G10 FX Week Ahead: Wary of a false ceasefire in trade wars

The topic of trade wars remains front-and-centre for markets this week, especially after the US trade policy announcements – the latest being a $50-$60bn tariff package on Chinese imported goods – have formally taken us into the realms of a protectionist world.

The implications for markets now rest on how major trading partners choose to retaliate; Beijing's response thus far has been the announcement of a $3bn tariff on imports from the US – though we note this is a response to US steel and aluminium import tariffs and not the latest US tariff package on China.

While weekend reports suggest trade wars may be following a more diplomatic path – with the Wall Street Journal reporting US and Chinese officials are quietly negotiating behind the scenes – we still see good reason for investors to stay wary.

We look for the relief rally in global risk sentiment to be short-lived – with trade war headline risks elevated.

Source: Shutterstock

EUR: US dollar to continue losing out under a 'Cold Trade War'

	Spot	Week ahead bias	Range next week	1 month target
EUR/USD	1.2340	Mildly Bullish	1.2240 - 1.2510	1.2500

- US trade policy remains front-and-centre for global markets this week - especially after the administration announced a $50-$60bn tariff package on China. The focus will be on whether major trading partners choose to materially step-up retaliatory measures against the announced US protectionist policies. While we - and Chinese officials themselves - will be waiting to see the full details of the US tariff measures on Chinese imports, it's clear that Beijing is likely to respond - but potentially in a more diplomatic manner. If so, one could imagine global risk sentiment to stabilise after the knee-jerk move lower in equity markets this week (which was already in motion due to the sell-off in US tech stocks). Trade war headlines remain a watch-this-space.
- In terms of US data, February core PCE inflation due on Wednesday, will the highlight in an otherwise quiet week. A print below the consensus of 1.6% year-on-year may keep the Federal Reserve hawks at bay - and any dovish Fed re-pricing here may, in fact, be supportive of risky assets. The Eurozone data calendar is also fairly light - with only second-tier data releases to keep an eye on. The latter part of the week will shift focus to individual country CPI data with Germany due on Thursday. EUR/USD neutral-to-higher in a weak dollar environment.

JPY: Looking for USD/JPY to stay anchored around the 105 level

	Spot	Week ahead bias	Range next week	1 month target
USD/JPY	104.80	Neutral	103.80 - 106.30	103.00

- With global trade wars in focus - and the yen the antithesis of US protectionist policies - expect the downward bias for USD/JPY to remain firmly in place. While we retain a target of 100 by year-end - we see heightened risks of this being crossed much sooner, while any escalation in the trade war - a broadening of US tariffs to other countries/sectors, seeing a more pronounced move lower into the 90s territory.
- The Japanese data focus will be on CPI, retail sales and industrial production. All of this is likely to play second-fiddle to the global risk environment. Look for USD/JPY to stay anchored around the 105 level in the absence of a further major downturn in global equities (a negative USD bias from White House policy uncertainty to cap upside in USD/JPY). Tail risk next week could be a sharp slide to 102.50 if global risk-off prevails.

GBP: Scope to be a relative G10 outperformer in a 'Cold Trade War' environment

	Spot	Week ahead bias	Range next week	1 month target
GBP/USD	1.4140	Neutral	1.3980 - 1.4350	1.4300

- All the cards needed to fall into place for GBP to breakout higher over the past week - and they pretty much did. The agreement of a Brexit transition deal, constructive UK macro data including a positive wage growth surprise and a hawkish Bank of England meeting with two dissenters voting for an immediate rate hike - all provided a mini-boost to the pound. Comments by BoE policymaker Vlieghe that we may see one or two rate hikes a year in this tightening cycle gave implicit support to a steeper UK rate curve - and should help GBP remain at these elevated levels under the status quo.
- In a quiet week for UK data - with only consumer confidence and the final reading of 4Q GDP to note on Thursday - GBP's near-term direction of travel will be a function of the trade war-driven global risk environment. Limited escalation and a stabilisation in the equity market sell-off could see GBP/USD push modestly higher towards the 1.4250-1.4300 post-Brexit highs. Indeed, we think GBP could be a relative G10 outperformer over the coming months amid a positive re-appraisal of short-term UK economic and political risks.

