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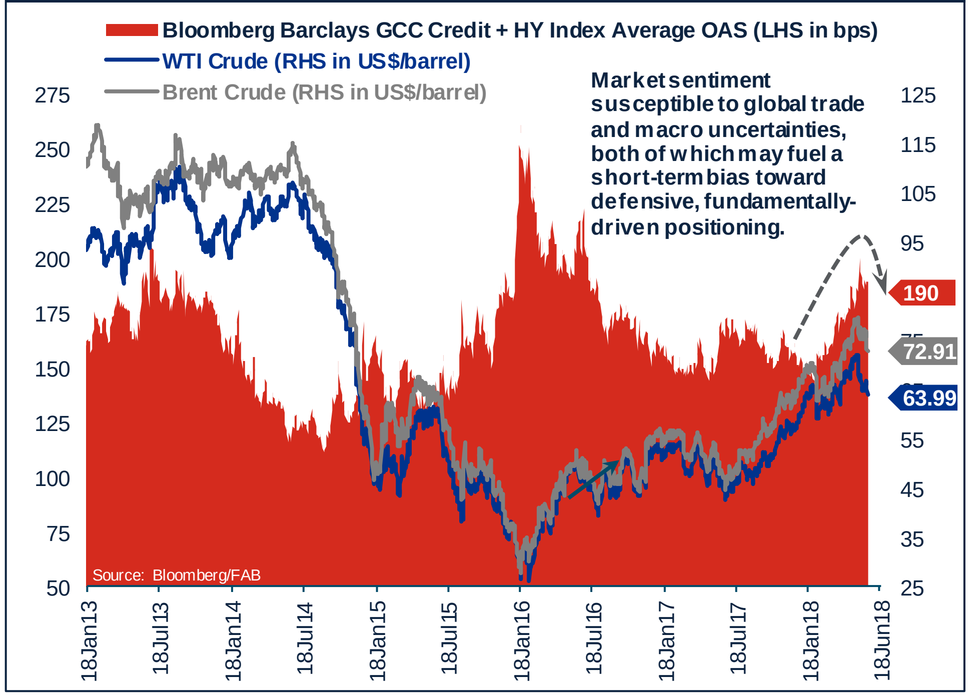
G10 Rates & FX, & Oil - The Traders' Views

Macro Strategy View: Positioning for a Confluence of Uncertainties

- We have long stated our belief that no one wins in a trade war, and as trade rhetoric heats up between the U.S. and China a softer bias is embracing financial markets this morning. This said, nothing seems to have really changed – or significantly deteriorated – on the global trade front in recent days, but as lower seasonal liquidity concerns perhaps begin to creep into investors' minds, so the market may prove to be more susceptible to headline risk over the coming weeks. As such, with China and Hong Kong markets closed today for the Dragon Boat Festival and Asian trading volume therefore sharply depleted, it is unsurprising that Japanese risk asset markets are leading the broader region lower, suggesting a fragile start to MENA markets at the return to work from the Eid al-Fitr extended weekend.
- The shift toward a more defensive market sentiment this morning has been a fillip for the yen, in turn is weighing on Japanese equities. Meanwhile, the specter of intensifying global trade tensions has also cast a fresh veil of uncertainty over oil prices. Both WTI and Brent crude are quoted lower this morning on Bloomberg, with the former currently shown at $63.84bbl, down from a recent high of $72.35bbl a month ago. The net negative effect of both of these moves seems set to dampen price action in MENA/GCC risk asset markets this morning, albeit that the sector should continue to benefit from its underlying fundamental strength and attractive yield levels.

Short-term caution?



- Looking ahead, we would suggest that markets could continue to see periods of heightened volatility over the summer months, fueled by the confluence of seasonality, global trade concerns and the broader implications of a still fragile outlook for global interest rates and central bank (Fed, ECB) monetary policy and balance sheet normalization. This said, we stick with our core view that investor capitulation is not a meaningful risk at this stage, albeit that against the backdrop of uncertainties we continue to advocate a bias toward fundamentally-driven, defensive positioning.

