedly, from 0.9% Y/Y to 1.0% Y/Y. The final reading is expected to confirm this outcome. **EMU M3 money supply** growth is expected stable at 4.7% Y/Y. The lending data are more important. We look out for signs of improvement after poor lending data in December. Another disappointing figure might be a slightly negative for the euro. The **US durable goods orders** are forecast to have rebounded by 2.7% M/M following a 5.0% M/M decline in December. **Following poor data in November and December, we see risks for an upward surprise.** Finally, **US initial jobless claims** are expected slightly higher from 262 000 to 270 000. **The US eco data might be slightly USD supportive.**

Of late **the dollar showed a diffuse price pattern with USD/JPY suffering from risk-off sentiment.** At the same time, **the euro struggled to prevent further**

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*Eco calendar heats up in Europe and in the US*

*USD trading still looking for a consistent trading pattern*

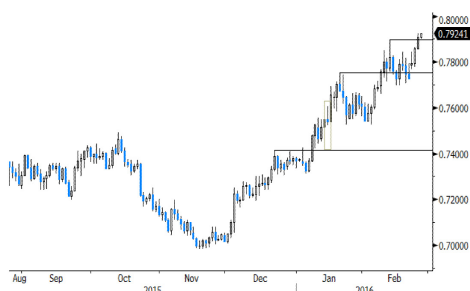
**losses against the dollar.** Yesterday's rejected test of the 111 area might be a signal that USD/JPY is ripe for some short-term consolidation, if the risk-off trade turns less intensive. For EUR/USD the picture remains inconclusive. **The euro recently didn't profit from negative news and the technical picture of EUR/USD deteriorated.** Will the dollar continue to profit (EUR/USD decline) if sentiment on risk improves again? Yesterday's intraday price action suggests some short-term consolidation. However, the jury is still out.

**From a technical point of view,** the correction high stands at 1.1376. Next important resistance kicks in at 1.1495. Recently, the dollar slowly fought back, but this move had no strong momentum. Monday's decline below 1.1060 is a ST negative for EUR/USD and might open the way to the 1.0810/1.0711 support area, but confirmation is still needed. **USD/JPY dropped below the key 115.98 pre-BOJ low.** Japanese officials warned on potential action, putting a short-term floor under the pair. Even so, it remains vulnerable and is nearing again USD/JPY the ST lows at 110.99. **Any rally might soon run into resistance (1.1487 recent high). The 115.98 January low is a next resistance.**

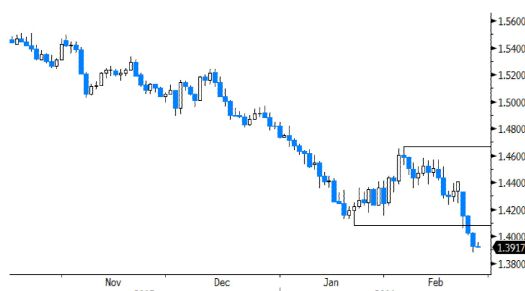
## Sterling decline continues

**On Wednesday,** the 'Brexit-repositioning' of sterling continued. Cable **declined another big figure and tumbled (temporarily?) below 1.39, the lowest level since March 2009.** Risk-off sentiment and a further decline of oil added to the sterling negative sentiment. The UK loans for home purchases were much higher than expected, but didn't help sterling much. CBI reported sales were marginally weaker than expected. Cable set an intraday low in the 1.3880 area around noon London time. EUR/GBP set a new short-term high north of 0.79. **The decline of sterling finally ran into resistance during the US trading session.** Cable 'rebounded' to close the session at 1.3927 (from 1.4022). EUR/BGP held close to the highs as the euro rebound later in the session. The pair finished the day at 0.7909 (from 0.7859).

|         |               |        |
|---------|---------------|--------|
| R2      | 0,8066        | -1d    |
| R1      | 0,7925        |        |
| EUR/GBP | <b>0,7913</b> | 0,0040 |
| S1      | 0,7695        |        |
| S2      | 0,7526        |        |



EUR/GBP sets new correction top



GBP/USD: decline continues beyond 1.40

**Today,** the details of the UK Q4 GDP will be published. A confirmation of the 0.5% Q/Q 1.9% Y/Y preliminary reading is expected. A weak contribution for net exports might be a negative for sterling. However, the focus remains on the Brexit debate. Even positive data had no lasting impact on sterling of late.

