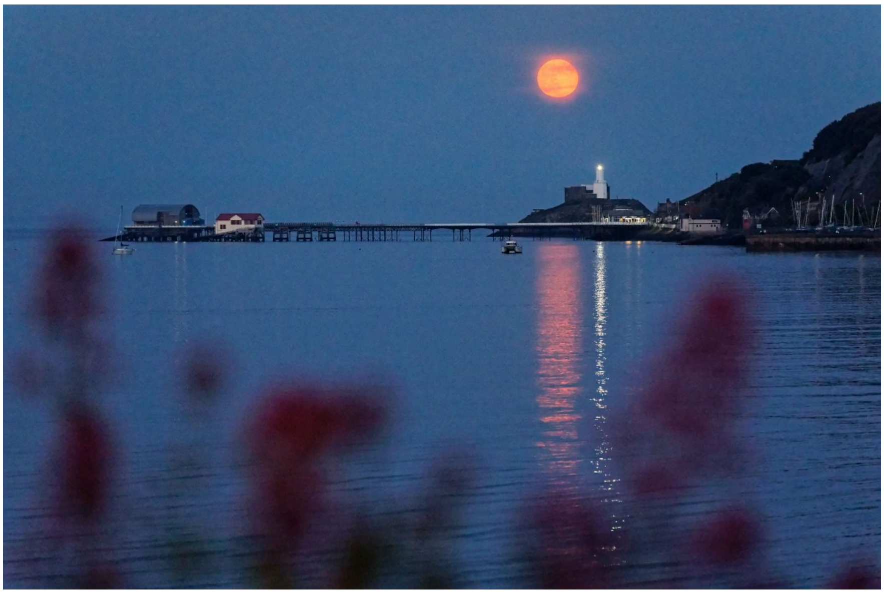
G10 FX Week Ahead: To the Moon

In a week which will see the year's first Super Moon and Elon Musk discussing moon colonisation plans, US activity data should also show a fast ascent, with the first look at 1Q21 GDP. It's too early to expect the Federal Reserve to rein that growth in, but overall we do still favour a soft USD backdrop on the global recovery story



USD: Strong growth, dovish Fed and proposed tax hikes – a bearish $ cocktail

	Spot	Week ahead bias	Range next week	1 month target
DXY	91.0430	Mildly Bearish	90.2000 - 91.5000	90.0000

- The DXY is well on its way to retracing two thirds of this year's rally and we think it can fall further. The week ahead is a very busy one on the US data calendar. It should encompass what should be very strong 1Q21 US GDP growth (perhaps as high as 7% quarter-on-quarter annualised), but a Fed still positioned very dovishly at Wednesday's FOMC meeting. Wednesday will also see Joe Biden's first speech to a joint session of Congress, where we might hear more about his plans to raise taxes, including a doubling of the capital gains tax for those earning over $1mn p.a.
- It is a also a big week for 1Q tech earnings – a sector perhaps most exposed to a capital gains tax hike after enjoying stellar equity returns over the last year. On balance, we think the dollar can continue to edge lower – especially were speculation over tax hikes to take some steam out of the US over-heating debate in 2Q. We will also see second tier US data in the form of March DGOs, April consumer confidence and the March core PCE deflator – expected to jump to 1.8% year-on-year from 1.4%. Month end portfolio re-balancing flows may also move against the dollar this week since both US equity and bond benchmarks have outperformed in April.

EUR: Fending off a technical recession

	Spot	Week ahead bias	Range next week	1 month target
EUR/USD	1.2055	Mildly Bullish	1.1980 - 1.2150	1.2200

- The week ahead sees the first look at eurozone 1Q21 GDP. This is widely expected to contract and signal a second technical recession within a year. This is all old news, however. Instead, eurozone confidence is picking up sharply as evidenced in Friday's flash April PMI releases and should be echoed in Monday's German Ifo readings. We'll also get our first look at April eurozone inflation – expected to jump to 1.6% YoY from 1.3% on base effects. The rise in inflation should shed a little more light on the European Central Bank debate ahead of the June meeting, where the hawks will want to see tapering of the more aggressive weekly PEPP purchases. Indeed, there were moments over the last week where the EUR rates markets were getting excited about tighter ECB policy.
- We'll also see a whole array of ECB speakers over the next week and we would expect more focus on EU national spending plans now that the Karlsruhe constitutional court has allowed the ratification of the EU fiscal stimulus plan to proceed. Also keep a look out for any fresh German opinion polls, where we think any further gains for the Greens will be treated as a EUR positive.

