Deutsche Bank
Markets Research
Global
Economics
Date
1 July 2014
Early Morning Reid
Macro Strategy
I'll be honest and say that yesterday's EMR was a bit of a daze. I had a belated
party for my 40th on Saturday and spent virtually the entire Friday night awake
with my builders trying to put a house back together that has been owned by
the builders for 8 months. I had 15 people there until 4am Friday night with 3
of them working non-stop until the first guests arrived at 230pm. Never have I
been so stressed and tired. So all day Sunday and Monday morning were a bit
of a daze. Sadly I'm now back living with builders again as they finish things
off after the party. It was blissful for the few hours we were apart. At least
we've moved out of the kitchen where we were living and sleeping for nearly 5
months before last week. Hopefully by the time the second half of the year
ends I'll never have to see a builder again.
Anyway, the second half has now begun for markets and in our H1/Q2/ June
performance review today we show that most assets have had a positive year
so far. So much so that if the year eventually goes to penalties it will end up
being a very poor second half showing in line with many of England's in recent
years!! We briefly review the numbers at the end but all the data and charts are
in the pdf of this document. Its pretty rare to have almost all main global assets
in positive territory this far into a year. Central bank liquidity continues to drive
markets in our opinion which has helped this synchronised uplift in valuations.
However we can't help sensing that there's less joy over these returns than
might be expected. Investors are worried about valuations in numerous assets
and worried that the Fed might become more hawkish soon. There's little chance of
the ECB following suit anytime soon though and European
Government bonds have had a very good 2014 so far.
Over the last month we've again highlighted how many European Government
bond markets have hit multi-century, all time yield lows. Well yesterday it was
the turn of the Dutch 10 year yield to go through it’s all time low again. The
Dutch series is where we have our longest history of any government bond

market with data going back to 1517 spanning almost half a millennia. The graph is in the pdf
today and further shows just how unique the current
situation is. The level of uncertainty about how this all ends must by definition
be very high given this.
So as we start H2, Asian markets are trading with a stronger tone this morning
helped by a solid start to the global manufacturing PMIs. The official Chinese
manufacturing PMI printed at 51.0, in line with consensus and at a six month high. The final HSBC Chinese manufacturing PMI came in at 50.7, slightly below the flash reading of 50.8, but this is also the highest print of the year.
The PMIs for other Asian bellwethers including Indonesia and Taiwan were also up on a month-to-month basis. The Nikkei (+1.2%) is the clear outperformer today, on decent volumes and despite a drop in the Japanese Q2 tankan manufacturing index to 12 from 17 previously and 15 expected. The capex component of the Tankan survey was above expectations however (+7.4% vs 6.0%) expected, which is strongest rate of growth since 2007. This has helped USDJPY (+0.1%) today. Outside of Japan, activity has been subdued with Hong Kong markets shut for July 1st holidays. The Indonesian

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Market Data
Index
ITX Crossover
ITX Europe 125
CDX 125
CDX HY - pts
S&P 500
Brent Oil^
Gold^
10 yr Treasury^
ITX Sen Fin
ITX Sub Fin
CDX EM
ITX Japan
ITX Australia
ITX Asia XJ
Euro NonSov
Euro Corp
Euro BBB
Sterling NonGilt
Sterling Corp

Sterling BBB
WTI Oil^
Dollar Index^
EUR/USD^
DJ Stoxx 600
NIKKEI
Hang Seng
VIX
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Close
242
62
59
Change
+3
+1
+1
108.66
1960
112.55
1327
2.52
68
103
237
68
85
105
69.15
103
133.94
115
139
176
105.65
79.82
1.369
342
15332
23191
11.57
-0.154
-0.04%
-0.66%
+0.83%
-1 bp
+2
+3

+4
-1
+2
unch
unch
unch
+1
unch
unch
unch
-0.09%
-0.27%
+0.31%
-0.03%
+1.12%
0%
+0.31
^ - Change from previous day's 05.30 GMT to 05:30 GMT. Levels as of 05:30 London time. European and US CDS indices above refer to 'old' off the run series
Upcoming Events
Release
ISM manufacturing (June)
Construction spending (May)
Unit motor vehicle sales (June)
DB
55.0
+0.5%
16.4M
Prev
55.4
+0.2%
16.7M
Con
55.8
+0.5%
16.3M
Topical DB Publications
World Outlook - The calm before the storm, 25 June 2014
FX Daily - The single most important question for policymakers, 24 June 2014
European Staffing - Later than it seems, 25 June 2014
European Equity Strategy - The return of the stock alpha, 20 Jun 2014
Focus Europe - Down but not out , 20 Jun 2014

