



Sunrise

Thursday, 19 October 2017

Rates: Shun Catalan political risk

Eco data and central bankers won't impact trading today. The Catalan-Madrid stand-off could escalate to a new phase. Cautiousness might be warranted. The Bund might profit in a daily perspective, with more outperformance vs the US Note future while Spanish spreads could widen.

Currencies: EUR/USD resilient despite Catalan uncertainty

Yesterday, the dollar rebound was a bit different from earlier this week. USD/JPY profited from higher core yields and a risk-on sentiment, but the US currency lost ground against the euro. Today, the focus for global FX trading will be on Catalonia. (Currency) markets are positioned for a non-disruptive outcome. This is far from sure. So, we see downside risk for the euro.

Calendar

Headlines

S&P	↗
Eurostoxx 50	↘
Nikkei	↘
Oil	↘
CRB	↘
Gold	↘
2 yr US	↘
10 yr US	↘
2yr DE	↘
10 yr DE	↘
EUR/USD	↘
USD/JPY	↘
EUR/GBP	↘

- **US stock markets ended** positive, but with big differences between S&P (+0.07%), Nasdaq (+0.01%) and Dow (+0.7%). Asian stock markets are mixed overnight with China underperforming (-0.3%).
- **China's economy expanded at a robust 6.8% pace in Q3**, meeting expectations, as traditional growth drivers such as manufacturing and exports gained steam. **September retail sales (10.3% Y/Y) and industrial production (6.6% Y/Y)** were close to consensus while **investments (7.5% Y/Y)** slightly disappointed.
- **Australia enjoyed another month of solid jobs growth in September (+19.8k)**, with the annual pace of gains sprinting ahead to the fastest in almost a decade and nudging the unemployment rate lower (5.5%).
- **Catalonia is on the precipice of losing its autonomy.** Regional President Puigdemont has until 10 a.m. local time to renounce his independence claims or have Madrid take control.
- While the **Bank of Korea** held interest rates at a record low, higher GDP/CPI forecast, hawkish comments from the governor and a dissenter calling for a rate hike indicate that **a change in monetary policy is getting closer.**
- **Republicans in Congress are examining how to block** a potential move by Trump **to pull the US out of NAFTA** as members of the president's own party also warn him that any such move could put a joint push for tax cuts at risk.
- **Today's eco calendar** contains UK retail sales, US weekly jobless claims and Philly Fed Business Outlook. Spain and France tap the market. EU leaders hold a Summit in Brussels.

Rates

US yield curve bear steepens

Spain underperforms

	US yield	-1d
2	1,56	0,02
5	1,98	0,04
10	2,35	0,05
30	2,85	0,05

	DE yield	-1d
2	-0,72	0,01
5	-0,31	0,02
10	0,40	0,03
30	1,25	0,03

Puigdemont: independence or not?

Risk aversion likely

Risk-on correction lower in core bond markets

Global core bonds lost ground yesterday in a risk-on environment. USD/JPY eked out nice gains and European equity markets added up to 0.5%. The move mainly occurred in the European session with once again an outperformance of German Bunds vs US Treasuries (dovish ECB expectations & European political risk). The eco calendar only contained weaker-than-expected, but distorted, US housing data. ECB Lautenschlaeger and Villeroy both suggested ending QE next year. This is perfectly possible in the currently rumoured extension (to September 2018) and recalibration (from €60 bn/month to €30 bn/month). Heavyweight NY Fed President Dudley sounded confident in the US economy and holds on to a 3-rate hikes scenario this year (one additional hike).

At the end of the day, the US yield curve bear steepened with yields 1.7 bps (2-yr) to 5.4 bps (30-yr) higher. Changes on the German yield curve ranged between +0.6 bps (2-yr) and +3.1 bps (10-yr). On intra-EMU bond markets, 10-yr yield spread changes versus Germany ended close to unchanged with Spain underperforming (+4 bps) ahead of today's supply and Catalan President Puigdemont's answer to Madrid on independence.

Eco calendar unenticing, eyes on Catalunya

Main attention goes to Spain today. Catalan President Puigdemont has until 10 am local time to formally declare or withdraw independence. Madrid indicated to trigger article 155, stripping the region from its autonomy, if he pushes through with the independence call. Dialogue is only possible if Catalunya withdraws its statement, according to PM Rajoy. We fear that tensions might escalate with an unknown outcome (new Catalan elections?). Such a context could cause underperformance of Spanish assets while the Bund might profit. The eco calendar contains US weekly jobless claims and October Philly Fed Business Outlook. Jobless claims are expected to stabilize near 240k and are probably no longer distorted by the Hurricanes. A small decline is forecast for the Philly Fed Index (23.8 to 22), but the volatile index remains near the highest levels. We don't expect the data to influence trading. The ECB's black-out period kicks in ahead of next week's key policy meeting. Kansas City Fed George speaks on the economy, but her hawkish views are well-known.



