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Weekly Report

G10 Weekly FX Update

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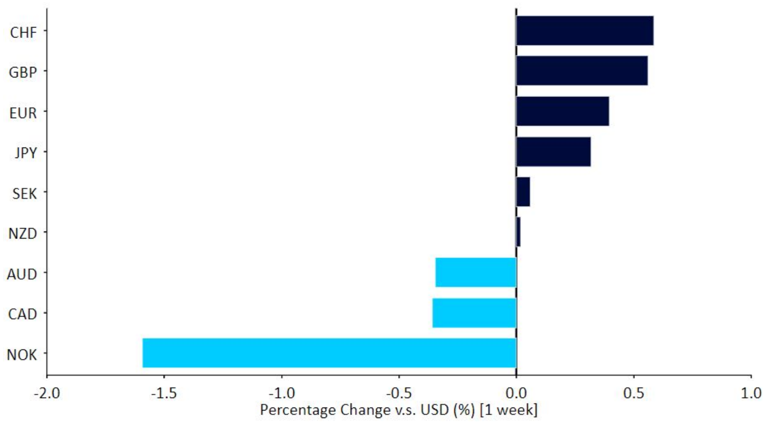
US yields rise again after bumper NFP report

The biggest story in financial markets remains the relentless march higher in long-term interest rates worldwide, led by US Treasuries.

Last week, however, rates failed to drag the dollar upward with them, and the US currency lost ground against most currencies, despite Friday's impressive nonfarm payrolls data. The main exceptions were commodity currencies, which suffered amid an oil-led sell-off in commodity prices. The strong payrolls report out of the US poured cold water on the notion that the US economy is slowing down, and markets are again pricing in a 50% chance of an additional Federal Reserve rate hike, further unsettling fixed income markets.

The Hamas assault on Israel over the weekend is another source of uncertainty, which will be felt in markets primarily through the oil price and concomitant pressure on inflation.The key question is whether the worst sell-off in US Treasury history will continue, dragging down with it risk assets and pushing the dollar higher. In this context, the US inflation report for September, out on Thursday, takes on added importance. Any signs of continued moderation in inflationary pressures would be very welcome to markets and could result in a significant euro rebound.

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



Source: LSEG Datastream Date: 09/10/2023

GBP

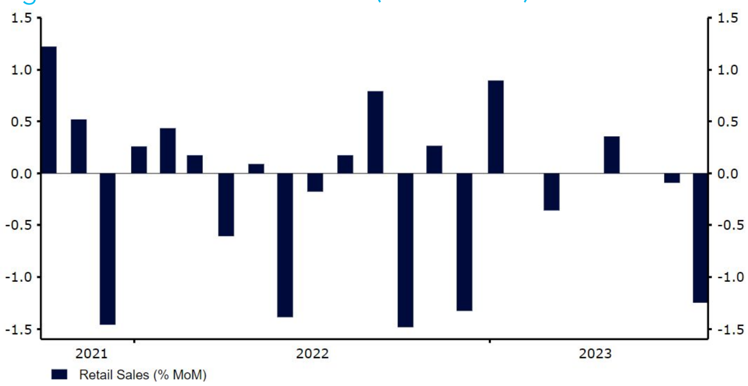
In a data-light week, the pound put in a decent performance, rebounding against both the euro and the dollar after weeks of losses. A lack of major newsflow out of the UK in the past week or so ensures that sterling has largely traded off events elsewhere. Last week's UK construction PMI was a big miss, with the index slumping to its lowest level since May 2020, though the minimal contribution of the sector to Britain's economy ensures that this was largely overlooked by markets.

This week there is a slate of August data on tap, including monthly GDP, industrial production and construction. They should paint a picture of moderate growth. GDP data, in particular, has tended to deliver positive surprises lately, which could work in favour of sterling this week. Signs of resilience here should bring an additional Bank of England interest rate hike into view, which remains less than 50% priced in by markets by year-end at the time of writing.

EUR

The euro's resilience last week on the fact of ever-higher Treasury yields and dismal Eurozone August retail sales data gives some hope that current levels are already pricing in a fairly negative outcome for the European economy. Retail sales contracted by 1.2% relative to the previous month in August, marking the largest downturn since December. While this data point clearly runs on a bit of a lag, the trend in activity is a troublesome one.

