

If the euro's on the way up, where's the dollar heading?

Fool me once over US tax reforms, shame on you; fool me twice..



Mixed messages for the dollar

The US dollar's luck seems to have run out as investors have been dealt yet another reality check on the prospects of tax reforms being swiftly implemented and signed into law. President Trump's social media feud with senior Republican Senator Bob Corker somewhat sums up the ongoing struggles the White House faces in pushing its ambitious policy agenda through a sceptical Congress. Plus, the administration's policy schizophrenia – with the focus intermittently changing between trade, healthcare and taxes – means that it's almost impossible for us to factor in any meaningful fiscal stimulus into our USD outlook.

While on paper tax reforms may be great for the dollar (though we have our reservations here now), the reality is that chasing this story has proved to be an unprofitable strategy this year. We don't expect this to change anytime soon and think the USD remains a sell-on-rallies. On the topic of Trump policies, it's worth noting that the President is reportedly set to unveil NAFTA proposals that may 'throw the deal into peril'. We think this is a case in point for staying cautious over the dollar in the medium-term. It would be remiss not to mention the September FOMC minutes today (1900 BST), but for some time now our motto has been that the Fed remains merely a subplot for the USD. If anything, the minutes will show the current dichotomy within the Fed on big-picture

issues related to the US economy. Such mixed messages are why we think markets will remain sceptical over pricing in a steeper US rate curve.

EUR: The window of opportunity for an ECB-led rally may now be open

The move by Catalan leader Carles Puigdemont to 'suspend' the referendum result is being seen as a conciliatory outcome. We've noticed a trivial relief rally in the EUR and think this may just be the start of a two-week window of EUR strength ahead of the big October ECB meeting. While political uncertainty hasn't fully faded, we see the focus for the currency turning back to the positive cyclical eurozone economic story and prospects of a more hawkish ECB QE taper announcement later this month. Certainly, our house view for a drop to €20-25bn monthly QE purchases from January 2018 (albeit for slightly longer) could see a one-off move higher in EUR pairs.

As for Scandi FX, the focus today will be on central bank talk. Deputy Governors at both Riksbank and Norges Bank are scheduled to speak and may shed some light on the respective central banks next policy moves. Of the two, it is Riksbank that is likely to turn hawkish first and this policy divergence story could easily see NOK/SEK testing parity very soon. A potential catalyst is Swedish CPI tomorrow.

CNY: Returning from the Golden Week holiday with a spring in its step

The Chinese yuan has returned from the Golden Week holiday on fire as solid Chinese macro data maintains the current optimism over the economic outlook. Comments from PBoC Governor Zhou hinting at a near-term easing of capital and currency controls have also helped fuel investor sentiment. Indeed, ING's Iris Pang notes ahead of China's 19th Congress next week that while we don't expect any exact details on RMB internationalisation reforms by the authorities – if the announced economic growth target is around 6.5%, then this still gives a sturdy fundamental background for CNY appreciation. A wider trading band post-Politburo is likely to support our view that USD/CNY could creep lower towards 6.40 by year-end.