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Global Bonds Weekly

US

US Treasuries continued to reflect mainly the risk sentiment coming from Europe. 10year(y) rallied strongly on Tuesday and Wednesday following the uncertainty surrounding the formation of a new Greek government, with yields hitting the lowest value since February (1.824%). Most gains were given back on Thursday on speculation about an impending recapitalisation of Spanish banks and a possible coalition government in Greece, the Bank of England's decision to abstain from more quantitative easing, and the USD 16bn supply of 30y Treasuries. With 2y rates relatively anchored, the 2/10s curve continues to be very directional, flattening to 156bps on Wednesday and steepening to 164bps on the next day. The week was quiet in terms of data, with Trade Balance deteriorating slightly above expectations (USD -51.8bn vs. USD -50bn exp.), and Jobless Claims coming in line with consensus (367K) - the lowest since March, producing the lowest Continuing Claims figure since July 08 (3229K). Bernanke gave some interesting comments on the US banking system, noting that while it is now much stronger, "banks still have more to do to restore their health and adapt to the post-crisis regulatory and economic environment".

Eurozone

Despite the limited reaction to the outcome of the Greek and French elections on Monday (with London out on holiday), the political uncertainty set the main tone for the rest of the week, with investors strongly favouring safe-havens and looking to reduce the systematic risk in their holdings. In Greece the two most voted parties were unable to reach an agreement to form a coalition government. If Pasok, the third most voted, also fails (which is expected) the most likely outcome is that new elections will be called for mid-June. According to polls and anecdotal evidence, Syriza (2nd place) has been gaining support from voters post-election, which given their radical stance on European issues (opposed austerity measures and promoted stopping debt servicing during the campaign, while supporting staying in the EUR) has led markets to trade with a heavy tone. Meanwhile the European Financial Stability Facility has decided to only disburse EUR 4.2bn of the EUR 5.2bn May tranche to Greece, which is exactly equal to the country's redemptions and interest payments over the next month. The outcome of the French presidential election was in line with expectations; Hollande has since been meeting several European officials to discuss adding growth elements to the fiscal compact, and will be meeting Angela Merkel next week, but headlines have so far been muted. In Spain the government announced that the FROB will take a 45% stake in BFA-Bankia, with some leaks suggesting that it will also announce more measures to try to stem the contagion from the banking sector to the real economy, such as raising provisions on non-problematic real estate loans and providing government guarantees for the liquidity needs of bad real estate holdings. This scenario of political ambiguity weighted on spreads, with Italy 17 basis points (bps) wider, Spain 30bps, and France 9bps wider on the week. Bunds continue to be the favoured vehicle to express flight-to-quality trades, with 10y rallying 7bps on the week, 2y rallying 2.5bps, and measures of systemic risk increasing considerably in these last days, as investors looked to place tail risk hedges.

Non-Euro

The 10 year gilt fell 14 bps to 1.92%, hitting all-time lows during the week (lowest yield recorded since 1703), 15 year fell 12 bps to 2.57% and 30 year gilt fell 8 bps to 3.22%. The Monetary Policy Commitee decided to leave interest rates at 0.5% and not addany further quantitative easing (QE) to its current programme of £325bn. The UK's manufacturing sector grew more strongly than expected in March, with Output growing by 0.9%, reversing February's 1.1% fall and stronger than the 0.5% predicted. Like-for-like sales fell 3.3% - the worst figure since March 2011, driven mainly by clothes retailers. House prices fell in April with average price dropping 2.4%, stated Halifax largest mortgage lender in the UK. The decrease leaves the average house price at £159,883, following an increase of 2.2% in March and making the three-month measure 0.3% higher.

Japan

It was an uneventful week in Japan, with JGBs advancing slightly on the back of their safe-haven status. The Current Account for March was released significantly above expectations (-8.6% deterioration YoY vs. -17.1% exp.) with the Trade Balance also surprising on the upside (JPY +4.2bn vs. JPY -42.8bn exp.). In terms of relevant speakers the Bank of Japan (BoJ) board member Shirai acknowledged this week that the BoJ bond buying program may pose risks to the financial system, while the Finance Minister warned about excessive appreciation in the JPY resulting from an increase in risk aversion, saying that they will "respond properly as circumstances warrant".

Credit

European credit continues to trade with a great deal of volatility due to numerous concerns, including the Spanish banking system and Greek political instability. We began the week trading with a weaker tone on the back of rumours that Bankia (one of the largest banks in Spain) would be nationalised; Spanish names underperformed in line with the sovereign. French banks have also slightly underperformed over the last couple of weeks in the build-up and subsequent result of the French elections. Amidst the volatility we have continued to see cash bonds outperforming CDS, although liquidity remains thin and the moves have been on the back of low volumes. Sentiment picked up slightly on Thursday afternoon after a weaker open, with some short covering following rumours of a Greek coalition. Still, iTraxx Main is +14bps wider on the week at 156bps and iTraxx FinSnr is +18bps wider at 263. Financial supply has been non-existent, but we have had a few new corporate issues including a Caterpillar 3yr issue at MS+45 and a Volkswagen 5yr issue at MS+65.

Currency

The outcome of the Greek and French elections has weighed heavily on sentiment, with the USD the favoured expression of a flight-to-quality trade in the currency space. The EURUSD fell over 2% on the week, breaking the 1.30 level after having traded in the 1.30-1.35 range for the last month. Other than sharing the downside due to worsening of risk sentiment, the Antipodean currencies of the AUD and NZD fell over 3% vs. the USD on the back of the broad decline in commodity prices and weak data out of China. We observed a similar pattern of preference for buying USD against emerging markets' currencies. Asian currencies outperformed CEEMEA and LatAm currencies. In terms of specific stories, Indian authorities have continued to look for ways to stem the depreciation trend of the INR, but despite new administrative measures announced by the RBI, investors have continued to express concerns regarding the widening current account deficit; the INR fell 1.65% vs the USD over the week. Poland unexpectedly hiked rates by 25bps however the PLN remained in line with the general risk averse tone.

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