Figure 2: Eurozone Retail Sales (2021 - 2023)



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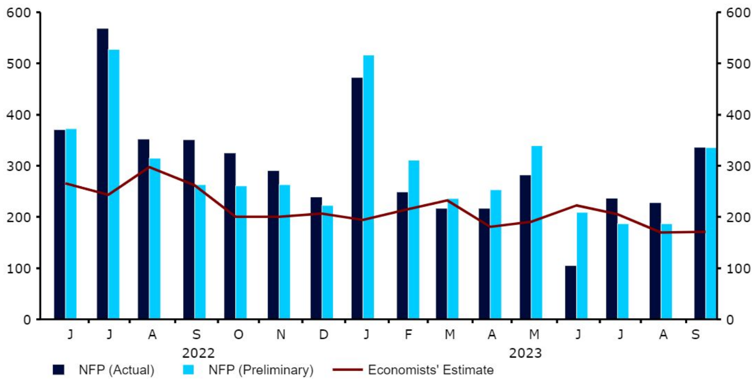
This week, the focus should be on the credit data for September, a somewhat-ambiguous but very timely indicator of business activity. Anything sort of the gloomy scenarios currently priced in could give the euro a boost. The latest meeting accounts from the European Central Bank will also be released on Thursday. Communications from ECB members last week were resoundingly dovish, pouring further cold water on the possibility of further monetary tightening. We suspect that the accounts will provide much of the same, and are unlikely to provide much upside for the beleaguered common currency.

USD

The US economy appears to have shrugged off the fastest increase in interest rate in its history, and Treasuries continue to sell-off as markets come to grips with the possibility of 5% rates as far as the eye can see. The key data point last week was the strength in the labour market, which confirmed the positive tone of higher frequency indicators like job openings and weekly jobless claims. Average earnings growth eased, and unemployment unexpectedly remained unchanged, although the net creation number smashed expectations, with the US economy adding a net 336k jobs last month, almost double economist's estimates.

Figure 3: US Nonfarm Payrolls (2018 - 2023)



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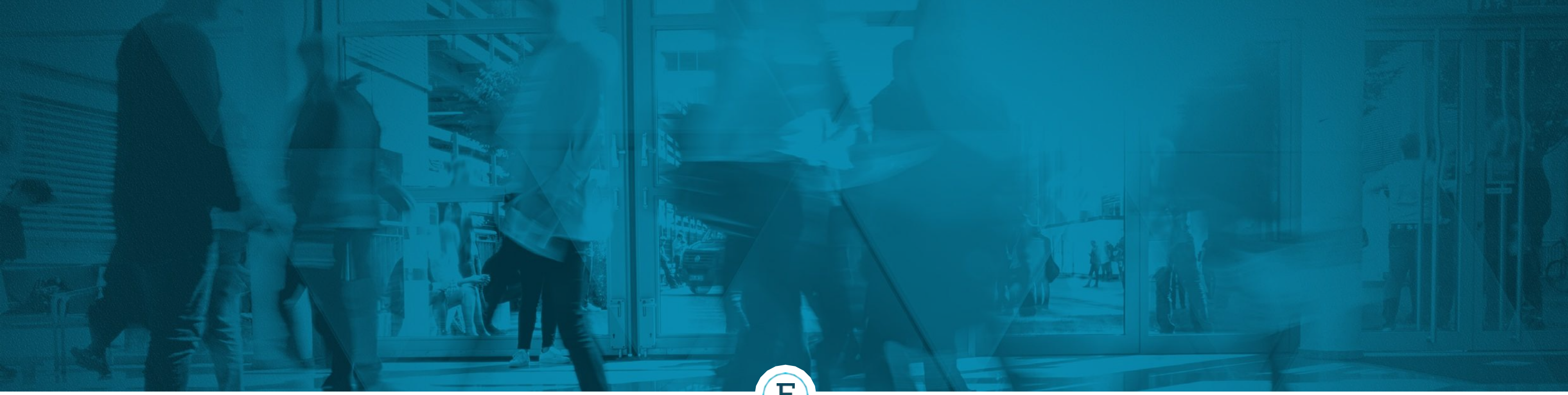
The inflation report for September is up next (Wednesday), and the frayed nerves in bond markets may not react well to an upside surprise. Expectations are, however, for relatively mild numbers, which would confirm the gently downward trend in inflation that the Fed wishes to see.