After the recent decline, quite some bad news should already be discounted for sterling. However, we see no trigger for a reversal especially as oil/the global context remains negative. **The medium term technical picture of sterling against the euro remains negative as EUR/GBP broke above the 0.7493 Oct top. The pair yesterday cleared the 0.7898 resistance. 0.8066 is the next important resistance.**

# Calendar

| Thursday, 25 February |  | Consensus  | Previous     |
|-----------------------|--|------------|--------------|
| <b>US</b>             |  |            |              |
| 14:30                 | Initial Jobless Claims                                       | 270k       | 262k         |
| 14:30                 | Continuing Claims  | 2253k      | 2273k        |
| 14:30                 | Durable Goods Orders (Jan P)                                 | 2.7%       | -5.0%        |
| 14:30                 | Durables Ex Transportation (Jan P)                           | 0.3%       | -1.0%        |
| 15:00                 | House Price Purchase Index QoQ (4Q)                          | --         | 1.3%         |
| 15:00                 | FHFA House Price Index MoM (Dec)                             | 0.5%       | 0.5%         |
| <b>UK</b>             |  |            |              |
| 10:30                 | GDP QoQ / YoY (4Q P)   | 0.5%/1.9%  | 0.5%/1.9%    |
| <b>EMU</b>            |  |            |              |
| 10:00                 | M3 Money Supply YoY (Jan)                                    | 4.7%       | 4.7%         |
| 11:00                 | CPI MoM / YoY (Jan)  | -1.4%/0.4% | 0.0%/0.4%    |
| 11:00                 | CPI Core YoY (Jan F)   | 1.0%       | 1.0%         |
| <b>Germany</b>        |  |            |              |
| 08:00                 | CPI EU Harmonized MoM / YoY (Jan F)                          | --/--      | -0.9%/0.4%   |
| 08:00                 | GfK Consumer Confidence (Mar)                                | 9.3        | 9.4          |
| <b>Italy</b>          |  |            |              |
| 10:00                 | Consumer Confidence Index (Feb)                              | 118.0      | 118.9        |
| 10:00                 | Business Confidence (Feb)                                    | 102.7      | 103.2        |
| 10:00                 | Economic Sentiment (Feb)                                     | --         | 101.5        |
| 11:00                 | Retail Sales MoM YoY (Dec)                                   | 0.1% / --  | 0.3% / -0.1% |
| <b>Spain</b>          |  |            |              |
| 09:00                 | GDP QoQ YoY (4Q F)   | 0.8%/3.5%  | 0.8%/3.5%    |
| <b>Events</b>         |  |            |              |
| 01:00                 | Fed's Bullard Speaks in New York                             |            |              |
| 14:15                 | Fed's Lockhart to Give Opening Remarks at Banking Conference |            |              |
| 18:00                 | Fed's Williams Speaks in New York                            |            |              |
| <b>US</b>             |  |            |              |
|                       | 7Yr Note auction (\$28B)                                     |            |              |

| 10-year | td    | -1d   | 2-year | td    | -1d   | STOCKS     | -1d                    |
|---------|-------|-------|--------|-------|-------|------------|------------------------|
| US      | 1,73  | 0,00  | US     | 0,75  | 0,00  | DOW        | 16485,16484,99         |
| DE      | 0,18  | 0,00  | DE     | -0,52 | 0,01  | NASDAQ     | for Exch - NQI #VALUE! |
| BE      | 0,52  | 0,01  | BE     | -0,37 | 0,04  | NIKKEI     | 16140,16140,34         |
| UK      | 1,39  | -0,04 | UK     | 0,31  | -0,03 | DAX        | 9167,8,9167,80         |
| JP      | -0,06 | -0,01 | JP     | -0,23 | 0,00  | DJ euro-50 | 2820,2820,24           |

|     |        |          |       |           |       | USD  | td          | -1d           |
|-----|--------|----------|-------|-----------|-------|------|-------------|---------------|
| IRS | EUR    | USD (3M) | GBP   | EUR       | -1d   | -2d  | Eonia EUR   | -0,247,-0,001 |
| 3y  | -0,124 | 0,882    | 0,786 | Euribor-1 | -0,26 | 0,00 | Libor-1 USD | 0,51,0,51     |
| 5y  | 0,035  | 1,104    | 0,934 | Euribor-3 | -0,20 | 0,00 | Libor-3 USD | 0,59,0,59     |
| 10y | 0,545  | 1,557    | 1,363 | Euribor-6 | -0,13 | 0,00 | Libor-6 USD | 0,74,0,74     |

| Currencies | -1d            | Currencies | -1d            | Commoditie | CRB      | GOLD    | BRENT |
|------------|----------------|------------|----------------|------------|----------|---------|-------|
| EUR/USD    | 1,1031,0,0019  | EUR/JPY    | 123,72,0,53    |            | 160,4359 | 1236,21 | 34,13 |
| USD/JPY    | 112,18,0,32    | EUR/GBP    | 0,7913,0,0040  | -1d        | -2,20    | 10,61   | 1,18  |
| GBP/USD    | 1,3936,-0,0044 | EUR/CHF    | 1,0899,-0,0037 |            |          |         |       |
| AUD/USD    | 0,7175,-0,0012 | EUR/SEK    | 9,3548,0,01    |            |          |         |       |
| USD/CAD    | 1,3717,-0,0079 | EUR/NOK    | 9,5542,0,08    |            |          |         |       |

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