Domestic Politics and the FX Markets

- Reaction to Indian & Australian elections provide useful prism through which to consider political drivers for markets
- EU Parliamentary elections might provide some useful indicators for changing face of national politics
- Helps set backdrop for potentially volatile summer in UK

The election results in India and Australia over the weekend (albeit just exit polls for the former) provided solid boosts for local equity markets as well as (at least temporarily) the INR and AUD.

The interesting point was that in neither case could it be argued that the rallies that emerged were particularly based on the economic records of the victors.

In India the election took place against a backdrop of what has been described as "acute agrarian distress and widespread youth joblessness" and memories of the 2016 demonetization drive.

While not as extreme, in Australia concerns over the outlook for the economy (related both to the cooling housing market and the trade relationship with China) was supposed to have been a major issue.

Given this backdrop, it’s arguable that it was relief from the

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Newswatch

1. Australia: Philip Lowe, Reserve Bank of Australia governor, says: “A lower cash rate would support employment growth and bring forward the time when inflation is consistent with the target. Given this assessment, at our meeting in two weeks' time, we will consider
fear of change that proved the driving factor behind yesterday’s moves.

In Australia the key driver appeared to be relief from concerns about Labour’s perceived radical reform agenda (with a particular focus on the financial sector), while in India political continuity and the promise of business-friendly reforms were factors cited behind the rally.

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While this is hardly a surprising insight, it still provides a useful prism through which to consider some of the other political risks that might arise elsewhere in the months ahead, most immediately this week’s European parliamentary election.

While the elections have barely stirred investor interest so far (despite signs of a real shift in the offing) they could end up mattering should they provide some fresh insights into domestic voting patterns.

Given the impact the French presidential election race in 2017 had on the EUR, along with the volatility that emerged in 2018 in the aftermath of the Italian election, this is therefore worth keeping an eye on.

Possibly the most closely watched results from the election will be those from the UK, given that the most recent polling shows the Conservative Party finding it hard to make it even into third place.

When coupled with the major losses seen for the party in the recent local elections it appears the stage is being set for what looks like another summer of political uncertainty in the UK, with even the possibility of a general election emerging either later this year or in 2020.

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2. **US/China:** Commerce secretary, Wilbur Ross, says that the administration will issue a licence that will allow US companies to keep doing business with Huawei for the next three months.

3. **US/China:** Chinese ambassador to the EU, Zhang Ming, says: “This is wrong behaviour (on Huawei), so there will be a necessary response. Chinese companies’ legitimate rights and interests are being undermined, so the Chinese government will not sit idly by.”

4. **US:** Federal Reserve Chairman Jerome Powell says that “business debt has clearly reached a level that should give businesses and investors reason to pause and reflect.” He adds that “another sharp increase...could increase vulnerabilities appreciably.”

5. **Japan:** Bank of Japan Governor Haruhiko
Some sense of the potential impact that the shifting tectonic plates in UK politics might have can be gauged from the fact that last week saw GBP put in its worst performance in at least six months against the USD despite the fact that most of what happened was less than surprising.

While geopolitics might not be impacting currency markets at present, it’s plain from the price action seen in a variety of markets over the past week that domestic politics remains a key factor, with fear of the unknown likely the main issue.

Please direct questions or comments to:

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Kuroda warns: “If trade tensions persist, they would have a widespread impact on global and Japanese economies via business sentiment and market developments.”

On the Radar

May 21, 2019

• UK May CBI trends - orders (1100 BS): Reuters consensus forecast -5; previous -5

• US Apr existing home sales (1500 BST): Reuters consensus forecast 5.35 mn; previous 5.21 mn

• EZ May consumer confidence (flash) (1500 BST): Reuters consensus forecast -7.7; previous -7.9

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