Financial intelligence
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The Context

September 17th 2018

Inside this week's edition…

Know The Flows - Investors Wait For Trade Negotiators And Central Banks To Show Their Hands

By Cameron Brandt, Director, Research

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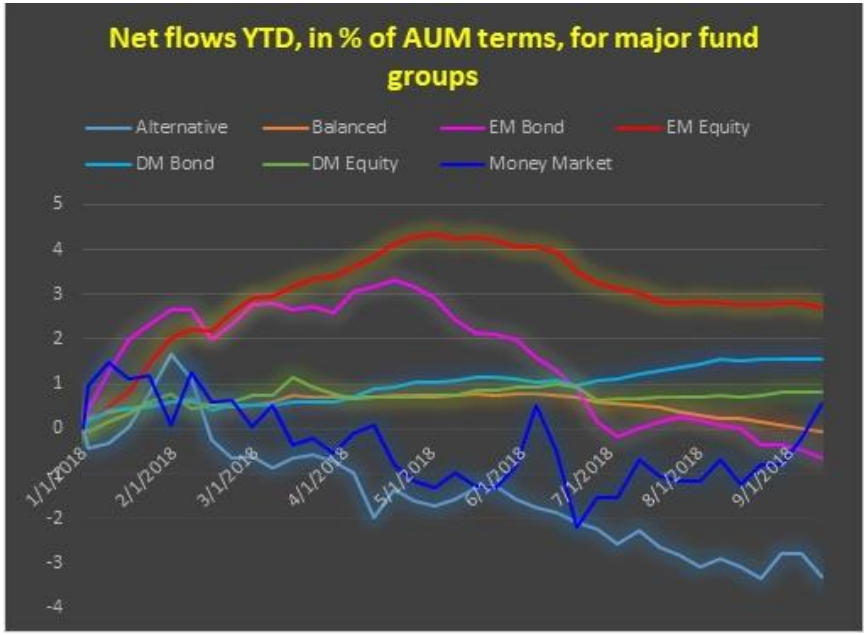
The prospect of more tariffs on Chinese exports to the US (and vice versa) and an impending round of central bank meetings kept the lid on mutual fund flows during the second week of September. As has been the case in recent months, the two themes that investors are willing to back is the recent outperformance of the US economy and the strength of China's domestic demand story. Among the major EPFR-tracked Equity Fund groups, only China, Japan and Latin America Equity Funds attracted fresh money while US Bond Funds stood out among the major Bond Fund groups.

Having snapped their third longest outflow streak on record the previous week, Europe Equity Funds posted outflows for the 26th time in the past 27 weeks. Redemptions from Europe Bond Funds, meanwhile, jumped to a 13-week high ahead of the European Central Bank's September 14 meeting when the ECB reaffirmed its goal of winding up the current asset buying program by year's end.

Appetite for Emerging Markets exposure also stalled. Emerging Markets Bond Funds posted their biggest collective outflow since late June and Emerging Markets Equity Funds since mid-July. Overall, EPFR-tracked Equity Funds saw a net $5.5 billion flow out during the seven days ending September 12. Investors pulled $840 million out of Alternative Funds and $14.5 billion from Money Market Funds while Bond Funds posted an inflow of $271 million.

At the single country fund level, Japan Bond Funds recorded their biggest inflow since the first week of 2017, China Equity Funds took in fresh money for the 26th time in the past 30 weeks and flows into New Zealand Equity Funds climbed to levels last seen in mid-February. Among the Europe Country Fund groups France Equity Funds posted their biggest inflow since mid-1Q18 and Greece Equity Funds their largest outflow since 4Q14.

Sector oriented investors remained on the defensive during the week ending September 12 as another US rate hike loomed larger. Consumer Goods, Utilities, Telecoms, Healthcare and Real Estate Sector Funds all



recorded inflows while investors pulled money out of Technology, Energy, Commodities, Industrials and Financial Sector Funds.

Flows into Telecom Sector Funds hit an 11-week high as they took in fresh money for the 12th time in the past 13 weeks. Fund managers have been more cautious in their assessments for this sector, which is engaged in the expensive process of developing and rolling out the fifth generation (5G) cellular phone networks. Allocations to the sector by China and Japan Equity Funds are at seven and 11-month highs respectively, but its average weighting among Europe and US Equity Funds remains close to the five-year and record lows posted in mid-3Q18.

Holding Pattern To FOMC

By David Ader, Chief Macro Strategist

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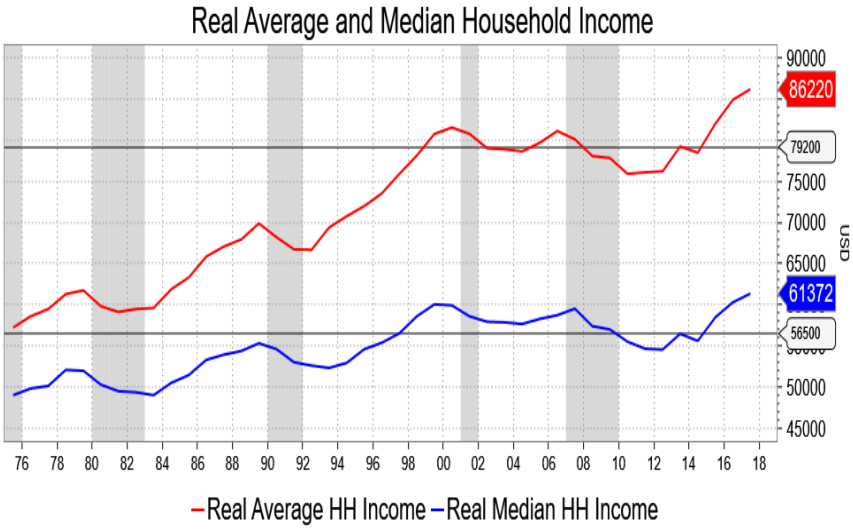
I have to again say, out of frustration, that I don't understand how the people can ignore the real wage components to the current narrative in light of recent CPI and AHE figures. I don't have any doubt that this will NOT discourage the Fed from hiking, but I don't understand how so many people and the press are willing to ignore the real component to income gains. I suppose the news is simply so good everywhere else that this particular aspect seems the anomaly, but not enough for me to avoid bringing it up again and again. In any event, with the release of August CPI at least the real Average Hourly Earnings YoY gain is in positive territory albeit a pretty lame gain of 0.2%.

Semi-related to such wage issues was data from the Census Bureau on Real Median Household Incomes. The headlines sound good along the lines of "Incomes Rise, Poverty Falls Again," and that is true; such incomes grew 1.8% over 2017, the 3rd consecutive annual gain (but at a slower pace). The flipside to that coin is that, according the Census, the gain is not 'statistically significant.' This is an interesting note because, as per the chart, the current level of $61,372 is barely above the prior peaks of 1999 and 2007, which is to say, we're not better off than we were then in purely income terms.

In fact, the story is especially interesting when you compare Average to Median. The Average Incomes are up somewhat more than Median pointing to an outsized gain by a few at the upper tier of the income gain. This underscores the wealth divergence, call it income inequality, of the last two decades.

I've read in recent days about higher Treasury yields as if another foray in 10s near 3% represents a new bear market. It's a case of I think over emphasizing price action in a narrow context amidst a lot of perhaps confusing inputs and noise out there. I don't see much direction. 10s have traded pretty much in a 20bp range since late May, and I don't yet see a break out. 2.80-3.00% has contained, what, 95% of the price action? That's remarkable and revealing in that it implies the market is either at fair value or simply frozen by events.



Source: Macrobond, U.S. Census Bureau

There's truth in both aspects, but I'll put more on the event component. We have ongoing trade tumult, the steady hand of the Fed (where Dec Funds now give 77% odds of a hike) boosting the dollar and flattening the curve with all that implies as 2s/10s flirt with 20bp. There's the repercussions for EM debt exacerbating the problems, political and financial, in specific countries and spreading to general risk aversion. There's the mid-term elections. And there's this Administration's foibles, a word which is giving it the benefit of the doubt.

