USD Poised to Soften After Bearish Reversal

- USD formed a bearish key reversal after the DXY made a marginal new high.
- CAD settles back into 1.34/1.35 range but still looks cheap versus FV.
- EUR rebound from 1.11 test looks impressive—bullish—on the charts.
- GBP rallies as May steps aside, Brexit deal still likely some way off, however.
- JPY softer as risk appetite improve. CPI picks up in Apr.
- AUD steady on the day, down 1.5 on the month as RBA cut bets strengthen.
- MXN stable ahead of final Q1 GDP, Apr Trade Balance data.

FX Market Update - Calmer markets prevail overall into the end of the week—and an early close for some US markets ahead of Memorial Day Monday (note UK markets are also closed for a Bank Holiday). Asian stocks were mixed but European equities have firmed and US futures have followed suit. US 10Y yields are steady but still trading below Fed Funds at 2.33%—reflecting the curve inversion seen through the 3M/10Y spread. For the G-10 currencies, the wobble in the USD overall yesterday has extended modestly, lifting the Scandi currencies in the main while the GBP has rallied on news that PM May will step down as party leader on June 7th. The improving risk mood leaves the CHF and JPY as the unsurprising underperformers on the day. The MXN is modestly firmer, as is the CNH. The next couple of weeks will be interesting for the FX markets—trade tensions continue to simmer and economic data suggest that the global economy may have stumbled in the spring (on the basis of yesterday weaker European and US PMIs). But price action yesterday overall looks clearly negative for the USD, with the DXY reversing bearishly from a two year high (forming a key reversal day) on the chart; losses so far today are “confirming” the signal and suggest a period of softness for the USD lies ahead.

USDCAD (1.3453) • The CAD is little changed in quiet trade despite the bounce in risk appetite feeding through to modest gains for energy prices. We remain a little bemused by the CAD’s inability to take full advantage of sharply narrower US-Canada short-term spreads and relatively positive domestic economic data which leave the Canadian economy tracking much better GDP growth levels than the Bank of Canada expected in its last MPR. That outperformance alone tilts the balance of risks towards a constructive assessment of prospects in next week’s BoC policy statement and provides the basis for a mildly hawkish hold decision from the policy makers. Recall that Governor Poloz just recently reiterated that he saw higher rates as the “natural tendency” for the economy, given the economy’s underlying strengths. We remain positive on the CAD and continue to see little justification for USDCAD to extend gains beyond recent peaks.

USDCAD short-term technicals: Neutral/bearish—short-term price action suggests another failure at the upper end of the recent trading range yesterday near 1.35 (still firm resistance) although that conclusion reflects the drift in price overnight rather than signs of a specific technical reversal. Price movement so far today does, however, lean towards the negative from a technical point of view but more sustained weakness is needed for a definitive signal. Intraday softness below 1.3445 (minor retracement support) should see the low 1.34s reached before the close of trade and put a little more pressure on the 1.3375/00 support zone next week.

EURUSD (1.1191) • EURUSD dipped to test the 1.11 area yesterday following the disappointing Eurozone PMI data but managed to recover and post a small, but
important, net gain on the day following the perhaps even more disappointing US data releases. The respite for the EUR may be significant as the USD has once again failed to really pressure the 1.11 area and the EUR might be able to cling to the modest narrowing in short-term spreads to –279bps—still massively in favour of the USD but still the narrowest yield gap since early 2018.

EURUSD short-term technicals: Bullish—Strong net gains on the day yesterday for the EUR looked an unlikely prospect early on but the huge lift off the intraday low (marginal new low for the move down) and firm close left a bullish key reversal print on the daily EURUSD chart by the close. Markets are mostly flat today but clear signs of another strong rejection of the 1.11 zone should see the EUR grind a little higher overall near term to test key resistance at 1.1315 (weekly trend resistance).

GBPUSD (1.2688) • The big—but hardly surprising—news from the UK today is that PM May has announced she is stepping down as party leader of the Conservatives on June 7th. She will, however, remain PM until a new party leader, and effective PM, is selected (likely by July). The GBP jumped in response to the news but we expect gains to be short-lived as the main leadership candidates all lean towards a “harder” Brexit. The parliamentary math that prevented May from making headway remains intact, however, and it might well be as difficult for the new PM to advance a negotiated Brexit in any form. Longer run GBP risks may hinge on whether the EU could contemplate another extension to allow the UK to try and sort itself out—in the event of a general election being called, for example, beyond Oct. UK data revealed better than expected Apr Retail Sales data but significantly worse survey data for the retail sector this month.

GBPUSD short-term technicals: Neutral/bullish—Cable’s rebound from the intraday low yesterday was less impressive, leaving spot little changed on the day, with the doji candle on the daily chart. But the stall signal was not entirely unexpected, given the extended run of consecutive daily losses for the GBP in the past couple of weeks. We think the GBP may be able to stabilize in the near term but rather expect only limited potential for gains (1.2750/75) before renewed selling pressure emerges.

USDJPY (109.67) • Japan’s CPI rose a stronger than expected 0.9% Y/Y in Apr (from 0.5% in Mar), with core price growth also picking up slightly (0.9% Y/Y from 0.8% in the prior month). Price trends may slow again in the next few months and leave inflation well short of the BoJ target (2%) into the end of the year. Sluggish price growth might yet compromise the government’s ability to raise the Sales Tax in Oct, as planned.
### TODAY’S CALENDAR

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