

Daily FX Strategy: Solid US data to signal only modest easing

US retail sales should be stronger while industrial production should post a modest increase, suggesting that aggressive monetary easing by the Fed is unnecessary. This should support the dollar today, especially against low yielders like the euro and yen



USD: Solid US data to confirm case for only a modest easing cycle

The expected solid US activity data today should confirm our view that a 25 basis point Fed rate cut in July (rather than 50bp) should be sufficient as a first insurance move to offset the negative effect of trade wars. US retail sales should be stronger, especially when the volatile auto and gasoline components are removed, while industrial production should post a modest increase given the fact that the ISM remains in growth territory. This is consistent with the idea that US

personal spending should grow around 4% in the second quarter – an environment which should not warrant material monetary easing. This suggests support for the dollar today, particularly against the low yielders such as EUR and JPY as (a) market expectations of an aggressive Fed easing cycle will be further tamed and (b) the sufficiently high interest rate differential will remain supportive for the dollar.

↓ EUR: German data unlikely to provide respite for the euro

The German ZEW survey for July is expected to decline, reflecting softness in the German economy and the general case for ECB easing in forthcoming months. We look for an ECB deposit rate cut by September at the latest. The expected decline in the ZEW today, coupled with solid US data, points to a lower EUR/USD today, with the cross retracing back towards the 1.1200 level.

→ GBP: Solid labour market report to have shallow effect on sterling

While UK May wage growth will likely reach the post-crisis high of 3.5%, this should not change the current market pricing of a partial interest rate cut over the course of the next 12 months, given Brexit uncertainty and generally deteriorating UK data- be it the forward looking PMIs or real indicators such as retail sales or the expected soft 2Q GDP. This suggests fairly limited and shallow upside to GBP from the expected solid labour market report today. EUR/GBP to remain around the 0.9000 level.

↑ NZD: Matching the US dollar today

The New Zealand dollar has been the top performing G10 currency overnight as 2Q core inflation accelerated by 1.7% year-on-year (vs 1.5% previously), in line with market expectations. For today, this is positive for the NZD as it should keep local rates supportive, partly offsetting the expected stronger US dollar dynamics coming from the US data later today.