# G10 FX Week Ahead: The last fireworks

Some profit-taking was likely behind the USD weakness today, but strong payrolls clearly argue in favour of USD strength against low yielders. Given the Independence Day holiday next week, we don't expect any more 'fireworks' for markets, also because the RBA may sound less hawkish than expected. Low volatility may once again be the name of the game in FX

Fireworks

Source: Shutterstock

## DXY: Dollar bulls book profits ahead of Independence Day

| | Spot | Week ahead bias | Range next week | 1 month target |
|---|---|---|---|---|
| DXY | 92.5220 | Mildly Bullish ↗ | 92.0000 - 93.0000 | 92.5000 |

- The dollar has enjoyed a strong start to July and a healthy June nonfarm payrolls release should keep the dollar bid against the low yielders at least. Though the unemployment rate was higher than expected, progress in jobs gains will be welcomed by the Federal Reserve and likely to keep US money market rates biased towards a 2022 rate hike. The sluggish dollar performance on Friday probably owed to profit-taking ahead of the Independence Day holiday and some large FX option expiries.
- US trading will likely be quiet in a shortened holiday week. The calendar is quite light, with the highlight probably being the release of the FOMC minutes on Wednesday evening. Much focus will be given to how the doves and hawks are arguing their cases – especially the seven members casting their Dots for the first rate hike in 2022. Internationally, the focus will be on whether the G20 on Friday formally signs off on new global minimum tax standards. We'll also be interested in Chinese Caixin PMI readings (Wednesday) and inflation readings (Friday). On the latter, investors will examine whether there remains a gulf between the PPI and CPI (9% YoY versus 1.3% respectively), meaning that Chinese policy makers will do their utmost to limit input prices.

## EUR: Time for some better hard data in Europe

| | Spot | Week ahead bias | Range next week | 1 month target |
|---|---|---|---|---|
| EUR/USD | 1.1837 | Mildly Bearish ↘ | 1.1740 - 1.1900 | 1.1900 |

- EUR/USD remains fragile and the better-than-expected NFP headline number will keep open the possibility of a drop to 1.1700. Expect the FOMC minutes on Wednesday to have a big say in how low EUR/USD goes this coming week.
- For the week ahead, the European data calendar is very light, with focus on more investor confidence surveys (Sentix Monday, ZEW Tuesday) and on Wednesday the release of the European Commission's summer forecast round. These presumably should see growth upgrades. Germany will on Wednesday see May industrial production – expected to rebound in line with the better sentiment indicators. Some improvement in the hard data could provide the euro with a little support.

## JPY: More big gains for the GPIF

| | Spot | Week ahead bias | Range next week | 1 month target |
|---|---|---|---|---|
| USD/JPY | 111.36 | Mildly Bullish | 110.80 - 112.20 | 111.00 |

- USD/JPY looks to be taking a breather ahead of multi-year resistance around the 112.20/40 area. It is hard to see US rates coming off too sharply from current levels and USD/JPY may well have built a new floor in the 110.40 area. There may not be enough in the calendar to drive USD/JPY through 112.20/40 in the week ahead – but it should stay reasonably well bid.
- Last week we were focusing on the release of the GPIF annual report and indeed it was very impressive, returning 25% in the Japanese fiscal year to March 21. Portfolio allocation for the world's largest pension fund is always a hot topic and there were some quite big changes in the quarter to March. Foreign bond holdings were cut to 24.6% from 25.7% (was the GPIF behind the 1Q US Treasury sell-off?), while both foreign and domestic equity allocations were cut below the 25% benchmark. The big winners were Domestic Bonds, increasing to 25.9% from 23.6% - a more conservative stance from the GPIF.

## GBP: Still unfussed by the Delta variant spread

| | Spot | Week ahead bias | Range next week | 1 month target |
|---|---|---|---|---|
| GBP/USD | 1.3777 | Neutral | 1.3700 - 1.3850 | 1.4100 |

- It's been a rather eventful week for the pound. The EU granted a delay to the chilled meat ban in Northern Ireland, temporarily calming market concerns about an escalation in trade tensions. Still, it appears that strong political divergences persist and the risk of a new round of tough EU-UK trade negotiations later in the year is very high. Domestically, the Bank of England Governor Andrew Bailey warned against overreacting to "temporary" inflationary pressures, prompting some re-pricing in tightening expectations.
- Overall, the pound has held up better than most of its G10 peers to the dollar's appreciating trend, which also denotes how the market continues to see the recent sharp rise in Delta variant cases in the UK as unlikely to derail the country's economic recovery. Our UK economist explores this topic in this article. In the week ahead, data releases should not be the main drivers, and focus will likely be on another speech by Andrew Bailey as well as any headlines from Angela Merkel's visit to the UK today. As long as the UK government does not suggest that the rise in cases will postpone the reopening further, there are few reasons for the market to turn more bearish on the pound compared to other G10 peers.

