

EUR: Cruising for a bruising

Global FX markets have started the week taking their cue from weekend events in China again, but we think the rest of the week will be about US third-quarter GDP, the Italian budget and the October ECB meeting



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➔ USD: Tale of two tax cuts... US-China trade war forces defensive local policies

Chinese equity markets surged higher after Beijing announced a more proactive fiscal stance – with pledged tax cuts worth around 1% of GDP. It may be an opportune time for authorities to take steps to buffer the economy – with the US-China trade war on pause and President Trump's attention focused on fighting battles at home ahead of the crucial midterm elections. Indeed, the POTUS himself announced that a win for the GOP could see another round of US tax cuts – though one would immediately question where the White House can find the fiscal space to achieve this (given that the US budget deficit is already ballooning after the 2017 TCJA stimulus).

As our economists note, the US data highlight will be 3Q GDP – with another strong outcome looking likely. We look for US growth to come in at an annualised 3.6% QoQ (consensus: 3.2%). This is set to keep US rates firm and the market continuing to guess where the top is for the Fed Funds cycle. Higher US rates are also making hedging USD forward exceptionally expensive for European

corporates and is probably seeing lower USD hedge ratios than would otherwise have been the case. A positive week for global equities could see high-beta EM FX recoup more of their summer losses.

⬇️ EUR: S&P Italy downgrade and a dovish ECB meeting may add significant pain

The week ahead will be about the Italian budget and the October ECB meeting. On the former, expect further dialogue between Brussels and Rome through the week – although it seems unlikely Italian politicians are prepared to back down from manifesto pledges.

As our [Rates Strategy team note](#), it's not a done deal that S&P on Friday will follow the Moody's example and downgrade Italy to one notch above junk (having upgraded the sovereign one year ago). If the rating agency just switches the outlook to 'negative', the 10Y BTP/Bund spread could fall back to 250bp. If S&P mimics Moody's decision, though, and the stand-off between Rome and Brussels is unresolved spreads could struggle to fall (much) below 300bp.

On the ECB, our team think the press conference could be a little more dovish, but not alter the core view that QE is ending in December. And in fact, we're more worried by signs that the US-EU trade detente is coming to an end; US tariffs on European car imports is certainly not priced into the EUR, and any indication that President Trump is losing patience with the EU is likely to be greeted poorly. We look for a bearish EUR/USD week with a fall to 1.13 possible.

➡️ CAD & SEK: Hawkish central bank steps will provide limited sustained FX uplift

The Bank of Canada meeting this Wednesday is one of the G10 central bank events of the week – and Canadian officials are set to continue their gradual tightening path and provide a 25bp rate hike. A follow-through of a hike should give the loonie a knee-jerk boost. However, with a 100bp of tightening already priced in over a 2-year horizon, we think there's limited scope for a sustained rally in CAD – unless the BoC send an ultra-hawkish signal. This seems highly unlikely given the wider global market fragilities.

Elsewhere, we aren't looking for any change from the Riksbank during Wednesday's meeting (neither in the level of interest rates nor the forward guidance) – with the central bank confirming its intention to hike rates in either Dec or Feb. EUR/SEK could move below 10.30 on a hawkish signal.