Sunrise

Thursday, 17 December 2015

Rates: Fed's message protects downside US rate markets

The Fed started its monetary tightening cycle by hiking its policy rate by 25 bps. In 2016, Fed governors pencil in 4 more rate hikes, which is more hawkish than markets/investors anticipated. The immediate market reaction was modest, though we think that the Fed's message puts a bottom below US rate markets and warrants a sell-on-upticks approach in US Treasuries.

Currencies: Dollar gains modestly on FOMC

The FOMC decision caused some volatility but in the end the dollar gained modestly on euro and yen. The risk-on sentiment overnight gives the dollar some more momentum. However, we don't expect a big leap forward. USD/JPY tests support at 122.25, EUR/USD may go for a test of the 1.08 handle. A break would improve the dollar picture technically.

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	↘

- Yesterday, **European equities** continued on their positive momentum and ended the session with modest gains. **US equities** perceived the rate hike as an end to uncertainty as US stocks close 1.5% higher. Overnight, **Asian equities** continue on the positive WS sentiment as all main indices show decent profits.
- **The Federal reserve decided to raise their benchmark interest rates by 25 bps to 0.5%**, exactly 7 years after they cut their rates the last time to 0.25%.
- **Argentina is lifting capital controls and will let the peso trade more freely with immediate effect.** This marks the **biggest move** yet by newly elect President Mauricio Macri **to open up the economy en regain investor's trust.**
- The **New Zealand economy expanded by 0.9% Q/Q in the third quarter, making it the strongest quarter this yea**r, taking the annual rate of **GDP growth to 2.3% Y/Y**, which was exactly in line with the consensus.
- **Another day, another lower fixing for the Renminbi by the PBoC**, making it the 9th straight session that the PBoC has set a weaker fixing for its currency.
- **Commodity prices felt some downward pressure** overnight, as the **Brent Crude** traded lower to **$37.20/barrel**. **Metal prices also felt pressure** as Gold is down -0.48%, Palladium fell -2.5% and copper is also down -0.6%.
- Today the **eco-calendar** contains **the Philly Fed business** outlook for December and the **weekly jobless claims** in the US. In the eurozone there is the German **IFO business indicator**. The ECB publishes its economic bulletin today and Norway decides on its benchmark interest rate.
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Rates

Fed starts tightening cycle

Yesterday, global core bonds traded with a marginal downward bias going into the FOMC meeting. European stock markets rebounded further, but oil prices were back under downward pressure. Brent closed below $38/barrel for the first time since 2008.

Fed starts tightening cycle

Governors expect 4 more rate hikes in 2016

The Fed started its monetary tightening cycle by hiking its policy rate corridor by 25 bps to 0.25%-0.50%. The unanimous decision marks the end of 7-yr ZIRP. *"We have very low rates and we've made a very small move"*, Fed chairwoman Yellen said. The Fed's decision reflects confidence in the US economy, citing a substantial improvement in labor market conditions and an economy on a path of sustainable improvement. Fed officials were reasonably confident that inflation would rise, but if it doesn't pick up, the central bank would need to reconsider the outlook and put in place appropriate policy. **Looking forward, the Fed dots signal 4 rate hikes in 2016 (1.375%). That's unchanged from the September projections and more hawkish than markets anticipated.** The median dot for end 2017 and end 2018 was slightly lower than previously (2.375% and 3.25% respectively) while the longer run neutral rate remained unchanged at 3.5%. GDP, inflation and unemployment forecast were also broadly the same. The market reaction following the historical rate hike was rather modest. US Treasuries were under slight downward pressure with the front end of the curve underperforming. US yields increased by 1.8 bps (30-yr) to 5.5 bps (5-yr) with the 2-yr yield breaking above 1%. The Fed funds future strip curve shifted around 5 bps higher and the market implied probability of a March 2016 rate hike increased to 40.5%.

