

Daily Market Strategy

Monday, 14th September 2009

Market Strategy

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- US/China trade war concerns
- UK 5y swap target lowered

Market Outlook

Kenneth Broux

Opening levels (7.15am)

£/\$: 1.6585, €/\$: 1.4527, \$/Y: 90.57

UK 5y sw: 3.26%, US 5y sw: 2.63%, EU 5y sw: 2.69%

Overnight

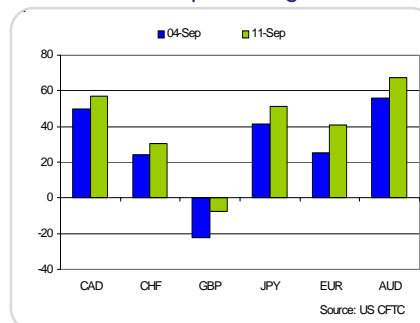
- The Observer reports UK small businesses will be able to borrow money from City pension funds and insurance companies under plans drawn up for the Pre-Budget Report
- US President scheduled to speak in Wall Street later today
- US Treasury to publish 'The Next Phase' outlining transition to rebuilding and rehabilitation of the financial system (WSJ)

The US decision to impose trade sanctions on Chinese tyre imports for three years sets the early tone for markets as the week gets underway. The Shanghai composite took the US announcement on Friday in its stride and is currently trading 1% higher. US futures and UK/European equities have opened the day lower and make it hard to turn bearish vis-a-vis government bonds. We have lowered our near-term forecast for UK 5y swaps to 3.20% following a test of 3.25%. With tame UK CPI and wage data looming over the next couple of days and the US Treasury not selling any supply this or next week, we suspect long-term yields and flatter yield curves could be favoured. EU-16 July industrial output is forecast to show a decline of 0.2% m/m.

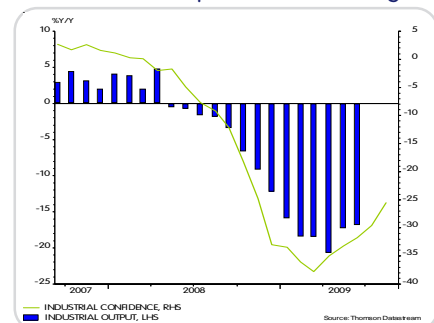
FX: IMM positioning data have admittedly not worked that well with regard to estimating short-term GBP flows/direction and we suspect the net decline in GBP shorts (sterling bullish) may not be of much value over the next few days either as dealers take (prospective) M&A flows into account. GBP/USD eased back to the middle of the recent range in place since August 5 around 1.6579. The return of risk aversion and the prospect of weak UK inflation (CPI/wages) data over the next couple of days could give sterling bears the upper hand and force a reversal towards initial 1.65 support. We are also keeping a close eye on CHF prior to the SNB meeting on Thursday, aware of the SNB's objective to weaken the CHF. EUR/CHF is still finding good support below 1.5150 and bounced off 1.5111 overnight.

Rates: UK 5y swaps opened at 3.26%, with the 2y/10y swap curve flattening to 207bps, down 3bps from Friday's close. Lower LT yields and flatter curves are our favourite call as we position for soft UK CPI tomorrow. US Treasuries are outperforming bunds and gilts as lower S&P futures trigger a flight-to-quality. Look for US 10y yields to test 3.30%. Greece/German 10y spreads approach 100bps support. The DMO sells the 6%, 2028 gilt today via mini-tender for £1.0bn.