JPY

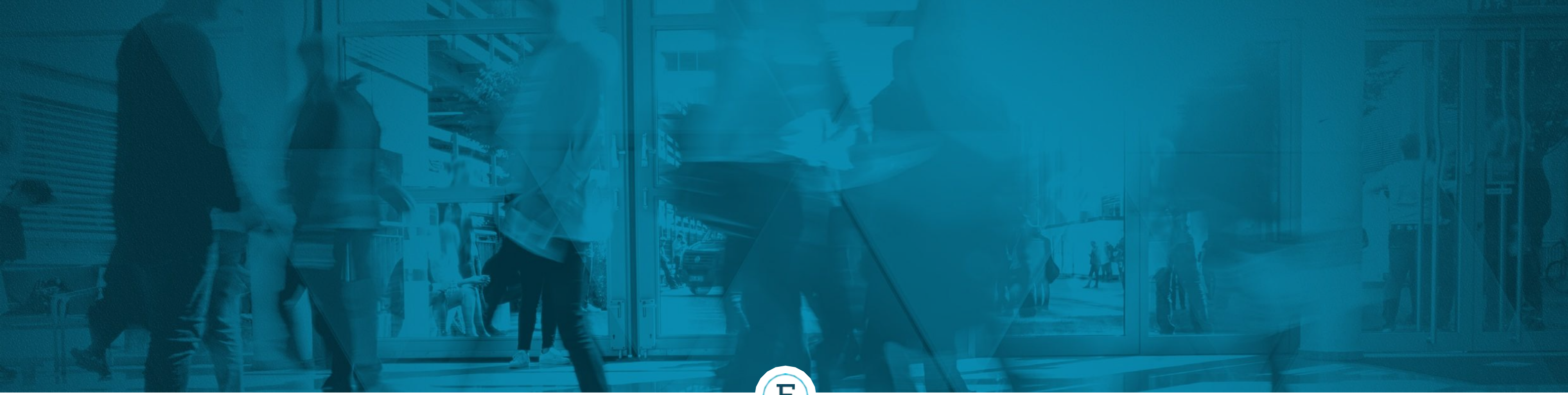
Last week was a particularly volatile one for the Japanese yen. The USD/JPY exchange rate rose above the 150 level at the start of the week, although the pair snapped back in a knee-jerk fashion on Tuesday, in what originally appeared to be the result of FX intervention. Data out the following day, however, suggested that intervention did not take place, while officials refused to comment on whether this was indeed the case, indicating to us that the move may simply have been a consequence of technical factors or trading algorithms. In any case, the yen managed to hold onto its gains, and ended the week modestly higher on the greenback.

There is a complete lack of major market moving news out of Japan this week. Speculation will likely continue as to whether Japanese authorities will step in to protect the yen should we see a fresh move above 150 in the USD/JPY exchange rate. There appears to be a reluctance to do so, and we may need to get a shift in policy stance from the Bank of Japan to see a meaningful snap back in the yen.

CHF

The Swiss franc ended last week near the top of the G10 FX performance dashboard, recovering somewhat following several weeks of depreciation. The currency performed well, despite the continued pricing out of another interest rate hike by the Swiss National Bank. Investors now see roughly a 1-in-5 chance of another rate increase, with the latest inflation data supporting the view that it is probably not on the cards.

Core inflation fell to 1.3% in September, below the 1.5% consensus, and the lowest level in around a year and a half. Headline inflation rose marginally to 1.7%, but was also lower than expected and the fourth consecutive month within the SNB's 0-2% target. Signs of limited price pressures assure us that the SNB has likely already ended its hiking cycles. There's not much on tap in terms of macroeconomic data from Switzerland this week, except for the September producers and import prices data on Friday. Global sentiment will likely be key for the currency this week. As a safe-haven, the franc is already on a stronger footing in the face of the tragic news from Israel over the weekend.

