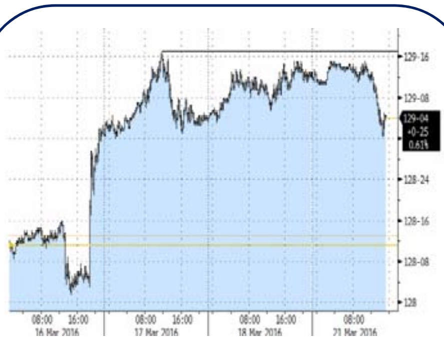
Sunset

Monday, 21 March 2016

Headlines

- European shares opened lower and tried to reverse their losses early in the session, but attempts failed around noon, when stocks dropped again. Currently, **most European indices trade 0.5% lower**. **US Equities trade slightly lower** too, but losses are more limited.
- **ECB's Liikanen reiterated that policy rates are expected to remain at present or lower levels for the an extended period of time**. Bank of France governor Villeroy defended the use of negative rates but also warned it has limits.
- **The German economy started 2016 in good shape** thanks to industrial production gaining traction and domestic demand providing support, the German Finance Ministry said today. The **Bundesbank** however warned that order data point to slowing growth momentum in the second quarter.
- After reaching its second-highest level since 2007 in January, **US existing home sales dropped twice as much as expected in February.** Existing home sales fell by 7.1% M/M to a total of 5.08 million, inventories however picked up sharply, boding well for future activity.

Rates



US Note future (intraday since dovish FOMC meeting): already signs of fatigue?

US Treasuries underperform on 1st hawkish Fed talk

Global core bonds traded with a downward bias after an initial jump higher with US Treasuries underperforming German Bunds. Higher oil prices and hawkish Fed comments partly explain the move. Risk sentiment on equity markets didn't impact trading. At the time of writing, the US yield curve bear steepens with yields 0.2 bps (2-yr) to 4.1 bps (30-yr) higher. Changes on the German yield curve vary between flat (5-yr) and +1.5 bps (30-yr). **On intra-EMU bond markets**, 10-yr yield spread changes versus Germany are nearly unchanged with Ireland (+3 bps) and Greece (+7 bps) underperforming.

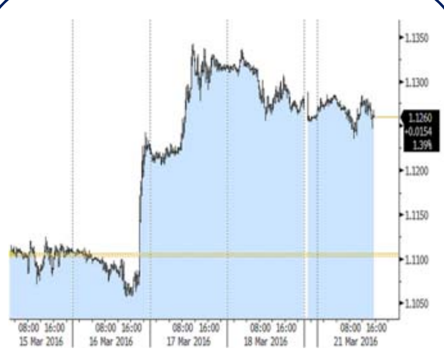
The Bund traded firm until European noon, outperforming US Treasuries, despite rising oil prices and positive risk sentiment on equity markets. Dovish comments **by ECB Liikanen** might have been marginally supportive, though he only stated the obvious by reiterating that policy rates are expected to remain at present or lower levels for the an extended period of time. *"If the outlook or financing conditions deteriorate, the ECB has still capacity to boost inflation and growth"*, he added. **ECB Villeroy** defended the use of negative interest rates though he stressed that they have their limits. Villeroy didn't think that deflationary dynamics are at work at this stage. **Richmond Fed Lacker**, hawkish non-voter, completed this morning's central bank talk by saying that he's confident that inflation will return to 2%: *"The recent data on inflation - because* *they have come in firmer than expected - suggests that upside risks to inflation have increased maybe not significantly, but I think noticeably and materially".*

Around European noon, global core bonds turned south without strong driver. **Oil prices continued their run higher**, while sentiment on stock markets soured. The underperformance of US Treasuries could have been driven by comments by **SF Fed governor Williams** (heavyweight centrist non-voter), who told MNI that he will be **advocating for another interest rate hike as early as the April meeting** or, failing that, at the June meeting provided that the economy continues to do as well as it has been. He said that *"in a vacuum, if it weren't for global factors, we would be rising rates sooner and I think more quickly than we are because of the global factors and because of the uncertainties around these factors at the zero lower bound"*. On Friday, Williams already downplayed the importance of soft market-based US inflation measures. **US existing home sales** disappointed, but were ignored.

