

# Daily Market Strategy

Tuesday, 29th September 2009

## Market Strategy

### Market Strategy Team

#### Paul Rodriguez

Senior Technical Analyst  
0207 158 1744

#### Kenneth Broux

Market Economist  
0207 158 1750

#### Naeem Wahid

Quantitative Strategist  
0207 158 1741  
naeemwahid@bostreasury.com

#### Altaz Dagha

Analyst  
0207 158 1747  
altazdagha@bostreasury.com

- ECB ready to offer unlimited one-year funds (LTRO)
- Equities and bonds rally; US 10y below 3.30%

### Market Outlook

Kenneth Broux

Opening levels (7.15am)

£/\$: 1.5917, €/£: 1.4625, \$/¥: 90.07

UK 5y sw: 3.28%, US 5y sw: 2.67%, EU 5y sw: 2.71%

#### Overnight

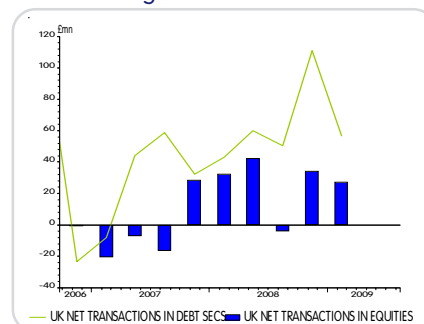
- UK car scrappage scheme extended by £100mn, Land Registry Aug house prices fall 0.1%
- BoE set to lower rate on reserves (WSJ)
- Fed's Fisher urges financial reform to restore central bank ability to manage an effective monetary policy (WSJ)

ECB president Trichet made a point yesterday that now was not the time to start unwinding policy stimulus. Helping to boost equities and bonds overnight, the central bank will be true to its word today when, for a second time in three months, it will offer unlimited funds for a one-year period at 1% (no refi premium). The flood of liquidity from the Bank back in June (€442.2bn) was to a great extent channelled into short-dated debt instruments, but a decline in overnight deposits with the ECB over the summer and a rally in equities and credit would suggest that funds could target riskier rather than risk-free assets. In the end, this unconventional credit easing measure should bolster bank lending and help investment and private sector spending to recover. In the UK, an upward revision to Q2 GDP is possible but this is backward looking data so impact on GBP and gilts should be marginal. The focus instead will be on how households are dealing with a world of tighter credit and rising unemployment. Households paid down debt in July and the latest figures are forecast to show the same for August. Q2 current account data will offer an update on overseas appetite for UK equities and gilts.

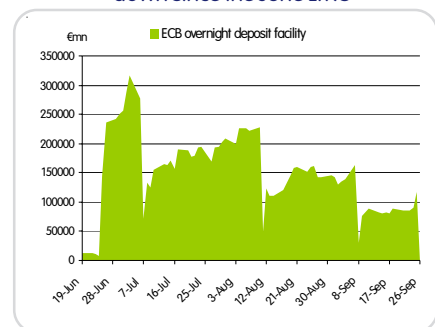
**FX:** Pro-risk trades were put back on overnight in the wake of stronger US stocks led through AUD and NZD, though the Shanghai comp is down a fraction. The dollar index backed off from a 3-week high overnight, and comments by Japanese finance minister Huji may help to protect downside in USD/JPY around 89.50. We still favour selling GBP rallies.

**Rates:** UK 5y swaps opened flat at 3.28%. Support runs at 3.26%. US 10y yields pierced 3.30% support and from here could target a break of the lower end of the 4-month trading range. The 2y/10y spread flattened below 230bps. The DMO auctions £3.75bn of 2022 gilts and BoE will buy £1.4bn in long gilts.

Did overseas buyers increase or decrease holdings of UK securities in Q2?



Overnight deposits with the ECB have come down since the June LTRO



	Close	Daily Change %
<b>FX</b>		
EUR/GBP	0.9206	-0.05%
GBP/USD	1.5882	-0.43%
EUR/USD	1.4622	-0.45%
USD/JPY	89.634	0.00%
AUD/USD	0.8725	0.52%
<b>Bonds %</b>		
US 10Yr	3.280	-3.9
EUR 10Yr	3.254	-0.2
UK10 Yr	3.610	-8.2
UK 5yr Swap	3.278	0.1
<b>Equities</b>		
S&P500	1062.98	1.78%
FTSE100	5165.70	1.64%
Eurostoxx50	2899.12	2.37%
Shanghai Composite	2763.85	0.01%
<b>Commodities</b>		
Crude Oil \$/bl	66.84	1.24%
Gold \$/oz	991.1	0.01%
Copper	272.7	-0.49%
Baltic Dry	2192	0.41%
<b>Other</b>		
VIX	24.88	-2.85%
iTraxx XOVER	569.91	-7.1

