

Daily Market Strategy

Tuesday, 15th September 2009

Market Strategy

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- Bond friendly UK CPI data expected
- GBP ignores Moody's report on UK banks

Market Outlook

Kenneth Broux

Opening levels (7.15am)

£/\$: 1.6647, €/\$: 1.4633, \$/Y: 91.06

UK 5y sw: 3.28%, US 5y sw: 2.73%, EU 5y sw: 2.72%

Overnight

- RICS says rise in UK house prices more widespread in August, balance climbs to +10.7 vs -5.7% in July, highest since May 2007
- Moody's predicts £130bn of new losses for UK financials (FT)
- RBA minutes say need to adopt less expansionary policy 'in due course'

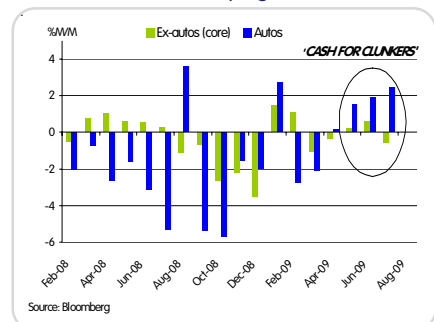
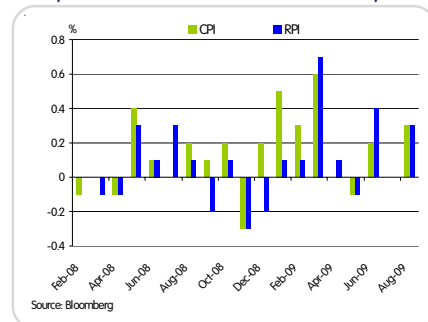
Dealers have been repeatedly taken off guard by stronger UK CPI data this year (a stronger number in four out of seven months, see panel below) so we suspect positions will be fairly light going into the August release at 09.30am. The consensus is for a drop to 1.4% y/y vs 1.8% y/y in July. UK 5y5y break even inflation has been trading in a narrow range around 1.8% since July - below the BoE target. A bond 'friendly' CPI number around 1.5% or lower, and BoE purchases of £1.4bn in long and ultra-long paper, should bolster support for long-term nominal rates and curve flattening in 2y/10y swaps towards 200bps. Separately, the MPC testimony to the Treasury Select Committee is about last month's Inflation Report and beyond a review of the macro outlook (will the Bank comment on Moody's report?), details of how the committee voted at the September MPC meeting and discussions about exit strategies/QE will probably have to wait until the minutes next week. The German ZEW survey, and US retail sales and PPI are also scheduled. With just one week to go to the next FOMC meeting, we doubt that chairman Bernanke will want to give anything away with regard to extending Treasury or the completion of MBS purchases.

FX: GBP crosses are bid this morning, taking a cue from the bullish RICS survey. The bearish Moody's headlines were completely ignored as markets continue to short the USD. EUR/USD could get a shot in the arm from a stronger German ZEW number at 10.00am. A breach of yesterday's 1.4653 high should be possible if US August retail sales (core) disappoint. EUR/GBP is stuck in a range around 0.8787. USD/JPY rallied for a 2nd straight session.

Rates: We are buyers of UK LT paper and favour curve flatteners ahead of UK CPI/wages/retail sales. We look for 5y swaps to reverse to 3.25% following yesterday's bounce.

Actual vs Consensus: UK CPI and RPI have surprised on 4 out of 7 months this year

Strong summer US auto sales mask weak underlying demand



	Close	Daily Change %
FX		
EUR/GBP	0.8817	0.80%
GBP/USD	1.6583	-0.44%
EUR/USD	1.4618	0.33%
USD/JPY	90.938	0.25%
AUD/USD	0.8622	-0.14%
Bonds %		
US 10Yr	3.421	7.4
EUR 10Yr	3.257	2.1
UK10 Yr	3.610	-6.8
UK 5yr Swap	3.283	2.8
Equities		
S&P500	1049.34	0.63%
FTSE100	5018.85	0.15%
Eurostoxx50	2829.25	-0.07%
Shanghai Composite	3039.45	0.42%
Commodities		
Crude Oil \$/bl	68.86	-0.62%
Gold \$/oz	1000.2	-0.50%
Copper	280.5	-1.48%
Baltic Dry	2450	-0.73%
Other		
VIX	23.86	-1.20%
iTraxx XOVER	563.13	0.0

