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The Day Ahead: Bonds Primed For Bad Bounce, Severity Determined Tomorrow

After an epic run to all-time Treasury lows (and nearly all-time mortgage rate lows) bond markets are flashing warning signs about a bounce. This sort of warning relies **almost exclusively** on the "technical" side of the analytical spectrum. (That's the side that is based purely on math applied to past and present movement in rates.) Technical analysis is far from a perfect predictor of the future, but it does a good job of letting us know when certain levels could be important to traders and when a shift might be happening.

Now is one of those times. The momentum indicators had been strong as rates continued to move lower, but even yesterday suggested waning momentum--the **first warning sign** of a potential bounce. In the following chart, we can see this in the middle section which is 'Fast Stochastics'--a jumpier, less reliable momentum indicator that lets us know when a move has entered the danger zone in terms of being at risk of a reversal.

MBS & Treasury Market Data

	Price / Yield	Change
MBS UMBS 6.0	100.61	+0.22
MBS GNMA 6.0	100.74	+0.21
10 YR Treasury	4.2939	+0.0121
30 YR Treasury	4.4881	+0.0024

Pricing as of: 7/8 3:55AM EST

Average Mortgage Rates

	Rate	Change	Points
Mortgage News Daily			
30 Yr. Fixed	7.03%	-0.05	0.00
15 Yr. Fixed	6.44%	-0.01	0.00
30 Yr. FHA	6.50%	-0.05	0.00
30 Yr. Jumbo	7.24%	-0.01	0.00
5/1 ARM	7.05%	-0.02	0.00
Freddie Mac			
30 Yr. Fixed	6.95%	+0.09	0.00
15 Yr. Fixed	6.25%	+0.09	0.00
Mortgage Bankers Assoc.			
30 Yr. Fixed	7.03%	+0.09	0.62
15 Yr. Fixed	6.56%	+0.09	0.54
30 Yr. FHA	6.90%	+0.11	0.95
30 Yr. Jumbo	7.11%	-0.01	0.50
5/1 ARM	6.38%	+0.11	0.54

Rates as of: 7/5

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The **tricky** thing about Fast Stochastics is that they will typically stay in that "danger zone" even as bonds continue to rally. It's when we looks at the Slow Stochastics (bottom of the chart) that we can confirm the danger is translating to actual harm for bonds. The upper section of the chart simply has some pivot points that are determined by recent levels where yields have shown a tendency to bounce or hold steady. Those pivots equate to a yard stick to measure how bad a potential bounce ends up being.

It's generally a bad idea to rely purely on technical analysis when there are compelling reasons to pay attention to the fundamentals (i.e. economic data and other externals news/events). This is all the more true when we're talking about historical big tickets like NFP and the Fed (and who could forget Brexit 2 weeks ago?). The **Fed just reminded us** that NFP matters in yesterday's meeting minutes--saying that the weakness in the last NFP report was part of their rationale behind keeping rates unchanged. They also said they're interested to see if the incoming employment data can clear the bar of "continued improvement in labor markets."

Opinions within the Fed will vary as to what "continued improvement" looks like in terms of an NFP number tomorrow, but there's a very real possibility that we'll see a number that **leaves no doubt**. NFP has a tendency to snap back after the type of report seen last time--even if the broader trend remains pointed toward decelerating job growth.

ALL of the above will be in traders' minds today. The bottom line is that we're at a clear disadvantage. It's easier to **expect weakness** and hope to be pleasantly surprised than it is to hope for more all-time lows. The unknown is how much weakness we'd need to see before buyers are excited about bonds again. That magic number will be much clearer after tomorrow's jobs data.

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