

Our summer of discontent

We expect investors to stay on the defensive over the coming months, as trade tensions escalate and political uncertainty weighs



USD: Trade wars, politics and higher US rates make dangerous cocktail

2018 is fast becoming the year of squandered opportunities for world growth. A fully-fledged trade war, major political risks and what looks to be a Federal Reserve wanting to take rates to neutral and beyond will prove substantial headwinds to growth. Over the near-term, the focus will be retaliatory tariff measures from the EU. As the second-largest economy in the world and with a population twice the size of the US, the EU will be less intimidated by President Trump than some. However, ahead of November mid-term elections, there is every likelihood that Trump will raise the stakes with proposed tariffs on the European auto sector, whose exports to the US are five times as large as the steel and aluminium sector. Trump will feel he has a stronger hand given the relatively closed nature of the US economy (the US vastly outperformed the eurozone in 1Q18) and the tailwind of fiscal stimulus. Which brings us to the Fed. In an articulate speech yesterday, former Fed dove Lael Brainard said the Fed's forward-guidance language 'is growing stale' – perhaps laying the groundwork for a hawkish shift in the FOMC statement 13 June. Add in unsettled politics in Europe and what should be a big win for the left in the Mexican Presidential election 1 July, we expect investors to stay on the defensive this summer. In FX that means the Japanese yen should do well on the crosses with the dollar staying strong. For today, we look for 0.3% month-on-month

growth in US hourly earnings (nonfarm payrolls due out at 13:30 BST), which could prove a slight dollar positive. DXY to trade 94-95.

EUR: Some stability in Italy, focus switches to Spain

The euro has found some stability after the Italian populists managed to form a government. The good news for the euro is that the populists did respond to market discipline. The bad news is that the new government will be on a collision course with Brussels, focusing the minds on what concessions, if any, EU leaders have for Italy at the June summit. For today, the focus switches to Spain where the removal of Spain's prime minister now looks a formality in a no-confidence vote. Euroscepticism is less entrenched in Spain than in Italy, but uncertainties about a weak Spanish government won't help the current mood. Charts suggest EUR/USD could have put in a significant low at 1.1510 this week, yet macro events suggest the bounce to 1.1720/1850 will be weak & vulnerability remains.

GBP: Manufacturing confidence coming off the boil

Sterling is performing poorly, failing to hold gains against a beleaguered euro. Trade trends won't be helping. Manufacturing confidence could dip today and if the dollar stays strong, we may consider a 1.31 scenario.

Asian FX: Holding up surprisingly well

We're surprised at how well Asian FX is holding up given the uncertain trade environment. Perhaps it's because equity investors have to invest somewhere.

Author

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

chris.turner@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10

Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.