FX: One week, two deals?

We struggle to see a breakthrough in either US-China trade talks this week, or Brexit negotiations. As such, we prefer risk-averse currencies

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USD: We'll know some more on US-China trade and Brexit by Friday

The sharp fall in US rates after a softish run of US data last week has seen the dollar soften a little and high-yield FX perform a little better on the view that the Federal Reserve may cut in October after all (a cut is now 79% priced). Shedding light on this outcome will be a speech by FOMC Chair Jerome Powell tomorrow night and also the release of the September FOMC minutes on Wednesday evening. But a Fed rate cut in October is certainly not a done deal. And we'll also receive insights on two of the biggest headwinds to the global economy this year: (i) US-China trade and (ii) Brexit. On the former, a senior Chinese delegation is in Washington this Thursday/Friday and failure to achieve a breakthrough will once again hit risk assets. On the latter, it seems the EU wants substantial progress on any Brexit deal by this Friday, such that EU leaders have a weekend to assess it before their summit on 17/18 October. At present, we struggle to see a breakthrough here either, meaning that European FX remains an underperformer. With the Trump impeachment process gaining a little momentum, in the G10 space we continue to prefer risk-averse currencies such as Japanese yen, probably against European activity currencies. DXY can stay bid near 99.00 unless there is surprise progress on either of these two, key deals.

EUR: ECB communication breaking down?

At the end of Mario Draghi's tenure at the European Central Bank, it certainly feels like internal resistance to expansionary ECB policy is growing, creating a difficult environment for incoming president Christine Lagarde. Internal divisions at the ECB won't be welcomed by international investors, recalling the discord and euro underperformance seen in the 1999/2001 period. Strong EUR/USD resistance may hold at 1.1020.

GBP: We're not hopeful of a Brexit deal this weekend

Our team only attaches a 10-15% chance of the UK and EU agreeing a new Withdrawal Agreement over the next week. The story will then move on as to whether Prime Minister Boris Johnson is forced to extend Article 50. Given little political risk premium priced into the pound around current levels, cable looks vulnerable to 1.21.

ILS: Bank Of Israel unlikely to turn Shekel bull trend

The Bank of Israel meets to set interest rates today and consistent with most central banks around the world is likely to convey a cautious message. Caution from the BoI is less about the global economy and more about the strong shekel, which is currently hovering near the highs of the year at 3.47-48/USD. Here, news that Israel will be included in the WGBI benchmark sovereign bond index next April, plus recently announced gas deals with Egypt, point to a strong Balance of Payments position for the ILS. BoI caution today looks unlikely to dent the shekel's bull trend, where we see USD/ILS edging to 3.45 and ultimately 3.40.

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