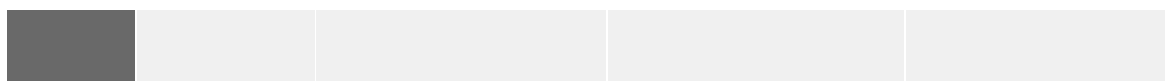


## G10 FX Week Ahead: It's getting hot in here

Despite the cooling trends of autumn, central bankers are feeling the heat of higher energy prices. How they respond to the risk of higher inflation will set the tone in FX. A good NFP should keep the Fed on track to taper later this year and tighten in 2022, and support USD. NZD may receive some help from a RBNZ hike, while the RBA meeting should be a quiet one



Gas storage tank



## USD: Dollar ready to blow the doors off?

	Spot	Week ahead bias	Range next week	1 month target
DX	94.0800	Mildly Bullish 	93.8000 - 95.0000	95.0000

- The dollar has recently pushed up to the highs of the year as both central bankers and investors re-assess both the transitory nature of inflation and what central bankers plan to do about it. Driving that re-assessment, particularly in the US, has been the hawkish set of Fed Dots and surging energy prices. We think the move in short-term US interest rates has played a major role in recent dollar strength. Both those themes will be in the spotlight this week. The first is whether Friday's non-farm payrolls report – we look for +450-500k – is enough to keep the Fed on track to announce tapering in November and on track to tighten in late 2022. We think yes. The second is whether OPEC+ increases supply on Monday by 400k barrels per day. Again we think yes it will, but rampaging gas prices look like they can keep the energy complex bid for a while longer and the inflation scare front and centre.
- Technically the dollar looks on the verge of a significant break-out and a strong US jobs report could cement that trend. We'll also focus on progress on the US debt ceiling – a stopgap bill has been signed to fund the government until early December – but brinkmanship in the Senate could easily lead to a mishap for risk assets at a time when earnings expectations are being revised lower. China is closed this week, which means perhaps less newsflow on challenges in the real estate sector. But the People's Bank of China is setting an example to the world right now by engineering a strong currency to secure commodity imports. Let's see if any others want to join it.

## EUR: ECB doves feeling the heat

	Spot	Week ahead bias	Range next week	1 month target
EUR/USD	1.1600	Mildly Bearish 	1.1500 - 1.1650	1.1500

- Eurozone inflation pushed up to 3.4% YoY in September and core to 1.9%. The European Central Bank had expected higher inflation, but not this high. So far the doves have been happy to ascribe higher inflation to transitory factors and warn against any over-reaction. This week we will hear from many ECB speakers, including core doves Lagarde and Lane. Plus we get to see the minutes of the September ECB meeting where a 'recalibration' of PEPP was announced. Normally these minutes are quite anodyne and rarely prompt a market reaction – but they will be under more scrutiny now especially since some members were already concerned that inflation forecasts were too low.
- On the data front, we should get to see a broader look at the October PMI releases and some investor sentiment indicators. The week will also see how the dovish ECB stacks up against other central banks in Europe. As usual, the Czech National Bank took no prisoners with a 75bp hike on Thursday. This week the focus switches to Poland where an inherently dovish central bank could be faced with inflation at 7.0% YoY later this year and a policy rate of 0.10%. We suspect Poland disappoints expectations of a large rate cycle. Back to EUR/USD, 1.1500 is a big support zone and may well be tested this week as long as US NFP delivers and ECB doves do not switch stance.

## JPY: Japan is on the wrong side of the energy story

	Spot	Week ahead bias	Range next week	1 month target
USD/JPY	111.06	Mildly Bullish 	110.50 - 112.00	112.00

- Japan's next PM will be Fumio Kishida, seen to be very much a continuity candidate and a subscriber to the JPY-negative Abenomics. The negative feel to the JPY at the moment is added to by the surge in energy prices. Japan's terms of trade are moving sharply in the wrong direction and we should shortly be seeing Japan's current account deteriorating as trade deficits erode the traditional net income surplus.
- USD/JPY did reject 112 quite abruptly last week. Yet higher energy prices and what we think could be a bullish run for the dollar should see good demand emerge under 111.00. Interestingly the JPY gained little from a difficult equity environment in September. October is typically a slightly better month for equities – November even better still – so a softer JPY profile may well come to pass.

## GBP: Stagflation is not all bad for the pound

	Spot	Week ahead bias	Range next week	1 month target
GBP/USD	1.3550	Mildly Bearish 	1.3400 - 1.3600	1.3400

- GBP volatility has been picking up markedly since September and is now back to levels last seen in July. The market seems a little unsure how to trade GBP on this energy story and early fears of stagflation. Bad for activity but good in the sense that it makes the Bank of England tighten earlier? For the shorter term, we tend to favour the dollar (GBP does not like risk aversion) and technically there is a case for a multi-day move in Cable to 1.32. Resistance at 1.3570/2620 should now be a tough nut to crack on the upside.
- Given that the market now prices a 10bp hike at the November BoE meeting and another 50bp in 2022, the market will hang on the BoE's every word. Here Dave Ramsden speaks on Tuesday. Ramsden is a hawk and recently voted to end BoE bond buying early. Let's see if he pours any more oil on the fire of early BoE tightening.

