G10 FX Week Ahead: Virtual healing

Thursday's virtual EU Council meeting will take centre stage this week. Eurobonds hardly look feasible but a new recovery fund perhaps? With the ECB standing ready to buy more Italian bonds, a debt crisis and a drop in the EUR - should be averted. The dollar should remain in a downtrend, while JPY still looks like the best value bet

Italian Premier Giuseppe Conte during a video conference with European leaders about the coronavirus situation

USD: The downtrend is slow progress

	Spot	Week ahead bias	Range next week	1 month target
DXY	99.8800	Mildly Bearish	98.5000 - 100.5000	95.0000

- There is a growing conviction that the dollar will take the mantel of the world's foremost funding currency and a recovery in risk assets will allow the dollar bear trend to win through. However, with Covid-19 curves still flat in the US and Europe, there remains the risks of lockdowns lasting a little longer and growth expectations being cut a little further. Thus the expected dollar bear trend may well be a function of how quickly readings of new cases/deaths actually fall. What is helpful, however, is that the aggressive actions of policymakers mean that a financial crisis is less likely this time around and that investors – now with high cash balances – will jump on clear signs of good news.
- On the calendar this week, we'll see more housing data (new home sales) from the US, durable goods orders and finally April consumer sentiment data. We'll, of course, be watching out for the weekly US initial claims data. Our US economist believes the weekly claims should drop to 3.5-4m from 5.2m, but with unemployment already heading from 3% to 15%, any bounce on this improvement may be limited.

EUR: All about Italy

	Spot	Week ahead bias	Range next week	1 month target
EUR/USD	1.0862	Mildly Bullish	1.0790 - 1.1030	1.1200

- Fears of a renewed eurozone sovereign debt crisis have been stalking debt and FX markets over recent weeks. There is now a sense that the European central bank may be buying (protecting?) Italian BTPs at a yield of 2.00%. This is why the EU leaders summit on Thursday addressing whether they have any plans for debt mutualisation (unlikely) or have something new to offer in terms of a recovery fund will be in focus. We also presume that Italian prime minister Giuseppe Conte will move to accept the ESM credit line, which would also open a new channel of support (OMT) for BTPs. In short, we expect the Europeans to muddle through again. Also on Friday lookout for S&P's rating of Italian sovereign debt, now at BBB. Our team think it may be too early and too political for Italy's rating to be cut.
- On the data side, we'll get fresh German confidence data in the form of April ZEW, Ifo and PMIs – all expected to fall further from the poor March readings. We do like EUR/$ higher this summer, but we will need to see: a) Italian risk contained and b) transparency on a clearly improving Covid-19 story coming through.

JPY: Our preferred choice

	Spot	Week ahead bias	Range next week	1 month target
USD/JPY	107.70	Mildly Bearish ↘	106.20 - 108.50	105.00

- Dollar funding issues seem to be improving as evidenced by the 30bp fall in 3-month $ Libor over the last couple of weeks. This is why we think this wall of dollar liquidity can start to filter through the system. A lower $/JPY remains one of our preferred routes given the uncertain outlook for activity and Japan's strong current account position.
- In terms of data, Japan will release the March trade balance early in the week. The market is expecting the adjusted monthly balance to dip back to zero. Over time, we'll be interested to see how the hit to Japan's exports is offset by a lower energy import bill. We'll also watch out for the central bank's plans for Japanese government bond-buying – although it seems to have done a good job at keeping 10-year JGB yields near 0%.

GBP: Poor UK data shouldn't make impact sterling

	Spot	Week ahead bias	Range next week	1 month target
GBP/USD	1.2455	Mildly Bullish ↗	1.2290 - 1.2660	1.2700

- As in other countries, hard data for March and the forward-looking indicators for April will be dismal in the UK, corroborating the sharp fall in Covid-19 related economic activity. But as this is a broader global trend, the weak UK data (on Thursday, March retails sales should fall by 10% while April PMIs should dip across the board further into contractionary territory) should therefore not lead to a material GBP weakness vs its peers.
- With the stabilising risk environment and the fall in volatility taking away some support from USD, GBP/USD should stay range-bound this week, with modest upside risks. We see more significant scope for GBP gains against EUR rather than against USD this week as the limited prospects of the agreement on debt mutualisation during the EU leaders meeting should be a marginal negative for EUR vs GBP. Sterling has also been shrugging off comments from UK officials who rule out the extension of trade talks with the EU beyond 2020. This could prove a larger GBP negative around mid year, but unlikely in the coming days and weeks.