  (Simon Ballard, Macro Strategist, Market Insights & Strategy)

Please find below views on G10 Rates & FX, & Oil directly from our traders.

The hawkish rhetoric post the FOMC decision did little to help lift yields as markets focused more on the extremely dovish ECB meeting and the continued volatility across EM assets. CT10's finished the week lower at 2.92%, with CT5 and CT2 at 2.80% and 2.55% respectively. Currently the market is pricing an additional 35bp of tightening by the FOMC for the remainder of 2018.

G-10 FX	Macroeconomic/Fundamental Analysis	Views (Bearish/Bullish) 2-week Time Frame	Intermediate & Long-term Views (3mth & 12mth Time Frame)
SGD	The Fed hiked 25bps last Wednesday, as the market expected, but surprised investors with a hawkish rise in the short-term Fed dot plot, which triggered some EM outflows. USDSGD spiked to 1.3460 which is close to recent high seen in May. US looking to impose tariffs on China on Friday also did not help risk sentiment due to Singapore's status as a leading global trading port. I would shift my stance to a more defensive position and expect the SGD to weaken slightly towards the mid of the SGDNEER as trade war tension looms again. Prefer long USDSGD for the time being or short SGD against the basket.	Bullish 1.3500	Bullish 1.3600
INR	USDINR spiked to 68.00 tracking the EM global outflow theme last week. Oil prices trading 2% higher also contributed to a negative factor for INR. Both bonds/equities saw outflows last week. Given the weak risk sentiment on high yielding global EM market, I will stay aside and wait for better levels to sell USDINR. Holding paper just for the high coupon carry is not a convincing trade now in my view.	Neutral 68.00	Neutral 68.00
CNH	USDCNH headed slightly higher last week with CFETS basket remaining roughly unchanged. Despite the 25bps rate hike by the Fed, the OMO rate in China remained unchanged instead of market expectation of a 5 bps hike. Market reads this as a result of deleveraging which drives a more challenging funding situation and slower economic growth expectations. Fundamentally, given weakening FAI data and the strong stance of deleveraging, I view that the growth rate in China will continue to slow down. I look to buy USDCNH and probably short CNH against the basket targeting a lower CEFTS level.	Bullish 6.4500	Bullish 6.4500

G-10 FX	Macroeconomic/Fundamental Analysis	Views (Bearish/Bullish) 2-week Time Frame	Intermediate & Long-term Views (3mth & 12mth Time Frame)
KRW	Despite a successful Trump-Kim meeting in terms of the photo opportunities and broad geopolitical sentiment, nothing concrete was agreed at the summit. Along with the weak risk sentiment and heavy positioning in short USDKRW FX ahead of the meeting, spot saw a big stop out move on Friday and closed at the high of 1097.80. Key resistance level is at 1100.00 which was February's high when US stocks flash crashed. I would remain cautious on low yielding currencies as the US-KRW rate differential continues to widen which makes KRW yield less attractive compared to the US.	Bullish 1100	Bullish 1150
EGP	The Egyptian pound spot market was very stable for the week at 17.80-17.90. We think the bias is clearly to the upside in the interbank market especially in view of the sell-off in EURUSD. The key economic release was the Urban CPI for May which came in lower at 11.4% than the prior month of 13.1%. This clearly paves the way for interest rate cuts by the CBE with the next meeting scheduled for 28 June. The reason why the central bank's policy was reserved up till now was because the government is planning to reduce subsidies for energy in the coming months starting with hikes in electricity prices. Thus there is an expectation that inflation might rise in H2 2018. Additionally, policy makers are worried by the weakness in EM currencies and how it might affect sentiment towards EGP Tbills and Tbonds where yields are still relatively high. Therefore it remains a tough call to say whether the CBE will opt for an interest rate cut at the next meeting. In the NDF market the demand for USD is very strong as investors are hedging their exposure. At the latest auction the yields of 6-mth Tbills and 12-mth Tbills printed levels around 18.50%-18.75%.	Neutral to bullish USDEGP 17.80-17.95	Neutral to bullish 17.50-18.50
NGN	The NIFEX and NAFEX rates printed levels around 342 and 360 respectively in the past week. Nigerian inflation declined yet again in May to a new recent low of 11.6% from 12.5% previously. The Nigerian spot and NDF markets are very quiet in the middle of the storm that is going through the EM space as high oil prices still boost the FX reserves of the central bank which is determined to keep the local currency stable. There has recently been an increase in oil breakdowns and stoppages in the domestic oil industry which hit the production levels which is estimated to be down to 1.4mbpd as of late from above 2mbpd earlier in the year.	Neutral NAFEX USDNGN 360-362	Neutral to bullish 345-365

