SMBC Capital Markets, Inc.

fxPoetry

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A Bronx Cheer

Unhinged is unique
To no one single nation
Rest in peace Shinzo

The terrible news this morning is that former Japanese PM Shinzo Abe was fatally shot at a campaign event for the ruling Liberal Democratic Party (LDP) ahead of Sunday's national elections. A suspect was arrested who apparently bore a grudge against Abe-san, but claimed it wasn't political. Abe was the longest serving PM in Japanese history and the namesake of Abenomics, the effort to shake Japan out of its deflationary mindset and enhance GDP growth. He was still relatively young, at 67, and there was talk that he may run again in the future after recuperating from the illness that led to his resignation. Frighteningly, this appears to be a sign of the times, where disagreement no longer leads to discussion and debate, but to violence. While the news is awful, market participants did not appear to consider it sufficient to change the narrative and I fear it will be forgotten all too soon. RIP Abe-san.

While payrolls are now front of mind
Investors are lately inclined
To gladly accept
A Fed that has kept
On claiming they'll not fall behind

Alas, we continue to hear
More talk that, the rest of the year
Fed funds must move higher
To sate Jay's desire
Inflation, to give a Bronx cheer

As the week comes to a close, all the attention will be on this morning's employment report at 8:30. Current expectations are as follows:

Nonfarm Payrolls	268K
Private Payrolls	237K
Manufacturing Payrolls	21K
Unemployment Rate	3.6%
Average Hourly Earnings	0.3% (5.0% Y/Y)
Average Weekly Hours	34.6
Participation Rate	62.4%
Consumer Credit	$30.8B

Source: Bloomberg

Yesterday we heard from two of the more hawkish FOMC members, Waller and Bullard, and both were talking up 75 basis points later this month with at least 50bps for September. Bullard would like to see Fed Funds between 3.50%-4.0% by year end, which implies a lot of 75bp hikes between now and then. Remember, earlier this week we also saw a better-than-expected ISM Services number of 55.3, although that was still a decline from the previous month. The point is that the recession narrative took a small hit, and even the Atlanta Fed's GDPNow forecast rose to -1.865%, albeit is still showing a pretty big negative outcome.

Thus, today's data will really help inform a lot of thoughts regarding whether or not the US economy can readily withstand the mooted rate hikes promised by the Fed and priced by the market. While the expected NFP number is a sharp decline from last month and would represent a continuation of the downtrend from the beginning of the year, it would still be a very solid number in the scheme of things. For instance, the average NFP number in the 5 years prior to the Covid dislocation was 193K. As well, there are other indicators that the job market remains tight, notably the JOLTS Job Opening report which Wednesday printed at 11.254M openings, more than twice as many as there are allegedly people looking for jobs. That dynamic continues to support wage growth and is the basis of the Fed's claim the economy is strong. As I said, today's data seems to hold great significance for the near-term activity in markets. We shall see.

Leading up to the data, it should not be surprising that risk attitudes are somewhat mixed. Asian equities saw much smaller movements than we have been getting used to with the Nikkei (+0.1%) and Hang Seng (+0.4%) both managing gains while Shanghai (-0.25%) edged lower. European bourses are behaving better on the continent (DAX +1.25%, CAC +0.55%) than in the UK (FTSE 100 0.0%) although there really hasn't been any data of note. The UK story remains dominated by the leadership change with the latest controversy over how long it will take to elect a new Tory leader, thus how long BoJo will remain head of the caretaker government. The pound (-0.3%) which rallied on the Johnson resignation yesterday, seems to be coming back to reality and appears to have much further to decline. Finally, US futures are pointing lower by about -0.4% ahead of the numbers.

In the bond market, 10-year Treasuries are lower by 1.3bps this morning and hovering just below that key trading level of 3.0%. Traders are trying to figure out if the Fed's aggressiveness is going to cause that recession (lower yields) or not be sufficient to halt inflation (higher yields) and 3.0% seems to be the current pivot. There is ample opportunity for a large yield move today on a NFP print that is far from expectations. As to the continent, Bunds (-4.9bps) and OATs (-4.8bps) are both rallying as the market unwinds some of yesterday's movement and looks ahead to more comments from Madame Lagarde. BTPs (-8.7bps) are outperforming as there is a growing belief Lagarde will reiterate the ECB's determination to prevent fragmentation.

Oil prices (-0.2%) are consolidating after a very strong day yesterday that saw a nearly 3% rally. NatGas (-1.4%) is also consolidating after an even bigger rally, 15%, yesterday which also saw European and UK gas prices explode higher. While these markets remain extremely volatile, the longer-term structural issues have not, and almost certainly will not, be adequately addressed on a timely basis. It becomes very easy to envision a situation come the autumn when Vladimir Putin turns off the gas taps to Europe and the devastation, for both individual health and the economy, is dramatic. Rationing is already beginning, and I fear things will only get worse. In the metals markets, gold is unchanged this morning while copper (-1.9%) is reversing some of its sharp gains yesterday, as is aluminum (-0.55%). I haven't highlighted grain prices as they have all fallen from the peaks seen in the spring, but the question of supplies around the world remains open and fears of famines in parts of Africa and Asia remain quite real.

Lastly, the dollar is back to its winning ways against most of its counterparts with only JPY (+0.1%) managing to eke out some gains vs. the greenback in the G10 space, although the magnitude of today's moves is much less than we saw earlier in the week. So, CHF (-0.3%), NOK (-0.2%) and EUR (-0.2%) are really the laggards along with the pound. That said, I would be remiss if I didn't point out that the single currency has traded to new lows for the move (1.0072) and seems to be approaching parity inexorably. In fact, a very strong number this morning may be sufficient to get our first real test.

In the emerging markets, the picture is the same, with most of the bloc softer vs. the dollar and only a couple of minor positives. THB (+0.35%) is the leader of the pack despite comments from the central bank that they will not get involved if the baht weakens further on news from the US. Meanwhile, the other gainer of note was PHP (+0.25%) after comments that hinted at the possibility of a 50bp rate hike by the central bank there. On the downside, ZAR (-1.4%) and HUF (-0.7%) are the worst performers with both feeling the heat of a declining risk appetite and concerns over a more aggressive Fed.

And that is the day. Historically, after the payroll report is released, there is a flurry of activity but things definitely slow down quickly. As we are already in the middle of the summer and market liquidity is suffering accordingly, my sense is if large exposures need to be hedged, earlier is clearly the best choice. For now, I remain very constructive on the dollar and will be that way until they start to explain they have achieved their goals. Of course, at that point, the dollar will have already fallen a bunch. In the meantime, look for parity soon, and a run toward 0.95 as the summer progresses.

Good luck, good weekend and stay safe
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