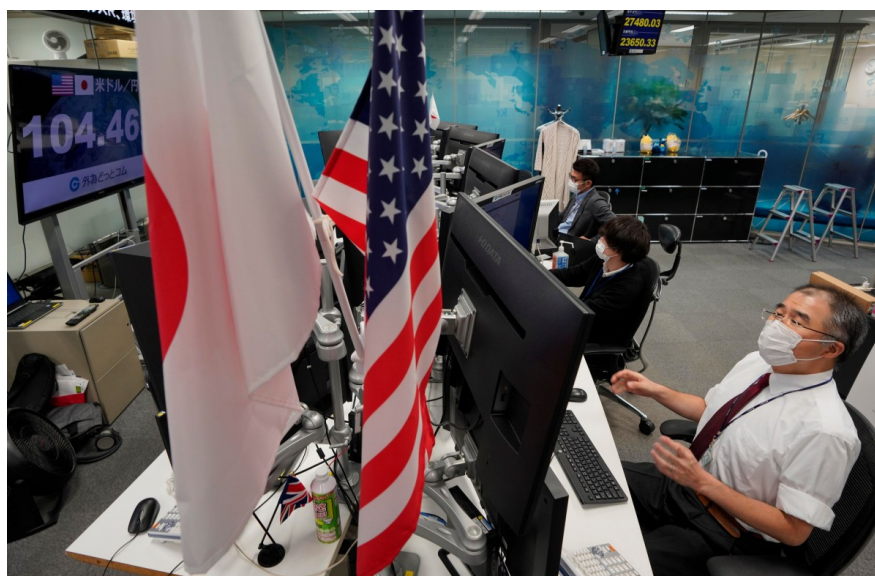


FX and the US election: Too close to call

One of the few things clear so far is that we are not going to see a Democrat landslide win as polls had suggested. That has wrong-footed an FX market which was positioned for some clarity. High beta FX, such as NOK and AUD in the G10 space and MXN, CNH and ZAR in the EM space look set for more volatility potentially into Friday



Hold your horses

FX markets had gone into Tuesday's election priced for a clean Biden win. This was evidenced by the likes of MXN and CNY trading close to their 2020 recovery highs against the dollar – the countries of these currencies some of the most exposed to Trump's protectionist agenda.

Instead, early news that Republicans had performed well in Florida and that exit polls pointed to a much closer race than had been expected have warned of a return of the Red Wave. In response, CNH briefly sold off nearly 2% in early Asia on the Florida news, before recovering a little on news that the Democrats had re-taken Arizona.

Based on polling and results so far, most political pundits suggest the Presidential election race will come down to the results in Pennsylvania, Michigan and Wisconsin – or the key rust belt states that Trump wrestled from the Democrats in 2016. However, given the close race and the counting of postal votes in those states – which has only started today – a clean result from Pennsylvania

and Michigan may not be seen until Friday. Wisconsin is expected to produce a result Wednesday morning, apparently.

More volatility into Friday

Given the lack of clarity, expect to see more volatility in FX markets into Friday. For example, it now seems the path of Wisconsin (US Wednesday morning) could move markets, and then we will be left with partial counting of Pennsylvania and Michigan potentially into Friday morning.

This very close outcome brings back the risk of a contested election or one – like that seen in 2000 – which could be decided by the courts. That certainly wasn't priced into FX markets and we would say the JPY should stay supported on the crosses – potentially into Friday. We pick out the JPY since, in the G10 space, it has been least correlated with the very popular reflation narrative of a steeper US yield curve, firmer equities, and higher commodity prices.

Elsewhere, the market had gone into this election reasonably short the dollar, and this unexpectedly close race could trigger a little more short-covering. So far EUR/USD has held the bottom of its range at 1.1600, but unless Biden starts to quickly pick up some swing states like Georgia or N. Carolina, 1.1600 could come under pressure again.

As we highlighted in our [G10 FX Election Scorecard](#), the NOK and AUD look most exposed to the gyrations of the Presidential vote (one-week implied volatility in these two are the highest in the G10 space at 16% and 12% respectively).

Given that the risk of a contested election is higher than priced by the market – and that US equities sold off 8% while the Supreme Court decided what to do with the Florida recount in 2000 – our overall bias is that risk assets and risk-sensitive currencies will remain vulnerable this week.

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