

G10 FX Week Ahead: Keeping the V on the road

After signs in Europe that that rebound in activity may be stalling, market focus in the week ahead will be on whether policymakers can keep recovery hopes alive. Progress on the next US stimulus plan will be watched closely as will a Jackson Hole speech from Fed Chair Powell on Thursday



Source: Shutterstock

USD: Keeping the V shape show on the road

	Spot	Week ahead bias	Range next week	1 month target
DXY	93.2790	Neutral	92.5000 - 93.8000	91.0000

- The dollar has entered into corrective phase after the July FOMC minutes failed to feed the rally in risk assets. For the reflation and declining real yields narrative to keep the dollar under pressure, we need to see: a) supportive evidence of a 'V' and b) signs that the Fed will keep rates low and is prepared to do more. On the former, the debate about fresh US stimulus rumbles on, with hopes that Saturday's vote on the US postal service could restart negotiations of a slimmed down stimulus deal. Also into the V category would fall any new update on US-China relations – the Chinese suggest a review on the Phase One deal will be taking place after all. And the week ahead for US data does not look too bad. August consumer confidence and DGO data may surprise on the upside.
- In terms of the Fed story, this week could be interesting. The two-day Jackson Hole symposium starts Thursday and the theme is 'Navigating the Decade Ahead: Implications for Monetary Policy'. Once again, the market will be on the look-out for any indications that the Fed is close to adopting Average Inflation Targeting and to better understand the conditions that would prompt Yield Curve Control. The focal point at this event will be an address from Fed Chair Powell on Thursday at 15:00 CET. Given Jackson Hole, we doubt investors will want to chase the dollar too much higher and would think that the DXY correction could stall before 94.00. If we're underestimating the scale of the dollar rally it may be that events in Belarus – were they to deteriorate – could have triggered a larger EM correction.

EUR: First signs of fatigue

	Spot	Week ahead bias	Range next week	1 month target
EUR/USD	1.1778	Neutral	1.1690 - 1.1900	1.2000

- The EUR/USD sell-off gained some momentum on Friday when Eurozone August PMIs largely disappointed – led by services. With Covid cases resurgent in many parts of the world, the fear is now that we've seen the best of the recovery figures and that V shape expectations will take a knock in September. Shedding some more light on this will be Tuesday's German August Ifo data. The best case will be that manufacturing offsets the decline in services such that the overall number does not disappoint.
- EUR/USD could briefly dip under 1.17 if the correction gains momentum, but we do not see wholesale changes taking place to the factors which have driven the rally and thus are happy to keep a one-month target at 1.20.

JPY: On notice for an asset market correction

	Spot	Week ahead bias	Range next week	1 month target
USD/JPY	105.98	Neutral	105.20 - 106.30	104.00

- US Treasury yields have been trapped in relatively tight ranges, thus keeping USD/JPY subdued. The biggest benefit to the JPY near term would probably be a correction in global asset markets given the cross-correlation is so high. 'Nowhere to hide' would be the remarks made during an asset market correction. For the time being, however, the view would be that either Congress, the Fed or probably both would come to the rescue at the first sign of trouble and that betting on an equity market correction remains frustrating.
- Given the JPY and US Treasury relationship, Jackson Hole will of course be important. Less important will be the Japanese data calendar which only sees August Tokyo CPI and the regular international portfolio data. Once again USD/JPY seems to be finding support near 105.00 and we suspect Japanese fund managers are the big buyers here.

GBP: Will BoE shed some light on negative rates?

	Spot	Week ahead bias	Range next week	1 month target
GBP/USD	1.3075	Neutral	1.2980 - 1.3160	1.3100

- UK and EU politicians on Friday did little to hide the fact there had been no progress made in trade talks. GBP duly handed back some gains after a promising rally backed by some better data. The week ahead sees little on the local data calendar but we will have BOE speakers in Haldane (Wednesday) and Bailey (Friday). Haldane is at the optimistic end of the spectrum, but the market will probably be more interested in Bailey's views on negative rates. They are still on the table and a renewed threat to use them could prove some trouble for GBP.
- Positioning data shows that speculators have been unwinding GBP shorts and this community may now be flat after the break above 1.32 earlier in the week. However, messy Brexit discussions into October are likely to discourage a build-up of GBP long positions and choppy range trading looks more likely.