Weekly IMM data show reduction in GBP short positioning



Worst may have passed, but EU-16 industrial output is still contracting



	Close	Daily Change %
FX		
EUR/GBP	0.8747	-0.08%
GBP/USD	1.6657	0.03%
EUR/USD	1.4571	-0.08%
USD/JPY	90.710	-1.12%
AUD/USD	0.8634	-0.07%
Bonds %		
US 10Yr	3.347	0.0
EUR 10Yr	3.236	-6.8
UK10 Yr	3.678	-8.1
UK 5yr Swap	3.255	-4.3
Equities		
S&P500	1042.73	-0.14%
FTSE100	5011.47	0.48%
Eurostoxx50	2831.37	0.49%
Shanghai Composite	3025.50	1.19%
Commodities		
Crude Oil \$/bl	69.29	-3.68%
Gold \$/oz	1005.2	0.86%
Copper	284.7	-1.04%
Baltic Dry	2468	-0.96%
Other		
VIX	24.15	2.55%
iTraxx XOVER	563.17	-19.0

Today's Events

	Time	Consensus	Previous
Japan Industrial Output, Jul	05:30	n/a	+1.9%
EU-16 Industrial Output, Jul	10:00	-0.3%	-0.6%
Canada Capacity Utilisation, Q2	13:30	65.0%	69.3%
BoE buys £1.4bn of gilts: UKT_5_070325, UKT_4.25_071227, UKT_4.75_071230, UKT_4.25_070632, UKT_4.5_070934			
Fed speakers: Duke (13:35), Lacker (17:30), Yellen (20:50)			

Paul Rodriguez, Senior Technical Analyst

- The temptation to sell the FTSE on a '5' handle together with the nervous nature of the market short term has set-up a retracement phase for UK stocks. Whilst Dec. FTSE futures target 5,338 and S&P cash targets 1,106, the route could be via a retracement. Despite this, the view is still seen as a rally in a bear market from a long term-perspective. Whilst support in the S&P holds at 1,018, the view is bullish for the medium term. Shanghai stocks are modestly bid with the composite Index breaking through key resistance at 3,000, but the market is focusing on the Nikkei which is down 2.32% and the Hang Seng which has failed to hold 21,000 support.
- With stock futures lower this morning and commodities easing back from Friday, the dollar has rebounded. Resistance at 77.45 could well be tested in the DXY before the trend reverses. 75.00 remains the target. Commodity currencies have been hit on the back of this and GBP is under pressure. It feels more like a Monday morning pullback than a change in trend, but the market is sensitive to equity weakness.
- Yields continue to soften, encouraged by the albeit modest retracement in stocks. UK 2y swaps key support at 1.80% - a break creates a new record low. UK 5y swaps ease below the 200 day m.a. (see below) with support at 3.20%. The longer-term bias is bullish, but traction is limited. UK 2y yields still need to break through 1.00% to complete a reversal pattern. This is unlikely with stocks easing lower.
- Gold slips below \$1,000 having traded up to \$1,010 on Friday. The swings are getting larger as the battle between the gold bugs and the deflationists hots up. The technical bias is bullish, but it would help if base metals could extend through range highs - particularly copper through 300 c/lb. After weeks of consolidation, if a break upwards is not forthcoming soon, the corrective risk will become compelling. This could be a pivotal week for the commodity markets as crude oil eases back below \$69.00. A break of \$65.50 completes a short-term reversal pattern.

Chart of the day: GBP 5-year swaps



Key Levels

	EUR	GBP	JPY	EUR/GBP	GBP/EUR
R2	1.4865	1.7044	95.15	0.8910	1.1905
R1	1.4720	1.6746	93.41	0.8835	1.1819
Current Spot	1.4531	1.6587	90.56	0.8761	1.1415
S1	1.4330	1.6113	90.30	0.8461	1.1319
S2	1.4177	1.5975	87.14	0.8400	1.1223

Spot prices as of: 07:08:42 Source: Bloomberg

Yields remain soft despite the ongoing rally in equities. GBP 5-year swaps sink below the 200 day m.a. at 3.2853%. 3.20% is a major support point.