Today's Events

Time	Consensus	Previous	
UK RICS House Prices, Jul	00:01	+10.7% A	-5.7% R
UK CPI, Aug, Y/Y	09:30	+1.4%	1.8%
UK RPI, Aug, Y/Y	09:30	-1.5%	-1.4%
UK DCLG, Jul, Y/Y	09:30	-9.5%	-10.7%
France CPI, Aug	07:45	-0.5%	+0.4%
German ZEW survey, Sep	10:00	+60.0	+56.1
US PPI, Aug	13:30	+0.8%	-0.9%
US PPI core, Aug	13:30	+0.1%	-0.1%
US Retail Sales, Aug	13:30	+1.7%	-0.1%
US Retail Sales core, Aug	13:30	+0.4%	-0.6%
NY Fed Manufacturing Survey, Sep	13:30	+14.5%	+12.1%
US Business Inventories, Jul	15:00	-0.8%	-1.1%
BoE buys £1.4bn of gilts: UKT_4.25_070336, UKT_4.75_071238, UKT_4.25_070939, UKT_4.5_071242, UKT_4.25_071246, UKT_4.25_071249, UKT_4.25_071255			
BoE MPC members testify to the Treasury Select Committee (09:45)			
Fed speakers: chairman Bernanke (15:00)			
ECB speakers: Stark (16:00)			

- Some calm has been restored to the equity markets which had a whiff of Monday morning lethargy yesterday. As Chinese stocks remain steady, the upward trend in core equities remains intact. FTSE futures target 5,338 with DAX index futures looking set for a push towards long term objectives at 5,750. Whilst resistance in the S&P cash gets left behind at 1,039 (1,049), medium-term objectives at 1,106 look set for year-end.
- Yesterday's pullback in the dollar which was exacerbated in the Eastern European currencies saw short stops being triggered. However, the sense that this was just a retracement prior to a continued fall in the dollar kept the currency in check and the target of 75.00 in the dollar index remains a minimum objective. At the very least, positions have not reversed as risk appetite remains. The cyclically sensitive period carries a weight of expectation of a large correction, but will it deliver this time? Implied option prices are steady, but the VIX continues to ease lower refuting such expectations. A break of 23.00 would be a new low for 2009 and since September last year - the favoured view.
- Yields remained steady from the open yesterday, shrugging off equity weakness and the first sign that perhaps a significant low has been reached. UK 2y swaps were brushing close to a massive level at 1.80%, but UK 2y cash yields are still holding over the 0.81% level - assumed as the low point from a technical perspective. 1.00% resistance needs to be cleared here to reverse momentum to the upside. UK 5 year swaps are whip-sawing the 200 day m.a. at 3.2845 - breakout levels are at 3.20% and 3.40%.
- The lack of a sharp squeeze in gold has disappointed some gold bugs. Resistance was there for the taking at \$1,032, but volatility ahead of this level has increased. Despite this, the broader price action is bullish, although it may take a sharper drop in the dollar to convince gold bulls to chase the market higher. Copper resistance remains at 300 c/lb. This week is pivotal for the base metal.

Chart of the day: Copper, Dec. future



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	1.4631	1.6650	91.08	0.8787	1.1380
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: 07:16:33 Source: Bloomberg

The consolidation below 300 c/lb continues but the technical pattern continues to resemble a bullish ascending triangle formation. A break above 300 c/lb is the main signal to confirm the bullish trend and is the preferred technical scenario.