In short, I think we wait. The hike this month is all there with the nuance being is it a 'hawkish' hike that points to confidence (as per so much of recent Fedspeak) or a 'dovish' one hinting at a pause. My thoughts are they stay optimistic and can nuance things as those events I spoke of unfold.

Leveraged Loans: Refinitiv To Set The Tone

By Giles Hamblett, Loans Editor

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As the first big, post-summer financing Refinitiv will set the tone for what is a fairly busy back-to-school period in the debt markets.

The financing has been a long time coming with Blackstone and Thomson Reuters agreeing the transaction back in January, with the private equity firm taking a 55% stake and TR retaining the rest.

The size of the financing (USD8bn loans, USD5.5bn bonds) meant it was always going to provide a useful yardstick for the market but given the timing of the transaction it has taken on even greater significance. The deal will not only reopen the leveraged market after the summer, but also after a period of increased investor pushback and price widening.

Spread the joy

The pendulum may have swung back towards investors but there is still plenty of money looking for a home and pricing on the TLB has generally been well received.

'Pricing looks fairly sensible looking at secondary. Paper paying 350 over is trading around par so there is a bit of fat in the new prices,' said a banker away from the deal.

In the doc

However, while pricing has garnered positive responses, documentation has created quite a stir. Covenant Review adjudged the deal as having some of the weakest investor protections since the financial crisis and urged investors to push back.

The call to arms will be preaching to the converted as investors will feel emboldened by some notable victories over the summer months. However, it has been a very long road to get to this point.

One banker commented that he could not remember a deal he had launched in 2018 that did not receive pushback but it was only in the last couple of months that investors had been affecting a change. And even after the successful tightening, documentation still includes more flexibility than could realistically ever be used.

'Pushback took a long time before it got some momentum,' said one banker, 'and investor victories have only rolled back docs to where they were about three months.'

As for Refinitiv, a source close to the deal acknowledged that some of the t+c are aggressive, before pointing out that some flexibility on documentation had increasingly become general market practice over the last two or three months.

Pipeline supports

While the lack of protection is said to be troubling some investors, fear of missing out could play a big part in getting accounts to accept the rather accommodating documentation (particularly on the EUR TLB).

'Anyone with principles will push back but investors will have one eye on the pipeline. It looks good until the end of the month but October looks awful. If you miss out on 50 million plus ticket on this one, that's a lot of paper to source elsewhere,' summed up one source.

Despite a heavy line up for September with, including Refinitiv, Starfruit, DSP, SUSE, Garrett and Ammeraal, the Q4 cupboard currently looks rather bare.

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Leveraged Loans: Refinitiv To Set The Tone - Cont'd

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And that lack of visibility is at a time when there are a lot of mouths to feed. One banker, estimated around 38 CLOs are currently in the works, noting, 'You can't source that volume of paper in secondary.'

The supply side could also take a hit should the IPO market pick up. SIG Combibloc, for example, plans to pay down around EUR1bn of debt when it floats, replacing just over EUR1bn of TLB paper with a new EUR350m TLB facility.

Currency in the mix

With Refinitiv seeking a mix of USD and EUR facilities across bonds and loans, the structure lends itself to some competitive tensions and there has been plenty of talk that, given the stronger response stateside, some (or even all) of the EUR debt could migrate over to dollars.

However, while there certainly appears excess demand in USD, this could be down to a more nimble US investor base having the ability to revert more quickly.

One banker close to the deal commented that although there is some scope to adjust the currency mix the deal has been structured fairly USD-heavy, which limits the opportunity to further skew the currency mix.

In terms of the geographical spread of the Refinitiv business a decent EUR portion makes sense, even if USD is the more popular sell, while the overall size of the transaction favours the kind of liquidity offered by the twin-centred deal.

Starfruit awaits

The general market view is that securing the EUR TLB within guidance would be a decent result, while a print at the tight end would be a significant achievement. Wherever pricing settles, it will be a benchmark for the subsequent Autumnal issuance, particularly **Akzo Nobel Specialty (Starfruit)** which is expected to price its jumbo USD/EUR offering next week.

'Refinitiv is a line in the sand but purely on size alone you would expect it to come wide of subsequent deals,' predicted one banker.

Look At All That Economic Liquidity!

By Marcus Dewsnap, Senior Analyst/Editor

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It is the 10-year anniversary of the Lehman's bankruptcy. The following graphic shows the vast amount of economic ***LIQUIDITY*** that has been unleashed on the financial system by the Fed, ECB and BoJ during the intervening period. Indeed, most of it remains.

Sum of Fed, BoJ and ECB Balance Sheets - Trillion Usd

After peaking around $15tn earlier this year, a slight fall followed before stalling. In terms of percentage change, the growth rate has slowed markedly.

Sum of Fed, BoJ and ECB, Usd Trillions y/y % change

The next important step comes with ECB halving purchases from October onwards (this is still balance sheet expansionary). Along with the Fed's ongoing balance sheet contraction and depending on BoJ machinations, the Global CB balance sheet might (as many predict) begin to *contract* in Q4. With the ECB on course to stop expansionary policy in the New Year, this global balance sheet contraction will be more permanent than previous short-lived episodes. Almost everywhere but the US, risk asset prices have been under the cosh this year. There is an uncanny profile for the MSCI ex-US with the slowdown in the global central bank balance sheet growth.

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Look At All That Economic Liquidity! – Cont'd…

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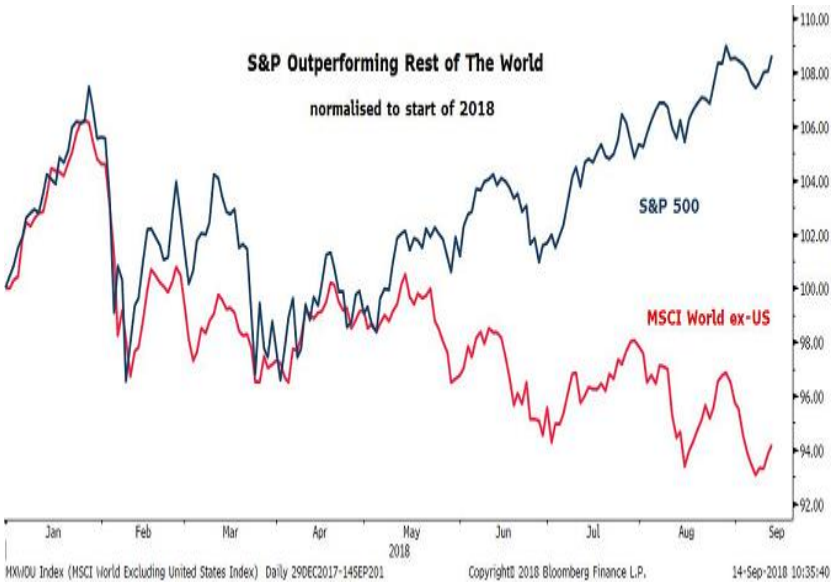

This simplifies the comparison somewhat. Trade war talk/build-up has clearly and negatively impacted outside of the US and a significant element of US equity market outperformance is tech related. Share buybacks are non-trivial too. It all makes folks wonder what is in store for markets once the global balance sheet contracts on a sustained basis and liquidity is in the aggregate pulled (the PBoC to fill?) – first port of call might be Emerging Markets if Dollar strength continues … which makes this ING piece (HERE) suggesting the time to 'Ditch the Dollar' might be approaching interesting. Steeper yield curves are a worry, especially in the Eurozone. Steeper yield curves equal tighter financial conditions.

So, even with the political backdrop (trade, Brexit), we should not be ignoring the central bankers. The ***FED*** enters purdah ahead of the September FOMC – which should give everyone time to read Brainard's recent speech (HERE). The significance of Brainard's comments are that she used to be considered on the dovish end of the spectrum. To be fair, she has moved ground towards the centre, but there is nothing dovish about comments that suggest hiking may need to continue until past neutral. This because of more of a focus on the low unemployment rate and strong growth as opposed to about target inflation.

