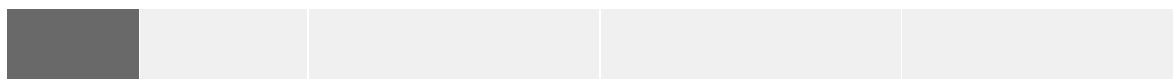


G10 FX Week Ahead: We need to talk about deficits

In a quiet week for events, FX markets might wake up and take note of the advanced release of the US April trade balance. This is expected to show a record \$92bn deficit. Does the dollar need to cheapen? Elsewhere, while swings in commodity prices will remain in focus, the RBNZ might start to lean in favour of slower asset purchases, which could support NZD



USD: Is it time to start focusing on the US trade deficit?

	Spot	Week ahead bias	Range next week	1 month target
DXY	89.841	Mildly Bearish 	89.5000 - 90.5000	89.0000

- DXY continues to slip and is less than 1% away from the lows of the year. That is quite remarkable given that US 10-year yields have risen 70bp and a number of Fed participants want to be talking tapering sooner rather than later. Yet the weakness in the dollar owes a large part to a core of the Fed unhurried about the need to withdraw stimulus and recovery stories elsewhere in the world. These core views are unlikely to be challenged in the week ahead. We say this because the US data calendar is relatively light. Here the focus will be on any possible upward revisions to 1Q21 GDP, but what may be some softer home sales and durable goods orders data. We will also see May's advanced US trade balance. A \$92bn deficit is expected. Yes that's \$92bn. That is quite a large hole to fill when the US exceptionalism of the 2018-2020 period is being challenged by the overseas recovery and US real rates remain very negative.
- The week ahead will also see a variety of Fed speakers, who largely sit on the dovish end of the spectrum. Away from the US calendar, the market will keep close watch on volatility in crypto-currencies and tech stocks as well as developments in the Renminbi. Any signs of independent Renminbi strength could lend weight to the notion that the PBOC wants a stronger currency to insulate against imported commodity price rises. This would be bearish for the dollar [in our opinion](#).

EUR: EU summit in focus

	Spot	Week ahead bias	Range next week	1 month target
EUR/USD	1.2206	Mildly Bullish 	1.2150 - 1.2310	1.2300

- EUR/USD continues to hold up well and a key story here is probably the rotation into European asset markets as confidence in the recovery intensifies. In local currency terms, Eurostoxx has outperformed the S&P 500 and flow data suggests US investors are increasingly interested in Eurozone equity ETFs. Somewhat surprisingly the Treasury:Bund spread has also been narrowing since a wide of 200bp in late March – a move which could discourage some of the reverse yankee issuance which had been weighing on the EUR. For the week ahead, the highlight of the Eurozone data calendar will be May readings for consumer and business confidence. We'll also see the May reading of the German Ifo, which risks come in a little softer based on the manufacturing PMIs.
- The early part of the week will also see a special European Council meeting. Top of the agenda here is climate change and the EU's plan to implement a net reduction of greenhouse gases of at least 55% by 2030. Increasing interest from the corporate treasury community in the hedging of carbon emission allowances will see much focus on what the EU does with allowances and whether the spot price will surpass the recent peak of EUR56/MT.

JPY: Stalled US yields, stalled USD/JPY

	Spot	Week ahead bias	Range next week	1 month target
USD/JPY	108.69	Neutral	108.35 - 109.50	108.00

- US Treasury yields have stalled around the 1.60/65% area and there does not seem a clear catalyst in the week ahead as to what will drive them higher. This has taken some of the steam out of the USD/JPY rally. And indeed if any currency pair showed a hinted of reacting to last week's crypto-crash – it was USD/JPY. Let's see whether the dollar starts to take any notice of the US trade deficit this coming week – if so USD/JPY might start to soften were a risk premium start to be priced into the dollar.
- The Japanese calendar is really quiet this coming week. We have been hearing more about a foreign rotation into Japanese equities, but so far there is no evidence of that in the Japanese MoF weekly portfolio flow data. Let's see whether that changes.

GBP: On the verge of breaking the multi-year GBP/USD high

	Spot	Week ahead bias	Range next week	1 month target
GBP/USD	1.4200	Mildly Bullish 	1.4010 - 1.4380	1.4400

- GBP/USD managed to shake off the recent USD rebound quite well and in line with the other European FX it now continues grinding higher. The strong UK May PMIs have underlined the optimistic case for the UK economic outlook and it is a clear tailwind for GBP. Although domestic data are unlikely to provide much boost to GBP next week, as long as the soft USD environment remains in place, GBP/USD is likely to breach the multi-year high of 1.4237 quite soon and head towards the 1.44, in line with our 1-month forecast.
- It is a quite week on the domestic data front, with April UK public finance numbers (Tuesday) to have a limited effect on GBP.

AUD: FX market not too worried about iron ore, for now

	Spot	Week ahead bias	Range next week	1 month target
AUD/USD	0.7781	Neutral	0.7700 - 0.7830	0.7800

- AUD has received mixed signals from the data side and commodity side this week. Unemployment fell to 5.5% in March, but the number of people employed actually shrank. All in all it was a broadly positive read as it shrugged off the concerns about the impact of the end of the JobKeeper wage subsidy scheme. Ultimately, it may have applied a little more pressure on the RBA to sound less dovish, although there are no speeches or policy meetings due soon, so we will have to wait longer for any potential change in rhetoric.
- On the commodity side, iron ore showed signs of recovery at the start of the week but then followed other commodities lower and broke decisively below 180 USD/Mt. It is still trading at very high levels compared to historical standards, although markets will remain highly focussed on any signs the slump in prices has further to go. For AUD, this remains (along with any other developments in the Aussie-China trade relationships) the main short-term downside risk.