148/04/2014.

rupiah is poised to record its strongest three-day rally in about fourth months –
spurred by comments last week from the Bank of Indonesia that the country's trade balance returned to surplus in May. The AUDUSD is also poised for a solid gain (+0.25%) after the RBA maintained its neutral tone in today's policy
meeting.
The last trading day of 1H14 failed to bring with it any volatility associated with
month-end and half-end portfolio rebalancing.
Indeed, yesterday's S&P 500
volumes were about half that compared to the last trading day of 1H13. Adding to that, the S&P 500 closed virtually unchanged at -0.04%, and for the record the last time we saw a gain or loss of more than 1% in the index was April 16th. One theme to note though was the continued underperformance of European banks across the equity and credit spectrum. Yesterday's underperformance was sparked by a 17% fall in the stock of Banco Espirito Santo which is Portugal's largest bank. The price action was dictated by reports that regulators were concerned over corporate governance between the bank and other related companies and there were also reports that Luxembourg justice authorities had launched an investigation into one of the bank's holding companies (Reuters). Portuguese securities regulator banned naked short selling on the bank's stock for one day. The news weighed on Portuguese bond yields which added 8bp, and also on European banking stocks in general (-0.75% vs Stoxx 600 -0.09%). Peripheral bank credit traded about 3-5bp wider yesterday - and the European senior financials index (+2bp) underperformed Main (+1.375bp). The two credit indices were trading flat to each other in the middle of June but the recent underperformance of banks has pushed the basis back to nearly 6bp. We still think its likely that Fin Senior will
trade through Main in H2 though.
Across the Atlantic, there was focus on the Chicago PMI and home sales data, following which treasury yields spiked up briefly before retracing the move to
be largely unchanged on the day. The US Chicago PMI was slightly below expectations 62.6 (vs 63.0 expected) and also below last month's 65.5. Still, our economists note that the PMI was consistent with a large snapback in growth in Q2, and they noted the three-month to June average was 63.7 which is the highest since the three months to April 2011. The other regional activity
indicator, the Dallas Fed manufacturing outlook rose to 11.4 (vs 8.5 expected and 8.0 prior). Pending home sales rose 6.1% MoM (1.5% expected) which benefited US homebuilders on the equity side (+1.5% yesterday). In terms of Fed speak, the SF Fed's Williams commented that a first rate hike in 2H15 will
be appropriate, but he also reiterated that it may be optimal for the Fed to let
inflation run above target in order to balance the Fed's dual mandate.
Perhaps one of the key themes of 1H14 was the surging M&A activity globally.