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GCC FX Commentary	
SAR	The SAR FX curve was lower on the week with the 1Y FX swap trading at 45 mid, 5 points lower, while the 2Y and 3Y swaps are at 185 and 365 mid, both lower by 5 points. SAR FX spot is currently trading at 3.7504 mid, 3 pip higher on the week.
AED	The whole AED FX curve remained unchanged with the 1Y FX swap trading at 25 mid. AED FX spot is currently trading at 3.6730 mid, unchanged on the week.
KWD	The KWD FX curve continued to be softer and flatter this week with the 1Y FX swap moving 20 points lower to trade at -250 mid. Shorter dates moved lower by 5-10 points, while longer tenors moved lower by as much as 20 points. KWD FX spot is currently trading at 0.30270 mid, 73 pips higher on the week.
OMR	The Omani FX curve remained unchanged on the week with the 1Y FX swap trading at 305 mid. OMR FX spot is trading at 0.38598 mid, a pip lower on the week.
BHD	The Bahraini FX swaps curve continued its move higher and steeper on the week. The 1Y FX swap is currently trading at 280 points mid, up 40 points on the week. USD/BHD spot is trading at 0.37785 mid, 15 pips lower on the week. The most recent 3-month BHD T-bill issuance yielded investors 3.62%, up 7 basis points from the previous auction. The coverage was also higher at 122%.

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Interest Rate and FX Options Commentary

- Currency markets were fairly calm throughout last week as the Trump / Kim summit went smoothly but volatility returned yet again in the latter part of the week in the wake of a Dovish ECB and the Fed rate hike. This combination boosted the USD across all pairs and sent FX volatility firmly bid. The market is now watching key levels in G10 FX, but with US equities still trading close to historic highs and the USD losing momentum, we think volatility may ease in the coming days; the major political events and economic releases are also behind us for now.

- Meanwhile, we saw some buyers of interest rate volatility early last week ahead of the Trump/Kim summit in Singapore. It seems US rates volatility buyers gave up after the success of the U.S. and North Korea leaders' meeting. Market participants gave top priority to this event and then moved on; US rate vols went offered with the market rallying back. Looking ahead, we expect USD interest rate volatility to keep trading cheap; FED was on the hawkish side but the overall reaction in rates was tepid and vols got sold. In the GCC markets, liquidity in AED and SAR rates volatility is quite scarce – AED and SAR rates vols are stable/soft side.

Oil Commentary

- Last week was another interesting week, as oil kept being impacted by both bullish and bearish news, thus trading within a range. Bearish API numbers (API reported post-settlement a 0.8 mln bbls build in US crude inventories last week, with gasoline and distillate also witnessing a build), combined with the headlines about Russia willingness to return back to Oct16 production levels are pressuring the oil price. Venezuela and Iran production uncertainties/issues is still supporting the oil price.

- Inventory EIA Report: Crude Oil fell 4.14 MLN BARRELS, exceeding market expectation of -1.1 mmbbl draw. Gasoline & distillate inventories as well fell significantly making the report bullish.

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