	US yield	-1d
2	1,0087	0,0366
5	1,7241	0,0331
10	2,2623	-0,0017
30	2,9659	-0,0197

US 2-yr yield above 1%

	DE yield	-1d
2	-0,3230	0,0110
5	-0,0205	0,0239
10	0,6767	0,0208
30	1,4574	0,0274

German IFO & Philly Fed Business Outlook

Upside risks Philly Fed Business Outlook

Today the eco-calendar contains the Philly Fed business outlook for December and the weekly jobless claims in the US. In the eurozone there is the German IFO business indicator. The Philly Fed business outlook is expected to decline from 1.9 to 1.0 in December, but we see some upward risks to the number. The initial jobless claims are expected to decline from 282k to 275k, and the continuing claims are expected at 2200k, down from 2243k last week. We side with the market consensus. In Germany, the IFO business indicator is expected to remain stable at 109.0, with a stabilization of the current assessment indicator at 113.4. The expectations indicator is expected to increase from 104.7 to 105.0, we side with the market expectations. The ECB also publishes its economic bulletin today and Norway decides on its benchmark interest rate.

US Note future (black) and S&P future (orange): historical rate hike, but modest market reaction

US 2-yr yield moves above magical 1%-border for the first time since 2010

R2	161,71	-1d
R1	160,66	
BUND	**157,36**	-0,3300
S1	156,4	
S2	154,54	

Event risk negative for Spanish auction

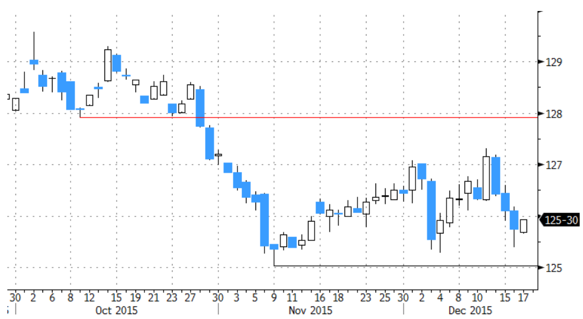
On Thursday, the Spanish debt agency auctions the on the run 5-yr Bono (1.15% Jul2020) and two off the run Obligacions (4.4% Oct2023 & 4.9% Jul2040). On the Spanish yield curve, the Jul2020 bonds is a little expensive while the Jul2040 offers pick-up against surrounding Obligacions. Spanish bonds cheapened slightly in ASW spread terms the past couple of days. Apart from the supply, this has also to do with this weekend's general election. This event risk could weigh on supply at this final Spanish auction of the year.

Today: Firm bottom below US & European rate markets

Overnight, Asian stock markets build on yesterday's positive momentum on WS. Japanese and Chinese indices outperform, trading up to 1.5% higher. The US Note future trades off yesterday's lows.

Today, the eco calendar contains German IFO, Philly Fed Business Outlook and weekly claims. However, yesterday's FOMC decision will be today's hottest talking point. Earlier we argued that the **December ECB meeting took the angle out of the threat that the ECB will ease policy forever. That put a bottom under European rate markets. Yesterday's FOMC decision and Yellen's guidance suggests that also in the US a firm bottom is in place.** The future path remains of course data dependent, **but we prefer a sell-on-upticks approach in US Treasuries with an underperformance of the frond end of the curve expected (bear flattening).** Short term, risk sentiment on equity markets and commodity prices remain a wildcard.

German Bund: Sideways trading range



US Note future (March contract!!): Topside protected by start Fed tightening cycle

Currencies

Dollar gains modestly on FOMC outcome

Dollar gains modestly, but we don't expect big leap forward.