	Spot	Bias	Entry	Target	Stop	Comment/Levels
EUR/USD	1.4631	Bullish	1.4350	1.4720	1.4465	Stop raised.
USD/JPY	91.08	Bullish	<u>89.90</u>	96.00	89.30	
USD/CHF	1.0346	Bearish	-	1.0300	-	
GBP/USD	1.6650	Bullish	1.6480	1.7000	1.6480	Stop raised.
EUR/GBP	0.8787	Bearish	0.8835	0.8400	0.8835	
GBP/JPY	151.66	Bullish	151.50	156.00	151.50	Stop hit.
EUR/JPY	133.27	Bullish	<u>132.00</u>	139.14	131.20	
CAD/JPY	84.23	Bullish	-	90.35	-	
AUD/USD	0.8624	Bullish	0.8305	0.9000	0.8530	
USD/CAD	1.0813	Bearish	1.0800	1.0000	1.0920	Stop hit.
NZD/USD	0.7032	Bullish	0.6860	0.7447	0.6860	
USD/BRL	1.8125	Bearish	1.8338	1.8000	1.8455	Add on a close below 1.8040.
USD/PLN	2.8589	Bearish	<u>Current</u>	2.7000	2.9210	Stop hit.
USD/HUF	186.23	Bearish	<u>Current</u>	180.00	191.10	Stop hit.

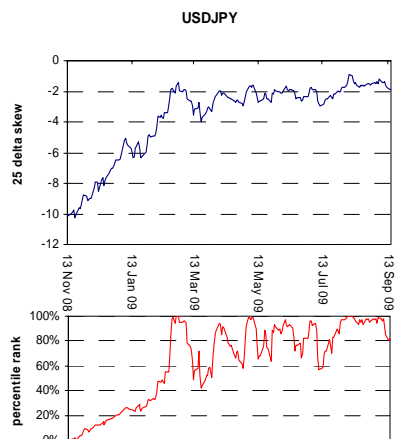
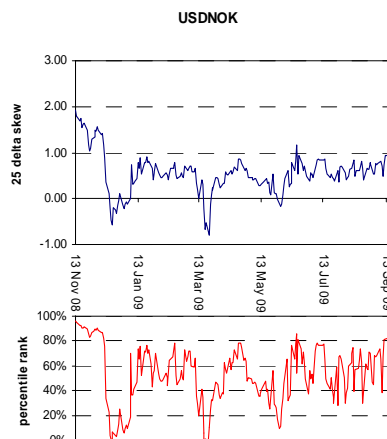
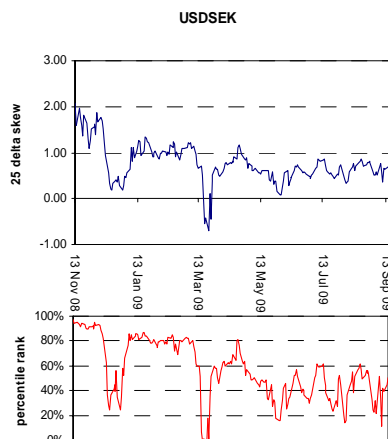
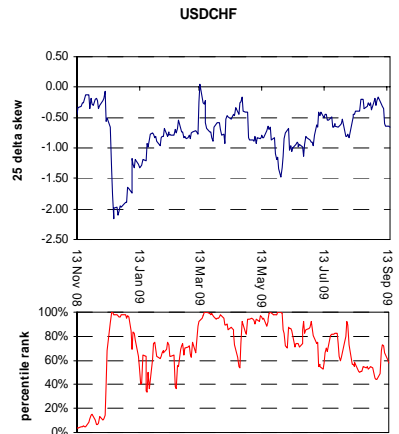
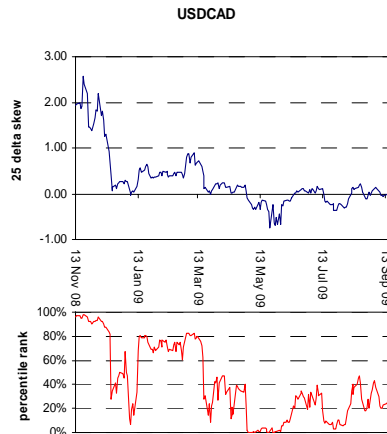
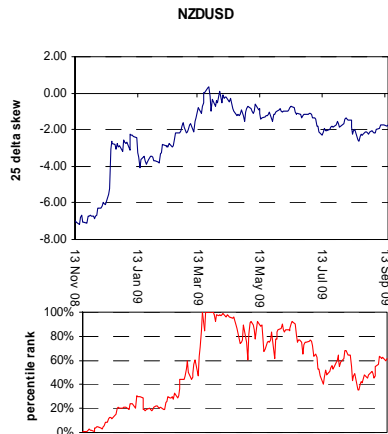
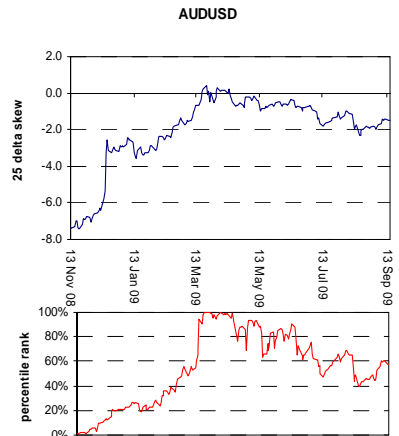
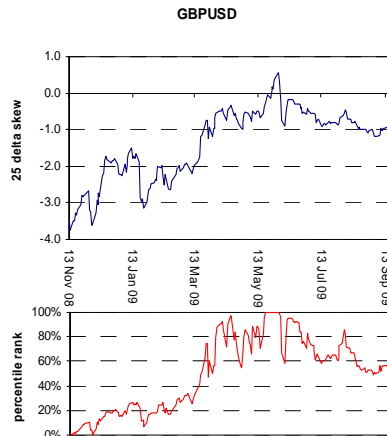
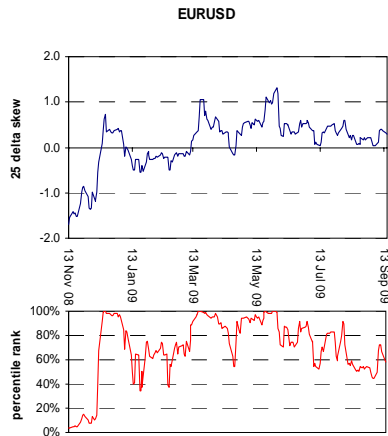
Spot prices source: Bloomberg

