


## G10 FX Week Ahead: When the music's over

The “music” for stock markets has stopped and concerns about the USD funding markets have taken over and generated high volatility in FX – with the USD the only winner. We think the Fed has addressed these issues, but restoring confidence will take time. For now, the dollar may remain bid, which could re-open the door for FX intervention speculation



## DXY: Where did all the dollars go?

|     | Spot     | Week ahead bias  | Range next week     | 1 month target |
|-----|----------|--|---------------------|----------------|
| DXY | 102.5000 | Mildly Bullish  | 101.0000 - 103.7500 | 100.0000       |

- Ever since the US Commercial Paper (CP) market seized up on 11 March, the dollar has gone bid. The CP market is a crucial source of short-term USD funding for corporates and banks. Just as in 2008, dislocations here can trigger temporary demand for dollars. The Fed and US Treasury are working quickly to fix the issue, but it may take a few weeks for confidence to be restored. In the meantime, the relentless run of alarming news on Covid-19 – prompting an ever-greater response in terms of social distancing – will likely keep risk assets pressured.
- The DXY has rallied nearly 10% since early March. Given that we've entered another round in the currency war, we doubt the White House will welcome \$ strength. It may be reluctant to intervene to weaken the dollar given its uncertain outcome – no intervention is better than failed intervention. It may instead just increase pressure on the Fed to grow its balance sheet even more – e.g. undertaking an extra US\$1tr worth of QE in the US version of the ECB's Pandemic Emergency Purchase Programme (PEPP). Buying corporate assets is tricky for the Fed because of Dodd-Frank, but let's see if there's any pressure for a change in legislation. Early this week we should see a new US\$2.0tr fiscal stimulus pass in Congress. That's damage limitation at the moment and not until new Covid-19 cases start to slow will markets start to stabilise and the macro story begin to play a greater role in FX markets.

## EUR: Ripping up the rule book

|         | Spot   | Week ahead bias  | Range next week | 1 month target |
|---------|--------|--|-----------------|----------------|
| EUR/USD | 1.0700 | Mildly Bearish  | 1.0550 - 1.0850 | 1.1000         |

- Trying to pick a low in EUR/\$ has been a futile exercise. No one knows for sure when this dollar demand will stop – is the demand bank, corporate or retail-driven? We do think, however, US authorities will get to the bottom of the dislocation over coming weeks and as always the Fed will flood the market with liquidity. The ECB moved impressively fast to address problems in EZ peripheral debt markets. This week we'll see if European politicians, particularly the Germans, can deliver on sizable stimulus packages. If they can it might take pressure off the ECB to do more and could, at the margin, provide the EUR with some support.
- It is hard to rule out a EUR/\$ drop to 1.05 this week. While the ECB has usually welcomed a weaker EUR, a disorderly fall below 1.05 could prompt at least some verbal intervention, i.e. that they are monitoring conditions closely. Macro data will take a back seat as a sharp contraction and 1H20 technical recession in the eurozone is now widely expected. As an aside, our rates team believe the ECB will use its PEPP powers to keep Italian 10-year BTP yields under 2%. Let's see.

## JPY: Roll on Japanese Fiscal Year End

|         | Spot   | Week ahead bias  | Range next week | 1 month target |
|---------|--------|------------------|-----------------|----------------|
| USD/JPY | 110.20 | Mildly Bullish ↗ | 108.90 - 112.00 | 108.30         |

- It is an understatement to say that the USD/JPY move has surprised. We think the 10% rally last week owes a lot to the dollar funding squeeze. Here the JPY basis remained wide all week – despite Fed measures – with some suggestions that Japanese banks are scrambling for USD funding before financial year-end on 31 March. Let's see if that starts to calm down; we suspect it will.
- Like other central banks, expect the BoJ to keep close watch on the market and to continue to provide liquidity through various open market operations and asset buying. Any Japanese asset manager having bought US Treasuries over recent weeks (unhedged) is probably sitting on a nice profit. We suspect that any further buying will be saved for \$/JPY trading sub 105 again – which is our preference later in the year when markets calm and the dollar adjusts to its new world – having joined the zero rates + QE crowd.

## GBP: Life after the big sterling collapse

|         | Spot   | Week ahead bias  | Range next week | 1 month target |
|---------|--------|------------------|-----------------|----------------|
| GBP/USD | 1.1600 | Mildly Bearish ↘ | 1.1410 - 1.1940 | 1.1800         |

- GBP/USD reached the lowest level since 1985 as the market rout and the dollar funding squeeze made the external financing needs dependent GBP vulnerable. The UK current account deficit (the largest in the G10 FX space) has been a long-standing negative for GBP. Additionally, GBP was the only G10 currency where the speculative community has been net long vs USD, with positioning likely exaggerating the GBP fall.
- With UK-EU trade negotiations (already postponed due to the Covid-19 crisis) now already irrelevant for GBP trading, the direction of risk assets and the evolution of the dollar funding squeeze will remain key for GBP/USD price action in the near term.