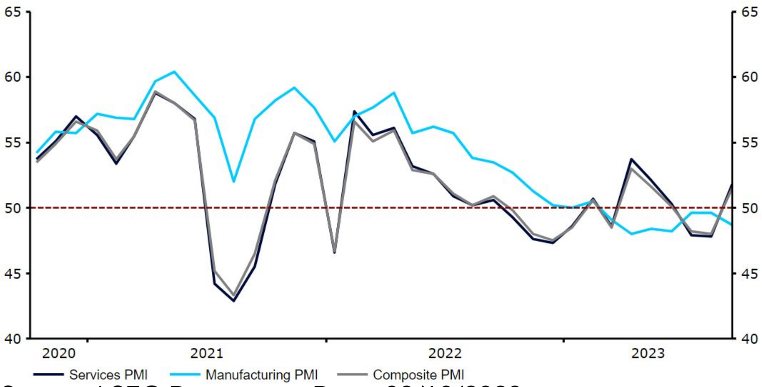


AUD

As anticipated, the Reserve Bank of Australia kept interest rates unchanged for the fourth straight meeting last Tuesday, Michele Bullock's first as the new governor of the central bank. The Aussie dollar traded somewhat weaker following the announcement, as while the RBA kept open the possibility of another hike, it failed to provide a hawkish tilt in its communications that might indicate one is on the way at either of the next couple of meetings. This reaffirms our suspicion that the hiking cycle is likely over, and that the RBA will instead opt to hold rates at current levels for a prolonged period, at least through to late-2024.

There is reason for optimism, however, as economic news out of Australia has taken a slight turn for the better. Last week's services PMI unexpectedly rose back to 51.8, lifting the composite index to 51.5 - its highest level in four months. This should calm concerns over a slowdown in growth in the second half of the year, which may provide some tailwinds for the Australian dollar in the coming trading sessions.

Figure 4: Australia PMIs (2021 - 2023)



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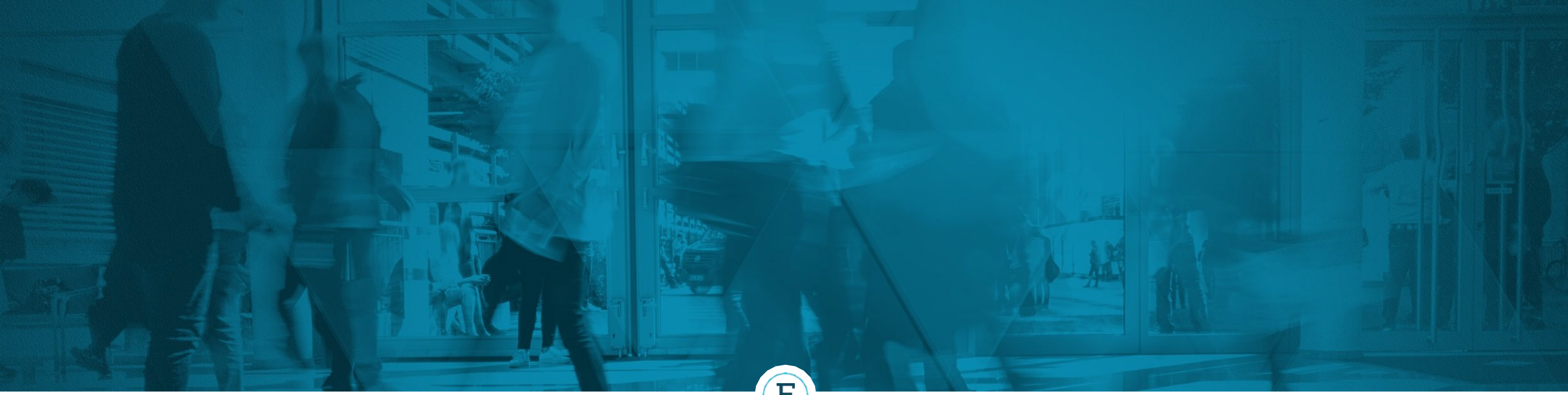
NZD

There were no big surprises from last week's Reserve Bank of New Zealand meeting. Rates were left unchanged, as was universally anticipated, with policymakers saying that previous hikes were continuing to constrain economic activity and bring down inflation. The communications continue to suggest that the RBNZ has effectively no appetite for additional hikes, and will instead opt to keep rates at current levels for a prolonged period of time, in line with similar stances adopted by most of the world's major central banks.