German Bund (orange) & German Dax (black)(intraday): risk-on weighs on Bund during European trading



German/Spanish 10-yr yield spread: Impact Catalan crisis remains modest until now. Escalation today?

R2	163,43	-1d
R1	162,19	
BUND	162,13	-0,44
S1	160,49	
S2	159,80	

France and Spain conclude scheduled EMU bond supply

The French treasury taps two on the run OAT's (0% May2021 & 0% Mar2023) and an off the run OAT (1.75% Nov2024) for a combined €6-7bn. The amount on offer is relatively low and should be easy to digest. We expect a decent auction. Additionally, the French Treasury wants to raise €1.25-1.75 bn via three inflation-linked OAT's. **The Spanish debt agency sells three on the run bonds (0.05% Jan2021, 1.45% Oct2027 & 2.9% Oct2046) and one off the run Obligacion (4.65% Jul2025) for a total amount of €4-5 bn.** The timing of the Spanish auction isn't the best one. Catalan President Puigdemont needs to declare/withdraw independence ahead of the auction. We fear that he won't give in to Madrid demands, causing risk aversion and volatility in Spanish bonds by the time of the auction. Therefore, we fear that many investors will decide not to participate in today's auction.

Shun Catalan political risk

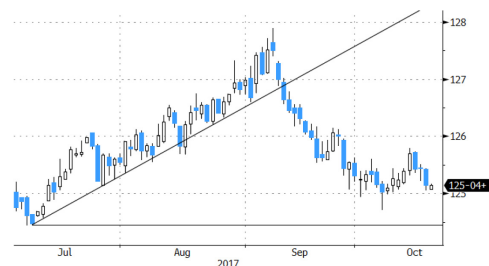
Asian stock markets trade mixed overnight with China underperforming (-0.50%) despite robust Q3 GDP data. The US Note future trades stable and we expect a neutral opening for the Bund.

Eco data and central bankers won't impact trading today. The Catalan-Madrid stand-off could escalate to a new phase (see above). Cautiousness might be warranted. The Bund might profit in a daily perspective, with more outperformance vs the US Note future while Spanish spreads could widen. Q3 earnings are a wildcard for trading via stock markets. US and German indices are at all-time highs, suggesting they are prone for a correction.

Technically, the German Bund broke above the 162 mark, implying a full retracement towards the contract high. European election outcomes (Germany, Austria, Catalonia) and ECB rumours caused outperformance vs the US Note future. **We hold a sell-on-upticks strategy in the US Note future (entry around 126), but put it on hold for the Bund.**



German Bund: Break above 162 suggests retracement towards September high



US Note future: underperformance vs Bund. Consolidation pattern still in place

Currencies

EUR/USD resilient despite Catalonia

USD/JPY outperforms

Dollar rebound against the euro runs into resistance

EUR/USD returns to the 1.18 area

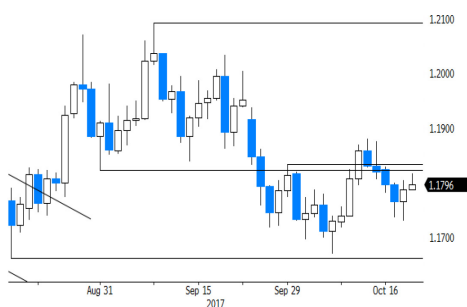
USD/JPY and EUR/JPY outperform

The dollar initially stayed well bid yesterday. However the relative performance of individual USD cross rates was different from earlier this week. The dollar struggled to make further headway against the euro, despite the Catalan uncertainty. Some 'hawkish' ECB comments blocked the euro decline. There was also talk of substantial EUR/JPY buying. EUR/USD closed the day slightly higher at 1.1787 (from 1.1766). USD/JPY outperformed, supported by higher core US/EMU yields and by a strong risk sentiment. The pair finished the session at 112.94 (from 112.10).

Overnight, the Chinese Q3 GDP was in line with expectations. The composition was OK. September retail sales and production were also as expected. **Even so, the Chinese data were not enough to enhance the Asian risk rally.** Most regional indices show modest losses of less than 0.5%. Japan outperforms on overall yen weakness. USD/JPY is testing the 113 level. EUR/JPY is trading well north of 133. EUR/USD maintains yesterday's intraday gain and trades in the 1.18 area. The **Aussie dollar** profited temporary from good labour data but failed to maintain the initial gain. AUD/USD trades again in the mid 0.78 area.

