

# FX Morning Adviser

## Rates Over-rated?

FX

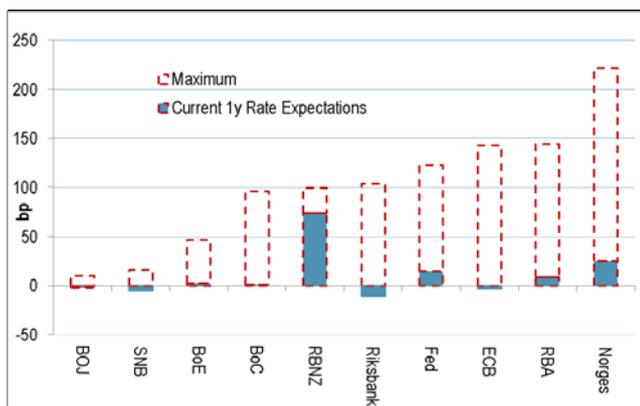
Global

### Rates are helpful in places, not as hurtful in others

As bumpy as the road may be, there is a realisation that the majority of G10 economies are well on the mend. As a result, on balance the next policy move for these central banks is probably a tightening step, no matter how far off actual execution may seem. For some currencies the prospect of early normalisation appears to be a pillar of strength. On the other hand, looking at the entire post-2009 performance of currencies relative to shifts in interest rate expectations, the overall relationship is far less clear-cut.

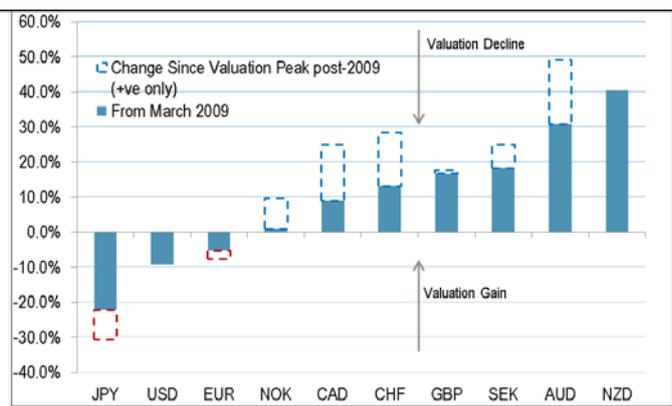
Using the 1y OIS (and forward swap rates where applicable) for G10, we can see that all G10 central banks at present have interest rate expectations below their post-crisis peaks. The fact that most central banks were more optimistic at certain points after March 2009 (e.g. the ECB even hiked rates in the first half of 2011) underscores the stop-start nature of the recovery. At present, the ECB and its closest 'shadow central banks' – the SNB and Riksbank – are the only ones where further easing is being suggested. In addition, Frankfurt and Stockholm have also seen their own policy expectations come off sharply since recent highs (140bp & 103.5bp, respectively, both reached in April 2011). However, in terms of currency valuation changes (measured by REERs), there is no consistency: the euro's REER is effectively trading back at April 2011 highs (though not post-March '09 highs), and has improved from the lows. The fact that the G3 are alone in still trading below their March 2009 REER levels (given lack of inflation globally we ignore price effects for now) shows there was certain strength in the carry trade and the generic impact of low rates. Central banks may yet push on, but G3-funding is at extremes and additions require qualitative changes in policy.

**Figure 1: G10 OIS pricing remain below post-crisis highs**



Source: Bloomberg, UBS Calculations

**Figure 2: Currency changes fail to track OIS**



Source: UBS Calculations, BIS REER Indices

For the rest of G10, the currency-rates link looks tighter but key differences remain. Norges and the Riksbank have seen sharp revisions lower in policy expectations, but Nordic FX performance (as of Mar '14) has not been as problematic, even after a sharp correction. In contrast, the CAD and AUD have suffered sharply. All four have been affected to by excessive positioning in the 'super AAA' trade and its subsequent unwinding. However, AUD and CAD's weakness suggest investors believe their fundamentals have changed, and successful rebalancing requires larger terms-of-trade adjustment, especially compared to smaller and more nimble Nordic economies. This leaves NZD and GBP, which are near post-crisis peaks in both rates and FX. 'One-offs' (positive shocks in milk and FDI) feature for now, but *when* investors demand necessary rebalancing as well in the near future, the currency is more likely to buckle for both.