## AUD: A quiet RBA meeting

	Spot	Week ahead bias	Range next week	1 month target
AUD/USD	0.7260	Mildly Bearish 	0.7160 - 0.7300	0.7200

- We think next week's Reserve Bank of Australia rate announcement has a fairly low surprise potential. The Bank announced it will keep its policy tools frozen until February 2022, which should leave most of the focus on financial stability concerns ahead of the semi-annual Financial Stability Review on 8 October. Housing affordability should be a central theme in this sense: any indications the RBA will step in with macro-prudential tools to curb housing inflation may keep help the current forward guidance that no hikes will be needed before 2024.
- In the assessment of the economic outlook, the RBA is likely to welcome the easing of Covid restrictions in Australia, but should refrain from sounding materially more optimistic considering the risks of financial turmoil and economic slowdown in China and the strictly-related drop in iron ore prices. Markets are pricing in a mere 12bp of tightening in the next year which, despite being more hawkish than the RBA's forward guidance, is still quite conservative when compared to peer central banks. We doubt there is much more room for such timid tightening expectations to be scaled back and be translated into AUD weakness next week. Evergrande and global risk sentiment are likely to overshadow any post-RBA move (which should be quite contained anyway, in our view). Australia's position as natural gas and coal exporter may partly shield AUD from risk-sentiment hits as energy prices remain elevated.

## NZD: No more excuses for the RBNZ

	Spot	Week ahead bias	Range next week	1 month target
NZD/USD	0.6935	Neutral	0.6870 - 0.7000	0.7100

- Since leaving rates on hold at the August meeting, comments by Reserve Bank of New Zealand officials have strongly suggested we'll see a 25bp rate hike this coming week. In August, a lockdown announcement in New Zealand kept policymakers from pulling the trigger on tightening, now there appears to be no more "excuses" to delay the first hike. The only key release since the August meeting was activity data for 2Q, which came in on the strong side and beat expectations. We had previously flagged some risk of a 50bp hike, but recent comments by Assistant Governor Christian Hawkesby clearly pointed at a more gradual rise in rates.
- Markets are currently pricing in around 80% probability of a hike next week, and if the RBNZ delivers as we expect, we could see some moderate support for NZD. Markets will likely keep a close eye on the RBNZ outlook for the economy (especially in light of the recent Covid restrictions) to remain aligned with the Bank's projections that currently see the policy rate reach 2% in late 2023. We'll also see whether the RBNZ signals it will tighten loan-to-value ratio (LVR) restrictions further with the aim of curbing housing inflation (which reached 27.8% YoY in September), although that should not prove enough to make markets doubtful that monetary tightening remains necessary. Any positive impact on NZD from the RBNZ meeting may be, however, offset by an unsupportive risk environment next week: here, unlike AUD, NZD cannot count on domestic commodity exports to ease any selling pressure.

## CAD: Jobs numbers to strengthen BoC tapering case

	Spot	Week ahead bias	Range next week	1 month target
USD/CAD	1.2670	Neutral	1.2620 - 1.2800	1.2600

- CAD has managed to survive a tricky week for pro-cyclical currencies as it benefitted from the rise in energy prices worldwide (Canada is a major exporter of natural gas). This may continue to be the case in the week ahead, as more potential hits to risk sentiment and USD strength will likely challenge CAD's resilience again.
- On the domestic side, the focus will be on September jobs data in Canada, which will be released in tandem with the US NFP. We might see a more moderate increase in employment after August's 90k jump, but we expect the jobs report to by and large endorse the recent upbeat sentiment on the Canadian economic outlook, as well as market expectations on more Bank of Canada tightening before year-end. Ultimately, this suggests any headwind to CAD will only come from external factors as domestic drivers are set to remain supportive.

## CHF: Eyes on municipal elections in Italy

	Spot	Week ahead bias	Range next week	1 month target
EUR/CHF	1.0787	Mildly Bearish 	1.0720 - 1.0830	1.0900

- Yesterday's drop in US equities, paired with the lack of positive impact on the EUR from rising eurozone inflation, sent EUR/CHF back below the 1.0800 level, around one-month lows. As the environment may remain challenging for risk assets, the balance of risks still appears tilted to the downside for the pair in the week ahead.
- One story to keep an eye on during the weekend is the slew of municipal votes in Italy, including in the country's four largest cities (Rome, Milan, Naples, Turin). From a market's perspective, it will be interesting to see how the right-wing Eurosceptic parties will fare after the impact of the pandemic and the government reshuffle. A strong result of those right-wing parties may impact the BTP market – and by extension, EUR/CHF – on Monday, although the next general election is still too far away (2023) to see some material build-up of political risk for now. Domestically, the KOF indicator and CPI numbers for September may have only very contained impact on CHF after the SNB gave no reasons to think they will make any change to their current policy mix.

## NOK: Eying 10.00

	Spot	Week ahead bias	Range next week	1 month target
EUR/NOK	10.0200	Neutral	9.9500 - 10.1000	10.0500

- With the highest beta to equity movements in G10, it is no surprise NOK saw high volatility and downside pressure this week. However, NOK has received the same kind of protection offered to CAD and AUD from the rise in energy prices. After all, Norway is an even bigger natural gas exporter than Australia and Canada.
- After today's big move, EUR/NOK is very close to the 10.00 support, and a break below such level could offer some technical push to the krone. Still, the week ahead holds a big deal of uncertainty for procyclical currencies, and we are inclined to think we'll see more weakness emerging in the krone, but, once again, the energy crunch story may offer some shield.

## SEK: Holding pattern

	Spot	Week ahead bias	Range next week	1 month target
EUR/SEK	10.1560	Neutral	10.1200 - 10.2000	10.1500

- The widely-regarded Economic Tendency survey saw a contraction in September, which partly offset the positive news coming from above-consensus retail sales for August. Ultimately, it appears that the Riksbank cautious tone is being ENDORSED by not-so-good data.
- The week ahead should not bring more important data to the table, and EUR/SEK may continue to oscillate within its 10.12/10.22 range as risk sentiment swings do not appear to be providing clear direction to the pair.

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