



# Julius Bär

1/3

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## CURRENCIES & MORE OUR INSIGHT INTO THE WORLD'S LARGEST MARKET

**Euro: The hype around Catalonia's potential secession is unjustified, in our view**  
**Pound: FX markets have started to price out some of the hawkish news in September**  
**Aussie: The RBA left its Cash Rate unchanged at 1½ percent, reiterates warning on FX**

### Euro: Pain in Spain?

Frankly put, the Catalanian Referendum was a non-event for us as it was illegal and therefore not binding. However, as we received so many questions, some explanations and market observations might be appropriate. Admittedly, Sunday's vote was exceptional due to the explosive mix of emotions and intensity that have inoculated Spanish politics.

### Madrid vs. Catalonia



Source: Tjeerd Royaards / Cartoon Movement

Government Spokesman Jordi Turull said at a press conference yesterday that 2 million Catalans backed independence out of 2.3 million votes cast in total. Catalan President Carles Puigdemont claimed that based on this outcome "the citizens of Catalonia have won the right to have an independent state." However, nearly 5½ million

were eligible to vote. So 3 million Catalans preferred to abstain. Puigdemont could argue that those who are absent are always wrong. Indeed, most of them would have voted No as polls showed ahead of the independence vote that only 40 percent of Catalans supported it. Therefore, with a turnout of just 42 percent, it suggests that most of those who opposed independence stayed at home. With the Referendum turnout so low, Catalonia lacks legitimacy for its push for independence. Even more importantly, the Spanish Magna Carta, like the majority of European constitutions, does not contemplate referendums on self-determination. The illegal Referendum stated that independence would be declared within 48 hours of a Yes vote. This seems impossible to us as Catalonia does not currently have the institutions that would be necessary to run an independent state. If the Catalan Government really declares independence, Spain could invoke the never-before used Article 155 of the Spanish Constitution which allows Spain to take over a regional government that is acting against the national interest. Given the huge costs for both sides of a secession, we believe the most likely outcome is that a compromise will be reached that grants Catalonia more fiscal autonomy. Spain's economy is currently in a strong position and the Government's finances are in a better state than they were during the financial crises. The market seems to share these thoughts with a relatively muted reaction yesterday. The IBEX35 declined around 1.8 percent – although banks suffered between 3 and 5 percent – and the spread of Spanish govies over Bunds increased by 10 basis points, going back to the difference we saw throughout August.

**Conclusion:** Despite the Yes-vote in the Independence Referendum in Catalonia, there appears to be little chance that the region will secede from Spain. The most likely outcome is that a compromise will be reached that grants Catalonia more autonomy.

**Pound: Back to reality**

Following the hype around a likely rate hike in November, the Pound is clearly losing momentum in the past few days. With ongoing below-consensus macro prints (for instance yesterday’s Manufacturing PMI) and downward revisions (such of Q2 GDP), FX markets are starting to price out some of the hawkish news in September. The Pound recovered a textbook-like 50 percent from the April to August decline but is likely to weaken again.

**€/£ is turning around**



Source: Bloomberg Finance L.P., Julius Bär

**Conclusion:** We are short the Pound vs. Euro for our trading book.

**QUICK NEWS HEADLINES (time in CEST)**

The following four headlines might have an impact on currency markets today:

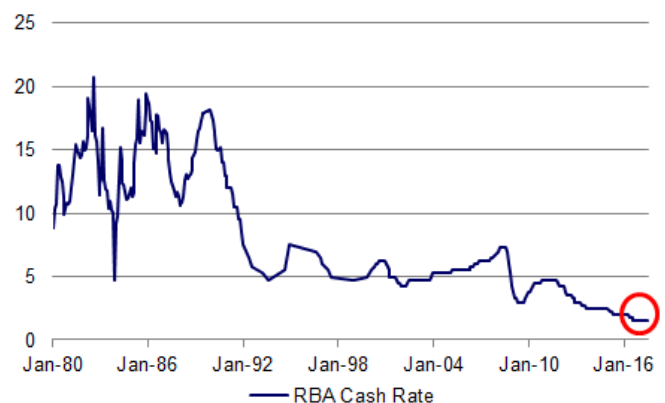
- Japan: The monetary base increased 15.6% in September y/y vs. 16.7% expected.
- Turkey: CPI is expected to have risen 11.1% in September y/y (09:00).
- Norway: The Manufacturing PMI is expected at 56.2 (09:00).
- Brazil: Industrial production is expected to have risen 5.0% in August y/y (14:00).

**Aussie: RBA on hold, neutral, warnings on FX**

The RBA left its Cash Rate unchanged at 1½ percent. By repeating at the end of the Statement released alongside today’s decision that “the Board judged that holding the stance of monetary policy unchanged at this meeting would be consistent with sustainable growth in the economy and achieving the inflation target over time”, the RBA maintained its neutral bias on the outlook in the coming months. Their assessment on the labor market is mixed.

On one side they note that “employment has continued to grow strongly over recent months”, on the other side the Statement says “wage growth remains low”. Finally, the RBA repeats its warning against a still too high Aussie: “The higher exchange rate is expected to contribute to continued subdued price pressures in the economy.” OIS futures indicate that an interest-rate hike is expected in mid-2018 at the earliest.

**The RBA’s Cash Rate since 1980**



Source: Bloomberg Finance L.P., Julius Bär

**Conclusion:** We stick to our bearish view on the Aussie (see also our 22 August edition).

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