FX Week Ahead: Divide and Conquer

The key focus for FX markets early this week will be the G20 meeting in Argentina. A show of unity looks very difficult to achieve and the Trump administration will be emphasising the need for 'fairer trade'. The threat of an escalation in the trade wars should trump a generally upbeat FOMC meeting on Wednesday. Expect the dollar to remain under pressure against the low-yielders

Source: Shutterstock

EUR: G20 dis-unity?

	Spot	Week ahead bias	Range next week	1 month target
EUR/USD	1.2330	Mildly Bullish	1.2250 - 1.2450	1.2500

• Before Wednesday's FOMC meeting the focus will be on the G20 meeting of Fin Mins and CB governors in Argentina. While we may see some US lip-service to a strong dollar, we doubt investors will respond. Trump's protectionsim embodies a weak dollar policy and instead we expect US authorities to emphasise 'fair' trade and the foreboding of further trade sanctions - with particular focus on China's infringments on intellectual property rights.

• We doubt the FOMC can provide much of a lift to the dollar. To secure a median view of four rate hikes this year in the Dot Plots, four to five Fed members will have to upgrade their view. Even if that happened, it might only be worth a 5-10bp rise in short-dated USD rates and only marginally support the dollar. In the Eurozone, the focus will be on March business confidence readings - potentially softening a little in light of protectionism.

JPY: 105 looks vulnerable

	Spot	Week ahead bias	Range next week	1 month target
USD/JPY	105.75	Bearish	103.80 - 106.75	103.00

• USD/JPY remains vulnerable as protectionist risks rise. The next major story here maybe the USTR making recommendations on trade retaliation against China's alleged theft of intellectual property rights. A range of sanctions will probably be recommended, but Trump has tended to opt for the harsher option. The threat of across-the-board tariffs cannot be ruled out and thus USD/JPY remains vulnerable.

• Japan will release February CPI on Thursday, which should head up to 1.5% YoY. The BoJ are trying to downplay fears of early tightening and frankly we think the prospects of a large fall in USD/JPY may well keep the BoJ side-lined well into 2019 (and beyond).

GBP: Make-or-break week may be more of an 'emotional' rollercoaster

	Spot	Week ahead bias	Range next week	1 month target
GBP/USD	1.3940	Mildly Bullish	1.3850 - 1.4250	1.4300

- We suspect a frenetic week may be in store for GBP markets as Brexit and Bank of England policy risks clash head on (see our note GBP: Risks are more making - and less breaking). The immediate focus for investors at the upcoming 22-23 March EU leaders summit is whether both sides can formally agree on a Brexit transition deal - which, if successfully achieved, would go some way to reducing the long-run risks surrounding the UK economy. In principle, if a deal can be finalised this week, we would expect GBP to see a sharp knee-jerk move higher - noting that this would be a positive surprise given that investors have downgraded their expectations for a transition being agreed as early as this week's summit, while more neutral GBP positioning and a small Brexit risk premium in the currency also lends support to a move higher.
- One of the channels through which we expect GBP strength to materialise in the event of a positive transition deal outcome is reaffirmed sentiment over BoE policy tightening. Not only would we see greater market conviction over a May rate hike (currently 70% priced in), but the potential for a re-invigorated UK economy in the near-term could also spur talk of a second BoE rate hike in 2018. The case for a steeper UK rate curve this week would find additional support from (i) a Brexit-contingent hawkish signal at the March BoE policy meeting (Thu) and (ii) a string of constructive UK economic data releases - namely core CPI inflation remaining sticky at 2.6% YoY (Tue) and headline wage inflation also showing signs of moving higher (Wed). If all the cards were to fall perfectly in place for GBP this week we could see a bullish GBP breakout (especially against a weak USD) and would not rule out a sharp move up towards the year-to-date highs around 1.4250-1.4300 (approx +2.0%). On the flipside, while it may be tempting to paint this week's EU leaders summit as a make-or-break moment for GBP, we would not see the failure of a transition agreement being reached this week as a reason to sell the currency.

AUD: Watching potential US tariffs on China nervously

	Spot	Week ahead bias	Range next week	1 month target
AUD/USD	0.7750	Neutral	0.7710 - 0.7920	0.7800

- With Trump's trade policy the dominant factor for global risk sentiment - commodity currencies remain caught in the crossfires of a less benign market backdrop and systemically weak USD. Bar any credible hawkish surprise at the March FOMC meeting - which seems unlikely, we suspect AUD/USD could remain neutral around the 0.77-0.78 level after the recent downward adjustment. Further downside would only materialise if the US escalates the current 'cold trade war' by imposing tariffs on China. Naturally, AUD's secondary linkages here would see it underperform in this near-term.
- The Feb Australian jobs report will be the main data point in focus over the coming week. The likelihood of a strong print (+20k) could support the AUD, though equally markets need to see more convincing signs over domestic inflation to start actively re-pricing the outlook for RBA policy. Currently, the curve looks instinctively flat given the fact that the central bank raising rates this year remains a remote possibility. The March RBA minutes (Tue) may implicitly endorse this sentiment.

