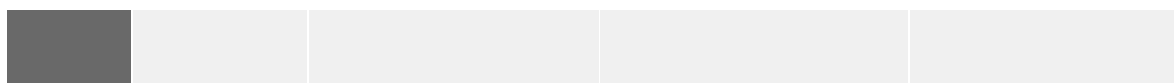


G10 FX Week Ahead: The dollar way or the highway

Markets appear less scared from the outbreak but are also pricing in the economic impact of a Chinese slowdown. In turn, a rebound in the most exposed currencies to China may still not be a story for next week (even if risk recovers), while grim data should keep JPY and EUR unable to recover. With no alternatives in G10, the dollar can hold on to its throne for now



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USD: No good alternatives in the G10 space

	Spot	Week ahead bias	Range next week	1 month target
DXY	99.2800	Mildly Bullish ↗	99.0000 - 110.1000	99.0000

- Excluding today's underperformance, triggered by some disappointing Markit PMI numbers in the US, the dollar is the big winner of this week. Indeed, the greenback presents an attractive carry, the second-best after CAD on a volatility-adjusted basis, safe-haven appeal and has previously been helped by data that keeps pointing at a robust US economic backdrop. However, an alternative perspective is simply that investors are quintessentially lacking alternatives in the G10 space. The outbreak of the coronavirus is still preventing a recovery in the Antipodeans. The CAD and NOK are curbed by both a choppy risk sentiment and an uncertain oil outlook, low-yielding EUR and JPY are unable to cash in on risk aversion due to the grim domestic outlook, CHF has already massively rallied and the risk of the Swiss central bank intervening is still material. Finally, the SEK has a very unattractive yield and is affected by Europe's economic woes.
- Unless we see a sizeable repricing of China-related risk, the situation appears unlikely to change next week. The economic calendar in the developed world looks quite unexciting, and in the US only durable goods orders, consumer confidence, and the second reading of 4Q GDP (all with limited market implications) are due. Some attention will be on Fed speak, with Richard Clarida, Charles Evans and James Bullard all set to make remarks. Except for some possible comments on the virus impact, the reiterated easiness of the Federal Reserve with the current policy stance suggests little scope for surprises. On the political side, keep an eye on the Nevada caucuses on Saturday. Given that Michael Bloomberg is not running in Nevada, so the spotlight will be on whether Bernie Sanders will be able to consolidate his lead and if Joe Biden continues to lose ground. All considered we think the dollar should at least retain its strength, with a chance for more appreciation. At this stage, we suspect that a break above 100 in DXY is just a matter of time.

EUR: Still no help from data

	Spot	Week ahead bias	Range next week	1 month target
EUR/USD	1.0861	Mildly Bearish 	1.0750 - 1.0900	1.0800

- EUR/USD has oscillated around the 1.08 mark this week, which was dominated by data releases, a strong dollar (until today's US PMIs) and tentative signs of recovery in risk sentiment. On the economic side, the picture for the eurozone hasn't improved. The ZEW sentiment indicator provided signals of mounting coronavirus-related concerns and the PMIs today were only good on the surface as they signalled a degree of supply chain disruption.
- Looking at next week's calendar, the German IFO will be one key challenge for the EUR. Consensus, according to a Bloomberg survey is centred at 95.2 in the Business Climate gauge (down from 95.9 in January) and our economists are looking for an even weaker reading at 94.9. Similar to what we saw earlier this week, a German survey may ignite the downtrend in EUR/USD: in this case, it would consist of a decisive move below 1.08. Other key releases will be inflation numbers for eurozone countries which will be interesting ahead of the March European central bank meeting and should mark a slowdown in CPI. While our economists believe the implications for the ECB may be limited, this may still stir some dovish sentiment among investors and surely would not help the EUR. In more general terms, the EUR still appears in an unpleasant position: the economic outlook for the eurozone keeps worsening and its funding characteristics still prevent it from taking full advantage of rebounding risk sentiment. When adding that the dollar may continue its bull run or at least remain relatively supported, we look for some downside towards 1.07 in EUR/USD next week.

JPY: Overstretched fall, but watch for more bad data

	Spot	Week ahead bias	Range next week	1 month target
USD/JPY	111.53	Neutral	110.60 - 112.10	109.00

- The yen has been the key underperformer in the past few days and is now trading around 112 versus the dollar. As [we wrote earlier](#), we think the yen's fall has been a combination of market shifting from short-term fears (i.e. global pandemic) to pricing in the long-term impact of a slowdown in China (and Japan is highly exposed in this sense); rising fears of recession in Japan after the grim 4Q growth data and finally speculation about sustained outflows from Japan as Japanese investors look for more attractive yields abroad as the financial year comes to an end.
- Looking forward, our short-term FX fair value model shows an overvaluation in USD/JPY over the 1.5 s.d. band, which makes a case for a mild correction or at least a stabilisation in the pair in the coming days. However, JPY may face more troubles on Thursday, when industrial production data for January may show a worse-than-expected slump, which would add to the negatives in terms of the economic outlook for the country. For the rest of the week, the coronavirus story will remain the key driver as investors are looking for more evidence that the pace at which the virus is spreading is gradually slowing.

GBP: Trade uncertainty to keep biting

	Spot	Week ahead bias	Range next week	1 month target
GBP/USD	1.2971	Bearish ↘	1.2780 - 1.3030	1.2900

- Despite CPI, retail sales and PMIs coming in quite supportive, sterling has not been able to move higher. We suspect that markets are increasingly pricing in the uncertainty related to the UK-EU upcoming trade negotiations. In this view, we would not be surprised to keep seeing data-driven GBP gains to be prevalently short-lived as investors turn increasingly bearish on the pound.
- Next week will be a quiet one in terms of data releases, which leaves the balance of risks for GBP/USD tilted to the downside, mostly because we expect any potential comment by both EU and UK officials about trade negotiations to be increasingly hawkish and hardly conciliatory. The budget, due to be released on 11 March is unlikely to match the expectations of an exceptionally aggressive fiscal stimulus.

