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Article

FX: Nowhere to hide (apart from the dollar)

Emerging market policymakers are struggling to contain losses. Our worry is that even good quality currencies could start to come under pressure

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USD: Pressure on EM broadening as local policy makers struggle to react

Emerging market currencies remain very fragile as an asset class, with local policymakers struggling to contain losses. The pressure is geographically diverse. Argentina leads losses in Latin America, where rate hikes, intervention and IMF support have done little to contain losses. In Asia, the focus is very much on the Renminbi, where the People's Bank of China may well reintroduce counter-cyclical fixing measures to prevent a 7-handle printing on USD/CNY. Indonesia may well hike again today and has recently introduced measures to address its Achilles heel of the trade balance. And in EMEA, those with large current account deficits such as Turkey and South Africa remain vulnerable. And our worry is that even good quality stories like the Polish zloty and Czech koruna start to come under pressure as deleveraging escalates. The decisive break lower in EUR/USD is only adding to the pain for emerging market investors and looks to be generating a self-reinforcing loop. This all seems far removed from the happy place which is the US, where consumer confidence remains strong and should result in another solid retail sales reading today. We are worried that the outlier here is the US equity market. We could see the Japanese yen outperform should US equities start to suffer – or President Trump tries to talk the dollar down – or even threatens intervention. The US dollar index remains on course for 97.80 – threatening 1.12 in EUR/USD.

EUR: Poor price action

If the options market is anything to go by, all that euro bullishness after the French election last May has evaporated. The one-year risk reversal, or the price the market is prepared to pay for a 25 delta euro put versus an equivalent euro call, is now at 1.36% in favour of EUR puts – the most EUR bearish since April 2017. With emerging markets on the back foot and de-leveraging triggering broad dollar demand, EUR/USD seems on course for 1.1200. If Turkey is adding to EUR underperformance, then we should look out for some potential key events such as: i) will US pastor be released by a deadline tomorrow and ii) will Turkish authorities offer anything new in an investor call on Thursday? But ultimately the strong dollar and US trade policy is driving FX markets right now.

GBP: Sideshow

GBP is playing second-fiddle to events in emerging markets and the strong dollar right now. The

UK's large current account deficit and exposure to the financial sector typically sees GBP trading as a risk-sensitive currency, warning of downside risks in GBP/USD given the current climate. Cable could see 1.2600/2620.

AUD: We're surprised AUD hasn't fallen further

With a nearly flat US yield curve and copper breaking to a new low this week, we're surprised AUD/USD has not fallen further. Expect a test of 0.7160, 2016 low.

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