

FX Daily: The cross-asset sweet spot

Looking past the short-term uncertainty of a contested US election, markets appear to be taking the scenario of a Joe Biden presidency and Republican Senate as a cross-asset sweet spot



Joe Biden arrives with his wife Jill Biden

Source: Shutterstock

📌 USD: Constrained Biden outcome still negative for medium-term USD outlook

Looking through the short-term uncertainty of the contested US election, markets appear to be taking the scenario of a Joe Biden presidency and Republican Senate as a cross-asset sweet spot as (a) there is clearly lower downside risk to bonds (vs the “blue wave” scenario given the likely smaller US fiscal stimulus); (b) there is still upside to equities (an albeit smaller US fiscal stimulus should still come; material tax hikes might be avoided, and there is likely to be an end to unpredictable trade wars); and (c) the outlook for cyclical FX remains constructive, both in emerging markets and the G10 FX space (for the same reasons as equities, with EM FX set to particularly benefit from the expected return of a rules-based system for international relations).

For sure, the scope for gains in cyclical FX and a more pronounced USD sell-off is now more limited vs the “blue wave” scenario but is still there nonetheless. We keep our bearish USD outlook for 2021 intact. In the near-term, if the election outcome is legally disputed, the associated period of uncertainty should pause gains in risk asset and introduce two-way volatility but if Biden is

eventually confirmed (and Republicans retain the Senate), the outlook for 2021 (mainly from Q2 onwards, once through the winter months) for pro-risk currencies looks constructive.

The FOMC should not surprise today and should have a limited impact on USD.

➔ EUR: Still constructive outlook

The "constrained" Biden scenario is not inconsistent with constructive 2021 EUR/USD outlook (recall this was the second most negative outcome for USD, as per our scorecard) as factors such as less aggressive US international policy, some limited US fiscal stimulus and still behind the curve Fed point to higher EUR/USD next year. In Norway, the NB to keep interest rates unchanged with the scope for a dovish surprise limited. EUR/NOK to stay below the 11.00 level

⬆️ GBP: Larger QE but limited hints of negative rates

While the [Bank of England delivered a larger QE top-up than expected](#) (GBP 150bn vs 100bn expectation), the limited new hints on the urgency for negative rates offset the larger QE in terms of the impact on GBP.

EUR/GBP to stay stable today

[Our bank of England reaction](#)

⬆️ CZK: Less dovish bias from the central bank than some may expect

The Czech National bank will stay on-hold today.

The new interest rate forecast shouldn't signal a rate cut to zero or to negative territory as (a) the latest downgrades to the Czech GDP outlook bring it back in line with the existing CNB forecast; (b) CPI is not expected to undershoot the 2% target.

With the market pricing in a partial rate cut, the cautious central bank stance should be positive for CZK today and help extend the recent CZK gains.