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Weekly Report

G10 Weekly FX Update

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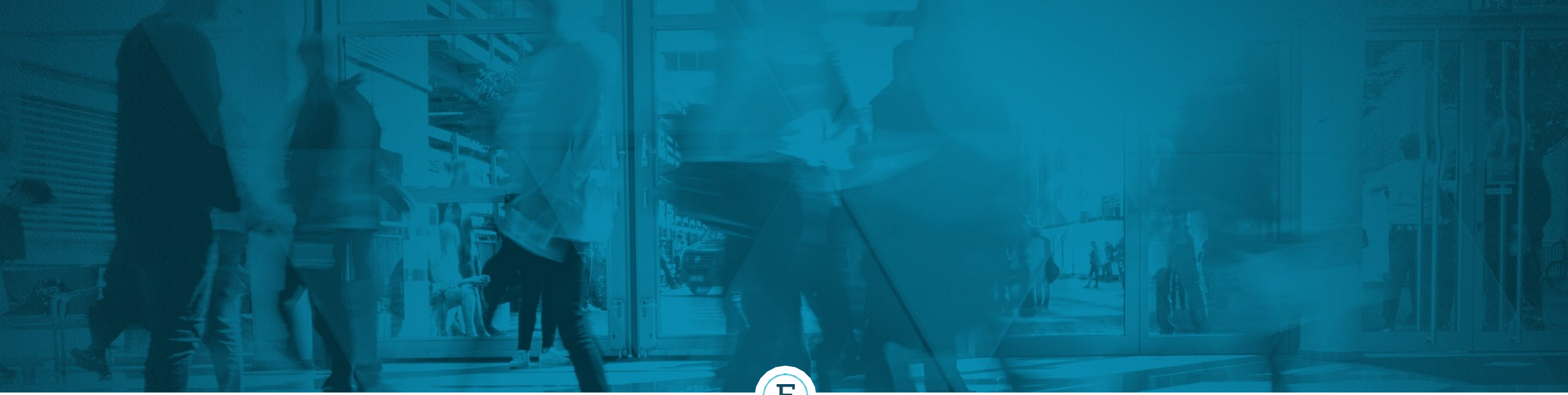
11th September 2023



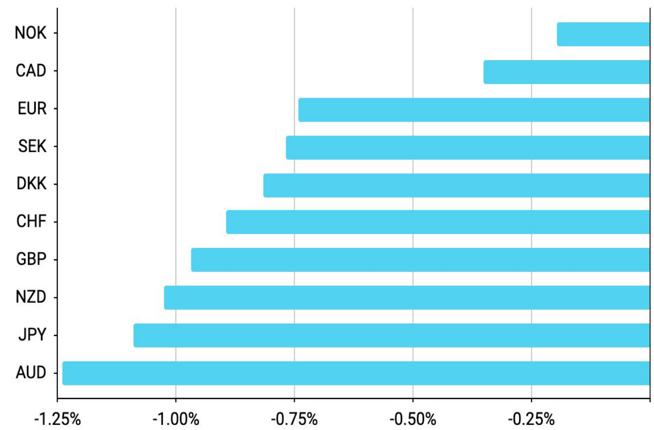
Dollar rises again as US economy continues to outperform

The US economy continues to defy the global downturn, and the dollar is reaping the benefits.

