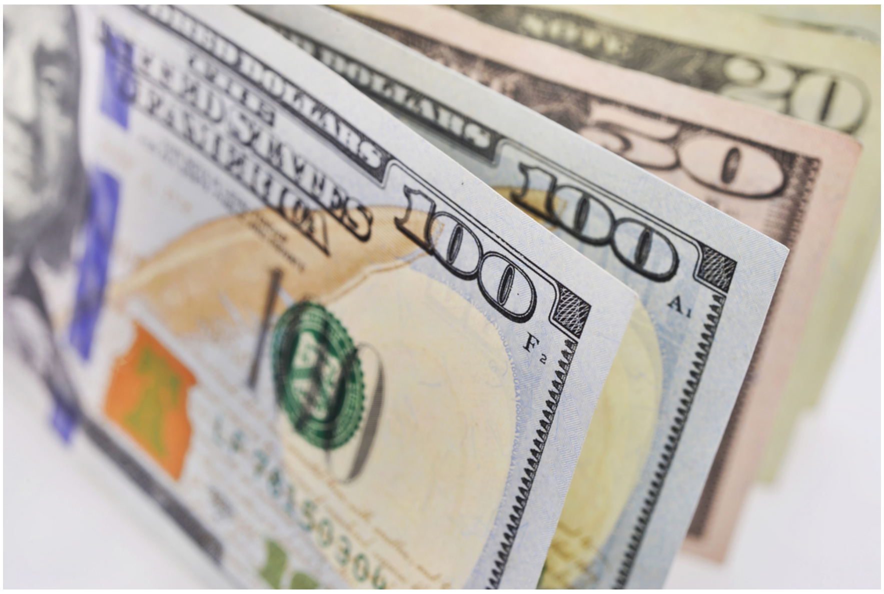
Inflation, Where Art Thou?

Looking beyond Jackson Hole, the focus next week will be on whether US data can inject some life into the dollar. Missing US inflation, however, is set to remain in the shadows.



Theme of the week: Missing inflation to remain in the shadows

Assuming the speeches at Jackson Hole don't derail asset markets, the theme for next week should continue along the lines of growth without inflation. In particular, Friday's US NFP headline figure should be robust enough (we forecast +160k) to maintain US 3Q17 GDP expectations near 3% annualised, while 2 extra working days in August should keep wages steady near 2.5% YoY. Following a strong set of European manufacturing confidence data this week, investors should see the glass as half – if not three-quarters full and continue to favour activity currencies and the carry trade – marginally at the expense of the dollar.

ING's Bert Colijn expects Eurozone inflation data next week (Thursday) to have remained weak in August, with the headline figure unchanged at 1.4% and core inflation remaining stable at 1.2%. A continuation of the current subdued inflation environment will no doubt be disappointing to the ECB and makes it increasingly likely that Mario Draghi keeps his cards close to his chest at Jackson Hole tonight. Given the mixed backdrop of improving growth and questionable inflation, we expect any tapering announcement in Autumn will be along the lines of a one-off reduction in monthly purchases to EUR 30 billion - that could last at least until June and further stretched limits on what the ECB can buy. A more flexible and open-ended ECB tapering may present greater two-way risks to markets and could come as a slight disappointment to those looking for another near-term move higher in the EUR.

Majors: Relative US-EZ inflation dynamics in focus

Next week will provide a stock take on US and Eurozone inflation dynamics, which will play a key role in both the Fed and ECB's near-term policy decisions

EUR: Hard to keep a good currency down

- Assuming Jackson Hole doesn't ignite too many fireworks, expect the benign market conditions to extend into next week and the EUR to remain supported. On the US side, a slightly lower nonfarm payrolls release in Friday's jobs report (we see +160k) is unlikely to dent the growth story, although our economists expect wage inflation to remain subdued.
- While Thursday's release of flash Eurozone CPI should portray a still subdued pricing environment, we doubt the EUR has to correct much lower. After all the risks of a US debt ceiling impasse seem to be growing, while the Eurozone macro story - which backs an eventual ECB tapering - remains firm.

		Week ahead bias	Range next week	1 month target
EUR/USD	Spot ref: 1.1820	Mildly Bullish	1.1750-1.1900	1.18

JPY: Moving lower on fading risk-off sentiment

- A mixed bag for US data next week might not spell massive USD upside, but when combined with a more stable global risk backdrop, we still expect the upside bias in USD/JPY to persist. Political risks in the US are likely to prevail, especially as we approach the debt ceiling limit later next month. But without an escalation of US or geo-political risks, it's hard to see safe-haven JPY demand continuing.
- While the uptick in August Tokyo CPI was encouraging for next month's national release, we note that inflation around 0.5% still remains well below the Bank of Japan's over-optimistic, and not very credible, 2% inflation target. Still, our economists believe that Abe and Kuroda's dogged efforts to achieve this are unlikely to be slackened anytime soon, making BoJ policy normalisation a far-distant reality.

		Week ahead bias	Range next week	1 month target
USD/JPY	Spot ref: 109.70	Neutral	109.00-110.80	113

GBP: Lacking a catalyst to break the negative psychology

- GBP is trading with a very negative psychology and at a disconnect with short-term financial variables, which may be justified given the string of domestic political and Brexit event risks over the next few months. However, any further idiosyncratic GBP selling could be seen as excessive now, with the current risk premium about right relative to the political risks at stake.
- It is worth noting that evidence of any GBP-specific risk premium is less prevalent in GBP/USD given that we have two politically paralysed currencies offsetting each other. Still, we are in need of something to break the current bearish GBP mentality; uneventful Brexit talks and a light week for data, with only consumer confidence (Thursday) and manufacturing PMI (Friday) of interest, are unlikely to provide the positive catalyst that GBP seeks.