	Spot	Bias	Entry	Target	Stop	Comment/Levels
EUR/USD	1.4531	Bullish	1.4350	1.4720	1.4465	Stop raised.
USD/JPY	90.56	Neutral	-	-	-	
USD/CHF	1.0409	Bearish	-	1.0300	-	
GBP/USD	1.6587	Bullish	1.6480	1.7000	1.6480	Stop raised.
EUR/GBP	0.8761	Bearish	0.8835	0.8400	0.8835	
GBP/JPY	150.22	Bullish	151.50	156.00	151.50	
EUR/JPY	131.60	Bullish	133.60	139.14	132.40	Stop hit.
CAD/JPY	83.48	Bullish	85.60	90.35	83.95	Stop hit.
AUD/USD	0.8567	Bullish	0.8305	0.9000	0.8530	
USD/CAD	1.0849	Bearish	1.0800	1.0000	1.0920	
NZD/USD	0.6975	Bullish	0.6860	0.7447	0.6860	
USD/BRL	1.8306	Bearish	1.8338	1.8000	1.8455	
USD/PLN	2.8826	Bearish	2.8638	2.7000	2.8555	Stop hit.
USD/HUF	188.03	Bearish	188.00	180.00	188.00	Stop hit.

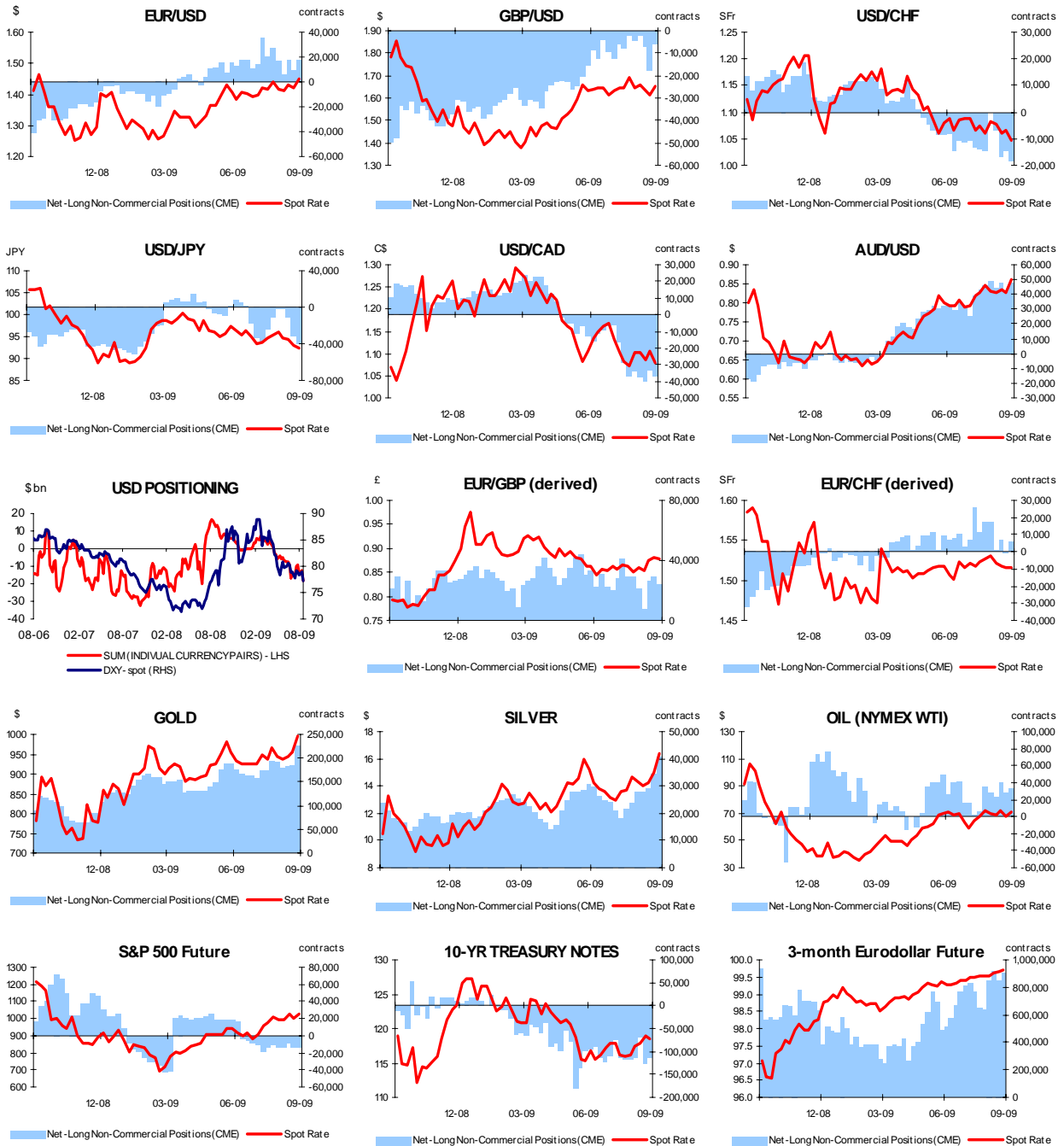
Spot prices source: Bloomberg

[ENTRY](#) - Targetted

ENTRY - Active

Quantitative Market Analysis

FX & Commodity Futures Positioning



Trend following model signals

Trend Following Model Positions			
	Signal	Date	Entry Level
AUDUSD	short	17-Aug-09	0.8327
NZDUSD	long	10-Jul-09	0.6298
EURUSD	long	09-Sep-09	1.448
GBPUSD	long	09-Sep-09	1.6490
USDCHF	short	17-Jul-09	1.0730
USDCAD	short	08-Sep-09	1.0780
USDSEK	short	09-Sep-09	7.0444
USDNOK	short	21-Jul-09	6.3025
