Bid on Brazil's Bolsonaro

The Brazilian real, which has now rallied nearly 14% since its low against the dollar in mid-September, has been pushing to new highs following the result of the presidential election

BRL: Bolsonaro's honeymoon begins, AMLO's ends.

Jair Bolsonaro was elected as the next President of Brazil on Sunday, running on an anti-corruption law and order ticket. Financial markets have rewarded the result with new highs in the Brazilian real, which has now rallied nearly 14% since its low against the dollar in mid-September. Our Chief Latam economist, Gustavo Rangel, thinks that the BRL should stay supported for a few months, (USD/BRL potentially making it to the 3.50 area) as Bolsonaro talks positively about social security and tax reforms, plus privatisation. However, it still looks quite a challenge to get these reforms through Congress and Gustavo thinks the current honeymoon may only last until late 1Q 2019. And on the subject on privatisation, Mexicans at the weekend voted overwhelmingly in a referendum to scrap a new $13 billion international airport. This news will not be greeted well by international investors, where complex FDI projects now become beholden to international referenda. The Mexican peso is an expensive sell but US markets could push USD/MXN through 19.70 to the 20.00 area.

USD: Investors continue to back the dollar

There seems little short-term catalyst for investors to move away from overweight positions in the high-yielding dollar. The geopolitical challenges faced currently by Asia and Europe are a far cry from the re-ratings stories those blocs saw last summer and which had contributed to the 2H17 benign decline in the dollar. Keeping the dollar bid this week should be a continuation of strong US data, culminating in a set of firm wage data in Friday's nonfarm payroll report. At the same time we will be watching developments in China, where USD/CNH is creeping ever closer to the psychological 7.00 handle. Were that to break, we would expect USD/Asia, and probably USD/emerging markets in general, to take another leg higher and the dollar to be bid across the board. For today, a strong set of personal income and price data should be positive for the dollar and could see the US dollar index retesting the highs for the year at 97.00.

EUR: Undervaluation is probably the only thing going for it

Another poor showing of the German government in a regional election (Hesse), where the CDU and the SPD both lost 10% of their support, raises further fears over the future of the Grand Coalition. Add in Italy's unresolved budget issues and low/negative yields across the region and you can see why, if international equity investors were desperate to rotate out of US equities, any investments into the eurozone would be FX-hedged. Probably one of the few supports to the euro right now is its low level, where European corporates might be tempted to sell expected USD receivables two years forward under 1.22 now.

GBP: No fireworks from the budget

We doubt today's budget will move the pound much - please see our FX Week Ahead.

Author

Chris Turner
Global Head of Markets and Regional Head of Research for UK & CEE
chris.turner@ing.com