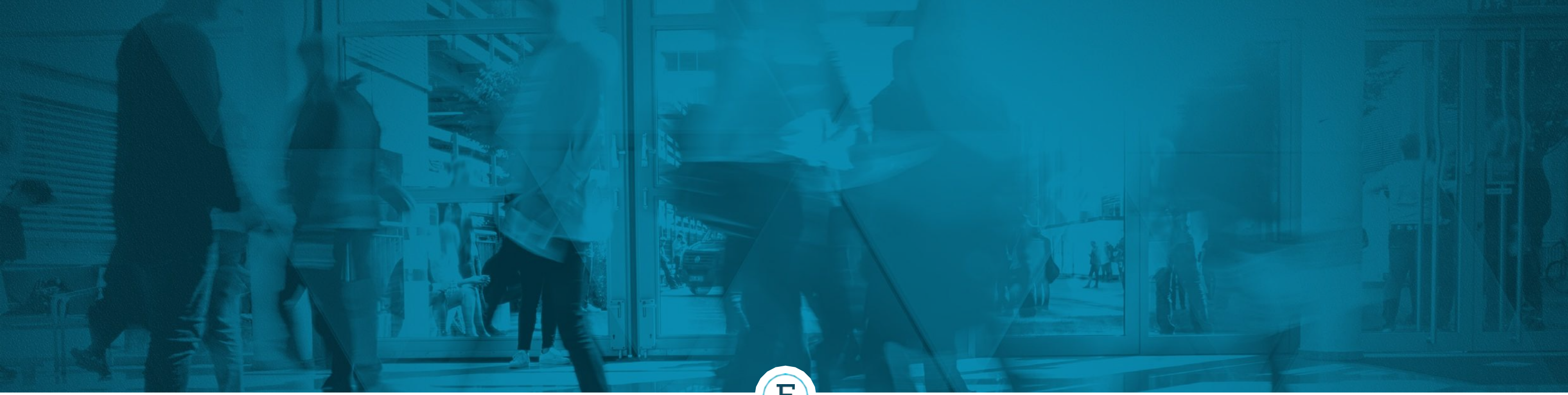
Dismal July data from German factories and more jitters about the Chinese downturn slammed equities worldwide, but US Treasury yields marched higher anyway. Not surprisingly, the dollar benefited from these worries, particularly since the US economy is so far shrugging off economic weakness elsewhere, and high-frequency data there are surprising to the upside more often than not. Almost every major currency lost ground against the greenback last week.

This week is shaping up to be a key one for financial markets. On Wednesday, we get possibly the most important single economic report worldwide, the August CPI inflation data out of the US. The recent gains in energy prices worldwide probably mean we will see a rebound, though, as always, the core index is more important. On Thursday, the ECB will hold its September rate-setting meeting. The ECB's decision is finely balanced as the central bank navigates between weak economic data on one side and stubborn inflation pressures on the other.

Figure 1: G10 FX Performance Tracker [vs. USD] (1 week)



Source: Bloomberg Date: 11/09/2023



GBP

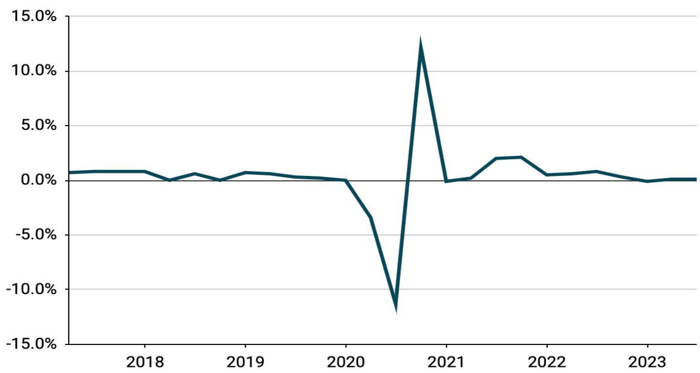
The PMI indices of business activity saw an unusually large upward revision last week. This didn't help sterling much, and the pound ended the week near the bottom of the G10 rankings, as markets continue to bring down their expectations of Bank of England terminal rates.

This week's labour market data will be key to the MPC's rate decision later in the month. Absent a very weak report, which we do not expect, the Bank of England should hike rates again to combat sticky wage inflation, which should lend support to the pound.