ECB Chief Draghi speaks (Tuesday and Wednesday). Compared to previous post-meeting pressers, he was fairly hawkish at the September episode (see HERE for our Takeaways). Positive on growth – the downgrade really should be taken as minor - it will be interesting to hear whether he continues in this form. Couere and Praet speak (Monday), latter also in New York (Thursday) - '*Challenges to monetary policy normalisation*' should be worth a listen.

The ***BoJ*** gathers (Wednesday). Amidst the Bank's concern about deteriorating market function as a result of QQE, and Kuroda's admission that a wider band for 10-year yields (-0.200% to 0.200%) will be tolerated, the inference is that there could be more JGB purchase cuts ahead. In addition, future fixed rate operations might be conducted at higher levels than previous (0.110%, 0.100%) … with more policy tweaks could be seen ahead. We also suspect an ultimate move to outright YCC parameter tweaks (via lifting the 10-year yield target to 0.150% and subsequently 0.200%).

GBP, EUR OIS Curves Creeping Higher As CB Dust Settles

By Robert Graystone, Fixed Income Strategist

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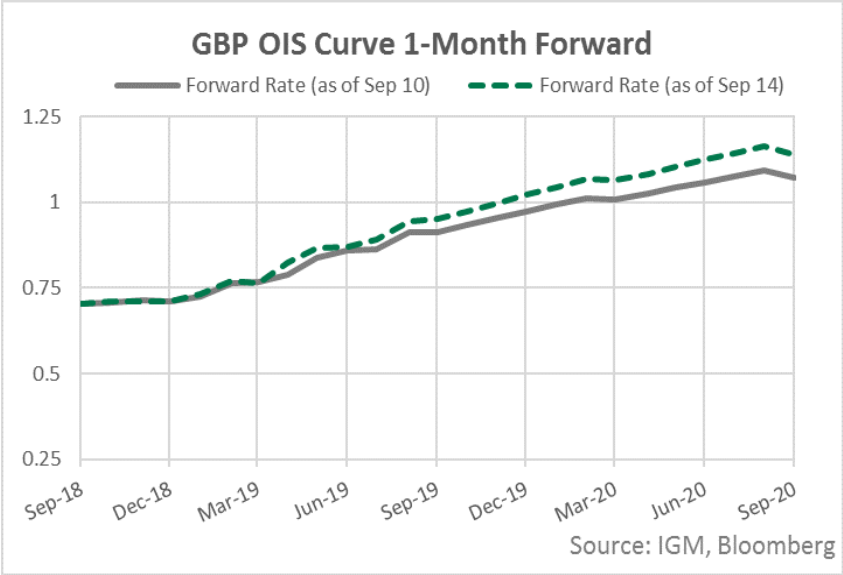
As the dust settles after a busy week of central bank meetings for European investors, we take the opportunity to examine how interest rate expectations have been shifted.

BOE

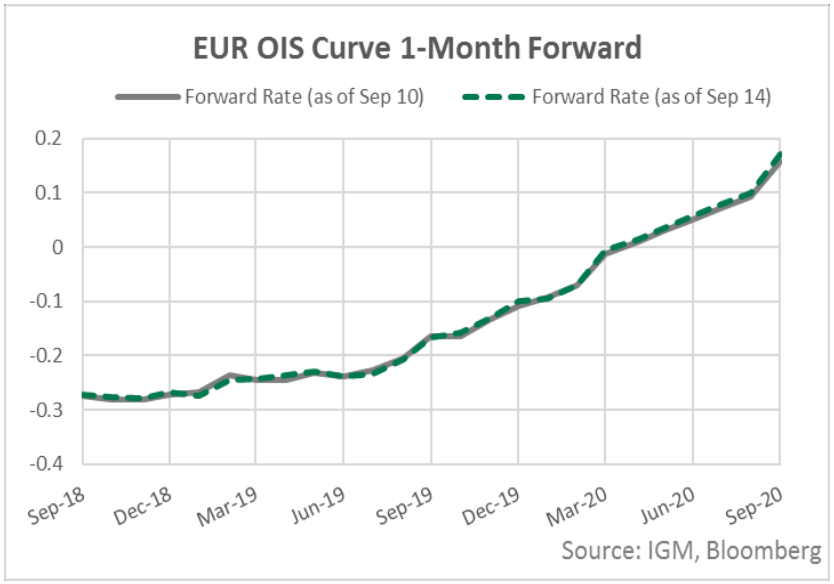
Governor Carney reportedly told PM May's cabinet meeting that a 'no deal' scenario would likely force the Central Bank to raise rates in order to counteract the inflationary impact of Sterling depreciation. Although rate setters flagged greater uncertainty surrounding Brexit in September than there had been at their last convene in August, markets have taken note of upbeat/optimistic verbiage from negotiators on both sides of the table.



Over the course of the week, interest rate expectations have crept higher, with the OIS curve pointing to a 25bp rate increase by mid/end-2019 and the 1-month forward rate at the 2 year horizon now ca 7bp higher. Our view is somewhat hawkish by comparison - rate setters could begin priming markets for further tightening to be implemented as early as Q2 2019 once there is further clarity on an orderly UK/EU divorce. See our BOE Insight for more.

ECB

Movement in the EUR OIS curve has been more contained, but markets have still reacted to Draghi's hawkish tilt at Thursday's presser where the ECB President sounded confident on the Eurozone economy and inflation. This was, of course, partly offset by the suggestion that risks (EMs including China, financial volatility and protectionism) have 'gained more prominence'.



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GBP, EUR OIS Curves Creeping Higher As CB Dust Settles - Cont'd

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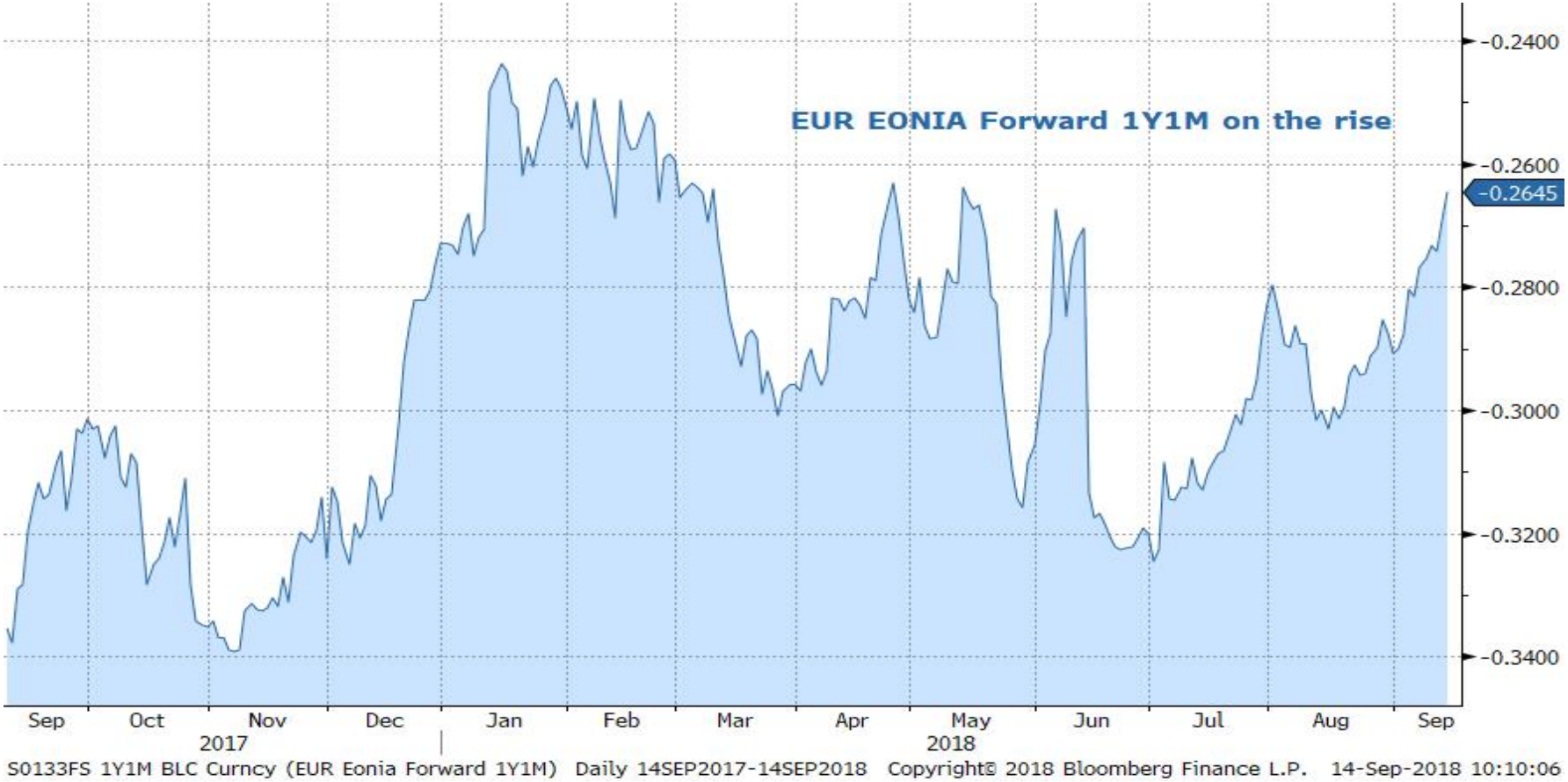
Although only a minor move, we would highlight that the last week marked a continuation of the ongoing push higher in the EONIA 1Y1M forward rate which is now more or less level with its April/May peaks,

