Opinion | 28 January 2019

Uneasy calm

The dollar looks weak against Asian FX and the majors. Over time, there is a very good chance that it will go weaker still against Asian FX. But the chance of a final market-busting hurrah remains. Here's how...

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Continued trade progress

Progress on trade negotiations, we are told, is ongoing. That is reason number one for taking a relaxed attitude to risk and holding any Asian currency except the USD. That trade progress may be supported by a foreign investment bill being discussed by China's NPC Standing Committee today, which will support US calls for China to open up its markets, and some further USD weakness.

At the same time as all this is going on though, the US, according to Bloomberg Daybreak, is charging Huawei with bank fraud (amongst other things) and it feels like the US is treading a dangerous path in seeking difficult concessions on one hand, whilst vigorously pursuing Huawei on the other. I'm not questioning the legal processes underway, but the timing could be better, just as the US and Chinese negotiators settle down to pivotal talks with just one month until the end of the trade truce. From March 1 onwards, assuming that China does get granted an extension to the truce (I don't expect it to be more than that), the scope for some pushback and worsening of the trade backdrop will rise. Markets may simply digest any March announcement and decide that it lacked substance on reflection. With it, the dollar's fortunes may also get revised.

Too much data

It will be hard to cope with the slew of US data scheduled for release today and over the coming weeks. Durable goods, trade balance, home sales, home prices, inventories, retail sales, building permits. It will be harder still to disentangle the signal from the noise of the government shutdown. Is weakness really weakness? The estimates of the hit to GDP (the data release of which may well be delayed because of the shutdown) abound. These are also weighing on Fed views, which are already primed for inactivity.

Adding to the sense of lassitude on rate policy, Arch-dove, Narayana Kocherlakota (and former Minneapolis Fed President) is arguing for rate cuts, not hikes, and for renewed net asset purchases by the Fed. We doubt Fed Chair Jerome Powell will feel the need to go this far after his FOMC press conference on Thursday, but he will most likely feel obliged to reiterate the message of caution expressed late last year, and which has provided the market with a much more benign Fed outlook than the one suggested by the dot-plot. All this is currently in the price.

But in case you were getting taken in by talk of recession and Fed easing, and assuming that this is is a one-way bet for Asian FX this year, don't forget, parts of the US economy are still red hot - the labour market in particular. We may not see that in this Friday's labour report, as the shutdown will likely have taken its toll. But in a month from now, this may, along with a revised view of trade, provide Fed expectations and the dollar with a further upwards boost before more data and sentiment take over.

Asia - quiet

Asia is pretty quiet in contrast to the US and will provide little cause to review currency or rate forecasts one way or the other today. New Zealand trade, already released, has remained fairly resilient in the face of global trade concerns, with December exports only fractionally undershooting expectations and imports only straying a bit below the consensus too. This leaves the December trade balance a small NZD264m surplus. This isn't enough to excite the FX markets, and both NZDUSD and AUDNZD are ignoring this data.

NAB business conditions and confidence due out shortly, have been trending down in recent months. A further decline may tilt down the balance of expectations for the Australian economy which is perched precariously between a strong labour market and rising wages, and a weakening housing market and deteriorating business outlook. One way to rationalise the dichotomy is that the labour market, and wages in particular, are the more lagging parts of the economy. These indicators may still be on an upward trend as the economy turns over. We'll let you know where our view lies just once we prise ourselves uncomfortably off the fence. For now, flat seems the safest call for the economy and the Reserve Bank of Australia.

And this from Prakash Sakpal on the Thai production data due out later this morning: The only other Asian economic data due today is Thailand’s manufacturing data for December. This will help us to fine-tune our GDP growth estimate for 4Q 2018. Coming on the heels of a steeper export contraction last month, this data is poised to provide a negative surprise to the consensus view centered on 0.6% YoY growth (prior 1%). The ING forecast is -1.0%. However, the low base effect is likely to have aided a slight pick-up in GDP growth to 3.5% in 4Q18 from 3.3% in the previous quarter. We are wondering why the Bank of Thailand even bothered to tighten the policy in December. We aren't expecting any move this year.

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