There are no important data in the EMU and **the US calendar is also thin.** Jobless claims are expected little changed. The Philly Fed business outlook is expected slightly softer at 22.0 from 23.8. **These data won't change the global picture for the dollar.** The deadline expires for Catalonia to renounce its independence claim. If it doesn't, Madrid said it will activate laws to suspend the region's autonomy. Until now, the impact of the Catalan tensions on broader European markets was limited. **Yesterday's price action of the euro suggests that markets assume that any action from Spain against the region will be modest/non-disruptive.** Even so, uncertainty on the next steps will probably persist. This might still be a (slightly?) negative for the euro. **On the dollar side of the story, the picture remains diffuse as well.** USD/JPY finally gained some traction on higher yields core yields (US & Europe). EUR/JPY also profits. At the same time, the dollar struggles to extend gains against the euro even as interest differentials are at cycle highs (2-y USD/Germ) or at a 'multi-month' top (10-y). This is disappointing for USD bulls. Earlier this week, we kept a neutral-to-tentatively negative bias for EUR/USD. We maintain this call, but due to uncertainty on Catalonia rather than on assumed USD strength. We remain cautious on USD/JPY despite this week's better performance. Event risk from whatever source might weigh on the pair.

R2	1,2225	-1d
R1	1,2167	
EUR/USD	1,1787	0,0021
S1	1,1662	
S2	1,1311	



EUR/USD: holding up well despite Catalan uncertainty



USD/JPY extends gains on higher core yields and risk-on sentiment

From a technical point of view, EUR/USD dropped below the 1.1823/ 1.2070 consolidation pattern, but no real test of the **1.1662 support occurred**. Last week, the pair even returned (temporary?) above the **1.1823 previous range bottom**, which was disappointing for EUR/USD bears. We maintain a cautious sell-on upticks bias. The pair needs to drop below 1.1670/62 support to really give comfort to EUR/USD bears. **The USD/JPY momentum was constructive in September**. The pair regained 110.67/95 (previous resistance), a short-term positive. The 114.49 correction top is the next important resistance. The rally lost momentum last week. A break beyond 114.49 looks ever more difficult.

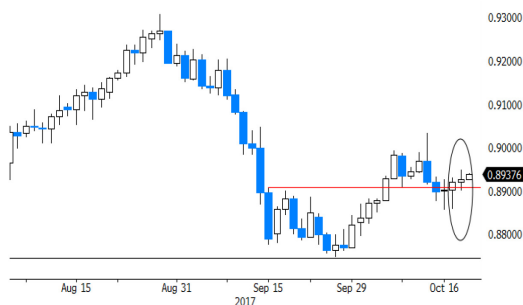
UK retail sales and EU summit in focus for sterling trading

Balanced comments from BoE governor Carney earlier this week convinced markets that any BoE tightening will be modest. This continued to weigh on sterling yesterday. UK labour data were mixed. Wage growth was marginally stronger than expected at 2.2% Y/Y, but real wages remain negative (-0.4%). **The small beat in wage growth didn't change market expectations that any BoE tightening will be very limited (probably only one hike)**. EUR/GBP temporary dropped a few ticks, but the move was soon reversed. The pair was further supported by a broader euro rebound later in the session. EUR/GBP finished the session at 0.8926 (from 0.8920). Cable was mainly driven by the overall swings in the dollar. The pair closed the session at 1.3205.

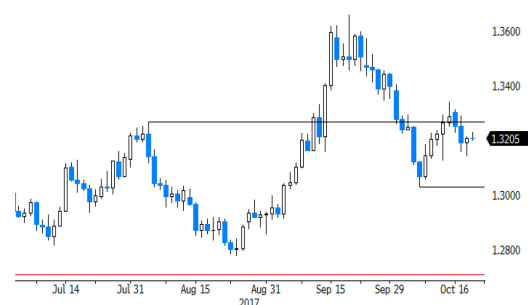
UK retail sales will be published today. Monthly data are very volatile. For September, a modest decline (-0.1% M/M) is expected after a strong rebound in August (1.0%). September CBI retail data were strong. **So, the report shouldn't be too bad**. Markets will also keep a close eye at the comments from the EU Summit. The UK will probably press to start with negotiations on trade and a transition period. The EU will probably repeat that there hasn't been made enough progress on the terms of the separation, but maybe the tone might be quite reconciliatory. **We don't expect the data or the EU summit to bring any breaking news for sterling. We hold on to the view that any upside of sterling will be difficult as the recent rally has run into resistance**. We look to buy EUR/GBP on dips.