#### Today's Events

Japan, National Core CPI, Aug  
UK GDP, Q2 final  
UK Q2 Current Account, Q2  
UK Consumer Credit, Aug  
UK Net Mortgage Lending, Aug  
UK Mortgage Approvals, Aug  
EU-16 Consumer Confidence, Sep  
EU-16 Industrial Confidence, Sep  
UK CBI Distributive Trades Survey, Sep  
US CaseShiller House Prices, Jul  
US Consumer Confidence, Sep  
UK DMO auctions £3.75bn, 4%, 2022 gilts  
BoE to purchase £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  
ECB speakers: Liikanen (09:00), Constancio (09:30)  
Fed speaker: Fisher (14:50)

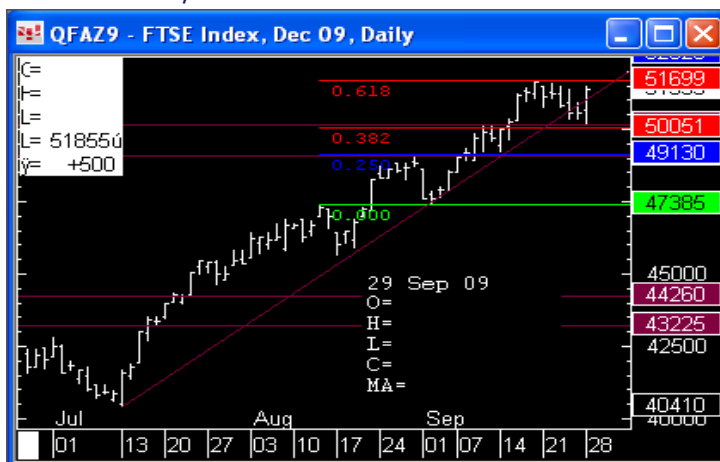
Time	Consensus	Previous
00:50	-2.4% A	-2.2%
09:30	-0.6%	-0.7%
09:30	-£7.8 bn	-£8.5 bn
09:30	+£0.1 bn	-£0.2 bn
09:30	+£0.2 bn	-£0.4 bn
09:30	51k	50.1k
10:00	-21	-22
10:00	-24	-26
11:00	n/a	-16
14:00	-14.2%	-15.4%
15:00	57.0	54.1

## Technical Analysis

Paul Rodriguez, Senior Technical Analyst

- Equity markets gripped support and a strong showing reversed the Monday morning blues for risk assets. However, the backdrop for this rebound continues against a relatively soft Chinese stock market and the fact that major bourses have been range-bound for the latter part of this month. Naturally, month and quarter-end positioning may be having some impact, but the recent high-water marks in equities are assumed to be the top for now with the bias towards selling (see chart below of FTSE futures). DAX index resistance at 5,764 is close (5,729) and it should be a formality for the bulls to take this level out - let's see if this is possible today.
- The pound managed to cling to the key 1.5800 level in London, forestalling a greater sell off. Whilst an oversold bounce is becoming more compelling here, nervousness as to the direction of key asset markets remains. A decent bounce for oil and a short squeeze in equities allowed the pound to tread water against the dollar and ease back from the overbought euro, but propelled the commodity currencies back towards the tops of their ranges. With the outlook for commodities and equities equivocal, the strategy for yesterday of selling into the risk rally continues, albeit in pared down form. EM currencies have held well and if there is to be another major upleg in liquidity rally, it is likely to be led through these currencies.
- US 10y yields continue to hover over key support at 3.25% - the lower end of the recent range. A loss of this level would not be taken well by the bond bears and would confirm a change in strategy. UK 10 y yields are a safe distance from the 200 day m.a. For the moment, yields have broadly held up well with sugar once again on a charge and gold holding on to \$990, but urgency has come out of the market and commodity bulls are taking a step back given the extended consolidation in base metals.

Chart of the day: FTSE 100 Index- Dec. Futures.



## Key Levels

	EUR	GBP	JPY	EUR/GBP	GBP/EUR
R2	1.4865	<b>1.6300</b>	95.15	0.9482	<b>1.1135</b>
R1	1.4728	1.5982	91.80	0.9300	1.1004
Current Spot	1.4628	1.5942	90.04	0.9176	1.0898
S1	1.4450	1.5802	87.14	0.9088	1.0753
S2	1.4407	1.5724	85.00	0.8981	1.0546

Spot prices as of: 07:18:02 Source: Bloomberg

Source: COG, Inc. © 2009 All rights reserved worldwide 09/29/2009

Key resistance is at 5,169 - This is a fibonacci target using the low from 4,041 to the support at 4,735 and projecting 0.618% from 4,738. The market hit resistance at 5,169 - today will see if momentum can continue to breack this high.

