

FX Positioning: The big Kiwi short

During the week of 12-18 February, markets took aim at the Kiwi dollar amid rising virus-related concerns. NZD is now the biggest G10 speculative short. EUR/USD positioning kept inching lower and CHF corrected to more neutral levels. The net long positioning likely points at GBP downside ahead



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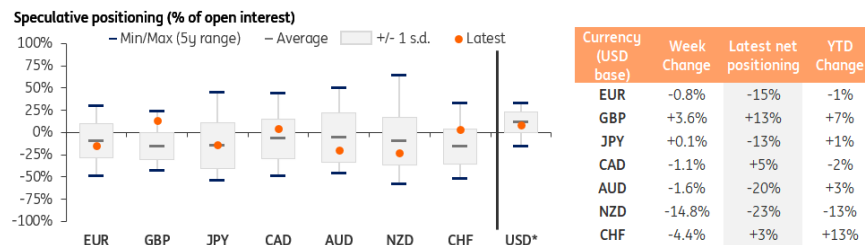
NZD back to being the black sheep of G10

For most of 2H19, the New Zealand dollar was the biggest short (positioning peaked at -57% of open interest in October) within the G10 space as US-China trade tensions posed a big risk to the New Zealand economic outlook and the Reserve Bank of New Zealand pioneered the global easing cycle. Last December, a big NZD short-squeeze (triggered by a risk-on run) helped the currency outperform most G10 peers. Its closest peer, the Aussie dollar, didn't show a similar bounce in speculative positioning data, with net positions lingering in short territory on the back of the bushfire emergency and RBA easing expectations.

When the Covid-19 outbreak became public in late January, there was a significant divergence between the NZD net positioning (+4% of open interest) and the AUD one (-14%). The rising concerns about the economic impact of a slowdown in Chinese activity affect both currencies and speculative markets did not see a reason to justify this more sanguine view on NZD.

The move in the week covered by the latest CFTC report (12-18 February) is in line with this, albeit very significant in size: speculators trimmed most of their net long positions and pushed the net positioning on NZD to -23% of open interest. This makes the NZD the biggest short in G10 (the table below provides an overview of G10 positioning).

FX Positioning Overview



*Note: Aggregate USD positioning versus G10 FX. As of 18 Feb 2020 (data reported with a lag).

Source: CFTC, Bloomberg, ING

We suspect the drop in NZD net positioning is overdone and may actually signal a relatively more stable environment ahead for the currency. While we acknowledge that the prospect of a Chinese slowdown doesn't bode well for the New Zealand economy, we also highlight that the fundamentals hardly warrant a more optimistic outlook for AUD than NZD, as shown in the positioning data.

The Australian economy is more reliant on the Chinese economy in terms of trade and the drop in commodity prices, particularly metals, is likely to hit Australia more than New Zealand, due to the composition of its exports. Incidentally, the RBNZ has retained a very sanguine approach when it comes to the impact of Covid-19 and sounded quite uneasy about any change in the monetary policy stance. However, we think that the additional downside risks to the outlook caused by the bushfires in Australia likely warrants another cut by the RBA sooner than later.

The more neutral positioning has proved to be a drag on the NZD since the start of the outbreak of the virus as it gave more room to investors to trim long positions compared to the already oversold AUD.

Now that this factor is out of the way, we expect AUD/NZD to have fewer frictions on any move lower, which is still warranted (in our view) by higher risks to AUD stemming from Covid-19 and the Chinese slowdown.

USD buying solid, CHF handled with care, GBP looks fragile

Amid the variable risk sentiment when it comes to the Covid-19 story, the dollar remains the currency of choice in G10 space. The EUR/USD net positioning kept inching lower, helped by rising concerns about the negative outlook for the eurozone economy as the virus disrupts supply chains. The extended downtrend in the spot market suggests more downside for the positioning gauge that may well keep moving towards the -20% (of open interest) mark, last seen in May 2019.

Buying of the Swiss franc kept slowing as the market begins to perceive that the current levels in EUR/CHF are close to the limit before the Swiss central bank intervenes. CHF net positions retracted to +3% of open interest after peaking at +10% earlier in February. Looking at the other safe haven, the yen, we expect the next report to display a jump in shorts, in line with movements in the spot market.

Elsewhere, GBP positioning rose on the back of rising fiscal stimulus expectations following the reshuffle in the UK Government. We think GBP positions as the biggest G10 long may well prove detrimental for the currency as it provides some room for short-squeezing once the uncertainty on UK-EU trade negotiations starts to bite more severely into UK sentiment.

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