NZD: RBNZ to start talking tapering?

	Spot	Week ahead bias	Range next week	1 month target
NZD/USD	0.7216	Mildly Bullish 	0.7150 - 0.7300	0.7400

- The decline in commodity prices had a magnified effect on NZD compared to other commodity currencies possibly due to NZD's rather stretched [net-long positioning](#) that left it more vulnerable to position-squaring-related corrections.
- In the week ahead, the focus will be on the Reserve Bank of New Zealand policy meeting. There is a rather contained risk of hearing any radical shift in the policy stance, although an expected lower bond issuance in New Zealand may prompt the Bank to start signalling the pace of asset purchases will slow. The jobs market has continued to prove strong by taking opposite directions to the pessimistic one seen in the February RBNZ projections, and commodity prices have boosted the NZ terms of trade. New economic projections will be released, and focus will be not only on the unemployment gauge, but especially on the growth and inflation figures, which were weaker than expected in February. Overall, we expect the balance of risks for NZD to be tilted to the upside ahead of the meeting, considering there is not much room for the RBNZ to sound reasonably more dovish and there is a possibility that the Bank will start talking about tapering.

CAD: Flirting with 1.20

	Spot	Week ahead bias	Range next week	1 month target
USD/CAD	1.2028	Neutral	1.1980 - 1.2100	1.2000

- CAD has continued to rally this week, this time pushed by a slew of supporting domestic data along with more evidence that the vaccination roll-out in Canada is keeping a high pace. Inflation rose to 3.4% in April, which is a quite high figure considering the restrictions in place in many parts of the country. Today, retail sales for March soared past expectations and came in at 3.6% MoM. The data flow has clearly gone in the direction of mitigating the grim jobs numbers for April, and this is ultimately supporting hawkish expectations on the Bank of Canada.
- Next week will be very quiet data-wise and there are no central bank speakers scheduled. External factors should therefore drive the large majority of CAD moves, and leave the loonie more vulnerable to potential unwelcome swings in commodity prices. USD/CAD is very close to the key 1.2000 support, which may well be heavily tested in a risk-on environment next week .

CHF: Is ECB tapering playing a role here?

	Spot	Week ahead bias	Range next week	1 month target
EUR/CHF	1.0957	Mildly Bullish 	1.0930 - 1.1030	1.1100

- EUR/CHF continues to trade on the soft side – even after what seemed to be quite a benign ruling on the Polish FX mortgage saga. Casting around for factors that could be depressing EUR/CHF, we note the recent rise in BTP:Bund spreads. The 10-year spread is gaining a little momentum to the upside (+20bp over the month), largely on the view that the ECB will reduce its aggressive PEPP buying scheme. Recall this scheme has primarily been buying government bonds and Italy had been a big beneficiary here. Wider BTP:Bund spreads can occasionally depress EUR/CHF. Further speculation over this PEPP slow-down could cause some more problems for EUR/CHF.
- Overall, however, we prefer EUR/CHF to trade back to 1.11 over coming weeks as confidence grows in the global recovery and EUR/USD stays supported. As a core view, we expect the Swiss National Bank to position itself substantially behind the ECB when it comes to policy normalization – a key factor that should drive EUR/CHF higher multi-quarter.

NOK: Underperformance that is not to last for long

	Spot	Week ahead bias	Range next week	1 month target
EUR/NOK	10.1500	Mildly Bearish 	9.9830 - 10.2760	9.9500

- NOK, among NZD, was the only G10 currency that did not manage to fully recover after the dollar strength earlier in the week, being clearly hit by correction in the oil price. However, we expect the NOK underperformance to be short-lived, particularly when the NB should remain ahead of the tightening back among the G10 central banks (in contrast to Riksbank). EUR/NOK to head back towards 10.00 and persistently settle below this level in summer.
- Data-wise, Norway 2Q consumer confidence (Tuesday), April retails sales (Friday) and May unemployment (Friday) should all have a limited impact on the krone next week.

SEK: The ongoing conversion towards the EUR/SEK 10.00 level

	Spot	Week ahead bias	Range next week	1 month target
EUR/SEK	10.1200	Neutral	10.0400 - 10.1930	10.1000

- EUR/SEK continues to hover around the 10.10 gravity line and even the recent Riksbank Vice Governor Jansson's comments about the cautious Riksbank approach (which points to Riksbank remaining at the back of the policy normalization pack among the G10 central banks) did not hurt SEK much. No tightening is expected this year and next and the main factor that is to benefit SEK going into the summer months is the move towards the synchronised global economic recovery
- On the Swedish data front, the main focus will be on the forward looking May Economic Tendency Survey (Thursday), 1Q GDP and April retail sales (both on Friday). Yet, given the clear message from the Riksbank, even positive surprises should not give a long lasting boost to SEK. Rather, the global factors remain more important for the krona.

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