

FX Daily: Big week for Europe

The EU council meeting on Thursday is likely to have a bigger impact on European currencies than the European Central Bank meeting on the same day. We can't rule out a negative outcome on both the Recovery Fund and Brexit



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➔ USD: Watch out for US Treasury yields this week

FX markets have started the week in quiet fashion. Chinese data was relatively healthy and news of a record \$75bn monthly trade surplus for China in November merely adds to the bullish case for the renminbi. After a [soft jobs report](#) on Friday, a big focus this week will be on whether Congress can make progress on the \$908bn bipartisan fiscal stimulus deal at a time when poor virus trends are threatening harsher lockdowns. In a week of heavy supply, one of the big talking points of the week will be whether US 10-year yields push above 1.00%. In such a case, expect Japanese yen underperformance on the crosses and perhaps some of the more fragile emerging market FX rates – such as the South African rand – to start to come under pressure. Overall, however, we suspect that any dollar bounce proves fleeting – especially with the Federal Reserve prepared to deliver more stimulus should it be required. Please see our [G10 FX Week Ahead](#) for our full preview of this week's events and what they mean for FX markets. DXY can drop to 90.

➔ EUR: Heading towards another crunch period

Suffice to say it is big week for Europe given both the European Central Bank meeting and the EU council meeting on Thursday. Please see our team's take on the ECB [here](#) and from the FX side, we suspect the ECB will have a tough time to significantly weaken EUR/USD given the broad and powerful dollar bear trend. The latter event will probably have a greater impact on European FX. The ability to get Poland and Hungary on board for the EU Recovery Fund (or cut them out – not ideal) will impact the euro this week and one can never rule out some disappointing news – so care should be taken. We do though think that EUR/USD should be receiving good demand from Asian FX reserve managers – recycling intervention proceeds – and think EUR/USD could push up to 1.2250 this week.

⬆️ GBP: Down to the wire

Cable has stalled at 1.35 – not a surprise given the genuine risk that neither the UK nor the EU fail to soften their core positions over new-found sovereignty or level playing fields respectively. Like most, we do tend to favour a deal being struck and given the EU leaders' summit on Thursday – this should be the week for a deal. We suspect a deal would trigger some strong gains through 1.35 and probably drag the European FX complex higher against the dollar.

⬆️ CNY: November FX reserves should be interesting

China releases its November FX reserves figure today and should be of interest given the \$13bn and \$10bn reserve increases already announced by Taiwan and Korea. The size of these increases represents the amount of 'smoothing' these central banks have had to perform in order to accommodate the surge in both portfolio flows and trade flows. A big rise in FX reserves should serve as a reminder that Asian FX is at the forefront of the EM FX recovery trade.

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