That being said, there are still plenty of unanswered questions regarding the ECB's balance sheet reinvestment policy, and 'Operation Twist'. See our main takeaways from the September meeting HERE.



The Yen Week - Bias is Bearish

By Tony Nyman, Head G10 FX

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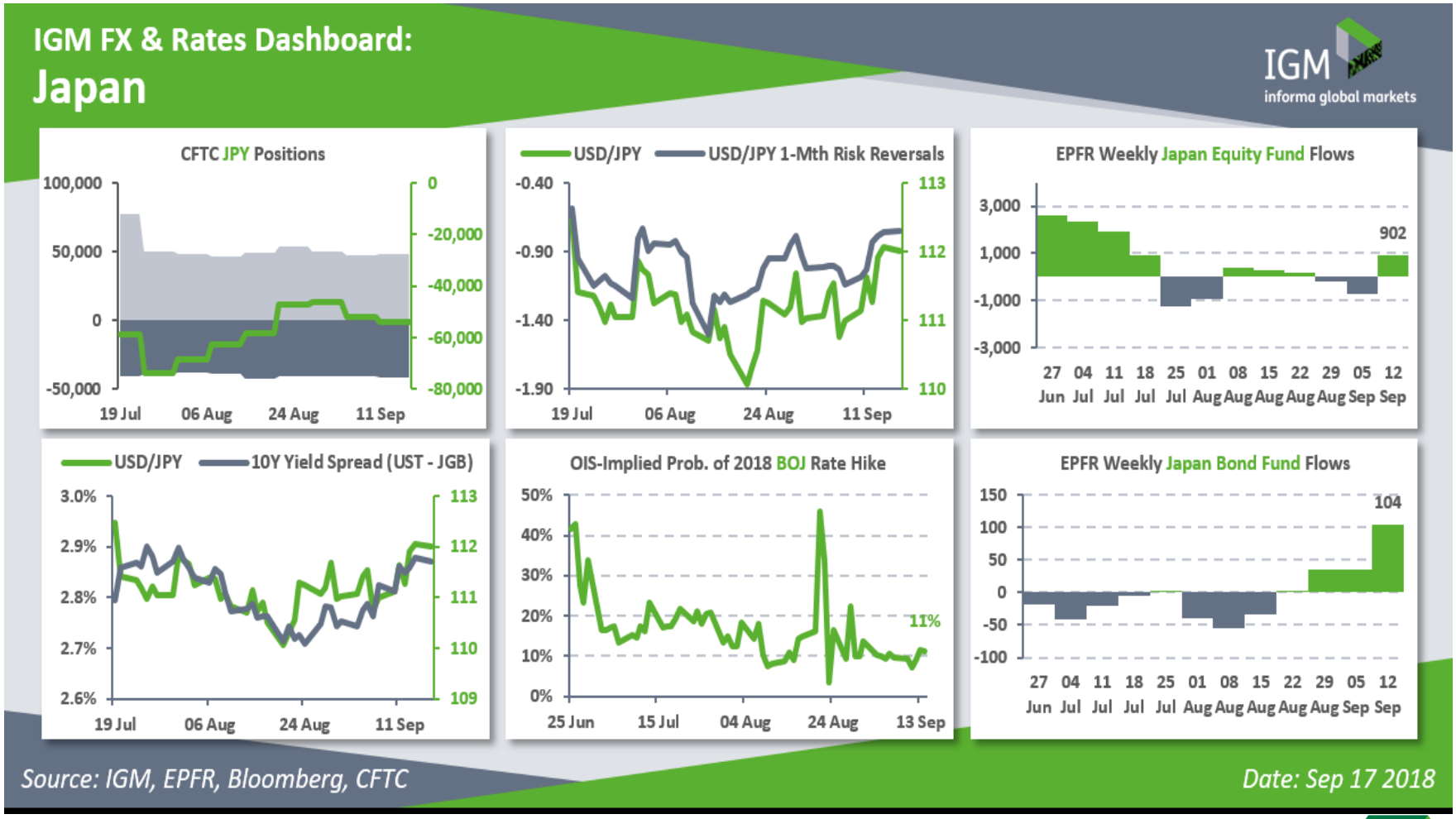
Expected Usd/Jpy trading range is 111.40/112.70, but note **112.00** is a major expiry area this week, which could work to rein in direction.



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The Yen Week - Bias is Bearish - Cont'd…

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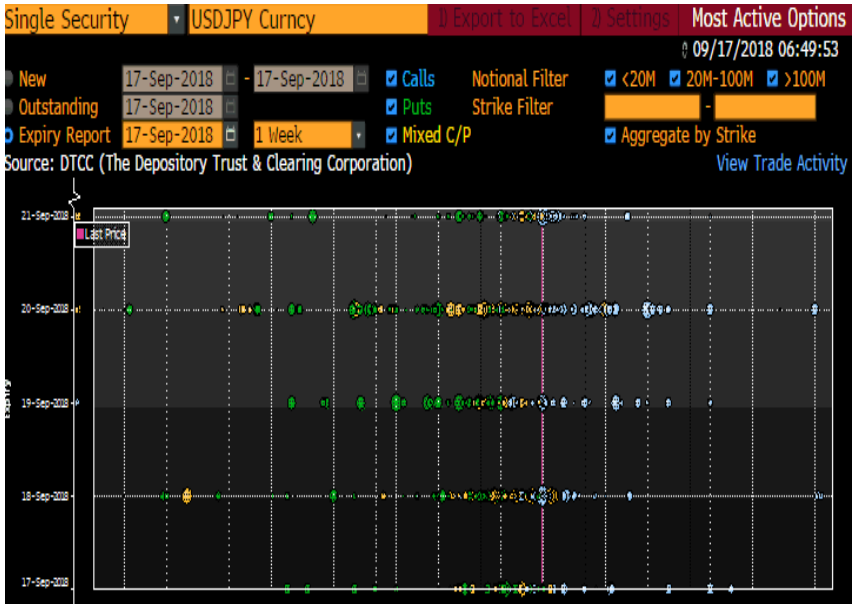

This bias has pretty much won out since mid-Q2, with the mantra there is *no Usd alternative* on growth and yield advantage cards.

That has won out within a 110.00/112.00 range, but can it inspire a big break for 113, even 115 handles for the remainder of the year?

