TD Securities

FX Daily Dispatch

Global Rates, FX & Commodities Strategy

21 October 2021

▶ G10 ▶ FX ▶ GLOBAL MARKETS

Change is in the Air

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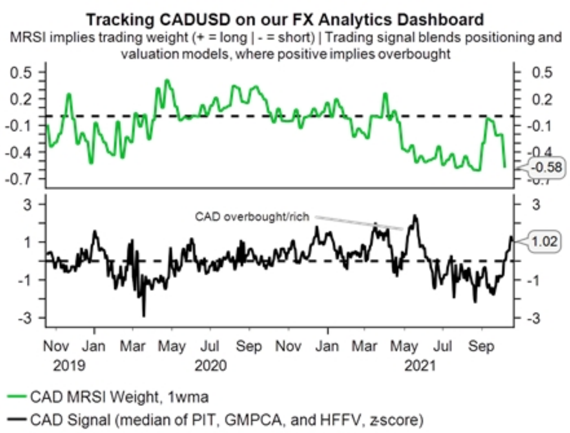
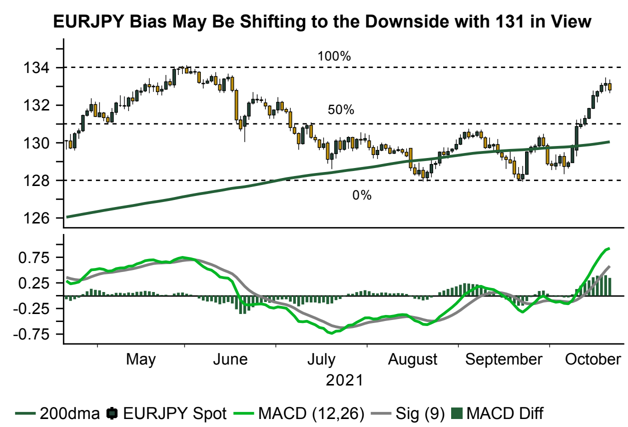
- A more consolidative tone has emerged out of the G10FX space after notable outperformance in commodity currencies. AUD and CAD are of particular interest. We see better value in the former but a rejection of the 200dma in AUDUSD and brief foray sub-1.23 for USDCAD may be early signals that the recent pullback in the USD may be nearing an end.
- Our rates team has indicated that the front-end repricing is largely mature and favor receiving in the 1y1y space in some markets (but relative to the US). We think that also bodes well for a return to USD firmness next month and once the BOC and ECB pushback against market pricing next week. The latter is more likely to affirm its commitment to policy sequencing, which should see it significantly lag the Fed.
- We reiterate that a lot of good news appears to be in the CAD price. And, as much as yen weakness is likely to persist over the medium-term, we think there is scope for a tactical reprieve as front-end receivers look more attractive in our view. Cross/JPY looks stretched, especially against AUD, CAD and the EUR. This should weigh on USDJPY as well but 112 looks to be formidable support especially with Fed pricing likely to remain sticky.

Charts of the Day



Source: Macrobond, TD Securities



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An early signal? A consolidative tone has emerged in most G10FX pairs with the USD staging a very modest comeback from the overnight lows. We're particularly interested in the commodity currencies and the yen at the moment. The former have been the winners in the USD pullback in recent sessions (and just better performers since the September Fed). That said, after putting in good work, USDCAD and AUDUSD have shown deference to notable technical markers. In the former, a dip below 1.23 did not have much follow-through, while AUDUSD rejected its 200dma at 0.7550 in what could be a sign of exhaustion and perhaps an early indication that the USD reprieve may be nearing an end.

Between the two, we think the AUD offers more value than the CAD on the basis of a pick-up in vaccinations, terms of trade shock and far more dovish central bank. Still, we think the repricing in the front-end is largely matured and the back-up in longer-term rates is plenty (it won't evolve in a straight line). We have already started to see pushback across central banks with regards to market pricing, in what is a sign that perhaps they are wary of being too trigger happy with rising inflation — unlike the BOE.

Pivot might occur after CB decisions. Next week will bring the BOC, the ECB and the BOJ. The BOC and the ECB will be interesting, while the BOJ is likely to downgrade its outlook and still remain committed to being inconsequential. We noted yesterday that a lot of good news may already be in the CAD price. Taken in conjunction with cross-asset FV, positioning and how it trades relative to our global macro PCA, the CAD is screening a little overbought on our dashboard. We think additional reluctance to break below 1.2250 around the BOC meeting could signal that a reversal may be in the offing.

The ECB has come out of the woodwork to push back against the hawkish repricing in the front-end recently. We're inclined to think that next week's meeting will signal fidelity to policy sequencing and its forward guidance. That is, both PEPP and APP must end before the ECB were to think of hikes. We think that the USD could begin to stage a comeback once we receive confirmation of such. That puts the ECB to be an appreciable laggard when it comes to tightening (if it can ever get itself to that point) relative to the Fed. That should leave EUR rallies rather limited, especially against the currencies that offer legitimate tightening prospects and superior carry.

A tactical yen reversal. And, as much as there is a solid case for yen weakness in this new rate regime, we think a modest bounceback in the yen is starting to look a bit more likely. This is especially true as our rates team likes receiving 1y1y in a number of markets. Our positioning tracker also shows the yen as experiencing the largest build of shorts over the last month. Taken in cross/JPY looking stretched in a number of pairs, but especially against high-beta commodity currencies like CAD and AUD. EURJPY has also stalled around 133, which is just shy of its cyclical high around 134. Given our view on the ECB and our bias for the EUR to remain relatively soggy, a retracement to 131 seems probable. This would also coincides with the 50% retracement of the high/lows since June. This should help pull USDJPY lower, though we are inclined to think that 112 should be rather solid support. We're less inclined to see much more of a pullback there as we anticipate Fed pricing in the EDZ2-Z3 spread to remain rather sticky and elevated. That said, we think that this may be as hawkish as it gets for the time being.