Positive risk sentiment extended overnight

R2	1,1124	-1d
R1	1,1087	
EUR/USD	**1,0859**	-0,0087
S1	1,0524	
S2	1,0458	

Yesterday, little occurred in the FX markets ahead of the FOMC. The Fed rate hike was widely expected and quite some policy divergence between the Fed and the likes of the ECB (and the BOJ) is already discounted. The Fed confirmed that policy normalisation will be gradual. **The Fed dots suggest** 4 additional rate hikes in 2016. This is no outright predication of what the Fed actually will do, but it is less dovish than we expected. **Short-term interest futures also incorporate a second rate hike in spring rather than in the summer**. This gives the dollar some additional interest rate support. The reaction on other markets (equities, oil..) will also have an impact on the performance of the dollar. If the risk-on rally slows, further sustained USD gains might be less evident short-term. Global market liquidity will also gradually dry up as soon as the post-Fed repositioning is done. Trading might become more erratic in nature. **To summarize: the Fed policy decision/communication is slightly positive for the dollar, but we don't expect a big leap higher of the dollar anytime soon. The downside of the dollar, especially against the euro, looks better protected now.**

Dollar technicals remain neutral

From a technical point of view, EUR/USD cleared the 38% retracement from 1.1714 to 1.0524 standing at 1.0979, making the picture again neutral. A previous range bottom/break down area comes in at 1.1087 and finally the 62% retracement from the October high at 1.1124. **If this area would be broken it would make the picture dollar bearish**. However after the Fed decision, this area looks better protected. A sustained decline below 1.0796 would improve the technical picture for the dollar. **USD/JPY dropped below a short-term range bottom in the 122.25 area, turning the short-term picture in this cross rate negative.** A sustained improvement in risk sentiment is needed to halt this decline. The pair currently tries to regain this previous support, but we are not convinced that this attempt will succeed.

EUR/USD: Will EUR/USD drop again below 1.08?

USD/JPY: Following FOMC, pair tries to regain 122.25 resistance

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Tion

EUR/GBP holding near the recent lows

R2	0,7493	-1d
R1	0,7302	
EUR/GBP	**0,7256**	-0,0017
S1	0,6983	
S2	0,6936	

On Tuesday, sterling entered calmer waters as risk sentiment improved, but the rebound missed conviction. Expectations that a BoE rate hike is still far away and lingering uncertainty on Brexit prevented a more protracted rebound. This pattern continued **on Wednesday, when the UK labour data were** mixed. The unemployment rate declined to 5.2% and employment growth was strong, but earnings growth slowed more than expected **Sterling lost temporary ground after the labour data. EUR/GBP jumped to the 0.7290 area, but the move petered out. Later, global market moves aftere the Fed decision dominated trading in EUR/GBP and cable. EUR/GBP retested the 0.73 area around the time of the Fed decision, but declined later in line with EUR/USD. The pair closed the session at 0.7273, little changed from Tuesday's close (0.7267). USD strength pushed cable temprory below the 1.50 mark. The pair closed the day at 1.5004 off from the 1.5040 opening levels.**

Today, the UK retail sales and the CBI trend orders will be published. ONS retail sales were volatile over the previous months. Domestic demand is still the key driver for UK growth. However, of late there were tentative signs that the momentum of private consumption/retail sales slowed. November retail sales are expected at 0.5% M/M and 2.2% Y/Y (after -0.9% M/M decline last month). **A figure below consensus might cement expectations the a BoE rate hike is still way off and thus be sterling negative**. **For now, we see little positive spill-over effects from the Fed rate hike on sterling (against the euro).** A sustained rebound of EUR/GBP above 0.73 would deteriorate the short-term picture for sterling. **We wait for clearer signs of a topping out process before reconsidering EUR/GBP shorts.**