We suspect there will continue to be plenty of natural profit taking interest in and around the figure at this juncture as investors toy with **mixed drivers**

BULLS

- The Fed is hiking still and two more are scheduled before 2018 is out. (However, this is largely priced).
- Firm US yields. (10-yr really needs a clear 3.00%-plus break though).
- The trade dispute - the Usd is a natural safe haven home vs the likes of Euro.
- The US is still releasing some very strong data (61.3 Aug ISM) deep in the cycle.
- Booming US stocks.

BEARS

- Trade dispute - if it escalates and Japan really comes under the microscope it could spark major Japanese investor repatriation.
- Concerns over Hurricane Florence.
- Trump and his apparent dislike of a strong Dollar and the US president not being shy about calling it out.
- The threat of inverted yield curves, recession ahead talk.
- This week also brings on the JAPANESE front:
- Wed - *The BOJ:* Domestically, the economy is doing pretty well, but the path to normalisation will not be rushed and late Thu's expected 1.1% y/y national CPI is unlikely to impact on market thinking.
- Thu - The LDP leadership election. Abenomics should be endorsed anew which should prove a relative prop here. If he suffers a very surprising defeat, the Yen could rally quite sharply on the possibility his reflationary policies could be watered down.

RISK: Any of the above - Abe, trade, a fresh 3.00%+ test failure. Do latest EPFR flows data (see RHS Dashboard) indicate trade dispute related Japanese investor repatriation has already begun?

Is The Worst Now Over For Turkish Assets?

By Natalie Rivett, Senior Emerging Markets Analyst & Ed Blake, Chief FI Technical Analyst

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Turkish assets had stabilised off their record/multi-month lows in recent weeks, despite the lack of any fundamental improvement in the domestic narrative that left traders facing the same lingering concerns surrounding fraught Turkey-US relations and the government's reluctance to return to policy orthodoxy.

This stabilisation had largely been a function of the CBRT's efforts to make it more expensive for speculators to short the Lira by increasing funding rates – a calmer Lira essentially setting the tone. However, Turkish assets were given an extra boost this week as the Central Bank finally showed it is serious about tackling sky high inflation, that approached 18% y/y in August. The CBRT had set the bar high for itself by announcing plans to adjust monetary policy, but the massive 625bp increase to the benchmark one-week repo rate, to 24.00%, still surpassed most analyst expectations and should succeed in restoring central bank credibility.

As such, Usd/Try has now eased some 17% and the yield on the 10-year local currency bond has retraced by more than 350bp from mid-August peaks, whilst the Borsa Istanbul has rebounded 10% from its mid-August trough.

Traders showing less appetite to short the iShares Turkey MSCI ETF

Additionally, the MSCI Turkey ETF has bounced 16% from its record low in mid-August that marked a ytd decline of more than 55%. Early last month, net cumulative flows into the ETF staged a sharp turnaround from negative to positive as traders looked to be increasingly establishing short positions, though these inflows have trailed off slightly in recent weeks, with the biggest daily outflow since early July recorded just this week. Additionally, puts as a percentage of the overall total of open interest stand at ca. 62% on a 5-day average versus 64% on a 20-day average, and together with the flows data, suggests there is now less appetite to short the ETF.

Please refer to the 'Dashboard' on the following page.

There is little appeal left in short selling

We recall one well known investment guru saying last month, at the height of the Turkish turmoil, that it was time to start investing in Turkish assets. Since then, at least one fund manager has openly announced that it has been buying Turkey stocks, citing near financial crisis valuation levels and a currency that is significantly undervalued. On the latter, Turkey's real effective exchange rate (REER) has contracted for seven consecutive months, to 64.82 in August, a new low since the index was created in 2003. Turkey's REER has seen one of the biggest deteriorations of all EMs this year, second to the Argentine Peso.

Several commentators had suggested in the lead up to the September 13th policy meeting that a rate hike was not needed anymore, given the economic adjustment already made due to the weaker Lira and higher borrowing costs. Economic growth moderated sharply to 5.2% y/y in Q2 from 7.4% in the first three months of 2018 and a market crisis of the magnitude seen ytd will likely weigh further on GDP growth going forward. It has already helped to improve Turkey's external balance, with the current account gap at its narrowest since Q3 2016 and even likely to turn positive in the coming months.

However, the Central Bank did need to hike, purely to rebuild market trust. Prior backdoor tightening measures were not a sustainable source of Lira support. We believe the significant rate hike from the CBRT this month has probably drawn a line under the recent sell-off and by improving the risk reward ratio for Turkish assets, in our opinion, it could encourage some previously cautious investors to return.

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Is The Worst Now Over For Turkish Assets? – Cont'd …

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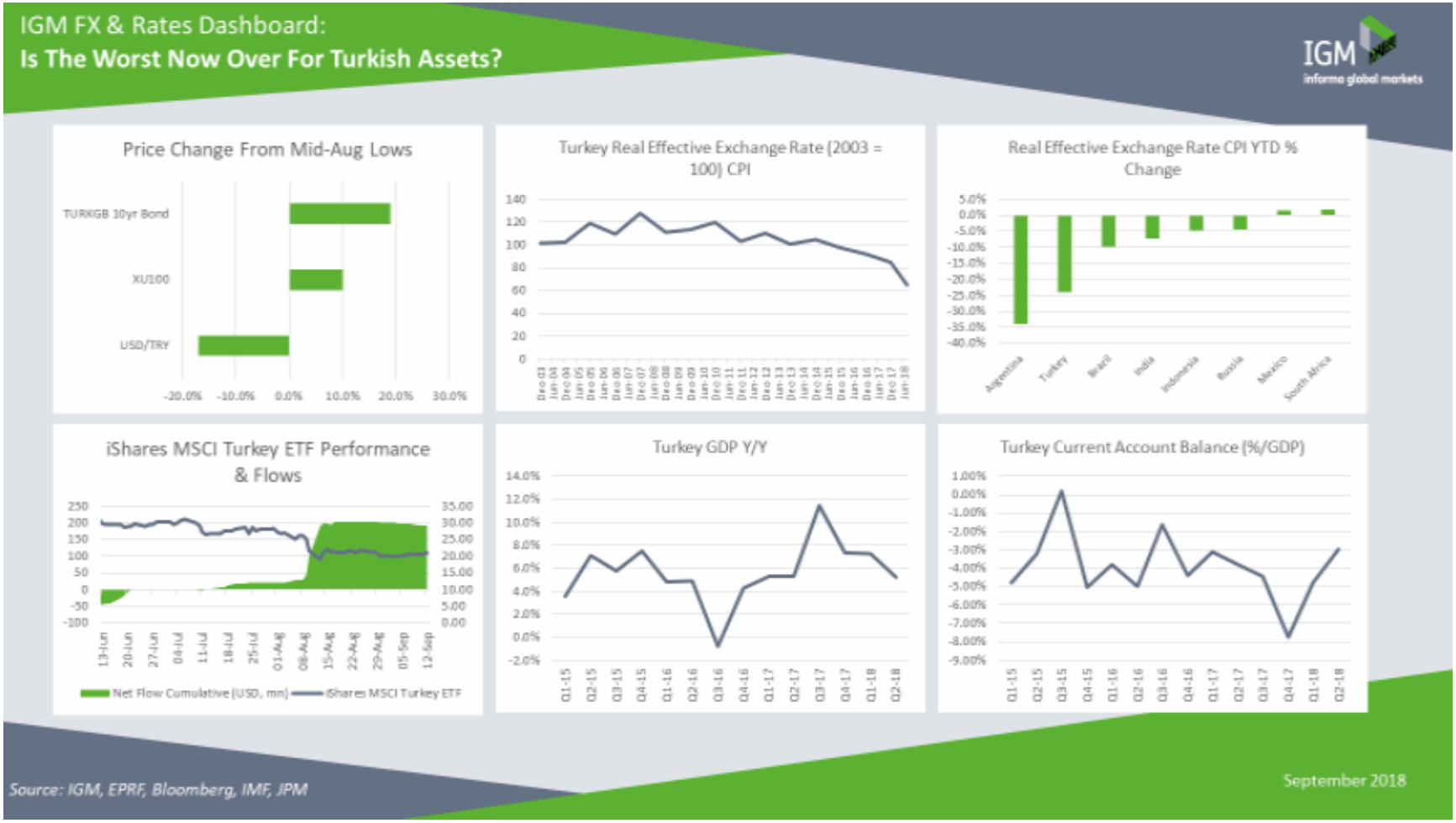