AUD: Less vulnerable than its peers

	Spot	Week ahead bias	Range next week	1 month target
AUD/USD	0.6358	Neutral	0.6170 - 0.6550	0.5900

- The AUD has shown some good resilience to the swings in global risk sentiment, mostly thanks to the Reserve Bank of Australia keeping its asset purchases contained and the relaxed lockdown measures compared to other major economies and some encouraging labour data.
- Arguably, the first two factors are likely to stay while data may turn grim, making AUD the least vulnerable in the $-bloc. However, the prospect of falling trade flows don't bid well for a very open economy such as Australia, so we are not convinced the AUD can still sustainably recover just yet. This week, eyes will be on the RBA minutes and a speech by Governor Philip Lowe, as markets look for more hints that the Bank is scaling down its quantitative easing programme.

NZD: Weakening fundamentals

	Spot	Week ahead bias	Range next week	1 month target
NZD/USD	0.6049	Neutral	0.5890 - 0.6260	0.5700

- The Reserve Bank of New Zealand has been moving in the opposite direction of neighbouring Australia. Ready to ramp up its asset purchases and recent hints at some openness to negative rates, it is surely taking away any solid floor below the NZD. Incidentally, with the currency being the key shock absorber for the country and the rising AUD/NZD exchange rate boding well for the 13 % of exports directed to Australia, the country is likely warming towards a weak NZD.
- This week's CPI data for 1Q20 will be watched but will hardly have any significant implications for the central bank. But the risk of another leg lower for the NZD appears quite material given the RBNZ's dovishness and the strict lockdown in New Zealand that may suggest a larger economic fall-out. Some help may come from a weakening dollar, but AUD/NZD will likely remain supported.

CAD: Oil outlook remains grim

	Spot	Week ahead bias	Range next week	1 month target
USD/CAD	1.4058	Neutral	1.3790 - 1.4300	1.4500

- OPEC+ has failed to provide much to battered oil prices to offset the rising concerns on the demand side. As a result, oil is still stuck at the US$20/bbl levels and the prospects for the oil-centred Canadian economy keep deteriorating. Our commodities team does not see oil prices rebounding before 3Q20 and this should keep CAD gains capped in the next few weeks.
- The fact that the Bank of Canada has extended its asset purchase program to provincial and corporate bonds isn't really helping the CAD either. Recent comments by Governor Stephen Poloz indicated the central bank has 'room to do more', and the chances of this happening appear quite significant.
- Keep an eye on retail sales for February and CPI for March, but overall we see CAD trailing other pro-cyclical peers for now.

CHF: Do we have a floor at 1.05?

	Spot	Week ahead bias	Range next week	1 month target
EUR/CHF	1.0516	Mildly Bearish ↘	1.0500 - 1.0560	1.0500

- CHF total sight deposits continue to rise and suggest the Swiss National Bank may have bought CHF30bn+ of FX since March. The central bank probably doesn't want to be backed into a corner with a new line in the sand at 1.0500, meaning that a EUR/CHF print sub 1.0500 won't necessarily trigger a waterfall of follow-through, but this topic will certainly be a story for the week ahead. Look out for SNB Chairman Thomas Jordan's speech on Friday, where he may be asked more about the FX intervention policy.
- We'll also see Swiss March trade data on Tuesday. Of course, the outcome of the EU leaders' summit on Wednesday and the path of Italian BTPs will also have a big influence on the direction of EUR/CHF.

NOK: Low oil price preventing a further recovery

	Spot	Week ahead bias	Range next week	1 month target
EUR/NOK	10.2700	Neutral	10.0000 - 10.5000	10.3000

- After the late March rally, we continue to hold a neutral stance on EUR/NOK, looking for a stable, range trading in the cross. While the risk appetite continues stabilising, the anchored oil price with downside risks towards the US$25/bbl level means that the scope for NOK rally is limited.
- It is a very quiet week on the data front, with February unemployment numbers due on Thursday which won't really capture the Covid-19 induced fall in the labour market.

SEK: Still fairly stable EUR/SEK

	Spot	Week ahead bias	Range next week	1 month target
EUR/SEK	10.8670	Neutral	10.7670 - 11.0340	10.9000

- In line with the global trend of collapsing forward-looking indicators, the March Economic Tendency Survey out on Thursday should dip further. With rates at zero and the QE maturing bonds being reinvested, we don't see a need for imminent action from the Riksbank at this point.
- We continue to look for a fairly stable EUR/SEK. The stabilising risk environment points to a modest bearish bias for the cross. SEK is no longer underperforming its cyclical G10 peers as (a) it doesn't exert any exposure to commodity prices, (b) although still having the lowest implied yield in its G10 FX peer group, the difference has narrowed significantly following the large cuts from Norway, Canada, Australia and New Zealand's central banks.

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