Fixed income weekly

FOR PROFESSIONAL INVESTORS

Just treats, no tricks

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by Satya Chakravarty
Investment Specialist, Absolute Return Fixed Income
satya.chakravarty@bnpparibas.com

Key takeaways

- The momentum behind tax cuts continues to build in the United States
- The House passed a budget resolution paving the way for tax law changes
- The structural reforms that China's President Xi has put into motion are critical to the country's growth in the coming years

Full commentary

While it increasingly seems like spooking this bull market will take some doing, politicians, central bankers, and economic data were in a benevolent state of mind in October. They all served up treats to the market, and the sugar high meant that risk assets globally experienced another excellent month of returns. The momentum behind tax cuts, if not tax reform, continues to build in the U.S. after the House passed a budget resolution that paves the way for tax law changes that could increase deficits by as much as $1.5 trillion over ten years. In Europe, the European Central Bank was clearly wary of any 'taper tantrum' type reaction, and after its policy meeting crafted a dovish messaging of a gentle taper. GDP data was robust in the U.S. and U.K., while the Catalan crisis could do little to impact economic sentiment in Spain, let alone the broader Eurozone region. Across Asia, a new era beckons China with President Xi wresting near-absolute control in the absence of a worthwhile successor, while Abenomics is here to stay after Prime Minister Shinzo Abe's resounding victory. Indeed, treats aplenty around the world, but as industry old-timers reminisced, with trepidation, the events on Black Monday exactly 30 years ago, it would be wise to keep an eye out for the odd trick that might be hidden amidst the candy.

Last week the House passed a budget resolution that included the Senate version of reconciliation instructions, paving the way for tax law changes that could increase the deficit over ten years by as much as $1.5 trillion. The vote in the House was relatively close, with a number of Republicans opposing the resolution. But the close tally is anything but a negative signal – a number of Republicans felt comfortable voting against the resolution only once its passage was secure, and then only voted "nay" to signal to the leadership that they will expect changes/concessions as the process moves forward.

In the US, Q3 GDP rose at a 3.0 percent saar in the first estimate, marking the first time since 2014 that the economy registered two consecutive quarters of growth at or above a 3 percent rate. Growth was fairly broad-based across major components – even net exports contributed with a 0.4 percent increase. But the headline number benefitted from a fairly sharp rise in inventories investment. In summary, the details of the report suggest an economy that continues to expand at a moderately above-trend pace, and we expect more of the same in Q4 2017. Recent core durable goods and shipments data indicate still-healthy levels of business investment, strong global demand could continue to support exports, while a tight labor market and rising household wealth will continue to underpin consumption.

This week's market developments

Tuesday, October 24

- France Manufacturing PMI Index decreased to 56.1 s.a. for October
- Germany Manufacturing PMI Index decreased to 60.5 s.a. for October
- Eurozone Manufacturing PMI Index increased to 58.6 s.a. for October
- US Manufacturing PMI Index increased to 54.5 s.a. for October

Wednesday, October 25

- Pan Germany Business Climate Index increased 116.7 for October
- UK GDP increased to 0.4% q.o.q. for September
- US Durable Goods New Orders Index increased to 2.2% m.o.m. for September

Thursday, October 26

- US wholesalers inventories decreased to 0.3% m.o.m. for September
- US initial jobless claims increased to 233k s.a. for October

Friday, October 27

- US GDP decreased to 3.0% s.a.a.r. for September
- University of Michigan Consumer Sentiment Index decreased to 100.7 m.o.m. for October

Source: Bloomberg, as of October 30, 2017

BNP PARIBAS ASSET MANAGEMENT

The asset manager for a changing world

China's President, XI Jinping, has cemented himself as the most dominant leader in the nation's history, since Mao. At the communist party's quinquennial meeting this month, the President's ideology was inducted into the Party's constitution, an honor previously reserved only for the legendary Mao Zedong. More importantly, the party did not name a successor for Xi, signaling that his reign could well continue beyond 2022. The structural reforms the President Xi has put into motion are critical to the country's growth in the coming years as its looks to transform itself in to a domestic consumer driven economy. Investor have for some time been concerned about China's manufacturing overcapacity coupled with debt-fueled growth, and they certainly hope that Xi's iron-clad grip will ensure some form of economic rebalancing, thereby preventing a market shock.

Next week's market developments

Monday, October 30

- Japan's unemployment rate is expected to remain at 2.8% s.a for September
- Japan industrial production is expected to decrease to -1.6% m.o.m for September

Tuesday, October 31

- France GDP is expected to remain at 0.5% q.o.q for Q3
- France CPI is expected to remain at 1.0% y.o.y for October
- Eurozone GDP is expected to increase to 2.4% s.a. y.o.y for Q3
- US Consumer Confidence is expected to increase to 121.2 s.a. for October

Wednesday, November 1

- Markit UK Manufacturing PMI Index is expected to remain at 55.9 s.a. for October
- Markit US Manufacturing PMI Index is expected to remain at 54.5 s.a. for October
- US Census Bureau construction spending is expected to decrease to -0.2% m.o.m s.a.a.r.

Thursday, November 2

- Markit Eurozone Manufacturing PMI Index is expected to remain at 58.6 s.a. for October
- Markit France Manufacturing PMI Index is expected to remain at 56.7 s.a. for October

Friday, November 3

- US Employees on Nonfarm Payrolls is expected to increase to 313k s.a. for October
- US unemployment rate is expected to remain at 4.2% s.a. for October

Source: Bloomberg, as of October 30, 2017

Central Bank watch

	Last move	Date of move	Current policy rate	Implied 3m rate on December 2017 interest rates futures contract	Next meeting
Fed	+25 basis points	June 14, 2017	1.00 % - 1.25 %	1.28 %	November 1, 2017
ECB	-5 basis points	March 10, 2016	0.00 %	-0.18 %	December 14, 2017
BoJ	-20 basis points	February 16, 2016	-0.10 % - 0.00%	0.07 %	October 31, 2017
BoE	-25 basis points	August 4, 2016	0.25 %	0.54 %	November 2, 2017

Source: Bloomberg