

The FX Trader Pressure on Euro eases for the moment at least

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Summary: The pressure on French sovereign debt peaked Friday and the pressure on the euro may have peaked on Monday temporarily, but the underlying issues have by no means yet been banished and will likely return again at some point down the road. Elsewhere, the US dollar peaked and rolled over slightly, even as US long-dated treasury yields hit new modern highs.

Euro pushed to new lows, but French bonds stabilize.

The pressure on France's sovereign debt saw a climax (for now) on Friday as the spread of French 10yr OATs to the German 10yr Bunds widened to a peak of 159 basis points before easing back lower to where it started the day closer to 140 basis points. At one point Friday, France's 10-year yield just missed the round 5% level, trading to a high of 4.995%. On Monday, the spread widened to 150 basis points before dropping back to below 140 basis points by late in the day and the pressure on the euro likewise peaked and retreated Monday. It's worth noting that the spike unfolded on the days ahead of and the actual day of the unveiling of the government's proposed 2027 budget Thursday. Will the systemic stress on French debt tame the National Assembly into passing this budget? Let's recall the budget drama last year, when the National Assembly played a game of chicken with Macron, with left-leaning parties threatening a no confidence vote until the budget was altered to suspend pension reforms. With this year's budget, the cuts are not trivial at an estimated EUR 54 billion, but debt servicing costs have risen so sharply that there is hardly any fiscal impact – an estimated fall of only 0.4% in the size of the deficit to a still too large 5%.

The ECB could in theory weigh in at any time if stress levels cross some unknown pain threshold, but the ECB's official "Transmission Protection Instrument (TPI)" for ensuring that no Eurozone member is suffering an unfair lack of monetary policy transmission isn't applicable as it excludes situations where debt stress is caused by large deficits and the country is not doing enough to address the situation. The political costs of a bailout would also weigh. Still, let's note that while the US Fed has begun modest balance sheet expansion and the ECB is still doing passive QT (not reinvesting maturing pandemic-era PEPP purchases), there are measures that could come into play.

Yesterday, Spain's embattled Prime Minister Sanchez called for snap elections after a plan to address housing costs failed. Spain's yields rose on the day, but the Spanish debt situation is nothing like it was during the sovereign debt crisis of 15 years ago, with only a 35 basis point premium in the case of the Spain-Germany 10-year yield spread.

Takeaway: The France and overall Eurozone sovereign debt issue will continue to lurk in the background even if things have calmed for the moment. One likely coincident indicator and stressor to keep an eye on is the direction of US Treasury yields, as new highs in US yields directly impact global funding costs. The next steps are the actual approval of a French budget, with the next steps starting later this week. Further ahead, the presidential election first round in April is the really critical structural event risk depending on who emerges to face (most likely) Le Pen in a run-off. Macron can't run again after having served two terms. The euro weakness looks stretched in the short term as long as we don't see fresh

signs of stress in French debt markets.

Chart focus: EURUSD EURUSD briefly broke down through the key range level near 1.1200 to start the week, an area that still looks important in the bigger picture, with a large zone of possible range to accommodate consolidation back toward 1.1325-1.1400 before any concern mounts that the chart risks a bullish reversal. Further to the downside are the next Fibo level in the low 1.11's followed by the 1.1000 psychological level and then the ultimate 61.8% Fibo retracement of the move off the 2025 lows near 1.0880.

US September ISM services and US September jobs report It was already established ahead of Friday's US September jobs report that the key focus for Fed policy now is on inflation and that we won't get a look at the next official US CPI inflation print until next Wednesday the 14th. But labor market data isn't unimportant and Friday's numbers had something for everyone. The headline nonfarm payrolls change number was far weaker than expected at +29k vs. +90k expected and the data of the two prior months was revised -60k lower, which isn't a good look, but it is well established that we are in a low hire, low fire environment and that this survey's quality has declined since the pandemic. Other data were a mixed bag, with the Unemployment Rate ticking up (bad news), but the Participation rate ticking up a solid 0.2% (good news). Very bad news for earnings and purchasing power, however, as the September Average Hourly Earnings. The ISM Services was in line with a solid expansionary reading of 54.9, a slight dip from August, but the employment sub-index rose to 50.1 from 47.8 in August and New Orders were a strong 59.8.

Looking ahead The focus remains very much on global sovereign debt markets after the long end of the US yield curve hit new highs since 2002 and posted its highest daily close since then on Monday. Higher global yields make things tougher for Japan's effort to strengthen its currency and as noted above are a stressor for Eurozone sovereign debt stability as well. Bank of Japan governor Ueda is out speaking in Tokyo today. It is his first appearance in a while and could see the latest attempt at impressing the market with resolve, although the finance ministry is generally more hawkish on the yen level. There is very little in the way of macro data from the US until the September CPI report next Wednesday, with the FOMC minutes up late tomorrow.

FX Board of G10 and CNH trend evolution and strength. Note: If unfamiliar with the FX board, please see a video tutorial for understanding and using the FX Board.

The euro has joined the kiwi and the Swedish krona in the basement of the G10, while USD strength remains the theme, even if some steam has come out here in the nearest term. A move of this size takes considerable energy to reverse, so we are in a strong USD regime until proven otherwise.

Table: NEW FX Board Trend Scoreboard for individual pairs. Euro pairs have tipped over into new bearish trends in line with the negative focus on EU sovereign debt markets. Can EURSEK join the crowd? Elsewhere, gold and silver remain in bear mode as real yields weigh, and JPY pairs risk backing up and disappointing the JPY bulls if these yields continue to rise.

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