EUR/GBP staged a strong uptrend from April till late August to set a top at 0.9307. Rising UK inflation data and hawkish BoE comments reinforced a sterling rebound, but **this rebound has run its course**. EUR/GBP supports at 0.8743 and 0.8652 proved difficult to break. **The recent rebound** above 0.89 improved the ST technical picture of EUR/GBP, but for now there were no convincing follow-through gains. **EUR/GBP 0.9026 is 50% retracement of the recent countermove**.

R2	0,9415	-1d
R1	0,9307	
EUR/GBP	0,8926	0,0006
S1	0,8743	
S2	0,8657	



EUR/GBP: sterling rebound runs into resistance as BoE tightening will be limited.



GBP/USD: no clear trend

Calendar

Thursday, 19 October		Consensus	Previous
US			
14:30	Initial Jobless Claims	240k	243k
14:30	Continuing Claims	1890k	1889k
14:30	Philadelphia Fed Business Outlook (Oct)	22	23.8
Japan			
01:50	Trade Balance Adjusted (Sep)	A:¥240.3b	¥367.3b
01:50	Exports YoY (Sep)	A:14.1%	18.1%
01:50	Imports YoY (Sep)	A:12.0%	15.2%
China			
04:00	GDP SA QoQ / YoY (3Q)	A:1.7%/6.8%	1.8%/6.9%
04:00	GDP YTD YoY (3Q)	A:6.9%	6.9%
04:00	Retail Sales YoY / YTD YoY (Sep)	A:10.3%/10.4%	10.1%/10.4%
04:00	Fixed Assets Ex Rural YTD YoY (Sep)	A: 7.5%	7.8%
04:00	Industrial Production YoY / YTD YoY (Sep)	A:6.6%/6.7%	6.0%/6.7%
UK			
10:30	Retail Sales Ex Auto Fuel MoM / YoY (Sep)	-0.3%/2.2%	1.0%/2.8%
10:30	Retail Sales Inc Auto Fuel MoM / YoY (Sep)	-0.2%/2.2%	1.0%/2.4%
Belgium			
15:00	Consumer Confidence Index (Oct)	--	3
Sweden			
09:30	Unemployment Rate SA (Sep)	6.5%	6.6%
Events			
Q4 earnings	Verizon (13:30), PayPal (22:05),...		
10:30	Spain to Sell 0.05% 2021, 4.65% 2025, 1.45% 2027 and 2.9% 2046 Bonds		
10:50	France to Sell 0% 2021, 0% 2023 and 1.75% 2024 Bonds		
15:30	Fed George Speaks about the US economy in Oklahoma		
10/19-10/20	EU leaders Hold Summit in Brusels		

10-year	Close	-1d		2-year	td	-1d		Stocks	Close	-1d
US	2,35	0,05		US	1,56	0,02		DOW	23157,6	160,16
DE	0,40	0,03		DE	-0,72	0,01		NASDAQ	6624,22	0,56
BE	0,66	0,03		BE	-0,57	0,01		NIKKEI	21448,52	85,47
UK	1,32	0,04		UK	0,44	0,03		DAX	13043,03	47,97
JP	0,07	-0,01		JP	-0,13	0,00		DJ euro-50	3619,65	11,88
IRS	EUR	USD	GBP	EUR	-1d	-2d		USD	-1d	-2d
3y	-0,07	1,93	0,93	Eonia	-0,3600	0,0010				
5y	0,21	2,08	1,07	Euribor-1	-0,3730	0,0000		Libor-1	1,2378	0,0000
10y	0,85	2,32	1,35	Euribor-3	-0,3290	0,0000		Libor-3	1,3573	0,0000
				Euribor-6	-0,2740	0,0000		Libor-6	1,5452	0,0000
Currencies	Close	-1d		Currencies	Close	-1d		Commodities	Close	-1d
EUR/USD	1,1787	0,0021		EUR/JPY	133,12	1,10		CRB	183,99	-0,25
USD/JPY	112,94	0,74		EUR/GBP	0,8926	0,0006		Gold	1283,00	-3,20
GBP/USD	1,3205	0,0015		EUR/CHF	1,1570	0,0058		Brent	58,15	0,27
AUD/USD	0,7846	0,0000		EUR/SEK	9,5982	0,0048				
USD/CAD	1,2467	-0,0055		EUR/NOK	9,3828	0,0349				

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