Currencies

USD drifts marginally higher in technical trade

Today, there was no clear story to guide USD trading. ECB policy makers kept a soft tone. Fed speakers were slightly more hawkish. At the margin, this combination was slightly positive for the dollar. US eco data were weaker than expected, but ignored. EUR/USD trades around 1.1260. USD/JPY rebounded to the 112.70 area.



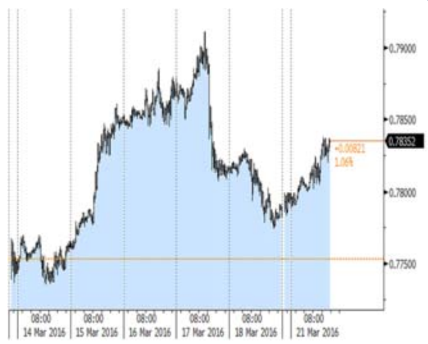
EUR/USD (1w): dollar gains marginally

This morning, Asian equities showed a mixed picture. Most indices recorded modest losses despite a positive close in the US on Friday. Chinese equities outperformed as regulators eased restrictions on margin lending. However, this was a China-specific issue and not really important for European markets. Oil also traded slightly lower this morning. The dollar was off the post-Fed lows as oil drifted again south. EUR/USD traded in the 1.1265 area going into the European market opening. Japanese markets were closed. USD/JPY held in the mid 111 area.

European (equity) markets didn't know which card to play. Indices opened in the red, but gradually returned back into positive territory. Oil also rebounded off the intraday lows. EUR/USD was initially under pressure in line with oil and set an intraday low in the 1.1236 area early in Europe, before rebounding in lockstep. In technical trade, the pair settled in a tight 1.1250/90 range. ECB Lilkanenen defended the aggressive ECB approach and indicated that the ECB has still capacity to boost growth and inflation. Short-term interest rate differentials between the US and Germany widened slightly, but the direct impact on currency trading remained limited.

There was still no clear driver during the US trading session. SF Fed Williams spoke out in favour of a rate hike in April or June. This was maybe slightly supportive for the dollar. US data (Chicago Fed activity/Existing home sales) were weaker than expected but had also no lasting impact on the dollar. Trading remained in the first place order-driven and technical in nature. At the margin, the dollar traded with a slightly positive bias. EUR/USD currently changes hands in the 1.1260 area. USD/JPY is fairly well bid and trades in the 111.70 area, admittedly in thin market conditions.

Sterling fails to extend rebound



EUR/GBP (1w): sterling rebound halts

After rebounding at the end of last week, sterling traded again with a slight negative bias today. Tensions in the UK government and uncertainty on Brexit weighed on the UK currency. The Rightmove house prices were strong. CBI orders (-14 from -17) improved as expected, but the data were again largely ignored as a factor for GBP trading. Cable dropped already below 1.44 this morning and struggled to regain this level later in the session (currently 1.4380 area). EUR/GBP traded with an upward intraday bias and set an intraday top around 0.7837 around noon. The pair currently still trades within reach of the intraday top. Several factors were at paly, but sterling weakness prevails.

16:00 CET

Daily EMU spread changes (bps)

	5-yr			10-yr			30-yr		
	Yield	Spread	Change	Yield	Spread	Change	Yield	Spread	Change
Germany	-0,29%			0,23%			0,94%		
Greece	#VALUE!	#VALUE!	#VALUE!	8,64%	842	1,8	#VALUE!	#VALUE!	#VALUE!
Portugal	1,84%	213	1,8	2,94%	272	0,4	3,83%	289	-2,5
Italy	0,29%	58	1,2	1,27%	104	-0,5	2,40%	147	-3,5
Spain	0,37%	66	1,2	1,45%	122	0,2	2,62%	169	-1,6
Ireland	0,07%	37	4,8	0,85%	62	3,4	1,81%	87	2,8
Belgium	-0,23%	6	-0,1	0,61%	39	-0,6	1,60%	67	-1,5
France	-0,16%	13	0,3	0,57%	34	-0,4	1,47%	54	-1,2
Austria	-0,27%	3	0,6	0,43%	20	-0,6	1,35%	42	-0,3
Netherlands	-0,31%	-2	-0,1	0,32%	9	-0,5	1,05%	12	-0,3
Finland	-0,16%	14	0,6	0,53%	31	0,3	1,13%	20	-0,2
US	1,36%	166	3,2	1,91%	168	2,0	2,72%	178	1,6
UK	0,89%	119	2,7	1,48%	125	1,8	2,33%	139	0,6

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