## AUD: We don't expect a material hawkish shift by the RBA

| | Spot | Week ahead bias | Range next week | 1 month target |
|---|---|---|---|---|
| AUD/USD | 0.7488 | Mildly Bearish | 0.7380 - 0.7520 | 0.7600 |

- The Aussie dollar was one of the main victims of the dollar rally this week, dropping in line with most pro-cyclical currencies. Now the focus shifts to the pivotal Reserve Bank of Australia meeting on Tuesday.
- Based on recent communications by the RBA governor, there are four main options for the Bank as it is set to re-adjust its quantitative easing: 1) ceasing asset purchases, 2) repeating A$100bn asset purchase scheme for six months and then reviewing, 3) conducting a smaller amount (like A$50bn) of purchases for six months and then reviewing, 4) repeating A$100bn for a longer period than six months. We expect the RBA to go for the second option, which would allow them to steer away from the tapering narrative while adopting a more data-dependent approach. If anything, we see option three as the second most likely, although that would likely be seen by markets as a hawkish shift. We think market pricing is standing somewhere between option two and three, which means that if our base case materialises (A$100bn for six months) the impact on the Australian dollar could be negative. More crucially, we think the RBA will not follow other developed central banks in signalling a rate hike in 2022, and markets may be forced to re-price some of their hawkish expectations, which could also put pressure on AUD.

## NZD: Quiet calendar before 15 July RBNZ meeting

| | Spot | Week ahead bias | Range next week | 1 month target |
|---|---|---|---|---|
| NZD/USD | 0.7000 | Mildly Bullish | 0.6940 - 0.7050 | 0.7200 |

- The Kiwi dollar continues to follow global trends due to a lack of domestic catalysts. This will continue to be the case next week as there are no data releases worth noting in New Zealand until the 15 July central bank meeting.
- A domestic development we still want to highlight is the resilience in housing prices. CoreLogic data showed a 22.8% year-on-year increase in prices in June, up from 20.5% in May. The inability of government measures to effectively curb the housing bubble in New Zealand is one factor that, in our view, continues to argue in favour of an earlier than expected tightening.

## CAD: Time to jump back on the Canadian horse?

| | Spot | Week ahead bias | Range next week | 1 month target |
|---|---|---|---|---|
| USD/CAD | 1.2372 | Neutral | 1.2260 - 1.2430 | 1.2200 |

- USD/CAD has witnessed a classic short squeeze. Like fellow commodity currencies, the toxic cocktail of Fed hawkishness and Chinese commodity intervention has taken its toll on heavily-backed trades. Yet it looks like the Bank of Canada will be well ahead of the Fed in tightening policy and now that the majority of the correction is over, speculators will be looking to reset CAD longs. The 100-day moving average at 1.2430 may be the area to try this.
- Canada's data calendar is light in the coming week – just April retail sales which are expected to fall 5% month-on-month with Canada in lockdown. We will also see the June release for the CFIB business barometer – which may well retest the highs at 68.2.

## CHF: FX transaction data shows the SNB stepping away in 1Q

| | Spot | Week ahead bias | Range next week | 1 month target |
|---|---|---|---|---|
| EUR/CHF | 1.0941 | Mildly Bullish | 1.0930 - 1.0990 | 1.1000 |

- Data released this last week shows that the Swiss National Bank significantly scaled back its FX intervention in 1Q21 to just CHF296mn.  That compares to peak intervention of CHF51bn in 2Q last year. The news was consistent with the SNB CHF sight deposit data and made sense since EUR/CHF was really rallying on its own accord in 1Q21. The same may not be said for 2Q21, however, where EUR/CHF has been under pressure and CHF sight deposit data may imply that the SNB could have intervened to the tune of CHF10bn again to keep EUR/CHF supported.
- There are few standouts in the Swiss calendar in the week ahead, but June FX reserve data released on the 7th could be interesting and add weight to the idea that the SNB did intervene more when EUR/CHF traded under 1.09. Assuming that eurozone hard data delivers on the bullish soft data this summer, we expect EUR/CHF to be trading well above 1.10 ahead of what is shaping up to be an important European Central Bank meeting in early September.

## NOK: Emerging as an attractive buy-the-dip option

| | Spot | Week ahead bias | Range next week | 1 month target |
|---|---|---|---|---|
| EUR/NOK | 10.2300 | Neutral | 10.1200 - 10.2800 | 10.1000 |

- The Norwegian krone has been the worst performer this week, largely due to the fact that it has the highest beta to risk sentiment among all G10 currencies.
- Higher oil prices have so far been unable to counter other external negative factors, but once risk sentiment stabilises, Norway's krone may emerge as one of the most attractive buy-the-dip options in the G10. Much will depend on developments at the OPEC+ meeting (we discussed this in the CAD section), but NOK can also count on one of the most hawkish central banks in the developed world, which should allow it to benefit from a search for carry. Next week, inflation data for June will take centre stage, with the headline CPI set to approach levels close to 3%. This should further endorse the Norges Bank's hawkish stance and offer some support for a recovery in NOK.

## SEK: Riksbank's lower-for-longer to keep appetite low for SEK

| | Spot | Week ahead bias | Range next week | 1 month target |
|---|---|---|---|---|
| EUR/SEK | 10.1600 | Neutral | 10.1100 - 10.2000 | 10.1500 |

- Despite being normally less vulnerable to negative turns in risk sentiment, Sweden's krona has come under a good deal of pressure this week. The Riksbank's rate announcement this week was largely a non-event for SEK, as the Bank reiterated that it will not deviate from its dovish tone anytime soon, despite showing some hints of optimism in its economic outlook (here's our economist's review of the meeting).
- Next week will be very quiet data-wise in Sweden, and should any rebound in activity currencies materialise, we continue to expect SEK to be a laggard as the markets may be inclined to reward currencies (like NOK) that are backed by hawkish central banks.

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