



10th July 2014

the technical analyst  
AWARDS 2011  
F I N A L I S T

# Market Update:

## Beware bonds, particularly UK Gilts

UPDATE  
Technical  
Fundamental

[Full performance of  
our Key Trades  
recommendations  
2006-13 here](#)



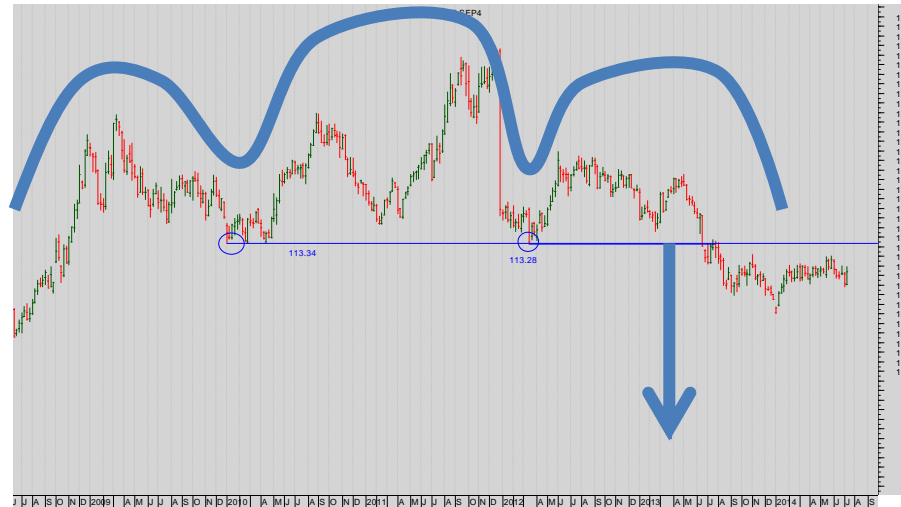
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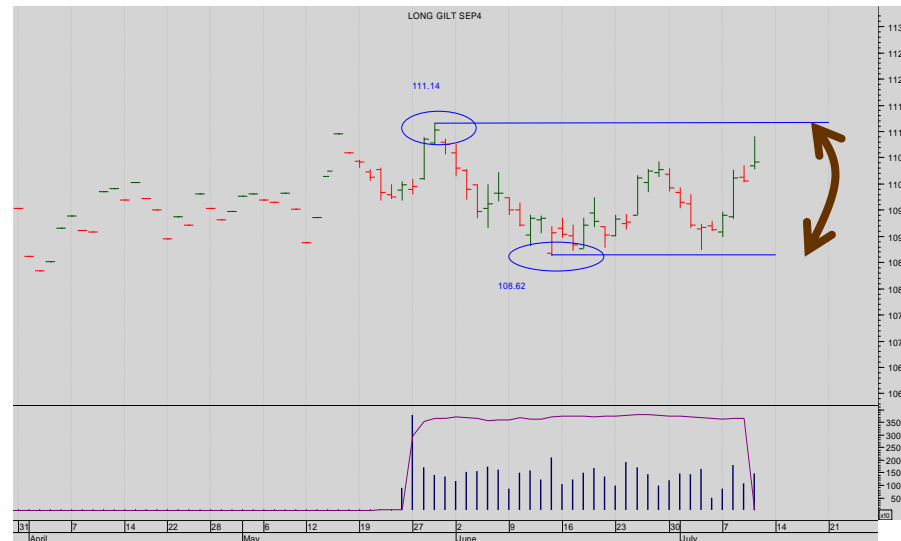
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### Weekly chart

The UK Gilt market has completed a large bear Head and Shoulders Top.

The minimum move is down as far as 93....



### Daily Sep 2014 chart

The trading range is clear. A break above 111.14 would disappoint the bears short-term, but overall, the technical picture is dominated by the large bear structure in the weekly chart.

Selling the market close to the top of the short-term trading range looks to be good value.

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More



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Technical  
Fundamental

**FUNDAMENTALS:**

After a strong bull run in equity markets, especially in the US, leading to speculation about when the turn in the long Bull run in Bonds will begin, Bonds are suddenly back in fashion; why?

Although stocks have enjoyed a prolonged spell of strength, bonds have failed to sell off as the economic recovery developed:

- In the US the Fed's policy stance has fuelled an equity market rally but offered Bonds a cushion,
- In the UK strong economic growth has fed into equity markets, but the Gilt has traded a clearly defined range, as the Bank of England has maintained record low interest rates frightened of acting too soon and damaging the recovery, and
- In the Euro zone the DJEUROSTOXX has rallied even though the economic recovery remains fragile, sustained by hopes the ECB may yet resort to a QE policy and foreign sentiment, while the Bund has remained a recognisable Bull market due to the same economic weakness.

But in recent days Bonds are once again in demand as traders fear a return of the Euro zone crisis, driven by fears a major Portuguese Bank is in trouble.

In reality a number of European Banks have question marks over their health, but traders had come to expect the authorities wouldn't let them fail. Having worked so hard to quell the Euro zone financial crisis are the authorities in Portugal or the wider Euro zone going to let a major lender fail and see a return to those roller coaster crisis days of 2012/13?

We think not.



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## FUNDAMENTALS: CONTINUED

Of the major Government Bond markets, the Gilt stands out as the one that has most resisted gravity. The UK economic recovery is well established and there is a growing debate about when the Bank of England will begin raising interest rates.

However, although growth is strong, inflation is below target and data released this week suggests competition on the high street will keep it subdued, meaning the Bank can afford to hold rates at current levels a while longer.

But with a red hot housing market and a prolonged period of low wage rises coupled with a tightening labour market policy makers shouldn't be complacent. After seeing inflation seriously erode living standards during the financial crisis/recession, public sector workers are feeling hard done by and as I write are on strike over a number of issues ranging from pay to pensions.

What does this mean for the Gilt?

For now we judge the Gilt will continue to trade within the clearly defined range, but if policy makers delay raising interest rates too long, further fuelling the house price boom, leading to a round of inflation busting wage demands as workers take advantage of a tightening labour market as they seek to rebuild their standard of living, the Gilt market could take fright as longer term interest rates start to do the work the Bank of England is reluctant to allow short term interest rates to do.

In summary the rally induced by the sell off in stocks is likely a short term phenomenon, the real question, especially in the Gilt market is, will UK policy makers keep rates too low for too long and allow a combination of rising house prices, rising wage demands and a re-appearance of inflation pull the rug from under the Gilt?



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SEVEN DAYS AHEAD

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