

FX Daily: German court ruling on ECB's bond buying

We expect Germany's constitutional court to rule that the European Central Bank's bond purchases are indeed legal. But a negative ruling would likely have a disproportionately negative impact on the euro



⬇️ USD: Back under pressure

Markets continue to take the glass-half-full approach, tentatively shrugging off the risk of a deterioration in US-China relations (the key factor weighing on risk assets in recent days) and instead focusing on reopening plans for various economies (California aims to start easing lockdown measures from Friday) as well as the improving outlook for WTI storage capacity (with reserves in Cushing increasing the least since mid-March). This is a positive for the procyclical commodity currencies, in both the G10 and emerging markets space today. In the EM space, we see the rouble as the most attractive currency within the higher yielding commodity FX segment due to its relatively better fiscal situation and stable politics (vs the South African rand, Brazilian real or Mexican peso). This, in our view, reflects deteriorating USD medium-term characteristics (such as the shrinking interest rate advantage) which makes USD less attractive than the safe haven Japanese yen even in benign markets. We expect USD/JPY to break below 105 this summer.



EUR: German constitutional court ruling on PSPP

The German constitutional court will rule today on the legality of the Public Sector Purchase Programme. We and the market expect the court to deem it legal. A negative ruling would likely have a disproportionately negative impact on the euro, not only because it would come as a meaningful disappointment, but also because it could re-introduce a risk premium back into the common currency, which the ECB has been able to contain thus far by keeping BTP-Bund spreads under control and reducing the odds of a renewed debt crisis. As we argued previously, EUR risk premia containment via ECB measures should facilitate a higher EUR/USD this summer, when broad-based USD weakness kicks in.

📈 GBP: Benefiting from risk sentiment but upside contained until late June

Risk-sensitive sterling bounced off the EUR/GBP 0.88 level and is now back in the middle of its one month trading range. As we approach the end of June deadline for the extension of the transition period (and the risk of it not being extended), GBP upside vs EUR should be limited and the cross is unlikely to persistently break below the 0.8700 level in coming weeks.

📈 AUD: RBA meeting non-negative for AUD

The Reserve Bank of Australia left the interest rate and the 3-year government bond yield target unchanged overnight but extended the pool of eligible securities accepted as collateral for liquidity operations. To the extent this helps in improving the transmission mechanism and smoothing the functioning of capital markets, this is a non-negative for AUD. With risk sentiment benign, AUD/USD should stay around the 0.6500 level today.

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