With 1H14 books closed, the final M&A tally was $2.2trillion according to Bloomberg which is a YoY increase of 77%. By region, leading the way was the resurgence of corporate activity in Europe (+109% YoY),
though this was
coming off a low base, followed closely by North America (+79%). In terms of industry the biggest pickup in activity came in pharma (+677%) and healthcare (+140%). One reason for the surge in M&A has been the accommodative
capital markets. We saw an example of that yesterday with a jumbo bond deal from Oracle who priced $10bn in bonds (the second largest USD offering in the year-to-date according to Bloomberg) to fund the purchase of Micros Systems. The deal was sufficiently large to drag other TMT bonds several basis points wider on the day.
Looking at some of the geopolitical headlines, Ukrainian President Poroshenko said late on Tuesday that we would end the cease-fire with pro-Russian rebels and vowed to intensify military operations in the country's east. However the president also made some concessions
including guaranteeing Russianlanguage
rights and more regional autonomy. Russia also offered some
concessions yesterday including allowing Ukrainian and international
observers
in its own border posts along the border with Ukraine. In Iraq, semiPage
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autonomous Kurds plan a referendum for
independence according to a
regional government spokeperson (Reuters). The Kurds plan to keep control of the Kirkuk oil fields.
There are some mixed headlines elsewhere in China. Firstly China's banking regulator announced a small change in the way that Loan-to-deposit ratios are calculated which our banking analysts think will reduce the system regulatory LDR ratio by 410bp based on end 2013 data. Our analysts think that this will pave the way for more relaxation of Chinese bank liquidity requirements. Secondly,
the latest Macau gaming numbers were reported which showed
June casino revenues fell 3.7% YoY in June. This is the first drop since 2009,
but some are attributing this to the effects of the World Cup.
Turning to the day ahead, the rest of the global manufacturing PMIs/ISMs will be released starting with the final PMIs for Europe. The US manufacturing ISM is expected to show a small bump up to 55.9 (vs 55.4 in May) which would mark a six month high. DB is expecting a print of 55.0. Other highlights on the
US data docket are May construction spending and the IBD/TIPP economic optimism index.
YTD performance review
In YTD terms, of the main indices we track the FTSE-MIB (+14.5%) and the IBEX (+12.8%) have been the star performers. Spanish, Portuguese and Italian bonds have not been far behind.
Interestingly commodities make up quite a
few of the other top ten places (with the CRB index, Gold, Silver and Oil returning between 7-11%), but also 2 of the worst 3 with Wheat and Copper both down more than 6%. Also negative was Chinese equities (-1.5%) after disappointing growth in H1 which may explain some part of the weakness for certain commodities. The Nikkei (-6.1%) was the only other asset lower YTD in our sample. Apart from these four all the other assets saw a positive 2014 total
return. Credit has put in a good performance in 2014 so far with most major indices returning between 4-7% which is impressive in the low yield,
spread environment.
low
For the full numbers for the year, Q2 and June see the charts and tables in today's pdf. We also show the YTD numbers all converted to dollars.
Happy H2!
Figure 1: Netherlands 10yr Government Bond Yields
0%
5%
10%
15%
20%
25%
30%
Source: Deutsche Bank, GFD

Netherlands 10yr
1517154715771607163716671697172717571787181718471877190719371967 1997
Deutsche Bank AG/London

Figure 2: Total Return Performance of Major Global Financial Assets – June 2014
-15%
-10%
-5%
0%
5%
10%
15%
Corp Bond Govt Bond
Equity EM Equity EM Bond
Commodity
FX
Source: Deutsche Bank, Bloomberg Finance LLP, Mark-it
Figure 3: Total Return Performance of Major Global Financial Assets – Q2 2014
-25%
-20%
-15%
-10%
-5%
0%
5%
10%
15%
Corp Bond Govt Bond
Equity EM Equity
EM Bond Commodity
FX
Source: Deutsche Bank, Bloomberg Finance LLP, Mark-it

Micex (Russia)
IBEX 35
Silver
Gold
Hang Seng
MSCI EM Equities
Silver
Bovespa
Copper
S&P 500
Brent
DJStoxx 600
EM Bond
US WTI Oil
BTPs
US Fin Sub
Gold
FTSE 100

Spanish bonds
EU Sovereign
US IG Non-Fin
DAX
EU Fin Sub
US IG Corp
EU IG Non-Fin
GBP/USD
Shanghai Comp
US HY
Nikkei
EU HY
Bunds
EU Fin Sen
US Fin Sen
JPY/USD
Treasury
CRB Index
Gilt
FTSE-MIB
EUR/USD
DJStoxx 600 Banks
Portugal General
Greece Athex
Corn
Wheat
Micex (Russia)
Bovespa
Nikkei
Brent
MSCI EM Equities
US WTI Oil
GBP/USD
S&P 500
Copper
Shanghai Comp
IBEX 35
BTPs
Hang Seng
Spanish bonds
EU Sovereign
US HY
CRB Index
EU IG Non-Fin
EM Bond
EU HY
Bunds
US Fin Sub
EU Fin Sub
EU Fin Sen
JPY/USD

EUR/USD
US Fin Sen
US IG Corp
US IG Non-Fin
Treasury
DJStoxx 600
Gilt
Greece Athex
DAX
FTSE-MIB
FTSE 100
Portugal General
DJStoxx 600 Banks
Corn
Wheat

Figure 4: Total Return Performance of Major Global Financial Assets – YTD 2014
-10%
-5%
0%
5%
10%
15%
20%
Corp Bond Govt Bond
Equity EM Equity EM Bond
Commodity
FX
Source: Deutsche Bank, Bloomberg Finance LLP, Mark-it
Figure 5: Total Return Performance of Major Global Financial Assets – YTD 2014 (in USD)
-10%
-5%
0%
5%
10%
15%
20%
Corp Bond Govt Bond
Equity EM Equity
EM Bond Commodity
FX
Source: Deutsche Bank, Bloomberg Finance LLP, Mark-it