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Is The Worst Now Over For Turkish Assets? – Cont'd …

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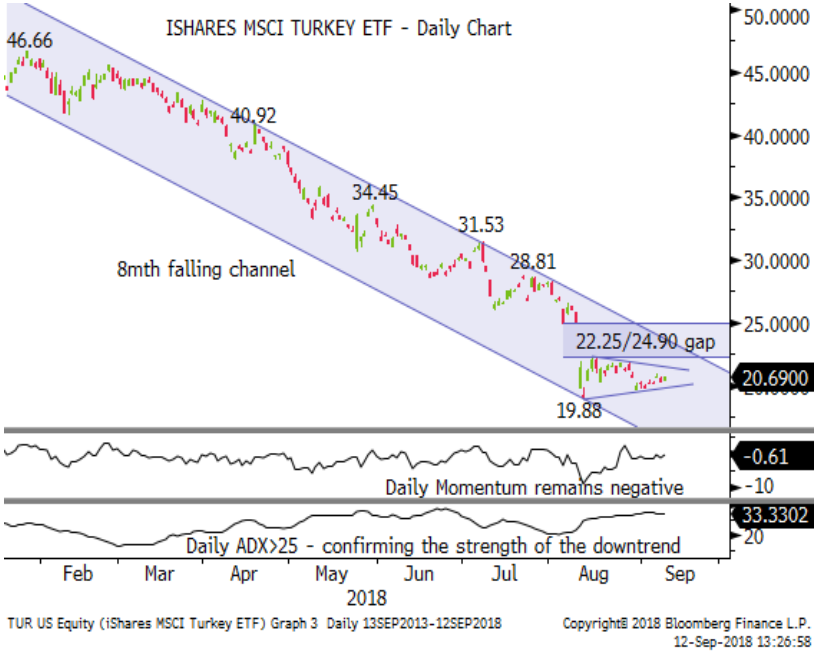
Reasons for caution

Interestingly though, we note that GAM's McNamara has suggested (via the FT) that previous EM crises indicate that markets begin to turn, not after the external balance has corrected, but when a contraction in economic activity slows or even ends. An example of this can be seen below, with Brazil's Ibovespa rebounding from its multi-year lows into mid-2016, once the economic contraction started to moderate from record levels, following the impeachment of former president Rousseff.

Turkey is, albeit, some way from the end of its economic slowdown and so, it is possible that most investors will prefer to wait until the economy has shown signs of bottoming out before turning constructive on Turkish assets. Moreover, US-Turkey relations are still showing no signs of improving and this political risk still has the potential to blow up so long as Turkey refuses to release the jailed US pastor, which would undo much of the CBRT's recent efforts.

Shares Turkey MSCI ETF - Minor bounce before the wider downtrend resumes

The technical outlook is still bearish for the iShares Turkey MSCI ETF, with daily-monthly studies suggesting near-term recovery towards 23.34, before the wider downtrend resumes. Above 24.90 is required to signal a more meaningful recovery.



- Retreated within an 8mth falling channel to 19.88 (2018 low - 13 August), ahead of the latest recovery above 22.25 (15 August high) to suggest a minor base
- Improving daily studies suggest additional near-term recovery towards 23.34 (8mth channel top), perhaps 24.90 (6/9 August lows/gap high), before the wider downtrend resumes
- Negatively aligned longer-term studies support this view and an eventual return below 19.88 risks 18.05 (20 November 2008 record low), perhaps 17.21 (.618 projection of 77.40/28.98 from 47.13)
- It would take closure of the gap down from 24.90 to suggest a more meaningful recovery towards 28.81 (23 July lower high)

China Insight: Trump Deals With China In Same Way As He Handled N.Korea

By Tim Cheung Head of China, Riki Zhang EM Analyst

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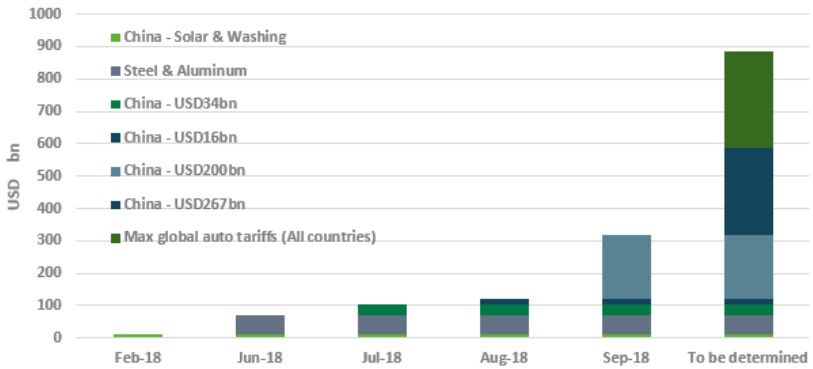
US President Donald Trump stated on 7 September that he's prepared to impose tariffs on additional USD267bn worth of Chinese goods, on top of the USD200bn already being considered. That is not a big surprise to us, as similar tactic was already adopted in dealing with North Korea at the beginning of the year, in which Trump kept putting pressure on Kim in order to maximize the chance of victory. In regard to the US-China trade war, an adoption of this tactic unavoidably will escalate the tension. Both Hong Kong equities and China A-shares plunged further on 10 September, suggesting the market was repricing the trade war scenario. Therefore, it is possible that any rebound of the Hong Kong equities and Chinese A-shares in the very near term will likely be very shortlived.

Chart 1 shows how the basket of imports to the US subject to increase in tariffs will change if Trump really goes ahead with what he has said.

Chart 1

The basket of imports to the US subject to increase in tariffs

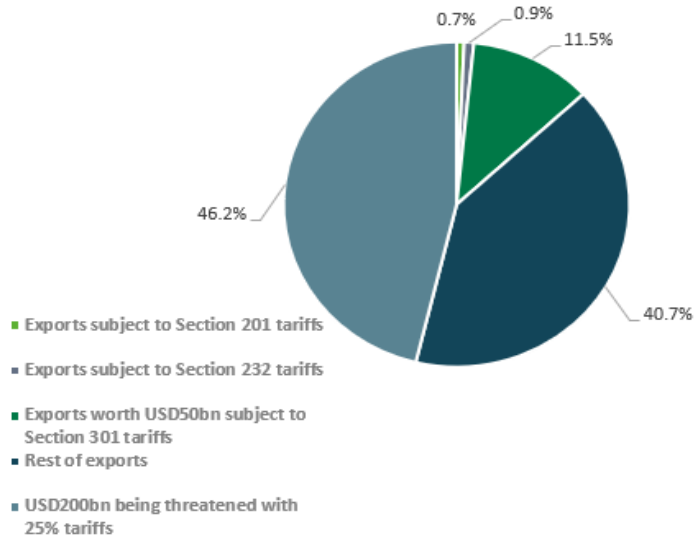


Data source: JP Morgan, Bloomberg

Let's temporarily ignore the potential tariffs on the USD267bn and place our focus on that on the USD200bn, which is very likely to come into effect soon. Compared to that on USD50bn already implemented, the tariffs on USD200bn will be more impactful in the sense that an additional 40% of China's exports to the US will be targeted on top of the 19% already hit and that a significant number of consumer products will be involved. Chart 2 show the breakdown of China's exports to the US, which are already and potentially hit by the tariffs. The US have various trade actions taken under a combination of three US Executive Authorities: Section 232 (known as national security clause); 301 (known as burden to commerce); and 201 (known as serious injury). Each authority has its own power to protect the US interests.

Chart 2

China's exports to the US already/potentially hit by higher tariffs



Note: the data is caculated in 2017 terms.

Data source: BAML

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China Insight: Trump deals with China in same way as he handled N.Korea - Cont'd..

