FX Daily: Rare earth exports now the lightning rod for trade

FX markets are reasonably calm as attention builds on China's export controls on rare earths. The decision to impose such controls has clearly touched a nerve in the US and across G7 nations. The ability or failure to get those controls negotiated away will be one of the hottest topics for financial markets over the next four weeks

China's rare earth export controls will be a key determinant of risk appetite over the next four weeks

USD: Dollar softer, but short term trend unclear

The dollar is a little softer as short-dated US rates sit at their lows for the year. Last night's release of the Fed's Beige Book suggests the Fed will have enough evidence to cut rates at the end of the month – even if official data releases remain suspended because of the government shutdown. Here, betting markets expect the government to remain closed into November.

The hottest topic for financial markets right now is US-China relations ahead of some key dates. Presidents Trump and Xi are meant to be meeting on the sidelines of the APEC summit in Korea in the 29-31 October window. This is before the 10 November deadline for the 90-day truce on tariffs, where no extension would see US tariffs on China revert to 145%.

The question for financial markets is whether China's proposed export controls on rare earths are merely part of a bargaining ploy to achieve greater concessions from the US. Or really whether it is a threat which would stick and greatly disrupt global supply chains, given rare earths' role in products like semiconductors, EVs, defence and advanced manufacturing. China's move has clearly exercised G7 nations, who are in the process of issuing a joint and rare statement protesting this. US Treasury Secretary Scott Bessent is keen to portray the controls as a move by an overzealous Chinese Commerce Department and has dangled a longer than 90-day extension on tariffs for the next rollover. But any failure to get these controls negotiated away could lead to a bumpy few weeks for global asset markets.

Elsewhere, some positive news out of France has helped the euro and softened DXY. Yet DXY could get some more support tomorrow should LDP President Sanae Takaichi be able to cut a deal with the Ishin political party. This would rebuild a minority coalition grouping and make it more likely that Takaichi is approved as Japan's next PM on 21 October. Her policies are seen as yen-negative.

US data is delayed today, but we do get speeches from two Fed doves, Christopher Waller and Stephen Miran around 1500CET today. Their speeches could mildly weigh on the dollar. DXY may not stray too far from 98.50 today.

Chris Turner

EUR: The double-edged sword of French politics

EUR/USD is enjoying a little more support as US rates soften and French PM Sébastien Lecornu looks set to survive two no-confidence votes in French parliament today – this after the Socialists were bought off with a delay in pension reforms. The euro and French government bonds see this as good news for the short term, although for the longer term the reversal of pension reforms merely makes the job of fiscal consolidation that much harder.

So far, bond investors believe the dropping of pension reforms is the lesser of two evils (the alternative being early elections) and have taken OAT:Bund spreads back inside 80bp. Presumably, FX traders will take their cues from the bond investors, and if this week's move is good enough for French debt, it is good enough for the euro as well.

It's hard to see EUR/USD breaking above the 1.1685/1730 area in the near term. However, the longer EUR/USD can consolidate here, the closer it comes to the seasonally bullish period of November and especially December. We retain a 1.20 year-end call.

Chris Turner

CHF: Sub-0.93 is rare for EUR/CHF

EUR/CHF is trading at sub-0.93, which is quite rare. Some may argue that it should be trading higher given some slightly better news out of French politics. However, it is probably the eurozone macro story which is playing out here. Hard eurozone data has been coming in on the soft side in recent months. This has seen a re-pricing of short-dated EUR swap rates, off around 10bp since their late September highs. Swiss rates are priced with a 'zero bound constraint' in mind. Even though the Swiss National Bank does not rule it out, it clearly does not want to take rates negative again. This is firming up the view that the SNB's hands are tied and leaves EUR/CHF offered.

We expect EUR/CHF to hang around this 0.92/93 area until there is some positive reappraisal of eurozone growth prospects, which may not happen until next year.

Chris Turner

AUD: Rising unemployment no guarantee of RBA cut

Australia reported an acceleration in the unemployment rate in September from a revised 4.3% to 4.5%, above the 4.3% consensus. Employment figures for August were also revised lower to -12k, and combined with September's 15k gain, they make for an essentially flat hiring over the past two months. So even if the rise in unemployment is primarily due to a higher participation rate and not necessarily signalling any material worsening in labour conditions, it does tilt the balance slightly on the dovish side for RBA expectations.

Does this mean the RBA will cut at the 4 November meeting (18bp priced in)? It will all depend on the 29 October third-quarter inflation numbers. Given two months of higher-than-expected inflation, we think there is a good chance the quarterly figure will remain too hot for a rather cautious RBA to cut rates already in November, even if the bar is now admittedly a bit lower.

We have published a scenario analysis for AUD/USD based on US-China trade development. The baseline assumption is that the RBA will cut in December, so an earlier move could shift the AUD/USD profiles slightly lower. Trade news will remain the biggest driver anyway, and we see a de-scalation; 0.68 remains a very reachable target for AUD.

Francesco Pesole

CEE: Waiting for a fresh story

On the data side, it remains quiet in the CEE region. Today we will see the final inflation figures for Poland, which should confirm September's figures at 2.9% YoY and show what we can expect from core inflation, which will be published tomorrow. The CEE market continues to be dictated by the global story, and yesterday's late turnaround higher in EUR/USD may provide some support for CEE currencies today. At the same time, HUF and CZK rates saw some stabilisation yesterday, while EUR rates continue to rally, also providing some support for CEE currencies from wider rate differentials.

EUR/HUF could test 390 and EUR/CZK levels below 24.250 today. On the other hand, EUR/PLN has little reason to change anything at current levels near the upper end of our range of 4.245-275. Still, the first appearances of CEE policymakers at the IMF meetings in Washington could bring some fresh air into the rather muted local story today.

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