		Week ahead bias	Range next week	1 month target
GBP/USD	Spot ref: 1.2830	Neutral	1.2780-1.2890	1.26

Dollar bloc: Missing global inflation may support G10 high-yielders

Lack of developed market inflationary pressures and limited upside in global bond yields could see a recovery in carry sentiment after a bleak August

AUD: Will Australia catch a bout of the political plague?

- The 2Q construction work done and private capex data (Thursday) will be the standout releases in a quiet calendar next week. While the RBA expect some pickup in non-mining business investment, the central bank may have to wait for any convincing evidence of this. A 'lowflation' economy is pretty much priced into the AUD curve, meaning any disappointing investment data next week - and possible downside risks to 2Q GDP - should have a limited negative impact.
- Our economists note that Australia may face a period of political uncertainty if the High Court rules against the parliamentary eligibility of seven lawmakers with dual citizenship. With a wafer thin coalition majority, much hangs on whether the High Court rules against Deputy Prime Minister Joyce, and requires him to stand in a special by-election. In any event, the chaos surrounding this issue is hurting the Turnbull government. AUD markets remain unmoved for now, but political vultures are beginning to circle.

		Week ahead bias	Range next week	1 month target
AUD/USD	Spot ref: 0.7910	Mildly Bullish	0.7840-0.7990	0.76

NZD: Cooling housing market easing RBNZ rate hike tail risk

- August QV house price data (Thursday) will be of domestic interest given signs of the New Zealand housing market losing steam. A further slowdown in house price growth (prior 6.4% YoY) would be a thumbs up to the RBNZ's macro-prudential policies put in place last year.
- From an NZD perspective, we note that this story reduces any tail risk of near-term rate hikes to address any financial stability concerns - which arguably may have been behind the Bank of Canada's recent hawkish shift. Supportive evidence for a wait-and-see RBNZ policy bias is likely to contain any domestically-generated NZD upside in the near-term. 2Q terms of trade data also due next week (Thursday) and we would expect growth here to slow given the recent price dynamics in the domestic dairy markets.

		Week ahead bias	Range next week	1 month target
NZD/USD	Spot ref: 0.7220	Mildly Bullish	0.7170-0.7320	0.71

CAD: Strong Canadian 2Q GDP already baked in the cake

- Ahead of the early September Bank of Canada (BoC) meeting, the focus will be on Canadian 2Q GDP data next week (Thursday). Market consensus is for a release in the region of 3.0-3.5% QoQ annualised, which would be slightly above the BoC's forecasts. Our economists note that growth has been very broad-based so far in 2017, which is encouraging, although the sub-2% inflation backdrop and the growing list of uncertainties (US politics and NAFTA) are reasons to remain cautious.
- With markets pricing in a 65-70% chance of an October BoC rate hike, any good news on the Canadian growth front is arguably already priced in. Of greater market importance may be the more forward-looking data releases, with July industrial production (Tuesday) and August manufacturing PMI (Friday) also due next week.

		Week ahead bias	Range next week	1 month target
USD/CAD	Spot ref: 1.2510	Mildly Bearish	1.2410-1.2580	1.30

EUR crosses: Questioning the Riksbank's credibility

Widening bond spreads in Sweden suggest the market is finally starting to question the Riksbank's credibility, while the focus for NOK turns to upcoming elections

CHF: Benign conditions to keep Swiss offered

- Unless Yellen and Draghi surprise hawkishly at Jackson Hole (seems unlikely) the risk environment should remain benign and CHF should stay offered. Here we note with interest the CHF20bn decline in domestic CHF sight deposits since June - perhaps suggesting some exodus from CHF.
- Swiss data next week sees KOF business confidence on Wed - picking up - but nowhere near the German IFO levels. Thus SNB can continue to take a back seat and allow EUR/CHF to drift higher on the ECB tapering story.

		Week ahead bias	Range next week	1 month target
EUR/CHF	Spot ref: 1.1390	Mildly Bullish	1.1350-1.1450	1.16

SEK: Bond market vigilantes arrive

- It seems the market is finally starting to question the Riksbank's credibility, now that core inflation and 5-year inflation expectations are running above the Riksbank's target. 10-year Swedish-Bund spreads have widened sharply and may give cause for the Riksbank to reconsider its super dovish stance.
- Swedish data next week is retail sales (Monday), Economic Tendency (Wednesday) and manufacturing PMI (Friday) - all of which should be positive. The case continues to build for a re-assessment of Riksbank policy, warning that complacency on EUR/SEK may be broken at any time by a drop below 9.45/47 support.

		Week ahead bias	Range next week	1 month target
EUR/SEK	Spot ref: 9.4970	Mildly Bearish	9.4700-9.5400	1.16

NOK: September election focus increasing

- NOK looks to be strengthening on slightly firmer oil prices, but also stronger than expected 2Q17 GDP growth - which plays a role in the forthcoming Sep-11 general elections. Better growth will support the incumbent centre-right coalition, which favour reform/smaller govt.
- Opinion polls also seem to be moving against the largest single party, the opposition Labour party. A few months ago, expectations were that Labour could build a centre-left, Red-Green coalition to unseat the current govt. Any polls this week showing further support for centre-right could help NOK.

		Week ahead bias	Range next week	1 month target
EUR/NOK	Spot ref: 9.2350	Mildly Bullish	9.2000-9.3000	9.15

Author

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

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