ENTRY - Targetted

ENTRY - Active

Quantitative Market Analysis

Option risk reversal skews



Market Summary

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AUD/USD	0.8622	-0.14%	FTSE100	5018.85	0.15%
EUR/GBP	0.8817	0.80%	Eurostoxx50	2829.25	-0.07%
GBP/EUR	1.1345	-0.76%	Shanghai Composite*	3026.74	0.45%
GBP/USD	1.6583	-0.44%	*latest price		
GBP/JPY	150.81	-0.18%	Commodities		
GBP/CHF	1.716	-0.80%	Crude Oil \$/bl	68.86	-0.62%
GBP/AUD	1.924	-0.30%	Gold \$/oz	1000.2	-0.50%
GBP/CAD	1.796	0.09%	Copper c/lb	280.5	-1.48%
GBP/NZD	2.366	0.47%	Silver \$/oz	16.55	-1.22%
GBP/NOK	9.798	-1.03%	Baltic Dry	2450	-0.73%
GBP/ZAR	12.371	-0.19%	Swaps %		
GBP/CNY	11.324	-0.47%	US 5yr	2.748	7.8
Bonds %			EUR 5yr	2.708	3.0
		bp	UK 5yr	3.283	2.8
US 10Yr	3.421	7.4	Official Rates %		
EUR 10Yr	3.257	2.1	UK	0.50	
UK10 Yr	3.610	-6.8	US	0.25	
Other			EU	1.00	
VIX	23.86	-1.20%	Japan	0.10	
iTraxx XOVER	563.13	0.0			
DJ Agriculture Index	57.38	1.12%			

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