

Euro Mkt Summary: EGBs Higher on Weak PMIs, Pre-ECB Position Squaring
by Charanjeev Chana

EGBs were trading higher [I think that should be higher not lower] on Wednesday afternoon with little bias. In the afternoon session, Bunds dipped lower following the release of September US ADP private employment data, which came in above earlier market rumours. Dec07 Bunds then pared gains on the release of September US ISM non-manufacturing data, which came in slightly above consensus estimates. EGBs opened higher on Wednesday morning, led by gains in short dates amid position squaring ahead of the ECB interest rate decision and press conference on Thursday. Volumes were thin, as German market participants were absent whilst observing the Day of Unity public holiday. Bunds rose sharply following the release of weaker Eurozone service PMI data - which fell to its lowest level since August 2005. The market posted little reaction to August Eurozone retail sales, which came in at the lower end of expectations in August.

Focus in Europe turns to the ECB interest rate announcement and subsequent press conference delivered by ECB President Trichet on Thursday. On the supply front, the AFT will issue between E3-3.5bln of the 4.25% Oct 2017 OAT and 6.00% Oct 2025 OAT.

In the forex markets, the dollar traded stronger against the major currencies. The EUR/USD was at 1.418 (+0.002), cable at 2.039 (-0.003) and USD/JPY at 116.36 (+0.69).

European equities were stronger in afternoon trade. The DAX was trading +0.47%, CAC 40 +0.61% and the FTSE +0.47% on the day. US stocks were weaker with the S&P 500 -0.05% and the NASDAQ -0.07%.

Gilts were also trading higher with short dated Gilts outperforming slightly on expectations of a November interest rate cut by the BOE. Gilts paid little attention to the September UK CIPS services PMI, which fell to a 13-month low in September to 56.7 from 57.6 in August - as expected.

Attention in the UK turns to the Bank of England interest rate announcement on Thursday. Whilst the BOE is largely expected to leave interest rates unchanged on Thursday, market expectations point to November for a possible interest rate cut by the Bank - which has underpinned the short end of the Gilt curve in recent sessions.

11:02 10/03 **DOLLAR VIEW:** The greenback is romping higher, led by dollar-yen which just hit a six week high near Y116.77. The higher employment component of the ISM non-manufacturing data would seem to underpin market estimates (MNI median +115,000) or even higher non-farm payroll number, which has caused players to pare back their dollar shorts or even flip to a dollar long. Ian Morris of HSBC reminds that the ISM non-mfg series was "an excellent indicator of last month's payroll weakness and may be pointing to a bounce in September." The average of the seven equations HSBC uses to estimate payrolls is 143,000, which is consistent with their official call of +140,000, Morris says.



[Times for Market News International stories are ET]

07:08 10/03 **GILT SUMMARY:** Gilts are higher, with the short-dated issues outperforming, amid continued expectations of an interest rate cut by the Bank of England's Monetary Policy Committee, as soon as Thursday's meeting. Gilts paid little attention to UK CIPS PMI services data, where the headline activity index fell to 56.7 from 57.6, a shade under analysts' median forecast for a 56.8 outturn and a 13-month low. However, the average prices charged component climbed to 53.7 from 53.1 in August and 52.2 in July, to stand at its highest level since April. The CIPS September manufacturing survey showed prices charged in that sector hitting a record high. Traders reported continued Gilt outperformance vs Bunds in early Wednesday session as the 10-year Gilt/Bund yield spread narrows to +69.8 bps vs +70.9 bps Tuesday, but since risen to +71 bps. The Gilt 2-/10-year yield spread was 0.8 bps steeper at -5.7 bps, whilst the 10-/30-year yield spread was 0.6 bps steeper at -37.1 bps. Dec Gilts are up 13 ticks at 107.38.

07:06 10/03 **BUND SUMMARY:** European bond prices are higher on Wednesday, with the belly of the curve outperforming the wings following release of weaker than expected German CIPS services data. However, volumes were reportedly thin, with German markets observing Day of Unity holiday. Bunds opened higher, with the short-dated issues outperforming, amid position-squaring ahead of the key ECB Governing Council rate decision in Vienna tomorrow. Traders also reported safe-haven buying following dramatic reversal lower in the Hang Seng index, which hit an all-time high of 28163.78 in morning trade, before profit-taking and investor unease sent the index tumbling to close 2.55% lower. Prices continued to squeeze higher on back of weak national PMI services data, where German September services PMI fell to 53.1 -- the weakest for 10-years vs 59.8 in August. The yield on the 4.00% Sept 2009 Schatz broke below the 4.00% level -- trading at its lowest level since Sept 17. Elsewhere, eurozone PMI services data came in at 54.2 in Sept vs flash estimate of 54.0.

(cont.)

06:59 10/03 **UK: Data** released in the UK Wednesday,
 ** CIPS Services PMI 56.7 in Sept vs 57.6 in Aug.

** BRC Sep shop prices index +0.2% m/m, +0.4% y/y

** NTC/REC: Salary Inflation Eases To 13-Month Low

- UK Sept Permanent Placements 60.2 Vs 60.1 In Aug

- UK Sept Permanent Salaries 61.1 Vs 61.5 In August

- Permanent Salary Inflation At 13-Month Low

** Nationwide Consumer Confidence Rebounds In Sep

- Sep Consumer Confidence Index Rises To 99 Vs 94 In Aug

06:44 10/03 **EUROZONE: Data** released in the eurozone Wednesday,

** EMU: Retail sales in August rose by a less-than-expected 0.1% m/m,
 while yearly sales accelerated to +1.0%

** EUROZONE: Eurozone Sept services PMI comes in at 54.2 vs 54.0 flash

* GERMANY: Sept services PMI falls 53.1 X vs 59.8 in Aug

* FRANCE: Sept services PMI fell to 56.8 vs 58.4 in Aug

* ITALY: Sept services PMI fell to 53.9 vs 56.2 in Aug

** ITALY: Q2 2007 budget surplus 2.0% of GDP vs 0.2% in Q2 2006

** SPAIN: Sep consumer confidence 80.2 vs Aug 86.5 - ICO

06:34 10/03 **EUROZONE: Reported comments from eurozone officials** Wednesday,

** BELGIUM FINMIN: ECB should keep rates unchanged, consider easing
 later if growth slackens

- Everyone agrees ECB management of subprime crisis was 'remarkable'

- Wants ECB to remain independent and accept debate. (Les Echos)

** EU: EU Employers; Euro level over pain threshold for business

- ECB monetary policy should be 'pragmatic' due to crisis

- Forex volatility should be a concern for ECB

08:41 10/03 **SONIA:** SONIA (Sterling Over-Night Index Average) Swap curve is now pricing reduced chances of a 25bps rate from the BoE at Thursday's MPC meeting. In addition, implied probabilities have also reduced for the November meeting, where the next BoE Quarterly Inflation Report is due to be published. That said, the curve is fully pricing in a 25bps cut by January 2008 and another 25bps move by June 2008.

Month	Rate	Probability (25bps cut)	Probability early week
October	5.700%	-20.0%	-46.0%
November	5.580%	-70.0%	-90.0%
December	5.580%	-70.0%	-90.0%
January	5.475%	-110.0%	-105.0%