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Article

FX: Chasing crude stories

Higher crude prices, thawing US-China relations and a re-steepening of the US yield curve could give investors a reason to put cash to work after a shaky start to the new year

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USD: Higher oil prices and US rates can see USD/JPY reclaim losses

On paper, 2019 is stacking up as a bad year for risk assets. Slowing world trade growth, late cycle economies and rising geopolitical risk all point to caution. However, investors' cash levels were reasonably high heading into year-end and a lot of emerging market risk assets were already trading with deep discounts. We prefer to think investors will be looking for opportunities right now. Some (at least short term) themes may be: (i) higher crude prices, (ii) thawing US-China relations and (iii) a re-steepening of the US yield curve. On the first, we think the Saudis may be limiting oil exports to the US to generate some big falls in the weekly US DoE oil inventory data. 1630CET today could see a much sharper decline in inventories than the 1.7mn barrels consensus expects. On the second point, the mood music on US-China trade has improved and it should be a good day for equities. And both of those two factors could contribute to a steeper US yield curve, with the Fed pause keeping the short-end anchored. What does this mean for FX? We'd favour USD/JPY back to 110 and as per our FX outlook, we'd see the Latam bloc as the biggest EM beneficiary of higher oil prices, suggesting the high-yield Mexican peso could make a run at 19.00/USD.

EUR: Not very attractive right now

Despite being cheap, the euro does not look very attractive right now and we doubt investors will want to take EUR/USD through 1.1485/1500. EUR/GBP also looks sidelined ahead of next Tuesday's meaningful vote. Elsewhere, today's Riksbank minutes should reinforce its dovish stance, reiterating the next rate hike is likely to come well into the second half of the year. With the domestic economy slowing, we think even one hike is not guaranteed. Swedish krona upside limited.

CAD: BoC may re-kindle tightening expectations

The Bank of Canada meets to set interest rates today and releases a new Monetary Policy Report. Its last meeting (5 December) was dovish – with its observation that there was 'additional room for non-inflationary growth' helping to wipe out tightening expectations. In fact, CAD money market rates priced two years out have fallen a huge 70 basis points since November to leave the 1.75% policy rate priced at flat over the next two years. We think there is some upside risk to CAD over the near term because: (i) the BoC Winter Outlook survey was reasonably upbeat and the BoC should re-affirm that policy needs to be tightened at some point, (ii) the cut in Alberta oil production of 325mn bpd has lifted West Canada Select oil prices and (iii) we're minded to think we could get some positive news on US-China trade which could lift equities and the CAD. USD/CAD is already 3% off its highs, but we think any correction is held at 1.3350 before a move to 1.3150.

PLN: Zloty to look through the NBP meeting

We expect the National Bank of Poland to remain on hold today, with the sharply falling Polish CPI over the past months (and lately even more disappointing core inflation) fully justifying the stance. With the market pricing in low odds of any tightening over the next two years (only 15bp of hikes priced in) and the hike-averse NBP bias well known, the on-hold decision and the likely dovish comments from Governor Adam Glapinski are unlikely to weigh on the zloty too much.

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