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US housing slowdown unlikely to last

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US Macro: Housing data cools, but likely temporary – Although housing data is volatile, the first string of home building data in August was softer than expected. Home starts declined by 5.8% from a downwardly revised 1.4% in July. This report suggests that there could be some payback from somewhat stronger housing starts the previous two months, which on average grew by 3.7%. Meanwhile housing permits also decreased by -0.4% in August from a downwardly revised -0.8% the previous month. However, we think the slowdown is likely to prove temporary. Indeed, a separate report, home builder's sentiment rose to an 11-month high in September rising to 65 from 59 in August. Sentiment was likely influenced by increasing home sales, particularly during the summer. We expect residential investment to continue to make a positive contribution to growth in the coming quarters, given that housing affordability remains at high levels, while the labour market remains strong. These factors should continue to spur home demand. In the past four quarters, residential investment has contributed on average by around 0.2ppts to quarterly GDP growth. (Maritza Cabezas)

Euro Government Bonds: Dutch budget remains focused on deficit reduction – The Dutch budget for 2017 was published on Tuesday. Financial windfalls have created room for the reversal of some of the earlier austerity measures and for supporting purchasing power. However, the total giveaway is modest (at 0.4% GDP) and the deficit should nonetheless drop sharply in the coming years, which will most likely lead to a lower borrowing requirement. Indeed, the government finances are among the healthiest of the big eurozone countries. This means that the DSTA is likely to issue at the lower end of its 2016 bond issuance target. In Q4, we expect the DSTA to announce two additional auctions of the 10y benchmark. This is the final budget by the current government. The fragmented political landscape will probably complicate the drafting of the 2018 budget following the March 2017 General Election. We expect the Dutch 10 year yield spread to remain stable until the end of the year. ECB purchases and the healthy public finance situation are positives. However, political risk – both in the Netherlands as well as in a number of other member states – could be a factor restraining further spread compression. For more please see our note Euro Watch – Dutch Budget: Focus still on deficit reduction (Aline Schuiling, Kim Liu & Nico Klene)

Global FX: Sterling still at risk of a short squeeze - This week the monetary policy decisions of the Fed and the BoJ are fully in focus. What often happens in such an environment is that financial markets freeze. There is a tendency among investors to wait until the decisions have been communicated. However, investors have not sat still in the sterling market. Over recent days sterling has come under pressure as investors are more concerned about the impact of Brexit on the economy. GBP/USD has been on its way to the low set on August 15 just below 1.29, while EUR/GBP has rallied towards the peak at 0.8685. The process of Brexit will take a long time and from time to time currency markets will focus on this even if there is no new information. A major risk for sterling remains the financing of the substantial current account deficit, which is close to 7% of GDP. However, speculators are very largely positioned for sterling weakness. We think that most of the negative news is reflected in sterling. In addition, financial markets still partly (for 30%) anticipate a BoE rate cut (not our base view anymore). All-in-all, it is difficult to fight the predominant negative sentiment. However, as we noted in yesterday's daily, if events or data remain relatively benign in the near term, then an aggressive short squeeze will occur. In other words, being short sterling at current levels implies a considerable risk. (Georgette Boele)