EUR

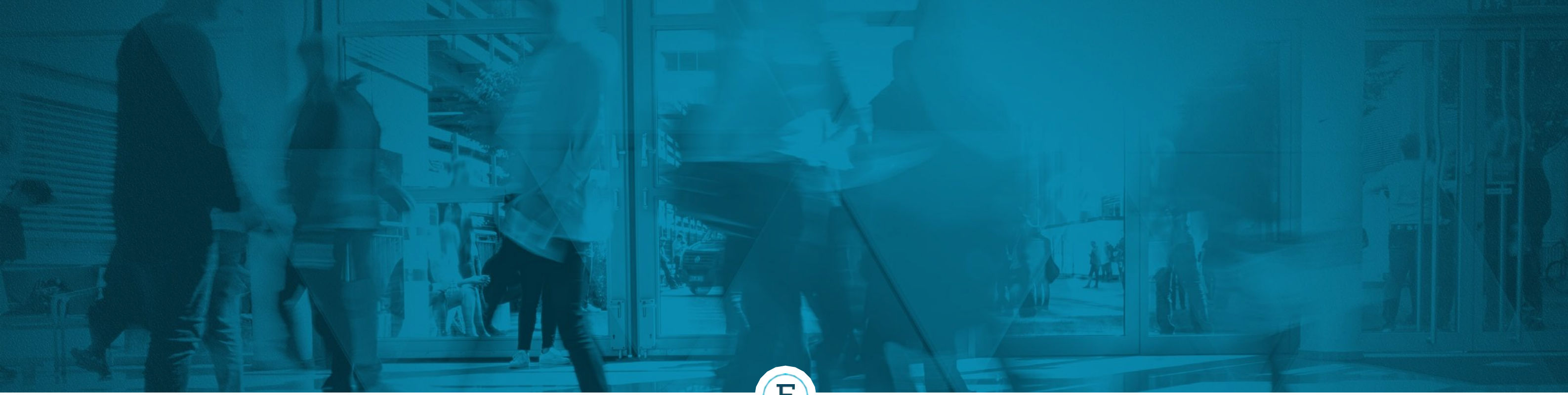
The streak of bad data out of the Eurozone continued last week. August PMI numbers were revised down from already depressed levels. The second quarter GDP growth was also revised down, further indicating that the Eurozone economy is stalling. German factory data for July was particularly dismal.

Figure 2: Euro Area GDP Growth [% QoQ] (2017 - 2023)



Source: Bloomberg Date: 11/09/2023

The ECB task at its meeting this week looks particularly difficult. On the one hand, the signs of an economic stall keep piling up. On the other hand, there are as yet no clear signs that inflation is trending down, at least not in the critical core numbers. The decision will be finely balanced, but we are now leaning towards a hike, which could help pull the common currency out of its doldrums.



USD

A spate of economic data last week suggested that the US continues to defy gravity. The US counterpart to the PMI numbers, the ISM, came out stronger than expected, as did weekly jobless claims. 10-year Treasury rates are hovering near 1-year highs, and the dollar is unsurprisingly benefiting from the gap in economic performance across the Atlantic. This week's inflation data is key. While the headline index may rebound somewhat, markets expect the monthly core number to be consistent with sub-3% annualized inflation, which should open the way for a Federal Reserve pause at its September meeting.

