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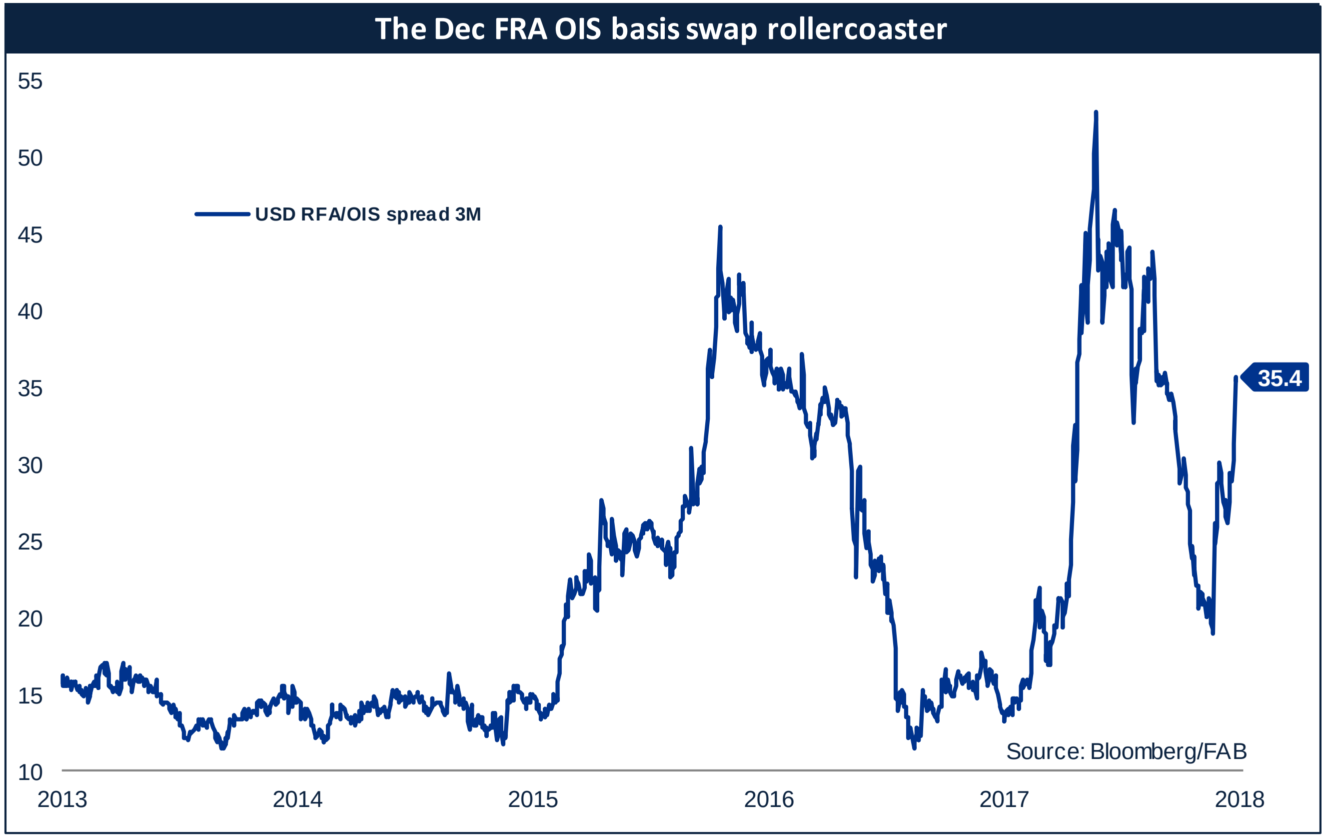
First Abu Dhabi Bank

G10 Rates & FX, & Oil - The Traders' Weekly Views

Market Overview: European event risk in focus

- There were two main focuses from the Brussels summit last week, one was the much vaunted discussions surrounding a Brexit deal (or not) while the other was a strong message from the European Union to Italy about its excessive spending. Both of these issues had serious repercussions in the market. The former pushed cable towards the big figure support at 1.3100 but the latter saw fall out across multiple European jurisdictions. Up until recently, Italy had been a largely idiosyncratic event risk in the broader Eurozone context, but weakness has begun to emanate more broadly in the past week.
- It will be interesting to see how the ECB handle the contagion at next week's press conference post the monthly rate setting meeting (where new expect no change to the main headline rates). With all Eurozone peripheral economies now coming under pressure from one fiscally irresponsible country, Draghi may be fairly limited in what he can actually do to address the situation - a situation that is compounded by the laissez faire attitude of the Italian government.
- Indeed, Italy's credit profile, clearly stressed, will again be firmly under the spotlight in this coming week. Moody's cut Italy's sovereign rating on Friday to 'Baa3' (from 'Baa2') leaving it staring into the the abyss of sub-investment grade territory. This follows Fitch's downgrade of the outlook on its 'BBB' Italy rating to negative from stable on August 31. Meanwhile, S&P is expected to announce the result of its rating review on Italy ('BBB') on Friday, October 26. Such uncertainty has manifested itself in the BTP Bund spread, which pushed to a historic high of 336bp.
- Portugal, Spain and Greece are all suffering on the back of Italy's woes, although, encouragingly, the EUR seemed to have found a base on Friday afternoon sitting around 1.1450.
- Funding pressure has become a mantra for our G10 desk who rightly point out that the cost of U.S. dollars has risen to 17% for the year end turn with expectations for this to move even higher over the coming weeks. Eurodollars came under pressure late last week as the Libor fixings seemed to reflect some of the pressure in the market, jumping 2bp and 1bp higher in 3m, Thursday and Friday respectively. The various USD basis curves also felt the pressure with widening across the board and the Dec Fra OIS basis swap above 35bp; this reached highs of nearly 53bp earlier this year. The chart below shows the path this basis has taken over the last five years.