	Spot	Bias	Entry	Target	Stop	Comment/Levels
EUR/USD	1.4628	Bearish	1.4700	1.4450	1.4770	Retracement against the trend could be worth exploring.
USD/JPY	90.04	Neutral	-	96.00	-	
USD/CHF	1.0324	Bullish	1.0225	1.0500	1.0160	Retracement against the trend.
GBP/USD	1.5942	Bullish	-	1.6000	-	Broad oversold bounce due for the pound.
EUR/GBP	0.9205	Bearish	-	0.9000	-	Overbought here- euro to weaken.
GBP/JPY	142.38	Neutral	143.20	150.00	1.41.95	Spike low implies a bounce.
EUR/JPY	131.05	Bullish	-	133.00	-	
CAD/JPY	82.78	Bearish	82.70	78.55	83.10	Strong bounce hit stops.
AUD/USD	0.8755	Bearish	0.8650	0.8450	0.8725	Potential reversal, but risk-on squeeze is greater than expected.
USD/CAD	1.0817	Bullish	1.0800	1.1200	1.0715	
NZD/USD	0.7206	Bearish	0.7200	0.6700	0.7255	Triangular constriction implies this short could get squeezed.
USD/BRL	1.7872	Bearish	1.8338	1.7000	1.8455	
USD/PLN	2.8683	Bearish	2.9000	2.7000	2.9110	Sell level hit but direction still inconclusive.
USD/HUF	184.40	Bearish	188.00	180.00	190.20	

Spot prices source: Bloomberg

ENTRY - Targetted

ENTRY - Active

## Quantitative Market Analysis

Naeem Wahid, Quantitative Strategist

The USD DXY index has tested resistance around 77.1, but has failed to close above this level. In this context it is not surprising that the trend following model has left its positions unchanged across developed market currencies. The model is broadly long of USDs with the exceptions against the British pound and the Canadian dollar. In emerging market currencies, the model has instigated a long position in USD/PLN this morning. Overall, price action remains mixed in EM currencies, hence this should be viewed as the model reducing its overall short USD position.

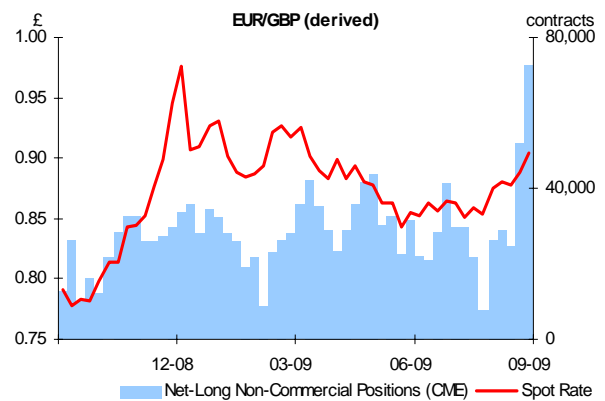
The S&P500 has opened the week strongly despite a poor performance last week, where a bearish engulfing formation was recorded. This technical formation has signalled many negative turning points over the past year and therefore we are somewhat cautious now. In addition to this, the Shanghai composite index continues to drift lower. We would look for further USD strength if equities gain downward momentum.

EUR/GBP was unable to capture any of yesterday's intra-day rally above £0.93, closing around £0.92. Weak individual state CPI reports from Germany and ECB President Trichet highlighting the importance of a strong USD have weighed on the euro. The currency pair is now over-bought on a RSI measure and speculative positioning in EUR/GBP (derived from IMM data provided for EUR/USD and GBP/USD) suggests the largest long position on record. On its own this is insufficient to warrant a short position, however it does highlight the risk of a squeeze if a trigger arises. Given the recent comments by BoE Governor Mervyn King, the UK current account needs to show a further improvement in Q2 this morning, if the slight dip over the past 24-hours in EUR/GBP is to continue.

Table 1: 1-month correlations

	AUDUSD	USDCAD	EURUSD	GBPUSD	USDJPY	EURJPY
2 YR SPD	-0.74	-0.35	0.49	0.64	-0.65	0.33
10 YR SPD	-0.63	-0.48	0.49	-0.30	0.34	0.64
S&P500	<b>0.90</b>	<b>-0.80</b>	<b>0.95</b>	-0.06	-0.71	0.41
Gold	<b>0.78</b>	<b>-0.78</b>	<b>0.75</b>	0.31	-0.56	0.33
Oil	0.13	-0.58	0.20	0.64	0.25	0.66
CRB	0.49	-0.72	0.63	0.27	-0.23	0.62