The New Zealand dollar briefly sold-off following the RBNZ announcement, although it edged higher during the rest of the week. We continue to hold a moderately bullish view on NZD, as a lack of appetite for central bank rate cuts should provide some currency support. News this week is light on the ground, although Thursday's PMI data could receive some attention among market participants.

CAD

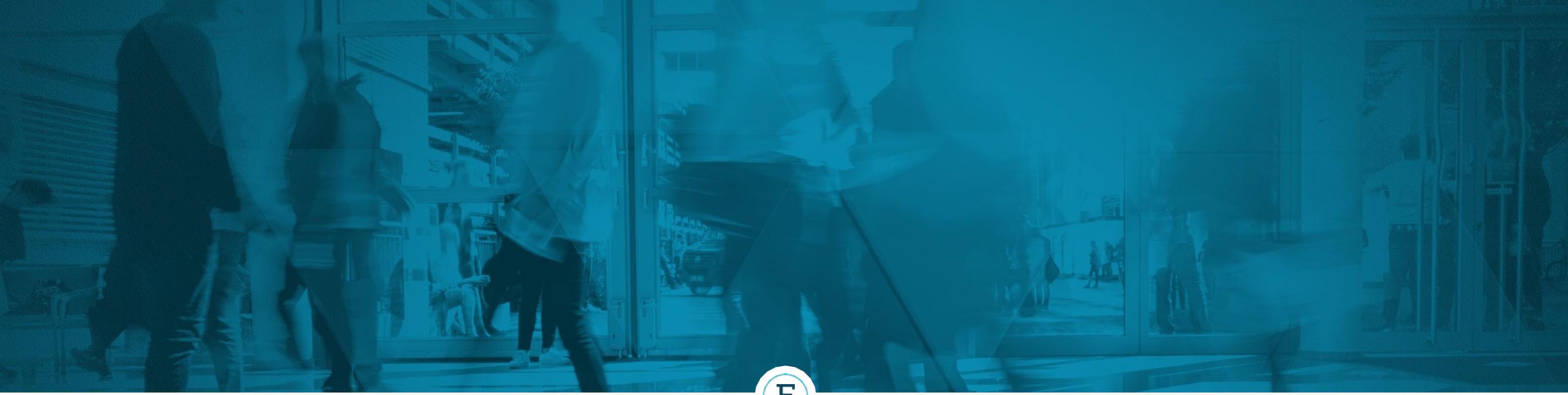
The Canadian dollar was one of the main underperformers in the G10 last week, as fears over a decrease in demand for oil send Brent Crude prices sharply lower, while OPEC+ members confirmed production cuts. This bearish development for CAD completely offset any positivity from last week's largely encouraging set of macroeconomic data out of Canada, most notably the resilience shown in the latest PMI numbers and the impressive jobs report. A net 64k jobs were added to the Canada economy last month, more than three times consensus and the highest number since January.

News out of Canadian economy has been far from stellar of late, though the lack of a deterioration in the labour market will provide investors with some comfort, and markets have subsequently not totally ruled out the possibility of another Bank of Canada rate hike. Upcoming inflation data (a week on Tuesday) will be key in guiding these expectations.

SEK

The Swedish krona depreciated slightly against the euro last week, although it is still trading near its highest level since August.

Last week's PMIs for September weighed on SEK, again showing signs that the Swedish economy is slowing. The Swedbank Manufacturing PMI fell to 43.3 in September, marking the fourteenth consecutive month of contraction. At the same time, the Services PMI slipped to 46.3 last month, from a downwardly revised 48.4 in August, the second month of contraction after recovering in July. Looking ahead, this Friday's inflation data will be key for the Riksbank's future monetary policy, and thus for the currency.

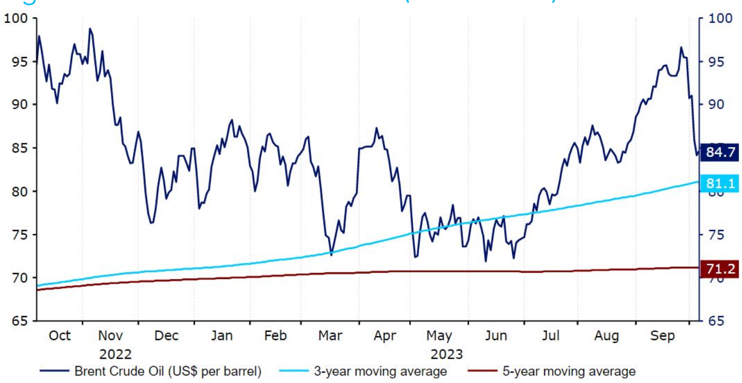


NOK

Like other commodity currencies, the Norwegian krone depreciated against the euro last week, as oil prices fell. Indeed, the international oil benchmark plunged by more than 8% last week on signs of weakening demand.

