

FX Daily: Commodity FX remains the most vulnerable

Concerns over the coronavirus are weighing on global markets, and commodity currencies- which have rallied since December- are most vulnerable to a pullback



➔ USD: Commodity currencies remain the most vulnerable

Concerns about the impact of coronavirus on the global economy continue to weigh on markets. Commodity FX has been underperforming within both G10 and emerging market FX (Norwegian krone and Australian dollar within the G10 and the Chilean peso and Russian rouble within emerging markets being the worst performers in the respective spaces since last week). The rally since early December (due to optimism associated with the 'phase one' trade deal) and subsequently less stretched valuations have provided scope for some reversal in these pro-cyclical currencies. As long as current concerns remain in place (also evident in the bond market where core yields have been dropping) the dollar and the yen should continue doing well while a rebound in EM FX and cyclical G10 currencies is unlikely. Price action overnight suggests some stabilisation in pro-cyclical currencies today (after the large declines yesterday) but without more progress / evidence of stabilisation, a more meaningful and lasting rebound is unlikely.

⬇️ EUR: Knocking on the EUR/USD 1.1000 door

Faltering risk sentiment and the uninspiring German Ifo yesterday point to a weaker EUR/USD as the dollar benefits from its safe-haven appeal while any ECB policy normalisation seems remote. In Sweden, December retail sales are expected to record another monthly decline today, underlining the state of the economy which is inconsistent with further Riksbank tightening. We look for higher EUR/SEK as negative risk sentiment is putting pressure on the Swedish krona – although the currency is likely to continue outperforming its Norwegian counterpart in the short-term as the decline in oil prices is, in relative terms, more negative for the krone.

➡️ GBP: Waiting for the BoE meeting

Sterling modestly weakened overnight but with the market split on the outcome of the January Bank of England meeting on Thursday (around a 60% probability of a rate cut priced in vs our on-hold call), the pound shouldn't move too much ahead of the actual rate decision.

⬇️ HUF: NBH still on autopilot

We expect the National Bank of Hungary to keep its policy stance unchanged today as the incoming inflation and economic activity data fit the central bank's base case. The recent change in FX swaps reflects the ongoing liquidity situation and we don't want to read too much into it. With the general risk environment being unfavourable for emerging market FX (within the central and eastern European FX space, the Polish zloty, Czech koruna and Hungarian forint have all been under pressure recently) and the forint exerting a deeply negative real rate, we continue to see the risks to EUR/HUF as skewed to the upside.