By Tim Cheung Head of China, Riki Zhang EM Analyst

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For now, the most optimistic scenario is the Trump administration chooses to break the USD200bn of Chinese goods into smaller batches and impose the tariffs on them in sequence; and/or delay the execution to some time after President Trump meets with President Xi in late-November. In contrast, the worst scenario is the US slaps on a 25% tariff increase on the entire USD200bn product list straightaway. Needless to say, the latter scenario will have a very negative impact on China's growth in Q4 and subsequently in 2019. Face with a more challenging-than-expected macro outlook, China will be forced to adopt more aggressive stimulus measures, including more RRR reductions, a drastic de-escalation (or suspension) of financial deleveraging and a launch of more infrastructure investment projects.

As far as CNY FX is concerned, we think PBOC will remain biased in favour of curbing CNY depreciation as long as President Xi still sees a chance of reaching a deal with Trump in late-November. In case a deal proves to be unreachable, the PBoC will just let CNY slide further to at least 7.00 against USD as China needs to seek more currency depreciation to offset the price pressure on the exports to the US as a result of the additional tariffs.

Emerging Asia Insight: We Will See The Last Light In Q4 Before Darkness Comes

By Tim Cheung Head of China, Riki Zhang EM Analyst

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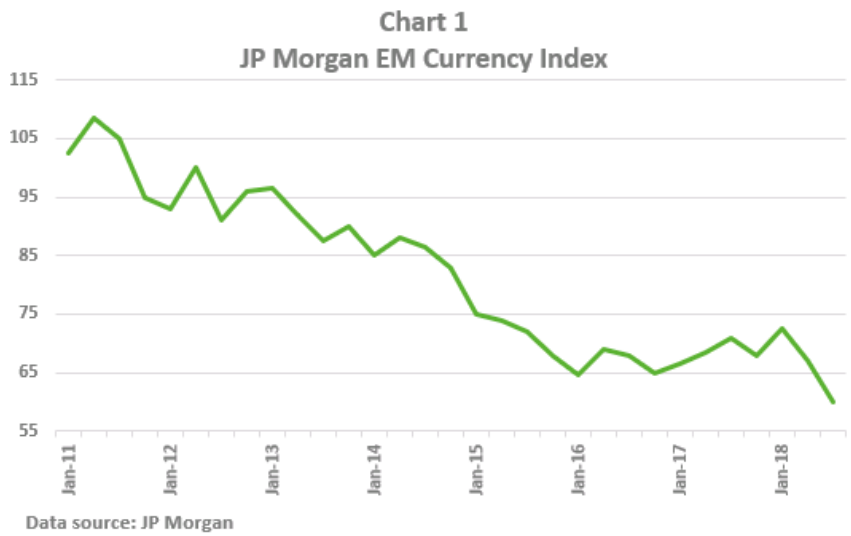
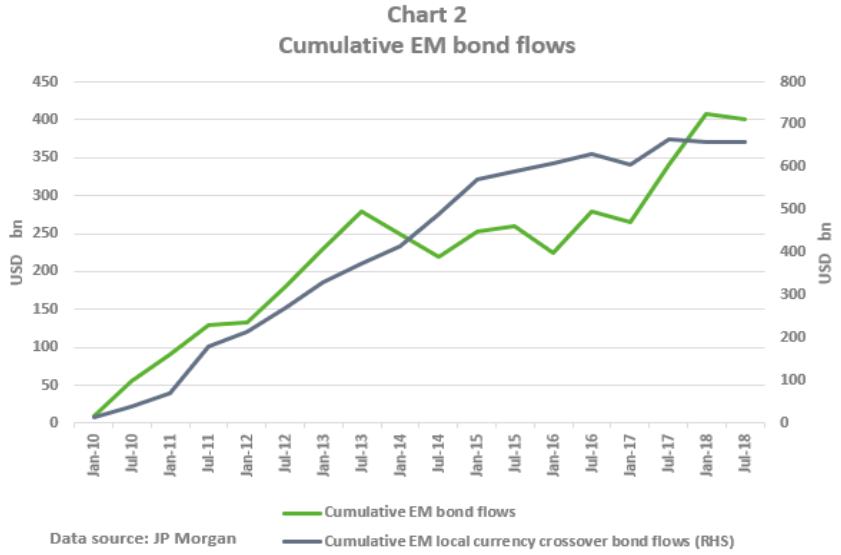
The outlook of EM markets, especially in the equity and the currency space, deteriorated again following July's brief relief rally. With Turkey's Lira, Argentina's Peso, India's Rupee and the Indonesian Rupiah seeing escalated depreciation pressure, more EM equity and currency investors have been forced to capitulate since the beginning of August.

Let alone the weakness of the MSCI EM equity index since August, merely the non-stop depreciation of quite a number of EM currencies in the same period is already scary enough to undermine the confidence of many investors in EM. Chart 1 shows that the JP Morgan EM Currency Index has already fallen below the crucial floor set in 2016. That means even those EM FX players who did successfully pick the bottom two years ago are already under the water if they are still holding on to their positions.



So far so bad. In our view, EM this time around in many aspects looks very close to the Asia markets during the 1997-1998 currency crisis. Somebody might argue that EMs now are in much better shape than Asia during 1997-1998 because so far their bonds have yet to see substantial outflows. Chart 2 shows that accumulated inflows to EM bonds are still staying at very high levels, which means EM bond positioning levels have not lightened meaningfully while equities and currencies are being sold off. That explains why most of the major EM bond indices (such as Bloomberg Barclay EM USD Bond Total Return, JP Morgan EMBI Global) lost no more than 6% year-to-date, versus as much as a 21% loss in MSCI EM Equity Index. Although somebody sees EM bonds as a stabiliser to the whole EM for now, we instead view it as a highly explosive time bomb. In our view, any large-scale capitulation of these bond investors will trigger an explosion of this time bomb, which in turn could spark an across-the-board bloodshed or even a meltdown of EM.



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Emerging Asia Insight: We Will See The Last Light In Q4 Before Darkness Comes - Cont'd…

