Emirates NBD

بنك الإمارات دبي الوطني

# FX Week

Weekly
17 May 2020

## USD advances amidst renewed uncertainty

With equity markets enduring a more volatile time, with US indices ending down over the week as a whole, it is not such a surprise that ‘riskier’ currencies have also lost ground, with the AUD, NZD and CAD going from the previous week’s best performers to being the worst. The USD advanced against all major currencies, enjoying its biggest weekly gain since late April, although the DXY index is still trapped in an overall tight range that has been in place since March.

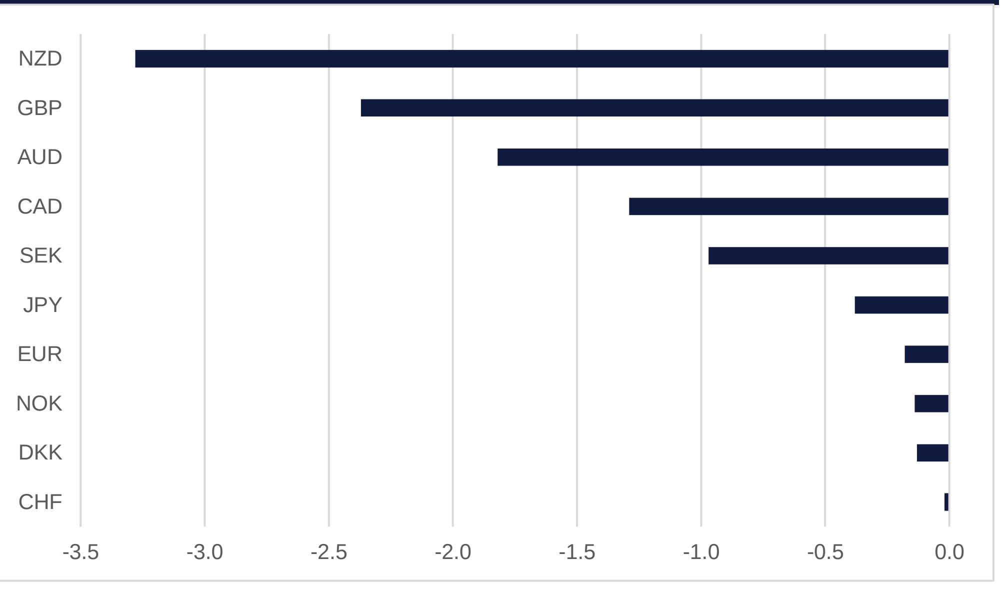
## More questions than answers

It is becoming clearer that the latest phase of the coronavirus crisis appears less straightforward than a month ago, when markets were recovering from steep losses after the initial shock of lockdowns, spurred on by enormous monetary and fiscal injections. Now with governments experimenting with easing these lockdowns markets are becoming less sure which way developments will go, especially with government policies often giving way to more questions than answers. This applies to the effect of easing restrictions on the incidence of the virus itself, but it also applies to the broader ramifications of emergency economic policies that have been applied in a hurry, but which could take years if not decades to unwind. Confidence in V shaped recoveries, popular a month ago, appears to be reducing, but uncertainty prevails about whether the eventual recovery path will be more U, W or even L shaped.

## Powell resists negative rates

Uncertainty about interest rates is also running high as Fed funds futures have continued to point to the risk of negative rates in the US despite Fed Chair Jerome Powell last week dismissing the strategy as inappropriate for the US at this juncture. To some extent the markets’ moves are understandable, however, with growth contracting in Q1 and likely to get much worse in Q2 (retail sales dropped 16.4% in April, while industrial production fell 11.2%), and with inflation turning negative (CPI fell -0.8% m/m in April). In such circumstances it is natural for some banks to hedge against the possibility of deflation, just as it will also be natural for others to buy inflation hedges if they are fearful of unlimited QE spilling over into resurgent price pressures further down the road. At this moment, the deflation threat clearly has the upper hand, but it should not be ignored that this trend could quickly reverse once the pandemic begins to retreat. Powell will testify this week where he is likely to repeat his cautious stance while repeating the need for more fiscal support.

**Weekly currency movement vs USD (%)**




*Source: Bloomberg, Emirates NBD Research*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## GBP back to March lows

Unwinding massive fiscal deficits is also receiving attention with the UK Treasury producing a paper on the steps which may need to be taken to repair a GBP300bn hole in the UK government finances in the aftermath of the crisis, including tax rises and spending cuts. This drew sharp criticism, however, at a time when the UK economy was already plunging into recession with a growth contraction of 2.0% reported in Q1. Critics said it would be 'economic suicide' to hike taxes to slash the deficit, with the government being urged to ignore the debt for now and promote growth as a way out of the crisis. GBP had one of the worst weeks of the major currencies, falling 2.37% against the USD to reach its lowest point since late March, which was also not helped by the high numbers ofcovid-19 deaths in the UK, confusion about government policies for ending the lockdown, and a breakdown in talks with the EU over post-Brexit trade arrangements.