NZD: RBNZ citing two-way risks to policy would be a kiwi negative

	Spot	Week ahead bias	Range next week	1 month target
NZD/USD	0.7230	Bearish ↘	0.7140 - 0.7320	0.7200

- After a disappointing 4Q NZ GDP print (0.6% QoQ vs 0.8% expected), the focus this week turns to the March RBNZ meeting (Wed). With no new projections due from the central bank, the only focus for investors will be the tone of language in the statement around the future policy outlook. Given the heightened downside risks to global growth stemming from a possible global trade war, one could imagine the RBNZ to turn pre-emptively dovish. Recent comments from central bank officials have suggested two-way risks to RBNZ policy (ie, keeping rate cuts on the table as well as rate hikes). A reiteration of this would be NZD negative.
- Also to note in the domestic calendar is the GDT dairy auction (Tue). Prices have been resilient in recent auctions, despite fluctuating sentiment over global commodities (largely in the industrial metals space). It'll be interesting to see whether global factors have spilled-over in any way. For now, terms of trade remains a factor supporting NZD.

CAD: Move above 1.30 looks like an overreaction... again

	Spot	Week ahead bias	Range next week	1 month target
USD/CAD	1.3080	Neutral	1.2920 - 1.3130	1.2700

- CAD has been the clear G10 underperformer in recent weeks - not least due to US trade policy and the prospect of a less hawkish BoC. Evidence of both were in play for the move above 1.30 - with Governor Poloz citing the potential need for policy patience (due to greater domestic slack), while President Trump once again flagged the US trade deficit with Canada in another sporadic tweet (albeit the trade deficit only exists in goods trade, the overall balance is a net trade surplus). Weak manufacturing activity data didn't help the loonie.

- We view the sustained move above 1.30 as an overreaction to the two stories (US trade frictions and less hawkish BoC). CPI inflation and retail sales data in the week ahead (both Fri) will be crucial for near-term BoC policy tightening sentiment. Markets have reduced their bets on a May hike (46% currently), though it would take some really soft data now to see this priced out. Consensus is looking for CPI at 2% YoY (core 1.9% YoY) and retail sales posting a 1.3% MoM gain.

CHF: SNB still intervening?

	Spot	Week ahead bias	Range next week	1 month target
EUR/CHF	1.1710	Mildly Bullish	1.1680 - 1.1780	1.1800

▪ EUR/CHF survived the quarterly SNB meeting, which did see the inflation forecast cut a little, but not much. The SNB is effectively still forecasting a return to 2% in 2020 - unlike the ECB. We think SNB may still be intervening under 1.1700, consistent with their policy of negative rates and continued intervention. At some stage this intervention could fall foul of the US Treasury.
▪ Protectionism and its negative connotation for risk is a CHF positive. This may prevent EUR/CHF rallying towards our preferred objectives in the 1.18/20 region this summer.

SEK: The correction in EUR/SEK lower largely exhausted

	Spot	Week ahead bias	Range next week	1 month target
EUR/SEK	10.0850	Mildly Bullish	10.0600 - 10.1840	10.3000

- It is a very light data week in Sweden, suggesting that EUR/SEK should be largely driven by the global risk sentiment. Given the ongoing overhang of the US tariffs (this time China is in focus) and global trade wars, we see the recent correction in EUR/SEK lower as largely exhausted and continue to see upside risks to the cross (our 1-month EUR/SEK forecast is at 10.30).
- We don't expect Riskbank board members speeches next week (Ohlsson and Floden) to materially affect SEK as the market already meaningfully re-priced (lower) the expectations for the Riksbank tightening cycle following the disappointing January Swedish CPI. EUR/SEK to return into the 10.10-10.20 area.

NOK: Some calm after the hawkish Norges Bank meeting

	Spot	Week ahead bias	Range next week	1 month target
EUR/NOK	9.5020	Neutral	9.4300 - 9.5680	9.5000

- Following this week's NOK strength in response to the more hawkish Norges Bank (the central bank brought forward the expected timing of the first rate hike), we expect EUR/NOK to stabilise this week, trading around the 9.50 level.

- This is because the scope for a further hawkish NB re-pricing is limited at this point (the market is already fully pricing 25bp hike by end-2018 and assigning a 50% probability to the September hike) while domestic data this week (Jan unemployment rate on Wed) should not translate into material NOK strength.

Author

Chris Turner
Global Head of Markets and Regional Head of Research for UK & CEE
chris.turner@ing.com