AUD: Falling iron ore prices add a layer of fundamental weakness

	Spot	Week ahead bias	Range next week	1 month target
AUD/USD	0.7710	Neutral	0.7630 - 0.7810	0.7800

- The US imposition of a $60bn tariff package on China may see AUD trade with a negative bias (more so relative to the other G10 FX) in the near-term - not least given it's high exposure to the China trade story. However, in the absence a material downturn in global risk - for which we would require an escalation in tariffs from either the US administration or affected trading partners (namely China) - we would look for AUD/USD to remain supported after the latest correction down to the 0.77 level.
- Australian data likely to play second-fiddle in the near-term, while our commodities team believe the sharp downward adjustment in iron ore prices - which has partly fuelled a softer AUD via the terms of trade channel - may find a base soon.

NZD: Set to stay resilient amid the global trade war fears

	Spot	Week ahead bias	Range next week	1 month target
NZD/USD	0.7240	Neutral	0.7150 - 0.7350	0.7200

- While the Reserve Bank of New Zealand policy statement last week was less dovish than markets anticipated - although policymakers did flag that domestic inflation may weaken further in the near-term - the NZD bounced sharply higher following the RBNZ meeting. The recovery came despite an escalation in global trade wars and a mini-rout in global equities - and may resemble some sort of 'flight-to-quality' sentiment for the currency.
- With only second-tier New Zealand trade data due Monday, we look for NZD/USD to consolidate in the 0.7150-0.7350 range given the cautious global risk backdrop. However, the NZD may perform well in the G10 commodity space given AUD and CAD are more directly exposed to a US-led trade war.

CAD: Volatile US trade policy makes chasing a hawkish BoC story somewhat unappealing

	Spot	Week ahead bias	Range next week	1 month target
USD/CAD	1.2880	Neutral	1.2720 - 1.2970	1.2700

- After Canadian inflation surprised to the upside, with the average core CPI reading now above the 2% mid-point of the Bank of Canada's target range for inflation, the focus this week will be on January GDP data due on Thursday. Activity data has been lacklustre in recent months - as shown by the softer than expected retail sales figures last week (+0.3% MoM vs +1.1% consensus).
- With the situation around NAFTA and US trade policy still extremely volatile, there is still a high bar for the BoC to raise rates again in May (currently 60% priced in) - and we think a wait-and-see policy approach may be more appropriate unless the near-term data is screaming out for an immediate rate hike. While we believe USD/CAD's gravitational pull is towards the low 1.20s under a scenario where we don't get a NAFTA break-up this year, we doubt investors will be chasing a move lower on any near-term BoC story. Look for USD/CAD to stay supported above 1.2700-1.2800 in a nervous global risk environment.

CHF: Bound by the strong EUR/CHF 1.1750 resistance level

	Spot	Week ahead bias	Range next week	1 month target
EUR/CHF	1.1700	Neutral	1.1630 - 1.1750	1.1800

- Given the challenging risk environment and soft equity markets, any EUR/CHF upside is fairly limited and likely to be bound by the strong resistance level of EUR/CHF 1.1750.
- On the data front, the focus will be on the regular sight deposit data due today and various economy surveys throughout the week, but this should not affect CHF in any way.

SEK: Threat of global trade wars exposes a fragile SEK

	Spot	Week ahead bias	Range next week	1 month target
EUR/SEK	10.1600	Mildly Bullish	10.1000 - 10.3000	10.3000

- SEK is one of the most vulnerable G10 currencies to the escalating trade war and its material underperformance last week provided a case in point. Expect a modest downside risk to SEK with EUR/SEK drifting above the 10.20 level.
- While we expect Swedish February retail sales due on Wednesday to improve, the consensus is overestimating the rebound, pointing to downside risk to SEK. We also believe that Economic Tendency Survey may be softer, also pointing at higher EUR/SEK throughout the week.

NOK: Some calm after the hawkish Norges Bank meeting

	Spot	Week ahead bias	Range next week	1 month target
EUR/NOK	9.5800	Neutral	9.5000 - 9.6220	9.5000

- It's a fairly quiet week on the Norwegian data front. Last week we saw the anticipated correction in EUR/NOK higher after Norges Bank induced NOK gains suggesting a further EUR/NOK upside is limited from here in the absence of material deterioration in risk appetite.
- February retail sales due on Wednesday should have a limited impact on NOK. Expect EUR/NOK to range trade.

Author

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

Disclaimer