AUD: Suffering from reflation doubts

	Spot	Week ahead bias	Range next week	1 month target
AUD/USD	0.7154	Neutral	0.7050 - 0.7250	0.7200

- AUD/USD may remain unable to sustainably trade above 0.7200 next week, as markets may start to doubt the reflation story after a set of grim surveys today. AUD continues to be the most overvalued currency among the G10 pro-cyclicals in a short-term perspective and may therefore be a key laggard if markets start pricing out some market recovery.
- Still, the generalized USD bearish sentiment is hardly going to wane anytime soon, which could continue to offer some floor to AUD/USD. Thus, AUD weakness may be more evident in the crosses. Except for the dynamics in the contagion curve in Victoria (which anyway have had a limited currency impact so far) domestic factors should play second fiddle for AUD given a quiet economic calendar.

NZD: Looking for the bottom

	Spot	Week ahead bias	Range next week	1 month target
NZD/USD	0.6529	Neutral	0.6530 - 0.6730	0.6700

- The Reserve Bank of New Zealand's continuous negative rates chatter is having the (wanted) effect of keeping NZD on the backfoot, although NZD has not diverged massively from its closest peer AUD. The negative rates story may start to have a lower impact on NZD, which could start to recover some ground to its pro-cyclical peers next week.
- The fresh lockdown measures in New Zealand will remain centre stage, but otherwise no other domestic drivers should warrant NZD divergence from the global risk sentiment dynamics.

CAD: Tougher than the rest

	Spot	Week ahead bias	Range next week	1 month target
USD/CAD	1.3196	Neutral	1.3110 - 1.3290	1.3200

- CAD continues to prove a more attractive option than AUD and NZD, largely thanks to WTI's broad resilience and also thanks to a somewhat less worrying contagion situation in the US.
- Next week, Canadian growth numbers for July will be watched, likely showing another MoM increase but with the YoY slump still hovering around -10%. Anyway, the read should not have make-or-break implications for the loonie, which – as long as the downside remains limited for oil – should still be more resilient than most of its procyclical peers to swings in risk sentiment. It will also be interesting to follow BoC Governor Macklem's speech at Jackson Hole, although we doubt he will signal any shift in the Bank's monetary stance.

CHF: What happened in USD/CHF?

	Spot	Week ahead bias	Range next week	1 month target
EUR/CHF	1.0749	Mildly Bearish 	1.0710 - 1.0800	1.0700

- One stand-out for us recently was that a sharp rally off 0.90 in USD/CHF on Wednesday, (briefly lifting EUR/CHF above 1.08), seemed to trigger the broader correction in USD/Europe. We wonder whether the Swiss National Bank chose to intervene there to prevent a sharp break below 0.90 triggering more out-sized gains for the CHF – where nominal trade weighted CHF indices are already on record highs. A break below 0.90 might therefore be needed to confirm the next wave of broad \$ losses.
- Thursday sees 2Q20 Swiss GDP expected at -9% QoQ (better than the Eurozone at -12%). Any worse-than-expected data could weaken the CHF on the view that the SNB does not merely need to contain CHF strength, but to reverse it.

SEK: Losing some resilience

	Spot	Week ahead bias	Range next week	1 month target
EUR/SEK	10.3620	Mildly Bullish 	10.3000 - 10.4900	10.2000

- SEK's exposure to Eurozone-related sentiment is indeed a worrying factor for the currency at a moment where fresh spikes in Covid-19 cases in the EU along with markets' partly repricing of the EZ reflation story are both at play.
- While SEK should still prove more resilient than its closest peer NOK to setbacks in risk sentiment, both Scandies may still lag the rest of G10 next week. Like in Norway, the 2Q GDP numbers will be in focus. Our economists are expecting a -8.6% YoY read, which is broadly in line with market expectations, confirming a less severe slump in Sweden compared to the rest of the EU.

NOK: Signs of fragility

	Spot	Week ahead bias	Range next week	1 month target
EUR/NOK	10.6500	Mildly Bullish 	10.5500 - 10.8000	10.5000

- The fierce NOK recovery is starting to show signs of fragility, despite the resilience in oil prices, and the Norges Bank having reiterated their cautiously optimistic view. NOK may be facing a physiological short-term setback – with grim EU contagion news and survey numbers adding downside pressure – and the risk of the reflationary push to risk assets waning a bit next week does highlight the risk of an extension in the downward correction.
- The notion that Norway has suffered less (economically speaking) than other European countries from the pandemic is a notion that has already been acquired by the markets. 2Q numbers released next week may well generate some volatility on NOK given the relatively upbeat market expectations.

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