

USD: Not so fast

An agreement between the US and Mexico has raised hopes that the US and China can also strike a deal on trade. But it's too early to signal the all-clear



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➔ USD: Mexico move supports risk, but it looks too early to signal all clear

The announcement on Friday evening that fresh US tariffs on Mexico have been 'indefinitely suspended' has supported risk assets. The assumption here is that this move demonstrates the pragmatic nature of US trade policy and raises expectations that Presidents Trump and Xi could find some room for accommodation when they meet at the G20 summit on 28-29 June. However, Mexico is not China and investors will want to see some clear signs of improvement in US-China relations before increasing exposure to risk assets. Before then the market is left focusing on: (a) poor Chinese import figures for May (-8.5% year-on-year) and (b) USD/CNH pressing the 6.95/96 area again as speculation builds over whether the People's Bank of China allows USD/CNY to trade through 7.00. Some caution on emerging markets is therefore warranted and creates a mixed environment for the dollar. With regard to easier Fed policy, there are no Fed speakers this week (ahead of the 19 June FOMC meeting) and data highlights this week will be the May readings for CPI (Wed) and Retail Sales and Industrial production (Friday).

➔ EUR: Is this the big turn?

Soft nonfarm payrolls data sent EUR/USD above 1.13 on Friday and it's certainly tempting to think this is the start of a major turn-around in the dollar. Holding us back from that conclusion is the fact that: (a) markets already discount substantial Fed easing and rate dollar differentials may not substantially narrow from here and (b) the ECB was very close to easing last week. We suspect that EUR/USD finds it tough going on the upside (perhaps limited to the 1.1350/1400 area) and could easily sink back to the 1.1250/60 area. It's a quiet week for eurozone data, thus the EUR/USD trend should be driven by the US trade/activity story.

⬇ GBP: Tory leadership ballot begins on Thursday

The Tory leadership ballot begins this Thursday and at present it looks that the roster of 11 possibles will be whittled down to Boris Johnson and Jeremy Hunt. Front-runner Johnson continues his battle with Brussels, extolling the benefits of retaining the £30 billion+ payment of the divorce deal in the event of a No Deal. EUR/GBP to 0.8940.

⬇ CNY: 7.00 remains in the frame

The renminbi has stayed quite soft over recent weeks, despite the prospect of Fed easing and Washington sounding a bit more pragmatic on trade. Look out for a speech from Larry Kudlow, Director of the National Economic Council, at the Peterson Institute on Thursday for clues on US trade policy. Until then, USD/CNH risks testing last year's high at 6.98.

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