JPY: No fireworks expected from the BoJ on Tuesday

	Spot	Week ahead bias	Range next week	1 month target
USD/JPY	108.01	Neutral	107.20 - 108.40	108.00

- USD/JPY downside has surprisingly picked up steam, even though the decline in US yields has stabilised and global equity markets remain not too far from their highs. It is really hard to make sense of USD/JPY at the moment. The week ahead sees a focus on Tuesday's Bank of Japan meeting – the first since its strategy change to more flexible asset purchases. In reality, the decline in global yields and JGB yields means the BoJ has not had to be too active here. The BoJ meeting will also see the release of its outlook report and a possible upward revision to growth forecasts despite Japan's current battle with Covid.
- As an aside, the BoJ in conjunction with other central banks on Friday agreed to discontinue the 84-day dollar swap with the Fed. A welcome recognition that USD funding markets have returned to normal.

GBP: A break above 1.4000 is within reach

	Spot	Week ahead bias	Range next week	1 month target
GBP/USD	1.3855	Mildly Bullish	1.3790 - 1.4030	1.4100

- This week's data-flow out of the UK was once again supportive for sterling, as strong retail sales, good PMIs, inflation rising (although slightly below expectations) and unemployment edging lower all endorsed the strong recovery narrative in the country. The data calendar next week is, instead, very quiet, and no Bank of England officials are scheduled to speak. With Covid-19 cases rising again across the world and the UK having recently relaxed containment measures, incoming contagion/hospitalisation data in the UK will be key to test the effectiveness of the country's vaccination programme, and ultimately drive expectations about the economic recovery.
- From a technical perspective, sterling still scores as undervalued against the dollar, suggesting GBP/USD should be able to break above 1.4000 (after failing to do so this week) in the coming days without excessive resistance, especially if our bearish view ahead of the FOMC meeting on Wednesday proves correct (see our USD section above for details).

AUD: Aussie-China tensions back on the radar

	Spot	Week ahead bias	Range next week	1 month target
AUD/USD	0.7732	Mildly Bullish	0.7670 - 0.7830	0.7800

- China-Australian relations are back in focus, and it is once again no good news for the Aussie dollar. The decision by the Australian government to scrap the Belt and Road Initiative (that would have allowed increased presence of Chinese companies in Victoria's infrastructure projects) is another worrying signal that the diplomatic and trade relationships between the two countries are set to stay fragile. The main risk for AUD is that China retaliates in the coming days by hitting Australian exports again. A new lockdown in Perth on the back of rising virus numbers may also cause some short-term headwinds.
- At the same time, there are a few factors offering support to the currency: iron ore prices have remained supported after a long rally and regardless of crude's ups and downs, USD has been under pressure and China's data flow has been broadly supportive so far. On the latter, Friday's PMIs out of China may drive a reaction in the China-sensitive currencies. Earlier in the week, Australia's CPI for 1Q will be in focus: consensus expectations are for headline inflation to climb to 1.4% from 0.9%. The bar set by the Reserve Bank of Australia with its inflation target is high (2.5%), but any signs of inflation recovering more than expected may cast some doubt on how long the RBA's ultra-dovish tone can reasonably last. All in all, supported risk appetite and an unsupported USD should allow AUD/USD to keep moving higher (also thanks to short-term undervaluation), but there are non-negligible short-term risks, so caution is warranted.

NZD: Room for consolidation

	Spot	Week ahead bias	Range next week	1 month target
NZD/USD	0.7174	Mildly Bullish	0.7140 - 0.7270	0.7300

- We were not surprised to see the Kiwi dollar outperform the likes of the Canadian and Australian dollars, considering a much smaller incidence of idiosyncratic risks in New Zealand compared to Australia (China tensions) or Canada (Covid-19 emergency). Incidentally, NZD had already faced an extensive trimming of speculative longs (here's our latest FX positioning note), and a rise in inflation (albeit in line with consensus) to 1.5% is set to put some pressure on the central bank to sound less dovish.
- Data-wise, the week ahead will be very quiet in New Zealand, with only trade data for March in focus: exports are expected to have risen, likely providing encouraging signals for the recovery. External factors should, however, dominate for NZD in the coming days, with a possible spillover from China-Australia tensions and China's PMIs in focus. But, as highlighted for AUD above, we expect commodity currencies to stay supported next week and the USD to stay pressured, so NZD/USD may consolidate above the 0.7200 mark.