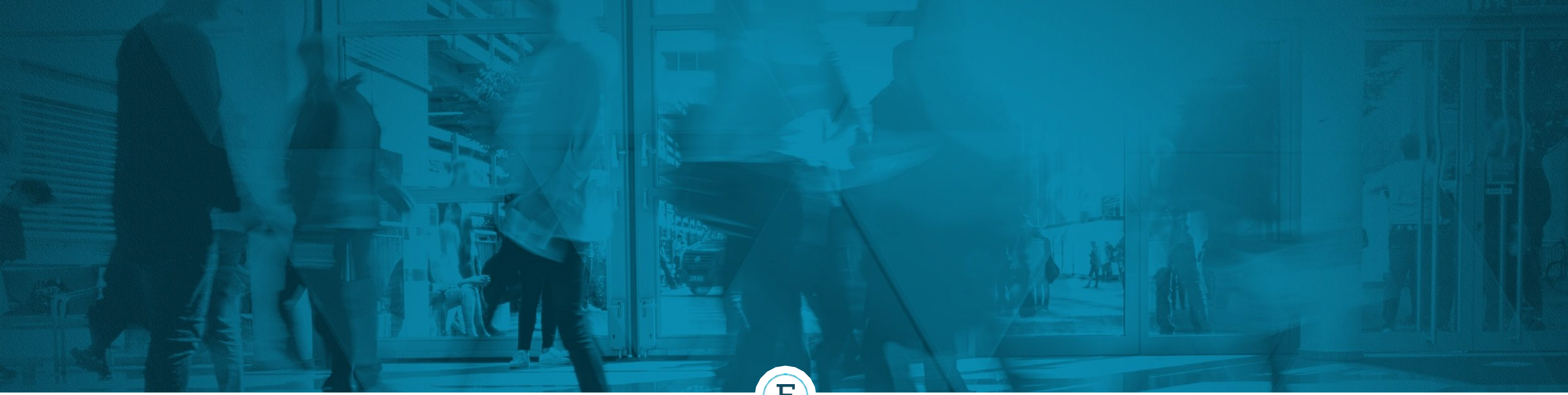
JPY

The Japanese yen was the second worst performing G10 currency last week, succumbing to pressure stemming from higher US yields and a stronger dollar. Last week's Q2 GDP revision showed a smaller growth than initially reported 6%, and disappointed, but 4.8% annualised is still a very rapid pace of growth for the Japanese economy, where strong expansions are rare.

Investors are eagerly awaiting the BoJ's upcoming meeting on 22/09. Particularly after Governor Kazuo Ueda mentioned in a recent interview with The Yomiuri Shimbun that the bank may lift its negative interest rate policy if wages and prices rise. He also signalled that enough data may be released by the end of the year for the bank to make a decision. This, alongside other comments from Japanese officials in recent weeks, adds to expectations that the end to BoJ's ultra-loose monetary policy is in sight and the market is now convinced that a lift-off will take place in January next year. The FX market reacted accordingly, sending the yen up by about 1% against the US dollar at the start of this week, the most in two months. 10-year Japanese yields marched up above 0.70% level today, reaching their highest level in nearly a decade.

Figure 3: Japan 10-year bond yield (2009 - 2023)

Source: Bloomberg Date: 11/09/2023



CHF

The franc ended the week little changed against the euro. The Q2 GDP data showed that the Swiss economy is at a standstill. This, alongside other economic data released over recent weeks, supports our view that in the not-too-distant future, the SNB will turn from focusing on price pressures to being more concerned with economic activity. Markets are betting that it might have already ended its hiking cycle, although we think a 25bps move later this month is likely, and it probably will be the bank's final.

There's not much on tap this week, except for producer and import prices data on Thursday. Therefore, investors are set to focus primarily on the outside news.

