

FX: Brutal quarter for emerging markets so far

The Russian ruble, Argentine peso and Turkish lira have fallen sharply against the dollar this quarter. Will the slump continue?



USD: Dollar holding strong, focus on Trump's Iran decision at 20CET

Broad dollar strength has delivered a brutal 2Q18 for emerging markets so far. The Russian ruble, Argentine peso and Turkish lira lead the pack with 7-9% losses against the dollar this quarter, followed closely by Mexico and Brazil. While we can blame all these moves on local (largely political) stories, it has been higher US rates and the strong dollar which have been the catalyst for losses. However, we are not looking for a major US dollar advance from these levels unless there is clear evidence the Federal Reserve is behind the curve and needs to hike more aggressively. On that story, we'll hear from Fed Chair Jerome Powell in Switzerland at 0915CET today and then see US PPI and CPI data on Wednesday and Thursday, respectively. Also today, look out for President Trump's decision on the Iran deal at 20CET. With hawks having recently joined his foreign policy team, investors believe he'll probably pull out of the deal (or at least threaten it) and demand a renegotiation. It's hard to rule out further upside in crude prices (450k barrels per day of Iranian production could be kept off the market) and we suspect USD/JPY would trade lower. DXY to trade 92-93.

EUR: German IP provides signs of life in the Eurozone recovery

We've been saying that a lot of the dollar outperformance over recent weeks has been driven by US outperformance of both growth and rates. Yet we doubt this divergence with the Rest of the World will last. Encouragingly, German industrial production has bounced back in March, suggesting February's weakness was strike/weather-related. We're not big fans of this EUR/USD correction extending to the 1.17 area - but will need to see more encouraging data from the Eurozone, and also the Fed credibly arguing that every tick higher in US inflation will not trigger an automatic policy response. We see EUR/USD in a 1.1880-1.2000 range near-term, but this is not a high conviction view.

GBP: More focus on the House of Lords

The government faces more diffidence from the upper house today, which seeks to amend Brexit legislation. EUR/GBP looks steady near 0.88, however.

SEK: Forecast change

Last Friday, our team released a new set of EUR/SEK forecasts which see a window for EUR/SEK to push towards 11.00 later this year. Despite remarks from the Riksbank on Friday that it may be taking a greater degree of interest in the Swedish krona decline, our team think that the bar is very high for the Riksbank to respond to SEK weakness with rate hikes. We calculate that even with EUR/SEK at 11.50, core inflation would remain within the Riksbank's 2% +/- 1% target. We no longer look for the Riksbank to hike this year and expect it to delay tightening to fall in step with the first ECB hike - probably summer 2019. Look out for a speech from Riksbank Dep Gov Thomas Jansson at 1030CET today.

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