## Technical FX

EURUSD	BEARISH	With the momentum falling and MACD threatening to cross below its zero line, there's risk for more weakness. Support is at 1.3762 ahead of 1.3664. Resistance is at 1.3831 ahead of 1.3906.
USDJPY	NEUTRAL	The latest strength has seen the test of the resistance at 102.73. There's potential for more upside to break above 103.06 and then 104.13. Support is at 102.03 ahead of 101.20.
GBPUSD	BULLISH	The important resistance focus is at 1.6878. A break above this would extend the uptrend to 1.7043. Support is at 1.6661.
USDCHF	BULLISH	The pair is regaining strength, with our resistance focus at 0.8873. A break above which would open 0.8981. Support is at 0.8744.
AUDUSD	BULLISH	Initial resistance is at 0.9461, a break above this would extend the strength to 0.9543. Strong support is at 0.9243 and 0.9206.
USDCAD	NEUTRAL	There's scope for a move higher to test resistance at 1.1069 and 1.1118. Support is at 1.0960 ahead of 1.0853.
EURCHF	BULLISH	As bullish conditions persist, there's scope for extension of the recent strength. Resistance is at 1.2285, a break above which would be positive, opening the way to 1.2395. Support is at 1.2141.
EURGBP	BEARISH	With the trending and momentum indicators pointing lower, there's potential for extension of the downtrend to critical support at 0.8158. Resistance is at 0.8260.
EURJPY	NEUTRAL	The cross is consolidating below the resistance at 143.79. It is supported by 139.97, a break below this will extend the correction to 138.79. Any upside in the interim will find first resistance at 142.18.

**\*NOTE:** The trend for each currency pair as defined in the table is determined by our proprietary model and is independent of our discretionary interpretation of price action

Source: UBS FX Strategy

## Key Events

Country	GMT	Release/Event	Freq.	UBS	Prev/Rev	Cons.	Actual
Australia	00:00	Conf. Board Leading Index (Feb)	m-o-m	n/a	0.20%	n/a	0.30%
Japan	05:00	Leading Index CI (Feb F)	index	n/a	108.5	n/a	
Japan	05:00	Coincident Index (Feb F)	index	n/a	113.4	n/a	
Switzerland	07:00	Money Supply M3 (Mar)	y-o-y	9.10%	8.80%	n/a	
<b>Sweden</b>	<b>07:30</b>	<b>Unemployment Rate sa (Mar)</b>	<b>%</b>	<b>8.00%</b>	<b>8.10%</b>	<b>8.00%</b>	
Euro Area	09:00	Construction Output (Feb)	m-o-m	n/a	1.50%	n/a	
Euro Area	09:00	Construction Output (Feb)	y-o-y	n/a	8.80%	n/a	
Canada	12:30	Wholesale Trade Sales (Feb)	m-o-m	n/a	0.80%	0.70%	
United States	13:00	FHFA House Prices (Apr)	m-o-m	0.50%	0.50%	0.50%	
<b>Euro Area</b>	<b>14:00</b>	<b>Consumer Confidence (Apr A)</b>	<b>index</b>	<b>n/a</b>	<b>-9.3</b>	<b>-9.3</b>	
United States	14:00	Richmond Fed Manufact. Index (Apr)	index	n/a	-7	2	
<b>United States</b>	<b>14:00</b>	<b>Existing Home Sales (Mar)</b>	<b>units mn</b>	<b>4.57</b>	<b>4.60</b>	<b>4.56</b>	
United States	14:00	Existing Home Sales (Mar)	m-o-m	-0.70%	-0.40%	-0.90%	
Euro Area	18:30	ECB's Costa Speaks					

Source: UBS Global Economics, Bloomberg LP, Reuters LP, Reuters, Market News International