FTSE-MIB
IBEX 35
Bovespa
Gold
CRB Index
Spanish bonds
Portugal General
BTPs
Silver
S&P 500
US WTI Oil
Gilt
US Fin Sub
EU Sovereign
US IG Non-Fin
DJStoxx 600
MSCI EM Equities
EU Fin Sub
US IG Corp

EM Bond
FTSE 100
US HY
EU HY
EU IG Non-Fin
Bunds
Greece Athex
JPY/USD
US Fin Sen
EU Fin Sen
Brent
GBP/USD
Treasury
DAX
Hang Seng
DJStoxx 600 Banks
Corn
EUR/USD
Nikkei
Shanghai Comp
Micex (Russia)
Copper
Wheat
FTSE-MIB
IBEX 35
Gold
CRB Index
Spanish bonds
Portugal General
BTPs
Silver
S&P 500
US WTI Oil
EU Sovereign
US Fin Sub
DJStoxx 600
EU Fin Sub
US IG Non-Fin
MSCI EM Equities
US IG Corp
EM Bond
US HY
EU HY
EU IG Non-Fin
Bunds
Greece Athex
EU Fin Sen
JPY/USD
US Fin Sen
Brent
Gilt

GBP/USD
Bovespa
Treasury
DAX
FTSE 100
Hang Seng
DJStoxx 600 Banks
Corn
EUR/USD
Micex (Russia)
Shanghai Comp
Nikkei
Copper
Wheat

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Assets
Credit
Figure 6: Total Return Performance of Major Global Financial Assets
Currency Instruments
Corp
EUR
Non-Fin
Fin Sen
Fin Sub
HY
GBP
Corp
Non-Fin
Fin Sen
Fin Sub
HY
USD
Corp
Non-Fin
Fin Sen
Fin Sub
HY
Governments EUR
Sovereign
Bunds
OAT
BTPs
Equity
GBP
USD
EUR
EUR
EUR
GBP
USD
USD
HKD
JPY
EUR
EUR
EUR
EUR
EUR
EM Equities CNY
BRL
INR
RUB
EM Bonds USD
Spanish bonds

Gilt
Treasury
DJ Stoxx 600
DJ Stoxx 600 Banks
DAX
FTSE 100
S&P 500
S&P 500 Financials
Hang Seng
Nikkei
Greece Athex
Portugal General
Irish Overall
FTSEMIB
IBEX 35
Shanghai Composite
Bovespa
Nifty
Micex (Russia)
USD MSCI EM
EM Bond All
EM Bond Asia
EM Bond Latam
EM Bond EEMEA
Commodity USD
EM Corp Bond All
CRB Index
Copper
US WTI Oil
Brent WTI
Sugar
Silver
Corn
Wheat
DM FX
N/A
Gold (spot)
DXY Index
EUR/USD
EUR/JPY
JPY/USD
GBP/USD
GBP/EUR
AUD/USD
CAD/USD
Note: Shaded column shows returns re-based in USD
Source: Deutsche Bank, Bloomberg Finance LLP, Mark-it
Jan 14
1.4%
1.5%
1.1%

1.7%
0.6%
2.0%
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2.8%
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-8.4%
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-7.5%
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5.0%
2.0%
-6.1%
4.8%
9.0%
4.5%
14.5%
12.8%
-1.5%
3.2%
21.8%
-0.7%
6.1%
5.6%
6.1%
8.5%
4.0%
6.5%
10.0%
-6.1%
7.1%
3.6%
1.3%
8.0%
0.5%
-6.7%
10.1%
-0.3%
-0.4%
-4.1%
3.9%
3.3%
3.8%
5.8%
-0.4%
YTD YTD (USD)

4.5%
4.8%
3.6%
6.1%
4.9%
8.2%
8.2%
7.4%
9.1%
9.6%
5.6%
6.4%
3.8%
6.7%
5.3%
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4.6%
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8.9%
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6.2%
0.9%
2.6%
5.4%
7.1%
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12.4%
-3.9%
10.2%
25.5%
-3.9%
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1.3%
8.0%

0.5%
-6.7%
10.1%

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