AUD

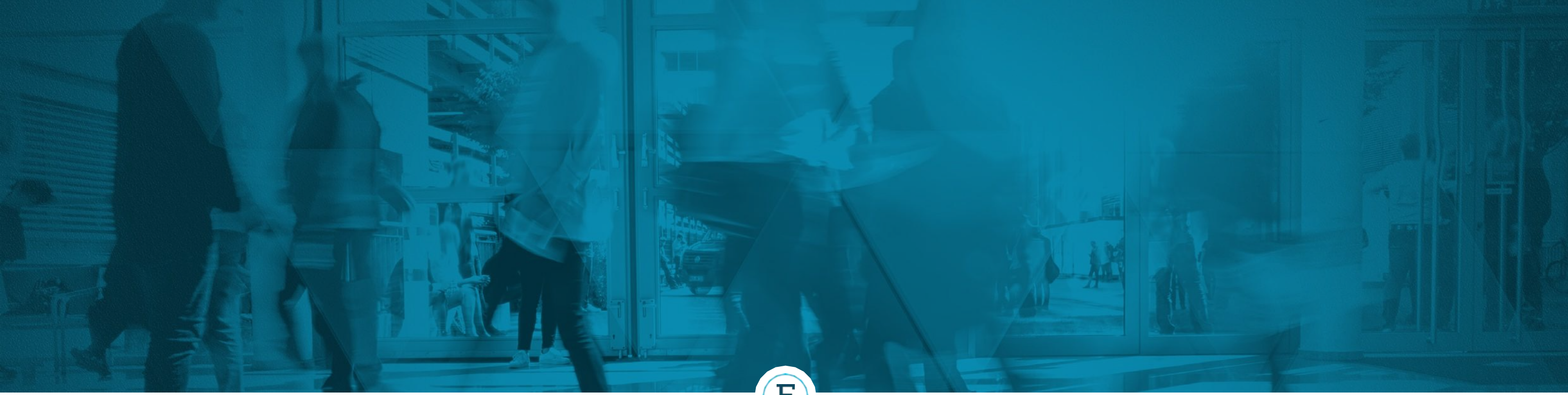
The Australian dollar landed at the bottom of the G10 performance tracker last week, pressured lower by the stronger greenback, disappointing PMI news from China, and a central bank, which appears to have ended the hiking cycle. As widely expected, the Reserve Bank of Australia kept rates unchanged at last week's meeting. Although it hasn't closed the door to further tightening, markets are betting that the bank is most likely to hold rates steady before cutting them in late 2024.

The GDP growth in the second quarter was somewhat better than expected, and the first-quarter data was also revised upwards. It was, however, not enough of a kick for a currency to rebound against a broadly stronger US dollar. Looking ahead, the focus in the first half of this week will be on sentiment data. Key this week will, however, be the August labour market report, which will be released on Thursday. It is expected to show an increase in employment after a surprise decline in July.

NZD

The New Zealand dollar underperformed most of its G10 peers last week. The currency closely tracked the Australian dollar and succumbed to pressure from the broadly stronger greenback and disappointing PMI news from China on Tuesday.

The focus this week will be on Thursday's PMI data. Aside from that, investors are likely to focus mostly on the outside news.



CAD

The Canadian dollar was the third best performing G10 currency last week. Aside from being close to the US dollar, the currency was supported by rising oil prices. As widely expected, the Bank of Canada left interest rates unchanged on Wednesday. It left the door open to further tightening, but its messaging was rather balanced and didn't stir the markets. We are standing by our call that the BoC hiking cycle is over – for markets, it's a coin flip.

This week is light in terms of economic releases from Canada. Markets will, therefore, focus primarily on the outside news.

SEK

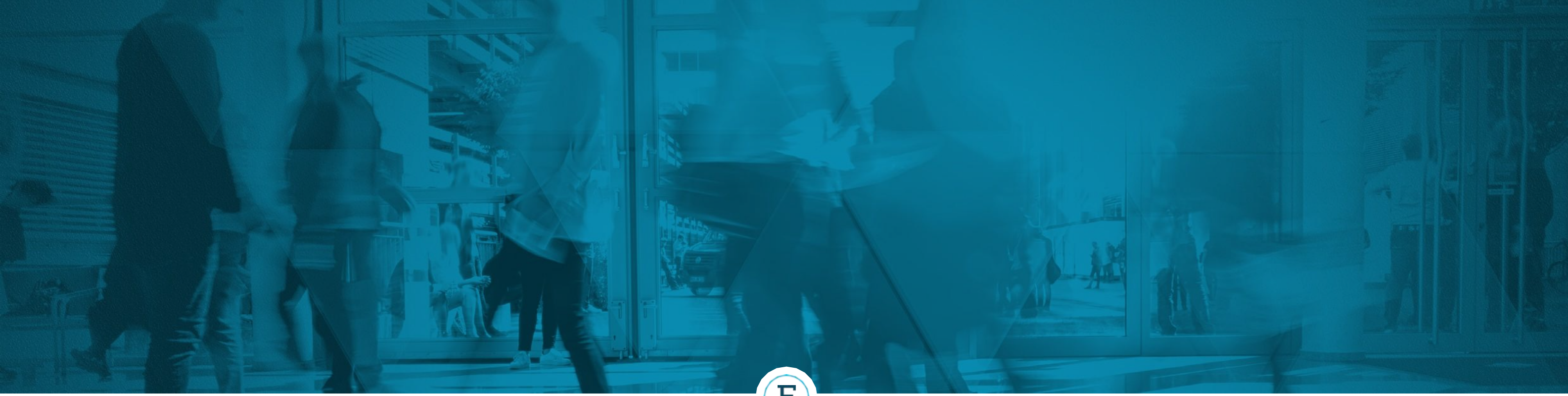
The Swedish krona ended the week practically unchanged against the euro.