EUR/GBP Little changed near the 0.73 big figure

Cable: towards lower end range after FOMC towards 1.50 barrier

Calendar

Thursday, 17 December		Consensus	Previous
US			
14:30	Current Account Balance (3Q)	-$118.6b	-$109.7b
14:30	Philadelphia Fed Business Outlook (Dec)	1.0	1.9
14:30	**Initial Jobless Claims**	**275k**	**282k**
14:30	**Continuing Claims**	**2200k**	**2243k**
16:00	Leading Index (Nov)	0.1%	0.6%
Japan			
00:50	Trade Balance (Nov)	A: -¥379.7b	¥111.5b
00:50	Trade Balance Adjusted (Nov)	A: -¥3.3b	-¥202.3b
00:50	Exports YoY (Nov)	A: -3.3	-2.1
00:50	Imports YoY (Nov)	A: -10.2	-13.4
UK			
10:30	**Retail Sales Ex Auto Fuel MoM/YoY (Nov)**	**0.5%/2.2%**	**-0.9%/3.0%**
10:30	**Retail Sales Inc Auto Fuel MoM/YoY (Nov)**	**0.6%/3.0%**	**-0.6%/3.8%**
12:00	CBI Trends Total Orders (Dec)	-10	-11
12:00	CBI Trends Selling Prices (Dec)	--	-2
EMU			
11:00	Construction Output MoM/YoY (Oct)	--/--	-0.4%/1.8%
11:00	Labour Costs YoY (3Q)	--	1.6%
Germany			
10:00	IFO Business Climate (Dec)	109.0	109.0
10:00	**IFO Current Assessment (Dec)**	**113.4**	**113.4**
10:00	**IFO Expectations (Dec)**	**105**	**104.7**
France			
22:00	Business Confidence (Dec)	101	102
22:00	Manufacturing Confidence (Dec)	102	102
22:00	Production Outlook Indicator (Dec)	--	10
22:00	Own-Company Production Outlook (Dec)	--	4
Italy			
10:00	Trade Balance Total (Oct)	--	2186m
10:00	Trade Balance EU (Oct)	--	760m
Norway			
10:00	**Deposit rates**	**0.75%**	**0.75%**
Sweden			
09:30	Unemployment Rate (Nov)	6.6%	6.7%
Events			
10:00	**EMU - ECB Publishes Economic Bulletin**		
10:30	Spain - Eur 2-3bn; 1.15% Jul 2020 Bono, 4.4% Oct 2023 Obligacion, 4.9% Jul 2040 bonds Obligacion		
10:30	Norway - Norway's Olson speaks following rate decision		
11:30	UK - Gbp 0.7bn 1.25% Nov 2032 I/L Gilt		
19:00	US - Usd 16bn 5-year TIPS auction		

10-year	td	-1d	2-year	td	-1d	STOCKS		-1d
US	2,26	0,00	US	1,01	0,04	DOW	17749	17749,09
DE	0,68	0,02	DE	-0,32	0,01	NASDAQ	'or Exch - NQI	#VALUE!
BE	0,99	0,02	BE	-0,30	-0,01	NIKKEI	19354	19353,56
UK	1,95	0,00	UK	0,62	-0,01	DAX	10469,26	10469,26
JP	0,30	0,00	JP	-0,01	0,00	DJ euro-50	3247	3246,78

							USD	td	-1d
IRS	EUR	USD (3M)	GBP	EUR	-1d	-2d	Eonia EUR	-0,241	-0,002
3y	0,044	1,306	1,207	Euribor-1	-0,19	0,00	Libor-1 USD	0,50	0,50
5y	0,323	1,655	1,500	Euribor-3	-0,13	0,00	Libor-3 USD	0,58	0,58
10y	1,000	2,150	1,956	Euribor-6	-0,04	0,00	Libor-6 USD	0,74	0,74

Currencies		-1d	Currencies		-1d	Commoditie	CRB	GOLD	BRENT
EUR/USD	1,0859	-0,0087	EUR/JPY	132,85	-0,52		174,2269	1067,2	37,25
USD/JPY	122,34	0,47	EUR/GBP	0,7256	-0,0017	-1d	-0,04	3,00	-0,92
GBP/USD	1,4958	-0,0088	EUR/CHF	1,0807	-0,0025				
AUD/USD	0,7180	-0,0020	EUR/SEK	9,2782	-0,01				
USD/CAD	1,3801	0,0065	EUR/NOK	9,5701	0,07				

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