

## What the State of the Union means for the dollar

President Trump delivers his State of the Union address later today. For investors, there are two specific points of interest



US President Donald Trump

### ➔ USD: Two points of interest in the State of the Union

President Trump delivers the State of the Union address today, with the focus on (a) comments on trade policies; (b) the outlook on the wall on the Mexico border and potential use of emergency power to build it. On the former, we don't rule out more optimistic comments given previous hints at the summit with President Xi. After the government shutdown, President Trump is likely to seek policy wins. On the latter, such an announcement would be modestly negative for risk (as it would risk further escalation between Democrats and the President), yet we don't look for a commitment to this today. Instead, we think it's more likely to be used as a threat. Elsewhere, the US ISM non-manufacturing survey for January should remain solid and within expansionary territory. This should be positive for the current risk friendly environment (solid US data, yet cautious Fed) and support emerging market FX vs the US dollar.

### ⬆ EUR: Another soft number from the real economy

We look for soft December eurozone retail sales in line with the trend of generally weak eurozone data of late. This should further cement the cautious ECB approach, particularly in light

of headline CPI declining further below the 2% target. As a result, the euro's participation in the current Fed-led risk rally is likely to be rather shallow. The euro's upside vs the US dollar should be fairly limited due in part to its negative depo rate, and there is a risk of the euro being used as a funding currency for emerging market FX longs.

### ⬇️ **GBP: Weak Services PMI in line with the trend**

Given the disappointing UK January manufacturing and construction PMI surveys, we see downside risks to the January services PMI today. This is largely due to firms seeming to take a more conservative approach to Brexit planning. We see modest downside risks to sterling today, with EUR/GBP testing the 0.8790 level, though the key driver for sterling is the Brexit negotiations. Here, we see it as unlikely that Prime Minister Theresa May will achieve any concessions on the backstop during the upcoming negotiations with the EU, with Parliament likely to propose further amendments next week.

### ⬇️ **CZK: Soft Dec retail sales to help the case for no CNB hike in February**

Our economists expect December Czech retail sales to show negative growth following the significant decline in new car sales. This should further support the view that the Czech National Bank is to remain on hold this Thursday. Look for some modest downside to the Czech koruna, with EUR/CZK moving above the 25.700 level. As per 2019 FX Outlook, we maintain a low conviction on CZK, given the cautious CNB and the still saturated long positioning. Our top central and eastern Europe pick for 2019 remains the Hungarian forint due to central bank policy normalisation and stretched short positioning.