August inflation data published on Thursday could be key to the Riksbank's monetary policy decision next week. Markets are now fully pricing in a 25bp rate hike from the Riksbank in September and another in November is possible, particularly should upcoming inflation prints once again beat expectations. However, recent signs of a slowdown in activity could reduce the need for further tightening.

NOK

The Norwegian krone was the second best performing G10 currency after the US dollar last week. An uptick in oil prices which saw the Brent rising above the $90 per barrel level helped the currency of oil-dependent Norway.

However, this morning's inflation data may put the brakes on the currency's recent gains. Headline inflation fell more than expected to 4.8% in August, the lowest level since March last year. Core inflation data, which is crucial for future central bank policy, also surprised to the downside: it fell to 6.3% in August from 6.4% the previous month, instead of rising to 6.6%. Continued moderation in inflation, coupled with signs that the Norwegian economy is slowing down could indicate that the end of the Norges Bank's hiking cycle is drawing ever closer.



CNY

Last week was historic for the yuan, as it fell to its lowest level since 2007 against the broadly stronger US dollar. However, the Chinese currency itself was not exactly weak; in fact, the opposite is true. In trade-weighted terms, it soared by 0.6% to its strongest level since June. We start the week off with the extension of this strength, with the currency rallying following verbal intervention from PBOC in addition to yet another stronger-than-expected fixing and better-than-expected financing data.

Economic data from China is not entirely positive, but no longer disappointing on all fronts. The Caixin PMI for the services sector was indeed worse than expected and showed the weakest reading this year. However, the composite PMI was almost unchanged from July, with the rebound in manufacturing offsetting the weakness in services. China emerged from a brief period of consumer deflation in August, as expected, with the CPI index rising by 0.1%. Most importantly, however, trade data surprised on the upside, showing smaller declines in exports and especially imports in August. It's also worth noting that Country Garden made interest payments on the US dollar bonds before the end of the 30-day grace period and thus avoided default. This week will be a very busy one in terms of economic news from China. We started it off with better-than-expected financing data. Ramped-up borrowing reinforces the impression that some stabilisation may finally be taking hold. Looking ahead, investors will focus on the package of key readings out on Friday and the PBOC MLF announcement on the same day. No rate adjustment is expected. Instead, the focus should be on the rollover.

Economic Calendar (11/09/2023 - 15/09/2023)

Economic Calendar	Country	Day	Date	Time (GMT)
Inflation (Aug.)	NOR	Monday	11/09	07:00
Employment Report (Aug.)	UK	Tuesday	12/09	07:00
Inflation (Aug.)	US	Wednesday	13/09	13:30
Employment Report (Aug.)	AUS	Thursday	14/09	02:30
Inflation (Aug.)	SWE	Thursday	14/09	07:00
ECB Monetary Policy Meeting	EZ	Thursday	14/09	13:15
Retail Sales (Aug.)	US	Thursday	14/09	13:30
PBOC MLF Decision	CHN	Friday	15/09	03:20
Retail Sales (Aug.)	CHN	Friday	15/09	03:00

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