- There are multiple different ways to hedge this funding risk so please do reach out to our teams to discuss further.



(Simon Ballard, Macro Strategist, Market Insights & Strategy)
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Please find below views on G10 Rates & FX, & Oil directly from our traders.

G-10 FX	Macroeconomic/Fundamental Analysis	Views (Bearish/Bullish) 2-week Time Frame	Intermediate & Long-term Views (3mth & 12mth Time Frame)
EUR	Last week carried yet another lower weekly close for EURUSD and the usual suspects were: Brexit/Italian Budget concerns/usd strength. The desk maintains its bearish view and short EUR position as the looming political uncertainties in Europe are unlikely to abate in the near future and will continue to weigh on the single currency; point made when the BTP/Bund spread gapped 20bps on Friday as the Italian BTPs traded at the highest levels since early 2014 and contagion fears drove yields in Spain and Portugal higher as well. This week is filled with European key events as we have Moody's potential downgrade to Italy, EU response to the Italian budget and the ECB meeting on Thursday, where the market will be watching closely if Draghi will crumble when asked about Italy.	Bearish	3m 1.1100 12m 1.1900
GBP	May's inability to make progress on a Brexit deal hit UK markets hard towards the end of last week with lower yields and cable challenging the 1.3000 support. Without sufficient momentum to warrant a November summit the last chance will be in mid December and the focus is turning towards no deal prep. It will be very difficult for May to push through an extension which leaves the UK and Europe in limbo for even longer but on the flip side it will be very difficult for Westminster to vote against a deal given the alternative. We remain divided on the desk but the expected range for cable is quite binary 1.15 on a no deal 1.50 on a deal. For short term focus 1.3000 remains key. This week is much lighter on data with Nationwide House prices and Mortgage approvals to look forward to Monday and Tuesday with the MPC and the BOE inflation report taking centre stage on Thursday. It will be an interesting read but Brexit headlines are likely to dominate and we expect no change.	Neutral	3m 1.3000 12m 1.4500
JPY	The strong USD was met with safe haven JPY demand that capped the USDJPY rally at 112.73 last week. Notably, the ongoing global political worries has taken a toll on the risk appetite, the market has shown clear signs of exhaustion and the market players refrained from adding fresh longs or shorts, evident by the fact that key support/resistance levels have not been broken yet across the board. Going into this week, USDJPY is likely to track equities and the market's risk sentiment.	Neutral	3m 110.00 12m 108.00
CHF	Swiss franc has really lost its shine as USD/CHF reaches levels not seen since August. Swiss watch exports for September fell 6.9% as compared to the previous year, shares in Swatch and other watchmakers fell immediately after the release. The wider stock market was not dragged down with the weak export numbers and Swiss economy is still forecast to expand by 0.4% in the final quarter of 2018. After a dip to below 0.9850 on Monday the franc has steadily declined against the U.S. dollar to reach a high of 0.9975 on Thursday.	Neutral	3m 0.9900 12m 0.9700

G-10 FX	Macroeconomic/Fundamental Analysis	Views (Bearish/Bullish) 2-week Time Frame	Intermediate & Long-term Views (3mth & 12mth Time Frame)
AUD	AUD/USD has erased its gains for this week as it dropped to 0.7089. Aussie has faded its upward move with the economy dilemma with Brexit, Italian bonds and China economy. Also, with economic releases; home loans, employment numbers were not as expectation and with the RBA minutes, the governments focused is on better employment numbers and increase in wages. The PBOC announced to support, the stock market and economy after, 3Q GDP numbers have missed. The Chines government will enhance its fiscal policy and infrastructure in the country. Positive news has given a small lift to Aussie as the two countries have strong trading partnership. The AUD/USD markets trading range 0.7080-0.7180 as support level 0.7080 and resistance is 0.7140.	Neutral	3m 0.6900 12m 0.6500
NZD	NZD has out preformed against its other pears for the week; with an upward momentum trying to break 0.660. NZD has been shield against the global drama that was reflected on the other currencies. However, the market is still bearish kiwi. Stronger Q3 CPI number gives more support to kiwi as also, RBNZ works on monetary policy statement with focus on inflation rates and economic growth. NZD/USD support level 0.6480 and resistance at 0.660.	Bearish	3m 0.6300 12m 0.6100
CAD	Good economic conditions in Canada are leading toward ongoing tightening by the Bank of Canada. The difference between the price of Western Canada Select and West Texas Intermediate is at its widest point in the last five years but the impact of the oil industry on the Canadian dollar is less critical than I once was. Market is pricing in four rate hikes over the next year. A hike at the next meeting at the end of October is about 80% priced in. USD/CAD traded down below 1.2920 on Tuesday then rallied over the week to a high of 1.3088 on Thursday.	Neutral	3m 1.2500 12m 1.2200

FX Options Commentary

- Volatility in USD pairs was slightly elevated this week; the biggest losers again the USD were EUR, GBP, Cad and CNH. The INR performed well and resistance around 74.50 looks strong. Implied volatility remains firm and this environment currently benefits clients who are looking for yield enhancement strategies like dual currency deposits, target notes and enhancer structures.
- The FXO desk took profit on a long gold position after a $50 rally in price over the last few weeks as topside momentum appears to be abating.

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