

FX Daily: Dollar crisis can extend

The dollar and Treasuries are acting as high-beta assets to risk sentiment and remain highly vulnerable to further selloffs. Even if the dollar bounces on any hint of positive news on trade now, we suspect repairing the damage will require a broader unwinding of Trump's protectionism policies. A move to 1.15 in EUR/USD is now a more tangible possibility



The dollar is now a high-beta currency

⬇️ USD: The new high-beta in town

A mad week for markets is ending with heavy losses for the dollar. The FX scorecard is speaking volumes; in G10, only the illiquid Norwegian krone is flat against the dollar since last Friday. Gains stretch from the “modest” 0.8% of the pound, to 2-3% of the euro, Australian dollar and New Zealand dollar and 4.5% of the Swiss franc.

The question of a potential dollar confidence crisis has now been definitively answered – we are experiencing one in full force. Yesterday's cross-asset price action demonstrated a radical shift away from US assets, with both equities and Treasuries declining despite a core CPI reading substantially below expectations (0.1% versus consensus 0.3% month-on-month).

Clearly, markets have dismissed March inflation as an outdated figure and remain concerned about the combined threat of inflation and growth deceleration. While the 30-year Treasury

auction demonstrated unexpected strength yesterday (mirroring Wednesday's robust 10-year auction), the USD swap spread expanded further (10Y now 56bp), and our rates team maintains a bearish Treasury view. We also cannot exclude that the budget resolution passed by the House yesterday, which poses significant funding questions for tax cut extensions, is adding another layer of risk premium to risk assets and Treasuries.

The dollar collapse is working as a barometer of "sell America" at the moment. The rotation to other traditional safe-havens like CHF, the Japanese yen or even the euro is justified by the loss of USD safe-haven appeal. But the USD drop against high-beta currencies (including the China-sensitive AUD and NZD) is a signal that markets are heavily building positioning for a broad-based dollar decline.

At this stage, picking a bottom in the dollar is as risky as trying to guess Trump's next move on tariffs. That's because the dollar is – like Treasuries – currently acting as a risk-sensitive currency, the opposite of a safe haven. This means USD can jump alongside battered equities at any hint of good news on trade, but we suspect that only a substantial reversal of protectionist measures, particularly regarding China, can sustainably fix the damage the dollar has been dealt in the past week. Downside risks to USD remain high, and DXY can easily clear the 100.0 support today.

On the data side, March PPI figures are released today. Those have quite a lot of relevance for the Federal Reserve's preferred measure of inflation – the core PCE. University of Michigan figures are also released, but we wouldn't be surprised by a limited impact from data. There are a lot of Fed speakers in the calendar, and markets will be quite attentive to whether the better CPI print leads to some members opening to an earlier cut to (implicitly) calm market jitters. The implied probability of a cut in May remains low, around 30%.

Francesco Pesole

EUR: 1.15 not unreasonable

The euro remains a key recipient of dollar outflows, and is currently trading around 1.125 after major overnight swings that saw it trade as high as 1.138. Alongside its attractiveness as a liquid reserve currency, markets probably remain relatively optimistic that the EU isn't willing to escalate the trade war with the US for now.

It's important to note that the massive EUR/USD rally is almost entirely a function of the loss of confidence in the dollar, and not at all justified by underlying short-term rate dynamics. The EUR-USD two-year swap rate gap has actually widened in favour of the dollar in the past week, currently standing at 155bp. That level is consistent with EUR/USD trading not far from 1.05. When adding the relative equity effect and the freshly inverted correlations with equities, we get a short-term fair value of around 1.09, according to our estimates. We must take that with a pinch of salt, as extreme market volatility and unconventional turns in correlations reduce the explanatory power of such models.

That said, EUR/USD is certainly overvalued at these levels, by around 4% in our calculations. But we note that relatively similar conditions in the summer of 2020 led to an overvaluation peak of 6% in EUR/USD. In current terms, that would roughly equal a move to 1.15. Given the high volatility and poor liquidity conditions of the FX market, 1.15 is a reasonable near-term target for EUR/USD unless decisions in Washington rebuild some sort of confidence in the dollar. Volatility is here to stay, so expect corrections in EUR/USD to be outsized too.

Francesco Pesole

📈 CHF: Betting on no SNB intervention

The Swiss franc had its biggest one-day rally since 2015 yesterday, emerging as the preferred recipient of safe-haven flows leaving the dollar. USD/CNH is tentatively rebounding above 0.820 this morning following an acceleration of the drop overnight that saw the 0.814 level being briefly touched.

It appears that the market's preference for the Swiss franc is mirroring the contained risk that the Swiss National Bank (SNB) will intervene to prevent excessive CHF strength. The reasoning here is that sustained, one-sided FX intervention would raise alarm bells at the US Treasury, which could then officially label Switzerland an FX manipulator and impose harsher tariffs.

On Monday, the SNB publishes sight deposit figures for March. A rise in sight deposits is generally a signal that the Bank is intervening to weaken the franc. That may not be too indicative of what the SNB is doing or is planning to do in April, as March's CHF gains vs the USD were considerably more contained (around 2%), and EUR/CHF actually rallied on the back of German fiscal stimulus. But a market that is clearly minded to over-reward defensive alternatives to the dollar may read stable sight deposits as another reason to stay bullish on CHF.

Unless the SNB does intervene to stop the rally or trade-related news turns the tide on the dollar, the risks remain on the downside for USD/CHF, which can test 0.800 before sustainably recovering.

Francesco Pesole

📉 CEE: Region under pressure once again

Today's data in the CEE region will again provide a bit of a local story, but probably won't change anything on the global lead, just like yesterday. This morning saw the release of inflation data in Romania – the latest in the CEE region for March. Inflation ticked down slightly from 5.0% to 4.9% year-on-year, in line with market expectations. Later today, inflation expectations in Turkey for April will be released, the first numbers since the March sell-off in the Turkish lira market. And we will also see current account numbers across the region today.

Still, the CEE market remains fully in the grip of the global story, which late yesterday switched the region back into risk-off mode. Contrary to our expectations, the Hungarian forint, as the most global beta currency, got hit and lost all the gains from the previous day's rally. EUR/HUF is thus heading towards the key 410 level again, which may be tested again today if market sentiment does not turn again. In Poland, after the market refused to price in any rate cuts, the zloty also came under pressure, reversing most of its gains. The Czech koruna remains a defensive play, and we continue to maintain a bias to see PLN/CZK lower from current levels.

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