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G10 Rates & FX - The Traders' Views

The Week Ahead: Aside from the ECB and BOJ monetary policy meetings this week and the US payrolls report due Friday, investor focus this coming week will likely fall on three main topics, all of which have the potential to impact risk appetite levels across the European, US and MENA regions.

Expect all eyes to be on (1) the outcome of the Italian general election that takes place today (Sunday March 4th) and its and European political ramifications; (2) analysis and digestion of last week's surprisingly hawkish testimony from Fed chair Powell; and (3) finally the market implications of rising protectionist rhetoric in the wake of Thursday's unexpected announcement by US president Trump of his steel and aluminium import tariff plans.

* The Italian elections that take place today have the potential to create a sharp spike in market volatility and to call into question the future of the eurozone project. Such concerns are driven by the recent momentum that has been enjoyed by the far-right Northern League party and its charismatic leader Matteo Salvini, which aims to purge Italy of what it classes as illegal immigrants. Immigration and the weakness of the Italian economy have been the two central pillars of the election campaign, which has ridden the recent Europe- and US-wide wave of political populism. Success of the Northern League and its centre-right coalition today would also put downward pressure on the Euro; the party has threatened to take Italy out of the single currency.

* The spectre of global trade wars also seems likely to weigh on market sentiment early this week after president Trump last week, quite unexpectedly, announced plans to impose tariffs on steel and aluminium imports. The threat of these tariffs – and the prospect of retaliatory measures being imposed against the US – will have negative effects on steel and aluminium exporters, but the risk of broader trade wars developing could be felt far more widely across the industrial space. Expect volatility to remain elevated and risk asset spreads under widening pressure until there is some clarity on the outlook for tariffs and manufacturing input costs.

* Meanwhile, near-term market sentiment also remains susceptible to the rates market outlook, in the context of the latest rise in yields following the hawkish tilt to Fed chair Powell's testimony last week. Government bond yields have retreated from their early February highs, but with central banks biased towards balance sheet normalization and on the back of Powell's comments, the path of least resistance for yields likely remains higher. We believe that hedging this implied rising interest rate risk should remain a key focus for investors over the coming weeks and months. However, it is the velocity of any renewed selloff in rates that will dictate the broader market reaction. We remain of the opinion that the 10Y US yield reaching 3% will have limited impact, but a yield approaching 3.50% may begin to have asset re-allocation implications, triggering steeper quality curves.

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

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

Despite a hawkish testimony from the newly appointed Fed chairman, bond markets have seen decent retracements in yields, as CT10, CT5 and CT2's moved lower last week to sit at 2.80%, 2.57% and 2.22%, respectively. Across the pond both bund and gilt yields have also fallen further on the back of the large negative supply expected in March. 10Y bund yields currently sit at 0.62% with 10yr gilts at 1.43%.

Attention remains on volatility levels on the US FRA/OIS spreads and the possible ramifications and the spill over into other markets. At one stage last week, March-18 basis was above 47bp before pulling back to 40bp. Investors with floating rate LIBOR liabilities can hedge their exposures by buying Libor/OIS structures and thus mitigating any widening of the LIBOR basis.

G-10 FX	Macroeconomic/Fundamental Analysis	Views (Bearish/Bullish) 2-week Time Frame	Intermediate & Long-term Views (3mth & 12mth Time Frame)
EUR	All eyes have been on the Italian election and the German coalition talks over the weekend. Italian politics has never been easy to predict; market research reports are suggesting a 55% probability of a binary outcome and a clear winner. With no polls published since the blackout, market sources point to the centre right having approximately 37% of the vote. EUR crosses remain supported favoring friendly political outcomes in Italy and Germany; it remains a EUR dip buying strategy for the bulk of investors.	Neutral	3m 1.2500; 12m 1.3500
GBP	Another week of discussions around transitions and some hardening of stance around the Northern Ireland border, has seen a decent rally in both gilts and short sterling and further flattening of curves. With the huge negative net supply in March it's difficult to see any steepening pressure in the immediate future. The only question is how far the market will continue to flatten, with 2/10's now back to 52bp (from 72bp two weeks ago). GBP remains on the back foot with cable at 1.379 and EURGBP at highs of 0.8915	Bullish	3m 1.4500; 12m 1.5000
JPY	In a surprise turn of events the BOJ has decided to follow in the footsteps of other central banks towards normalization as early as 2019, insinuating that the central bank would reach their 2% inflation target by April 2019. Data wise, the Japanese employment date surprised to the upside, with the jobless rate ticking down to the lowest level since 1993 at 2.4%. That said there is no sign of any change in wage growth. No doubt an issue that could be discussed at this week's BOJ meeting. Elevated European (Italy) risk this coming week will likely fuel safe haven demand for JPY, putting yet more pressure on USDJPY with really no material support levels especially if we break below 105.00.	Bearish USDJPY – with preference to sell the rallies above 108	3m 107.00; 12m 108.00

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CHF	It was a big week for the CHF, with a recognizable uptick in GDP along with better than expected PMI manufacturing data. This week's inflation data release will be watched closely, with EURCHF likely to be highly sensitive to Italian headlines on Monday. That said, the price has been fairly stable in EURCHF with a range of 1.1470-1.1644 last month, with a notable support around 1.1450 that held quite well. A break of either side is needed to set the tone for a new trend.	Neutral Swiss although we are still alert to any escalation in global political tensions for safe haven flow	3m 0.9300; 12m 0.9700
AUD	Softer risk sentiment saw AUD decline even further last week to a low of 0.7713 and despite other commodity linked currencies reacting to the US steel and aluminum tariffs, AUDUSD remained un-phased as its major steel trading partner is actually China not the US. Most notably AUD declined last week against JPY; AUDJPY dropped nearly three big figures to reach 81.50 territory, which held twice last year ahead of major rebounds. This week we will have the RBA rate release in which the market expects no change with the same old rhetoric.	Bearish	3m 0.7500; 12m 0.7500
NZD	Despite the fact that last week was filled with top tier data such as NZ trade balance and building permits, the Kiwi did really move on its own merits. NZDUSD spent the first half of the week drifting lower from 0.7345 to 0.7186 before recovering on the back of dollar weakness along with a selloff in AUDNZD. Due to the uninspiring price range, we would anticipate a pull back to materialize towards mid-0.7300s which would provide decent opportunities to fade the move lower, until then we would advocate being on the sidelines.	Neutral	3m 0.6800; 12m 0.6300
CAD	CAD has been the clear underperformer recently. USDCAD closed higher every day last week, and now eyes 1.3000 as a next target. The latest headlines that Trump is planning to impose tariffs on imported steel and aluminum fueled the move higher even more as this adds further uncertainty to Canada's trade relationship with the US along with NAFTA. Focus this week turns to the BOC rate decision. The market is expecting policy to be unchanged at 1.25%; focus will be more on the Bank's outlook and guidance.	Neutral	3m 1.2500; 12m 1.2200

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