

## In the dollar they trust

The dollar has been faring well in both good times and bad. Is there anything that could turn the tide?



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### ➔ USD: The dollar continue to perform very well

It was another strong day for the dollar yesterday, which seems to be faring well in the good times (Federal Reserve leading the charge on tightening) and the bad (safe-haven bid when Europe or emerging markets suffer). The Fed's Richard Clarida [made the point yesterday](#) that the transmission of global shocks to the US economy is via the stronger dollar and tighter financial conditions, which merits the offsetting dovish response from the Fed. Given that we're [not in the camp looking for a US recession anytime soon](#), the best chance of a negative turn in the dollar trend will have to come from re-rating stories overseas, such as: a resolution on Brexit/eurozone exit from its soft patch and/or some better activity news out of China. We believe those re-rating stories are still possible later this year, but for the time being, expect the dollar to hold onto its gains – especially because of the high dollar hedging costs in a bond bull market. For example, Japanese investors have to pay 2.84% annualised for rolling three month USD FX hedges – in excess of any yield currently available on the US Treasury curve. For today, core PCE should stay near 1.9% and quarter-end flows may dominate FX markets.

## ➔ EUR: Soft confidence and soft inflation

Disappointment in both the eurozone confidence and German March CPI data have left the euro under pressure. It now looks like the [package holiday effect](#) could send core eurozone CPI back to 0.9% year-on-year when it's released on Monday. However, one big supporting factor for EUR/USD is its level. Given narrowing yield differentials (two-year EUR/USD forward points are now 635 USD pips versus 820 back in October) and the decline in spot, the two-year outright forward is now at very attractive sub 1.19 levels for European corporates. We're thus not big fans of chasing EUR/USD lower from current levels.

## ⬇ GBP: MV2.5 set to fail again

1530CET should see Prime Minister Theresa May's withdrawal bill fail for the final time and lead to more focus on Indicative Votes on Monday. Whilst it's tempting to focus on the potential positives of: a) a permanent customs union or b) a second vote, May's impending departure and the risk of a more pro-Brexit PM arriving will curb investors' enthusiasm for sterling. 1.2950/3000 could limit cable weakness.

## ➔ ZAR: Moody's will probably hold off the downgrade

Moody's is the last of the major ratings agencies to hold South African sovereign debt on an investment grade rating and is due to review the credit later today. The threat of junk ratings has been hanging over South African asset markets for a couple of years now and a one notch cut in the local currency rating to junk would see South Africa expelled from key sovereign bond indices – prompting US\$1-2bn of enforced sales of SAGBs according to some estimates. Our sovereign credit strategist, Trieu Pham, thinks Moody's will retain the ratings at Baa3 with a stable outlook, since the agreed state support for Eskom has been more modest than feared and more conditional. While a re-iteration of its current Moody's ratings could be seen as a ZAR positive early next week, investors will want to see how week-end local elections in Turkey play-out before re-committing to the rand. 14.75/85 may cap USD/ZAR today.

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