CAD: BoC is a medium-term positive, but the short-term remains uncertain

	Spot	Week ahead bias	Range next week	1 month target
USD/CAD	1.2490	Neutral	1.2400 - 1.2550	1.2500

- Expectations that the Bank of Canada meeting this week would be an important one were not wrong, as Governor Tiff Macklem announced a (much anticipated) C$1bn per week cut of asset purchases, and (surprisingly) changed the forward guidance to keep rates low from 2021 to 2H22. That was largely due to a set of more upbeat economic projections that now see inflation moving sustainably back to target in the second half of next year. As discussed in our meeting review "Canada: Hawkish BoC to lead the tightening charge?", the BoC has set itself up as a leading voice in the tightening cycle for developed central banks: in the medium term, we expect this to provide support to CAD, and we expect USD/CAD to touch 1.20 by the end of the year.
- However, the short-term outlook for CAD remains strictly tied to the Covid-19 emergency in Canada, with many parts of the country still reaching new contagion peaks. The good news is that Canada has continued to step up its mass vaccination programme, which may help the country emerge from the current health crisis earlier. Another major driver of CAD, oil, has had a grim week and with virus cases rising in all of the world's regions except Europe, a strong rebound in crude may not be in the cards for a little longer. More pressure might come from the OPEC+ meeting on Wednesday if plans to add about 2m b/d of output from May to July find some consensus among members. CAD may still struggle to keep up with other commodity currencies next week. On the data calendar, Canada's February retail sales and GDP will be watched, but may have limited market impact considering the third virus wave and the BoC policy decision.

CHF: SNB's Jordan speaks on Friday

	Spot	Week ahead bias	Range next week	1 month target
EUR/CHF	1.1043	Mildly Bullish	1.1010 - 1.1100	1.1100

- EUR/CHF has been trading in narrow ranges recently, but pressure should be building for an upside break-out. The European story is improving and our core view is that precautionary CHF longs acquired during Trump's trade war can be offloaded. Better domestic news from Switzerland, in the form of another strong April KOF leading indicator, should also support this benign environment. And look out for a speech by Swiss National Bank President Thomas Jordan on Friday, addressing the SNB's annual general meeting.
- As we've been discussing over recent weeks, the Polish CHF mortgage story (circa CHF25bn in CHF mortgages still outstanding) still hangs over EUR/CHF as Polish banks await a local constitutional court ruling on 11 May. This story may hold EUR/CHF in check until mid-May.

NOK: Oscillating around the 10.00 psychological level

	Spot	Week ahead bias	Range next week	1 month target
EUR/NOK	10.0300	Mildly Bearish ↘	9.9200 - 10.0800	10.0000

- The krone weathered a week full of headwinds for oil prices relatively well, gaining around half a percent against the underperforming dollar and closing only marginally weaker against the outperforming euro. A break below the psychological 10.00 level in EUR/NOK was quickly reversed: another attempt at the level will be reliant on the performance of oil, which is facing the double threat of rising Covid-19 cases and variants worldwide and discussion around another possible output hike by OPEC+ (as discussed in the CAD section above).
- At the same time, supported risk appetite (which we expect heading into the Fed meeting) normally benefits the higher-beta NOK more than the EUR, so there may be some downside for EUR/NOK in the coming days even if oil prices struggle to recover. On the domestic side, March retail sales and April unemployment in Norway should have very limited market impact.

SEK: Another very quiet meeting by the Riksbank

	Spot	Week ahead bias	Range next week	1 month target
EUR/SEK	10.1400	Mildly Bearish ↘	10.0600 - 10.1800	10.0000

- The highlight of the week for Sweden's krona will be the Riksbank’s policy announcement on Tuesday. However, we expect it to be a rather uneventful meeting, with rates and the overall policy stance likely to remain unchanged. Despite mounting Covid-19 cases, the data-flow has been a little better than hoped in Sweden. Inflation is also poised to rise this year, though with little pressure from wages, there's not much to suggest price pressures will endure. We'd therefore expect the Riksbank to continue a flat rate profile for some time to come.
- In terms of FX implications, the impact on SEK should be marginal and short-lived. Other data in the week ahead include Sweden March retail sales and the Economic Tendency Index for April. However, recovery hopes for the eurozone rather than domestic factors are set to remain a key factor for the highly correlated SEK. We still expect EUR/SEK to break below 10.00 by the end of 2Q.

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