USDJPY	short	20-Aug-09	94.07

Trend Following Model Positions			
	Signal	Date	Entry Level
USDCZK	short	19-May-09	19.709
USDPLN	short	09-Sep-09	2.8278
USDSGD	short	08-Sep-09	1.4337
USDTRY	long	27-Aug-09	1.5093
USDZAR	short	31-Aug-09	7.7525

Market Summary

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EUR/USD	1.4571	-0.08%	S&P500	1042.73	-0.14%
USD/JPY	90.710	-1.12%	DJIA	9605.41	-0.23%
AUD/USD	0.8634	-0.07%	FTSE100	5011.47	0.48%
EUR/GBP	0.8747	-0.08%	Eurostoxx50	2831.37	0.49%
GBP/EUR	1.1432	0.11%	Shanghai Composite*	2989.79	1.30%
GBP/USD	1.6657	0.03%	*latest price		
GBP/JPY	151.09	-1.09%	Commodities		
GBP/CHF	1.730	0.03%			%
GBP/AUD	1.929	0.11%	Crude Oil \$/bl	69.29	-3.68%
GBP/CAD	1.794	0.04%	Gold \$/oz	1005.2	0.86%
GBP/NZD	2.355	-0.44%	Copper c/lb	284.7	-1.04%
GBP/NOK	9.900	-0.04%	Silver \$/oz	16.75	0.48%
GBP/ZAR	12.395	-1.63%	Baltic Dry	2468	-0.96%
GBP/CNY	11.377	0.04%			
Bonds %			Swaps %		
		bp			bp
US 10Yr	3.347	0.0	US 5yr	2.670	2.5
EUR 10Yr	3.236	-6.8	EUR 5yr	2.678	-3.9
UK10 Yr	3.678	-8.1	UK 5yr	3.255	-4.3
Other			Official Rates %		
VIX	24.15	2.55%	UK	0.50	
iTraxx XOVER	563.17	-19.0	US	0.25	
DJ Agriculture Index	56.75	-0.54%	EU	1.00	
			Japan	0.10	

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