Chart 1: Speculative Positioning - IMM data



## Trend following model signals

Trend Following Model Positions			
	Signal	Date	Entry Level
AUDUSD	long	15-Sep-09	0.8622
NZDUSD	long	10-Jul-09	0.6298
EURUSD	long	09-Sep-09	1.4480
GBPUSD	short	21-Sep-09	1.6270
USDCHF	short	17-Jul-09	1.0730
USDCAD	long	24-Sep-09	1.0745
USDSEK	short	09-Sep-09	7.0444
USDNOK	short	21-Jul-09	6.3025
USDJPY	short	28-Sep-09	89.64

Trend Following Model Positions			
	Signal	Date	Entry Level
USDCZK	short	19-May-09	19.709
USDPLN	long	29-Sep-09	2.8701
USDSGD	short	08-Sep-09	1.4337
USDTRY	short	15-Sep-09	1.4939
USDZAR	short	31-Aug-09	7.7525

## Market Summary

FX			Equities		
	Close	Daily Change %		Close	Daily Change %
EUR/USD	1.4622	-0.45%	S&P500	1062.98	1.78%
USD/JPY	89.634	0.00%	DJIA	9789.36	1.28%
AUD/USD	0.8725	0.52%	FTSE100	5165.70	1.64%
EUR/GBP	0.9206	-0.05%	Eurostoxx50	2899.12	2.37%
GBP/EUR	1.0863	0.04%	Shanghai Composite*	2763.53	0.01%
GBP/USD	1.5882	-0.43%	*latest price		
GBP/JPY	142.37	-0.44%	Commodities		
GBP/CHF	1.640	0.04%			%
GBP/AUD	1.820	-0.96%	Crude Oil \$/bl	66.84	1.24%
GBP/CAD	1.723	-1.00%	Gold \$/oz	991.1	0.01%
GBP/NZD	2.216	-0.06%	Copper c/lb	272.7	-0.49%
GBP/NOK	9.259	-0.02%	Silver \$/oz	16.18	0.78%
GBP/ZAR	11.815	-0.06%	Baltic Dry	2192	0.41%
GBP/CNY	10.843	-0.45%	Swaps %		
Bonds %					bp
		bp	US 5yr	2.635	-5.3
US 10Yr	3.280	-3.9	EUR 5yr	2.699	-0.6
EUR 10Yr	3.254	-0.2	UK 5yr	3.278	0.1
UK10 Yr	3.610	-8.2	Official Rates %		
Other					
VIX	24.88	-2.85%	UK	0.50	
iTraxx XOVER	569.91	-7.1	US	0.25	
DJ Agriculture Index	58.06	0.87%	EU	1.00	
			Japan	0.10	

This document has been prepared for information purposes only and is based on information believed to be reliable. This information is provided as a courtesy to you and does not create an obligation for Bank of Scotland Treasury ("BoS Treasury") or another Group company within Lloyds Banking Group to notify you of any changes to this data or to do so in the future. Changes in rates of exchange or rates of interest may have an adverse effect on the value or price of these investments. Spot and forward foreign exchange transactions generally are not 'designated investments' as defined in the UK Financial Services & Markets Act 2000 ("the Act") and therefore do not benefit from any of the protections contained either in the Act or in the rules of the FSA. Past performance is not necessarily a guide to future performance. This document has been written with market professionals in mind and recipients should seek guidance and advice from a suitably qualified professional if they find anything contained herein confusing or unclear. The distribution of this document in other jurisdictions may be restricted by local laws and recipients into whose possession this document comes should inform themselves about, and observe any such restrictions. This information has been provided for the use of the recipient only and must be treated as proprietary and confidential information. It may not be passed on or reproduced in whole or part under any circumstances without express written consent from BoS Treasury. Although the information contained herein is believed to be correct, Lloyds Banking Group does not guarantee its reliability or its accuracy. Opinions expressed are subject to change without notice, as are prices and availability, which are indicative only. In preparing this publication we have not considered your objectives, financial situation or needs. Appropriate independent advice should be obtained before making any such decision. Lloyds Banking Group specifically disclaims liability for any loss, claim or damage suffered by you or any third party resulting directly or indirectly from any use you may make from this data without limitation. Provision of this information does not constitute either a bid or offer to undertake any transaction or commitment by any Lloyds Banking Group company to make such an offer. Lloyds Banking Group or its employees may own or build positions or trade in such securities and derivatives and may also sell them whenever considered appropriate. Lloyds Banking Group may also provide banking or other advisory services to any company mentioned herein.

Bank of Scotland Treasury is a division of Bank of Scotland plc which is part of Lloyds Banking Group. Registered Office: The Mound Edinburgh EH1 1YZ. Registered in Scotland. Registered No SC 327000. Authorised and regulated by The Financial Services Authority, 25 The North Colonnade, Canary Wharf, London E14 5HS. Australian residents please note: In Australia, Bank of Scotland plc is registered as a foreign company, Australian Registered Body Number 126 955 557. The liability of its members is limited.