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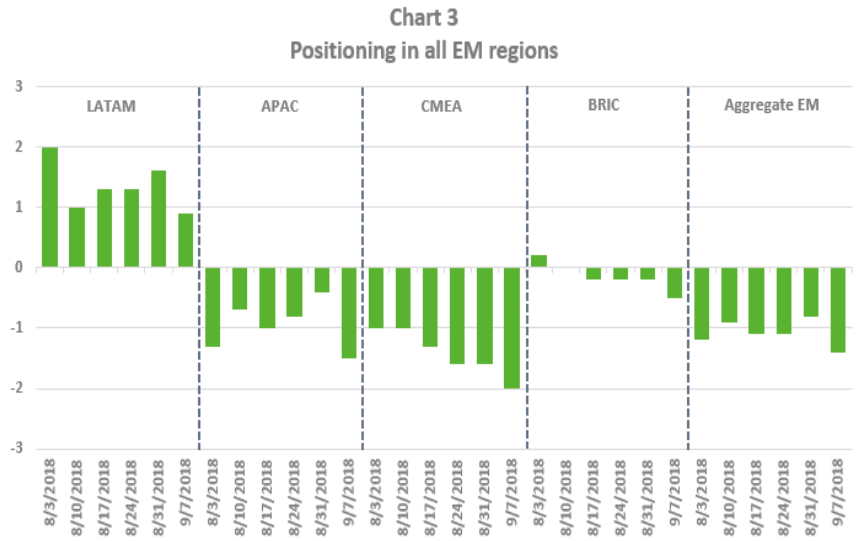
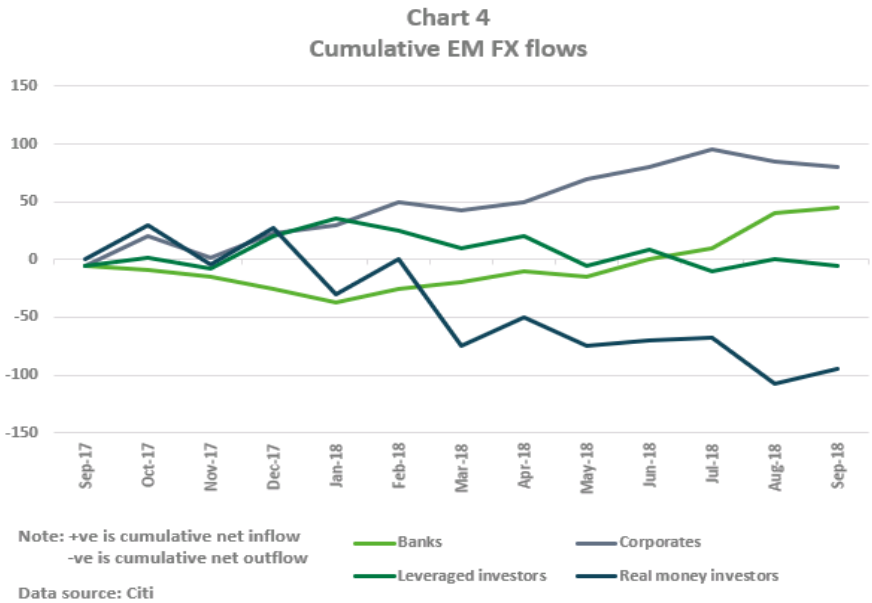
Pessimistic enough! However, before an across-the-board bloodshed occurs, there should be a decent rebound in equities and currencies (but not necessarily in bonds), which could last as long as 2 or even 3 months. Both the FX positioning outlook and real money investors' attitude give us a feeling that such a rebound will kick off as soon as this week or the one after. FX positioning data suggests except those in LATAM, the currencies in other EM zones have been deeply in short territory for quite some time (chart 3). Interestingly, real money investors who were the key driver of EM currency outflows in the first seven months of this year, somehow are starting to contribute inflows again (chart 4). Probably, the overall position of EM currencies is already short enough to encourage these people to buy rather than keep selling. If leveraged accounts follow suit, it is quite possible EM currencies will be performing better until November or even December. That, in our view, will likely lend support to the EM equities as well, which in fact are already pretty oversold.



Data source: Citi



Data source: Citi

The following pages are dedicated to Technical Analysis.

IGM's global team of Technical Analysts constantly look for interesting patterns in prevailing price action of a broad range of currency pairs, fixed income and commodity products.

We will highlight the most compelling on these pages.

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US 2 Year Yield – Upside Potential Seen To 2.831/2.998

Technical Analysis by Ed Blake

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- The yield has extended the long-term recovery via a 12-month rising channel to post new ten-year highs
- Constructive multi-timeframe studies suggest an initial extension within the channel towards 2.831
- Beyond opens clustered resistance at 2.997/2.998, perhaps the 3.072/3.114 zone on extension
- Any near-term corrective dips should hold over the 2.583/2.625 zone and only below damages for 2.449/2.491

STRATEGY SUMMARY

Buy dips in anticipation of an uptrend extension targeting 2.831 then 2.998. Place a protective stop under the 2.583/2.625 zone

Resistance Levels		
R5	3.333	14 December 2007 lower high, near 61.8% retrace of 5.275/0.143 fall at 3.315
R4	3.114	2008 peak – 13 June
R3	3.072	12-month rising channel resistance
R2	2.998	2.618 projection of 0.143/1.099 from 0.495, near 25 June 2008 lower high at 2.997
R1	2.831	24 July 2008 lower high
Support Levels		
S1	2.625	31 August/4 September 2018 lows, near 12-month rising channel support at 2.657
S2	2.583	20-22 August 2018 corrective low
S3	2.491	19 June 2018 low, near 28 June 2018 low at 2.492
S4	2.449	7 June 2018 low
S5	2.291	30 May 2018 higher low, near a former 18½ year falling trendline at 2.260

CHF/JPY – Bulls Look To The 2017/18 Highs

Technical Analysis by Andrew Dowdell

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- Marked out a major low at 108.52, just ahead of 61.8% of the 2016-17 advance at 108.34
- Momentum turning higher, with scope seen for a 118.56/61 re-test ahead of further targets at 119.32/120.57
- Bears need to breach this week's 113.90 low to derail the advance

STRATEGY SUMMARY

Scope is seen for a return to 118.56/61 followed by 120.57. Bears need to breach 113.90 to derail the advance

Resistance Levels		
R5	124.05	18 December 2015 high
R4	120.57	50% of January 2015 – June 2016 fall (139.14 – 102.00)
R3	119.32	29 January 2016 high
R2	118.61	10 July 2017 high, near the 2 February 2018 high at 118.56
R1	116.20	200-Week MA
Support Levels		
S1	115.30	30 August 2018 high, near the 7 September 2018 high at 115.10
S2	113.90	11 September 2018 low
S3	113.26	17 July 2018 high, near the 31 July 2018 high at 113.18
S4	112.09	9/14 August 2018 highs
S5	110.71	13 August 2018 low

CRB Raw Industrials Index – 19-Month Top Signals Risk To 462.88

Technical Analysis by Ed Blake

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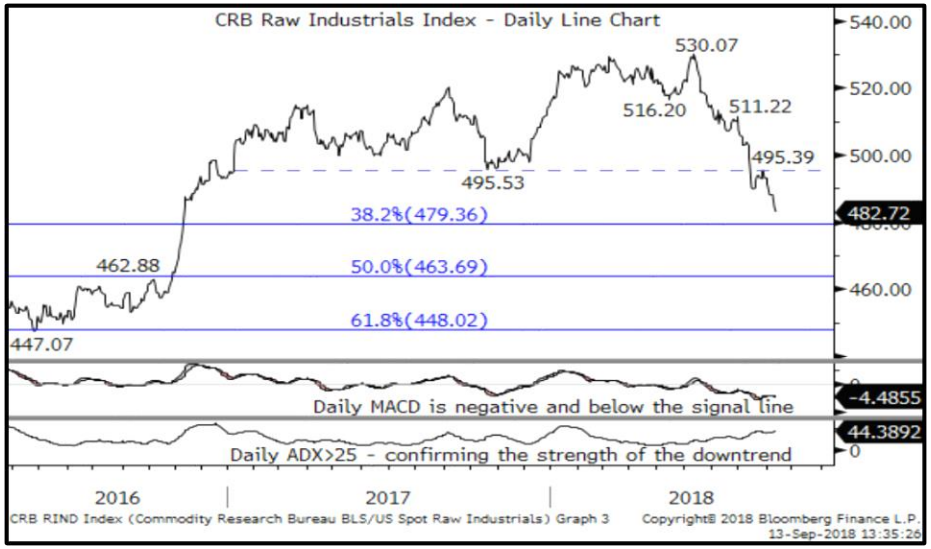
- The mid-August break under 495.53 (Oct 17 low) completed a 19-month top under 530.07 (12 June YTD high)
- Deteriorating daily-monthly studies suggest a downside extension targeting the 462.88/463.69 zone
- Sustained easing would then expose clustered support at 447.07/448.02
- Only a break above pivotal resistance at 495.39/495.53 would offer near-term relief towards 511.22/516.20



STRATEGY SUMMARY

Sell into any near-term rallies as we await a downside extension targeting 462.88/463.69. Place a stop above the former top trigger at 495.53

Resistance Levels		
R5	544.78	2014 peak – 29 April
R4	530.07	2018 peak – 12 June
R3	516.20	15 May 2018 former low
R2	511.22	31 July 2018 lower high
R1	495.53	20 October 2017 low (19-month top trigger), near 28 August 2018 lower high at 495.39
Support Levels		
S1	479.36	38.2% retracement of the 397.31-530.07 (2015-2018) rally
S2	462.88	5 October 2016 former high, near 50% retrace of the 397.31-530.07 rally at 463.69
S3	447.07	25 May 2016 higher low, near 61.8% retrace of the 397.31-530.07 rally at 448.02
S4	438.85	7 April 2016 minor higher low, near a 17-year rising trendline at 433.96
S5	428.64	76.4% retrace of the 397.31-530.07 rally

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