## Coronavirus blame game heats up

The blame game for the crisis is also picking up between the US and China, and not only in terms of rhetoric, with President Trump starting to take measures to punish China. The first of these saw President Trump direct a prominent US pension fund managing pensions of millions of federal employees not to invest in Chinese companies, threatening that the US could 'cut off the whole relationship with China'. The second saw a tightening of restrictions placed on Chinese technology company Huawei, preventing companies from selling products to it if these have been made using US technology or hardware.

## CNY softness resumes

Prior to this crisis markets had been hoping that US-China trade relations were on the mend, but now not only are they seemingly getting worse again, but they are also straying into the financial realm which carries different and perhaps greater risks. At a time when the US needs to issues trillions of more dollars in Treasury debt this year, provoking the second biggest foreign holder of US Treasuries in the world could easily backfire, certainly by generating renewed volatility. It seems likely that markets will have to endure many more months of heightened threats, counter threats, sanctions and retaliation, which are likely to keep risk aversion elevated, especially in a US election year.

## Hurting AUD and NZD in the process

This will underpin the USD periodically as it is at the moment, with the CNY beginning to lose ground again back above 7.10 at the end of last week. Our near term bias is also for USD firmness to continue in general whilst the visibility about the shape of the economic recovery remains poor.

Such losses for the CNY also translated into weakness for the AUD and the NZD, with the NZD having the biggest losses (-3.3%) after the RBNZ also signaled it was open to cutting interest rates lower, even potentially taking them negative from their current 0.25%.

## FX Forecasts

| FX Forecasts – Major | | | | | | Forwards | | |
|---|---|---|---|---|---|---|---|---|
| | 15-May | Q2 2020 | Q3 2020 | Q4 2020 | | 3m | 6m | 12m |
| EURUSD | 1.0820 | 1.0500 | 1.1000 | 1.1200 | | 1.0841 | 1.0863 | 1.0911 |
| USDJPY | 107.06 | 107.00 | 110.00 | 112.00 | | 106.91 | 106.72 | 106.28 |
| USDCHF | 0.9715 | 0.9600 | 1.0000 | 1.0000 | | 0.9689 | 0.9661 | 0.9602 |
| GBPUSD | 1.2116 | 1.2000 | 1.3000 | 1.3500 | | 1.2120 | 1.2124 | 1.2132 |
| AUDUSD | 0.6413 | 0.6300 | 0.6600 | 0.7000 | | 0.6414 | 0.6413 | 0.6411 |
| NZDUSD | 0.5935 | 0.6000 | 0.6400 | 0.6800 | | 0.5931 | 0.5928 | 0.5926 |
| USDCAD | 1.4109 | 1.400 | 1.3800 | 1.3500 | | 1.4106 | 1.4104 | 1.4102 |
| EURGBP | 0.8935 | 0.8750 | 0.8462 | 0.8296 | | 0.8949 | 0.8965 | 0.8998 |
| EURJPY | 116.02 | 112.35 | 121.00 | 125.44 | | 116.02 | 116.02 | 116.02 |
| EURCHF | 1.0517 | 1.008 | 1.1000 | 1.1200 | | 1.0509 | 1.0500 | 1.0481 |
| | | | | | | | | |
| | 15-May | Q2 2020 | Q3 2020 | Q4 2020 | | 3m | 6m | 12m |
| SAR | 3.7578 | 3.7500 | 3.7500 | 3.7500 | | 3.7605 | 3.7631 | 3.7740 |
| AED | 3.6730 | 3.6730 | 3.6730 | 3.6730 | | 3.6749 | 3.6773 | 3.6828 |
| KWD | 0.3093 | 0.3020 | 0.3020 | 0.3020 | | 0.3101 | 0.3109 | - |
| OMR | 0.3850 | 0.3850 | 0.3850 | 0.3850 | | 0.3886 | 0.3924 | 0.4008 |
| BHD | 0.3775 | 0.3770 | 0.3770 | 0.3770 | | 0.3760 | 0.3760 | 0.3782 |
| QAR | 3.6655 | 3.6400 | 3.6400 | 3.6400 | | 3.6634 | 3.6608 | 3.6573 |
| EGP | 15.7349 | 15.7500 | 16.0000 | 17.0000 | | 16.1750 | 16.6300 | 17.7500 |
| INR | 75.575 | 75.000 | 73.000 | 71.000 | | 76.8100 | 77.6600 | 79.3300 |
| CNY | 7.1019 | 7.2000 | 7.2000 | 7.2000 | | 7.1533 | 7.1785 | 7.2215 |
| SGD | 1.4268 | 1.40 | 1.40 | 1.35 | | 1.4270 | 1.4263 | 1.4260 |
| | | | | | | | 3.7503 | |
| | 15-May | Q2 2020 | Q3 2020 | Q4 2020 | | | | |
| MAD | 9.8884 | 10.5000 | 10.5000 | 10.0000 | | 9.9327 | 9.9623 | 10.0226 |
| TND | 2.9100 | 3.0000 | 3.2000 | 3.0000 | | 2.9900 | 3.0750 | 3.2800 |
| TRY | 6.9013 | 7.0000 | 7.2000 | 7.2000 | | - | - | - |

*Source: Bloomberg, Emirates NBD Research*
**Denotes USD peg*

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