AUD: Good news may not be enough to lift Aussie

	Spot	Week ahead bias	Range next week	1 month target
AUD/USD	0.6635	Mildly Bearish 	0.6560 - 0.6660	0.6700

- Despite market sentiment around Covid-19 has somewhat improved in the last few days, the AUD ends this week with an approximate 1.70% loss vs USD. This was partly due to labour data, which provided a mixed picture (unemployment rising along with full-time hiring) which sparked some speculation around more imminent RBA easing. However, more importantly, markets are starting to price in the impact of a slowdown in China and Australia's dependence on exports inevitably set AUD as a key underperformer.
- Next week will be quiet in terms of data releases, so attention will be only on Covid-19 developments. We feel even if positive news keeps dissipating the fears of a pandemic, this may not be enough to fuel an AUD rebound as markets continue to position for an impact on Australian data in the coming weeks.

NZD: Waiting to prove its resilience

	Spot	Week ahead bias	Range next week	1 month target
NZD/USD	0.6350	Mildly Bearish 	0.6280 - 0.6390	0.6400

- After the yen, the kiwi dollar has been the worst performer this week and this is despite RBNZ Governor Adrien Orr reiterating his relatively upbeat view on the impact of Covid-19 on the New Zealand economy. We suspect the NZD has suffered from an additional round of long-squeezing which has exacerbated the downside pressure on the currency. [As we've highlighted](#), NZD net speculative positioning (-8%) was still way less into short territory than the AUD one (-18%). This suggests that there was more room at the start of this week for mounting NZD shorts than AUD shorts.
- For next week, the story is going to be once again very similar to the AUD one. No guesses, but it'll all be about the virus, but good news may not equal a rebound in the currency as markets price in the economic impact on those economies that are most exposed. Simultaneously, we estimate the impact of the Chinese slowdown to be more material in Australia than New Zealand. This may become more evident in the coming weeks when more data will be published, but we think it is a matter of time before AUD/NZD moves back below 1.04.

CAD: Still the best risk currency in G10

	Spot	Week ahead bias	Range next week	1 month target
USD/CAD	1.3220	Neutral	1.3150 - 1.3310	1.3200

- The Canadian dollar is showing some decent resilience to the choppy risk sentiment, compared to its risk-sensitive peers. The good inflation data this week helped too. As we highlighted in our [CAD outlook update](#), hoping for a sustained downtrend in USD/CAD may still be early, particularly considering the still not constructive crude price outlook and scarce signs of an immediate dollar correction. Once risk sentiment stabilises, however, CAD has the best risk-adjusted carry in G10 – which would remain intact even if the central bank cuts rates - and this suggests it can be the key outperformer in the second half of the year.
- Looking ahead, we still expect CAD to outpace AUD and NZD as the Canadian economy is more protected from a Chinese slowdown. However, towards the end of the year, GDP data for 4Q may hit the loonie, as QoQ growth should come in almost flat (ING forecast: 0.1%, consensus: 0.2%). This may revamp some BoC easing speculation and the week might end on a negative tone for CAD.

CHF: The 1.06 dilemma persists

	Spot	Week ahead bias	Range next week	1 month target
EUR/CHF	1.0614	Neutral	1.0560 - 1.0670	1.0600

- EUR/CHF is back to pressuring the 1.0600 resistance, which is perceived by markets as a key level when it comes to testing the SNB reluctance to intervene. Even if the coronavirus story keeps improving, eurozone economic woes continue to make a case against any sustainable rebound in EUR/CHF.
- As usual, it is worth keeping an eye on Italian politics. In particular, the ruling coalition seems to be moving from one parliamentary gridlock to another, which not only translates into an inability to deliver on structural reforms but also poses the risk of an imminent collapse in government. We don't think that will be the case for now, but with the rates market currently pricing in a very "calm" rest of the year for Italian politics, caution is indeed warranted. The risk for the FX markets is that another round of Italian political risk may constitute the straw that breaks the camel's back and prompts an FX intervention by the SNB.

NOK: Enjoying some protection from the virus

	Spot	Week ahead bias	Range next week	1 month target
EUR/NOK	10.0800	Neutral	10.0100 - 10.1500	10.2000

- NOK, like its oil-peer CAD (but without help from data), has held relatively well compared to other risk-sensitive currencies this week and we expect this to keep being the case next week too.
- Norwegian retail sales and labour data next week should show the economy is in decent shape. Low breakeven rates in the oil industry mean the recent decline in crude prices may not have had a huge impact on activity in the short-term, but they will inevitably lower the chances of a Norges Bank rate hike this year.

SEK: EZ sentiment remains a concern

	Spot	Week ahead bias	Range next week	1 month target
EUR/SEK	10.5600	Mildly Bullish 	10.5100 - 10.6700	10.7000

- Sweden's looser ties to China likely put it on the list of those currencies that are somewhat more protected to the virus story, but we equally note that the highly uncreative yield and the spill-over from a European slowdown still pose downside risks for the krona.
- While there are early signs that sentiment might have bottomed off in Sweden, and the Economic Tendency indicator has rebounded last month, the data release traditionally has little impact on SEK and so is the case for retail sales. GDP is expected to reflect a subdued fourth quarter. Essentially, as none of that releases will impact the Riksbank decision to keep rates on hold for the next few years, investors are likely to look the other way. Eurozone sentiment – namely the German IFOs – deteriorating further is likely to be the main data driver for SEK next week.

Author

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

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