Turkey: Saved by the bell

Turkish policymakers have bought themselves some time but caution reigns as the White House keeps the pressure on and S&P gets set to downgrade Turkey's sovereign credit rating

Source: shutterstock

USD: Tariffs start to bite for US but troubles elsewhere keep USD aloft

'We're in the early innings' of a genuine economic boom is the message White House economic advisor Larry Kudlow delivered to President Trump's cabinet yesterday. This may have been a bit of an oversell. If we were to use a baseball analogy, the US economy is at best like a 'change-up' – it has slower 2% trend growth that is made to look deceptively faster by a short-term fiscal boost and low base effects. In fact, if there wasn't this ample degree of geopolitical noise bubbling in the background, we would be increasingly confident that the cyclical USD macro dynamics peaked in 2Q18. Leading US activity indicators have been coming off the boil in the past month (we note the sharp drop in the Philly Fed index yesterday) – while US import and export price data earlier in the week also showed that the economy may be starting to feel the bite of Trump's tariff war. In normal conditions, this may have weighed on the dollar more explicitly. But for now, troubles elsewhere are keeping the greenback aloft.

TRY: White House puts pressure on Ankara while FinMin buys time

All the noise from Turkey's Finance Minister Berat Albayrak appeared to be on the right lines in terms of reassuring global investors that Ankara remains credibly committed to addressing the country's inflation problem – and in the status quo free-market spirit. In effect, Turkish policymakers have bought themselves a bit of time – at least until early September, when markets will be expecting to see some sort of joint fiscal and monetary tightening in the Medium-Term Economic Plan. While we did see Turkey's sovereign CDS rally following the FinMin's investor call, the lira failed to push on much further beyond 5.75 – as markets had largely priced in a conciliatory outcome. S&P is due to downgrade Turkey's sovereign credit rating today – but again this is in the price of the currency. Expect TRY to tread water – with US-Turkey relations on a knife-edge, as the White House said it may increase sanctions. Next week's market holiday will offer some respite.

EUR: Eurozone current account to confirm exodus of equity flows

The final headline eurozone CPI reading for July is expected to nudge up to 2.1% year-on-year – but with core CPI set to stay at 1.1% YoY, we suspect the release is likely to be ignored. The ECB's balance of payments data doesn't typically grab the market headlines, though we will get a full picture for how net eurozone portfolio flows fared over 2Q18. The main story here will be the hefty exodus of eurozone equity portfolio investment – which has been the primary dragging force on the euro since April. Judging by ETF flows, outflows have continued throughout the current quarter – with overseas investors this week turning to euro-hedged eurozone equity ETFs. This suggests greater market uncertainty over the euro's broader direction of travel – which makes sense given that the political situation in Italy and Turkey still look precarious. EUR/USD closing below 1.14 will confirm the bearish theme.

CAD: Canadian data the only bright light

Watch out for Canadian inflation data today – which is likely to show headline CPI at 2.5% and core CPI at 2% (the midpoint of the Bank of Canada's target range). Nafta breakthrough hopes were also given fresh impetus by US Trade Representative Robert Lighthizer yesterday. However, general fatigue over this story means that the Canadian dollar will take its cue from geopolitics, oil and domestic data for the time being. Two out of three here are weighing on CAD. Solid data could send USD/CAD to 1.31

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