## AUD: Stil not at the bottom

|         | Spot   | Week ahead bias  | Range next week | 1 month target |
|---------|--------|--|-----------------|----------------|
| AUD/USD | 0.5785 | Mildly Bearish  | 0.5540 - 0.5740 | 0.5500         |

- Last week, the Reserve Bank of Australia cut the Cash Rate to 0.25% (signalling it will stay at such level for a prolonged period of time) and [started quantitative easing](#), aiming at keeping the 3-m yield at 0.25%. These measures are on top of the Bank's repo operations aimed at providing liquidity to the markets.
- In such a volatile market environment it is surely complicated to isolate the "QE effect" on the AUD/USD, which inevitably followed the swings in the dollar last week as the big USD funding story unfolded. This should continue to be the case this week, but the possibility of the USD giving up some of its gains (see USD section above) may partly offset the downside risks for AUD/USD stemming from the very fragile risk environment. Australia is entering the lockdown phase and the support from the fiscal side is still lacking, which makes the possibility of the RBA stepping in with more aggressive QE is all but material: markets know it, and this makes the prospect of buying the dips in AUD not very appealing.

## NZD: Finally, RBNZ QE

|         | Spot   | Week ahead bias  | Range next week | 1 month target |
|---------|--------|--|-----------------|----------------|
| NZD/USD | 0.5654 | Mildly Bearish  | 0.5370 - 0.5800 | 0.5400         |

- The Reserve Bank of New Zealand announced a much-awaited QE programme, worth NZD 30bn. The purchase programme will last for 12 months and will see the Bank buy bonds in the secondary market across multiple maturities.
- This announcement erases the notion that the RBNZ had been trailing the RBA in terms of unorthodox monetary easing, which makes another move towards parity in AUD/NZD (1.00 was briefly touched last week) less likely. In addition, the NZD lower liquidity compared to the AUD warrants some wider downside risks ([here's our analysis on FX and liquidity](#)).

## CAD: More weakness to come

|         | Spot   | Week ahead bias | Range next week | 1 month target |
|---------|--------|-----------------|-----------------|----------------|
| USD/CAD | 1.4437 | Bearish ↘       | 1.4170 - 1.4900 | 1.5000         |

- The timing of the next Bank of Canada cut (most likely, 50bp) may not matter a lot for the markets, which are mostly pricing in the move in the next few days or weeks. The notion that the BoC is piggybacking the Fed in dealing with the Covid-19 crisis may provide additional steam to USD/CAD as markets may start to price in BoC QE. We are starting to see 1.50 in USD/CAD as a feasible target now, although that may represent the top of the range for the pair.
- Oil remains a big element of uncertainty as the rebound on Thursday was quickly erased in late-week trading and the outlook remains quite grim. However, barring a rebound to pre-OPEC+ breakup price levels – that hardly seems to be feasible now – hard times are likely ahead for the Canadian energy sector (which makes up 12% of GDP) and this will inevitably be a constant drag on CAD ahead, regardless of daily noise in the oil market.

## CHF: More SNB interventions need ahead

|         | Spot   | Week ahead bias  | Range next week | 1 month target |
|---------|--------|------------------|-----------------|----------------|
| EUR/CHF | 1.0560 | Mildly Bearish ↘ | 1.0400 - 1.0670 | 1.0500         |

- The Swiss National Bank meeting last week did not yield a rate cut, but only a modification of the tiering system to ease the burden of negative rates to banks (for more details see [Swiss central bank: More to follow](#)). The key notion that emerged from the policy announcement is that FX intervention remains the key policy tool of the SNB.
- Despite the efforts to limit the franc's appreciation, the Bank has had to recalibrate their concept of "lower bound" in EUR/CHF on a weekly basis as panic spread in the markets. We suspect we may see some of that risk aversion partly ease this week, but the risks of another round of panic selling are high, which may prompt another leg lower in EUR/CHF. It would allow us to see how determined the SNB will be not to let the pair slip below 1.05.

## NOK: After the meltdown...

|         | Spot    | Week ahead bias  | Range next week   | 1 month target |
|---------|---------|------------------|-------------------|----------------|
| EUR/NOK | 12.6300 | Mildly Bullish ↗ | 11.6000 - 13.1790 | 12.2000        |

- The low liquidity, oil-exposed NOK experienced a meltdown, collapsing 13% vs USD so far in March. The issue of the (lack of) dollar liquidity and its eventual resolution will be the key driver of NOK. With the Fed making steps to resolve the USD funding squeeze, NOK downside might be more limited from here (vs the price action over the past few weeks). Nonetheless, the currency remains the most exposed in the G10 space given its poor liquidity, with clear downside risk
- Although Norges Bank slashed rates close to zero (the latest 75bp emergency cut), the NB policy is currently irrelevant for NOK with cuts not being negative for the krone. We don't expect NB to cut rates into negative or start QE.

## SEK: Still doing better than its G10 cyclical peers

|         | Spot    | Week ahead bias  | Range next week   | 1 month target |
|---------|---------|------------------|-------------------|----------------|
| EUR/SEK | 11.1700 | Mildly Bullish ↗ | 10.9550 - 10.4260 | 11.2000        |

- Although EUR/SEK broke above the psychological 11.00 level in the March market rout, it continues to outperform its G10 cyclical peers. This is a function of (a) its insulation to the fall in commodity prices (b) compared to its G10 cyclical peers, the Riksbank firepower to ease monetary policy is limited (low appetite to bring it back into negative while the bank continues reinvesting its prior QE already).
- The EUR/SEK path this week will be determined by global risk sentiment, with domestic data being irrelevant. We look for some stability should the USD funding pressure ease, yet a still a mildly bullish bias for EUR/SEK

There's more to read in our FX Talking report, 'I need a dollar'. Get it [here](#).

### Author

#### Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

[chris.turner@ing.com](mailto:chris.turner@ing.com)

#### Francesco Pesole

FX Strategist

[francesco.pesole@ing.com](mailto:francesco.pesole@ing.com)

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