Tomorrow's inflation data for September, together with oil price developments, will be key for the Norwegian currency. Both the headline and core indices are expected to decline from the previous month, although the latter looks set to remain high at 6%. At its latest policy meeting, Norges Bank pre-signaled one last hike in December, for a terminal rate of 4.50%, but a surprise in this data could change the bank's plans.

Figure 5: Brent Crude Oil Futures (2022 - 2023)



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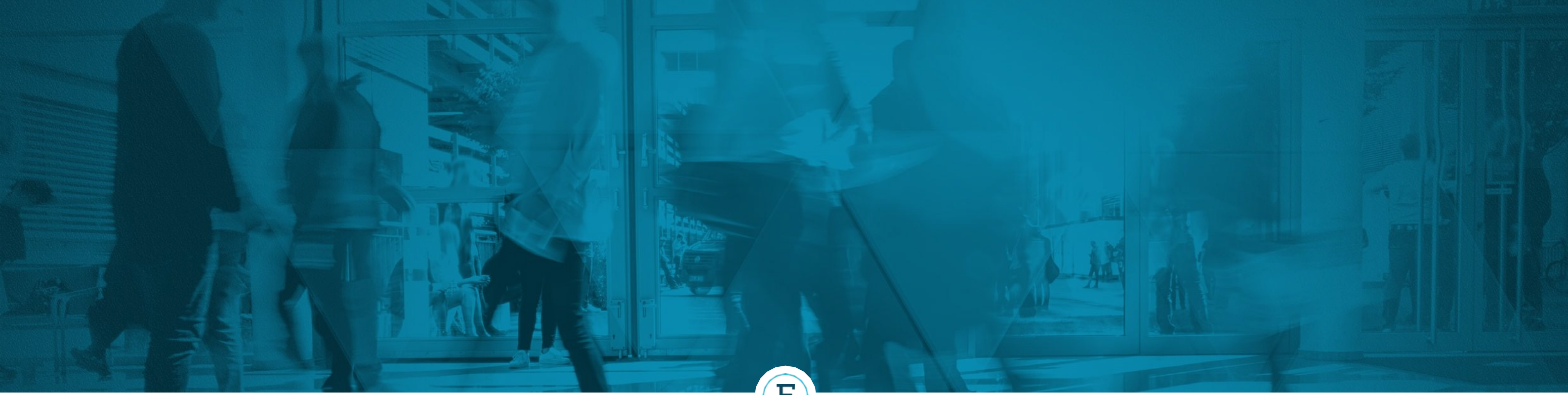
CNY

The mainland market was closed last week due to the Golden Week holiday. During this period, the offshore yuan (CNH) sold-off marginally against the US dollar. With a general lack of information, there was positive news on holiday spending – according to Shanghai Securities News, it surged by 153% on the Meituan online platform from the pre-pandemic 2019. Travel also recovered, although remains below pre-pandemic levels. This provides some hope that consumption in China is recovering.

In the coming days, investors will keep an eye on the financing data for September. On Friday, inflation and trade data for the same month will be out. The data has influenced the yuan exchange rate in the past; hence, we could see some additional volatility around the time of the releases, which are generally expected to show some improvement.



Economic Calendar (09/10/2023 - 13/10/2023)

Economic Calendar	Country	Day	Date	Time (BST)
Inflation (Sep.)	NOR	Tuesday	10/10	07:00
FOMC Meeting Minutes	US	Wednesday	11/10	19:00
GDP (Aug.)	UK	Thursday	12/10	07:00
ECB Meeting Minutes	EZ	Thursday	12/10	12:30
Inflation (Sep.)	US	Thursday	12/10	13:30
Inflation (Sep.)	CHN	Friday	13/10	02:30
Inflation (Sep.)	SWE	Friday	13/10	07:00

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