



Euro Mkt Summary: EGBs Higher on Risk Aversion, Weak Q3 Earnings
by Charanjeev Chana

EGBs were trading higher on risk-aversion buying with short dates outperforming, in turn steepening the Bund curve. Bunds hit session highs in afternoon trade after Bank of America reported at sharp decline in Q3 profits as capital market losses offset solid revenue growth in overall business. Prices also advanced higher following the release of US initial claims data, which rose above expectations, with the contagion from the fall out in the housing and mortgage markets noted for the surge in claims. Bunds then pared gains slightly on hawkish comments by ECB official Axel Weber, who said inflation risks in the euro area have increased since the most recent Eurosystem staff projections were published in early September, which could require further action on interest rates by the ECB. EGBs opened higher amidst reports of switch trades out of US Treasuries. The market extended gains in morning trade as European equity bourses pared gains from the open. Safe haven buying was also noted on geo-political jitters following reports that the Turkish parliament granted permission to its troops to initiate an attack against Kurdish rebels in Iraq. Strong demand for BTAN supply from France also underpinned sentiment. The AFT sold E1.365bln of 4.00% Sept 2009 BTAN, covered 5.513 times and E1.810bln of 4.50% July 2012 BTAN, covered 4.030 times.

German producer prices are due on the open on Friday morning and Belgian consumer confidence is expected on Friday afternoon. Speaker-wise, attention will turn to comments from ECB officials Gonzalez-Paramo and Axel Weber, due to speak on Friday afternoon.

In the forex markets, the dollar traded weaker against the major currencies. The EUR/USD was at 1.429 (+0.008), cable at 2.048 (+0.008) and USD/JPY at 115.71 (-1.05).

European equities were weaker in afternoon trade. The DAX was trading -0.82%, CAC 40 -1.01% and the FTSE -0.13% on the day. US stocks were also weaker with the S&P 500 -0.31% and the NASDAQ -0.31%.

Gilts were also trading higher, but underperforming trade in Europe. Stronger than expected UK retail sales, which rose at the fastest pace since September 2004 on an annualised basis, weighed on the Gilt curve on Thursday morning. The strength of the data heightened speculation of a pause in rates by the Bank of England in November, before making a decision to cut interest rates in 2008. Sources noted that volumes were light, with focus on G7 meeting and the Rugby World Cup final on Saturday between England and South Africa.

Attention in the UK on Friday will turn to the first estimate for Q3 GDP. We expect an inline reading to prompt little market impact.



[Times for Market News International stories are ET]

09:29 10/18 **ECB'S WEBER:** Inflation risks in the euro area have increased since the most recent Eurosystem staff projections were published in early September, and that could require further action on interest rates by the European Central Bank at some point, Axel Weber, a member of the ECB's Governing Council, told Market News International in an interview. Read the full MNI exclusive interview on Mainwire.

07:26 10/18 **GILT SUMMARY:** Gilts are higher, but underperformed Bunds following release of stronger than expected UK retail sales data, coming in +0.6% m/m, +6.3% y/y in September -- the annual rise was the highest since Septmber 2004 vs revised +0.7% m/m, +4.8 y/y in August (was +0.6% m/m, +4.8% y/y). The 10-year Gilt/Bund yield spread widened to +71.8 bps vs +69.7 bps Thursday. The Gilt 2-/10-year yield spread was 1.2 bps flatter at -20.8 bps, whilst the 10-/30-year yield spread was 1.5 bps steeper at -40.3 bps. Traders said volumes were light, with focus on G7 meeting and perhaps more importantly, the Rugby World Cup final on Saturday between England and South Africa. Dec Gilts are up 25 ticks at 106.84.

07:20 10/18 **BUND SUMMARY:** European bond prices are higher on Thursday on back of safe-haven buying as stocks fell following disappointing Q3 results from Bank of America. Bunds opened higher geo-political jitters with Iraq/Turkey, after reports that Turkey's parliament has granted its troops permission to launch an attack against Kurdish rebels inside Iraqi territory. Traders also reported switch trades from US Treasuries, amid profit-taking after strong outperformance by the latter in recent sessions. Traders also reported around 30k worth of stop loss buying in December Bund futures contract on a break above 112.19 technical resistance level -- falling resistance from September 10. Bunds extended move higher after Bank of America Corp announced Q3 profit fell 32% and earnings that fell short of analysts' estimates. Prices were also underpinned by strong demand at French auctions, where 2-year BTAN was covered 5.513 times and 5-year BTAN covered 4.030. France also sold 2010 BTANei issue, covered 5.338 and 2017 OATi, covered 3.841.

(Cont.)

07:11 10/18 **UK: Data** released in the UK Thursday,
 ** Sept. retail sales volumes +0.6% m/m; +6.3% y/y
 - Annual Increase In Sales Highest Since Sept. 2004
 - Sept retail sales well above median forecast for +0.1%; +5.6% y/y
 - Jul-Sep Sales Rise 1.7% Vs Apr-Jun -- Highest Since Jul 2006
 - August Sales Revised Up To 0.7% m/m Vs Previous 0.6%
 ** Sep PSNCR Stg8.964bn vs Stg12.310bn in Sep 2006
 - UK Sep PSNB Stg6.874bn vs Stg5.660bn in Sep 2006
 - UK Sep current budget -Stg3.842bn vs -Stg3.860bn in Sep 2006
 ** UK Sept BBA mortgage lending Stg5.8bln vs Stg64.1bln Aug.
 ** UK M4 rose 1.0% m/m, +12.8% y/y in Sep vs 1.3% m/m, +13.5% y/y in Aug
 - UK M4 lending up Stg23.0bln in Sept -- BoE.

08:08 10/18 **LIBOR:** Third consecutive session of LIBOR compression, 3 month LIBOR set 1.88 bps lower at 5.1800%, -3.44 bps for the week. Meanwhile, 1-month LIBOR set 2.37 bps lower at 4.9975%, -4.75 bps for the week. Net weekly recap:

| | 3-Month LIBOR | 1-Month LIBOR |
|-------------|---------------|---------------|
| Oct 8-12 | -1.93 bps | -6.19 bps |
| Oct 1-5 | +1.43 bps | -0.19 bps |
| Sep 24-28 | +2.63 bps | -0.75 bps |
| Sep 17-21 | -44.38 bps | -48.25 bps |
| Sep 10-14 | -7.87 bps | -21.00 bps |
| Sep 3-7 | +10.37 bps | +10.38 bps |
| Aug 27-31 | +11.57 bps | +21.75 bps |
| Aug 20-24 | +1.00 bps | -0.75 bps |
| Aug 13-17 | -7.50 bps | -10.88 bps |
| August 6-10 | +21.50 bps | +36.63 bps |

03:11 10/18 **JGB SUMMARY:** Japanese government bonds ended Thursday's session barely change, reversing the previous session's gains. However, traders said volumes were light, with a lack of economic data of fresh news keeping many players sidelined.
 -- Benchmark 10-year yield was unchanged at 1.645%.
 -- Benchmark 5-year yield was unchanged at 1.175%.
 -- Benchmark 20-year yield was 0.5 bps higher at 2.200%.
 -- Benchmark 30-year yield was unchanged at 2.445%.
 -- Lead Sept JGB futures contract was down 0.02 at 135.37.
 -- The Nikkei 225 was higher by 150.78 points, or 0.89%, at 17106.09.