

# FX Strategy

## EURphoria to continue: watch the canaries

- We view the current uptick in EUR/USD as a level shift and as tactical in nature.
- The key to further short-term optimism is a continuation of the rally in value assets.
- The key to 12M upside risk remains a Fed-driven reflation trend in H2.
- We revise our profile to 1.15 on 1M and 3M horizon and see 1.11 on 6M and 12M.

In our view, the recent move(s) has been a story of two parts. Initially, EUR went from 1.07s to 1.10, as extreme pessimism from worries about the long-term survivability of the EUR came to pass with the German-Franco fiscal deal. Second, when banks and EM currencies such as ZAR, BRL and TRY started to catch up, EUR took another leg higher as well. It has been a long held point of ours that EUR/USD is priced around the ebbs and flows of the global reflation trade, which these are proxies for.

After Thursday's ECB meeting, we now have an even stronger EUR but also more easing. In our view, this is arguably so as these actions indeed cap macroeconomic tail risks. Thus, the decline in uncertainty becomes a propellant of FX strength. **To keep the rally in EUR/USD going, the global investment environment needs to continue to favour a rotation towards 'undervalued' assets.** As a simple rule of thumb, look to the world's canary-in-the-coalmine to gauge this. Simply put, we need at least one of DAX, TRY, ZAR or BRL to continue to rise some 1-2% a day to further support EUR - but that may indeed stick with us a while longer.

### Euro optimism can go further but we (still) doubt it can stick

**We do not see much standing in the way of going to 1.15** - helped by speculation of a Brexit compromise - even if the latter is unlikely to be delivered near term, in our view. We thus **revise our 1M and 3M forecast to 1.15 while lifting our 6M and 12M forecast to 1.11.** This is a parallel shift upwards of six figures reflecting not only global reflation trends but also a one-off level from changed European tail risks. The key risk for our 6-12M view will be how Fed moves in H2.

In summary, we view the current uptick in EUR/USD as a permanent level shift (tail risks *have* faded) but as tactical in nature, as other drivers are likely to enter the stage in the coming months. In our view, longer-term issues have still to be addressed within core European industries (autos, banks, etc.), Brexit remains unresolved and Italy may enter new debt sustainability discussions by year-end. **Further, positive macro surprises in the US may help to stem USD weakness.** Lastly and most importantly, we have yet to see real commitment from the Fed to pursue inflation overshooting. If we change our view on the latter, we would change our view on the slope of the profile.

### Close long EUR/USD via seagull

We have been long EUR/USD via a seagull since 1.0788 and close this at a profit of 1.8% (roughly max gain in the trade).

As per the above, we will likely try to time a contrarian move in EUR/USD as the next trade idea, e.g. by means of a risk reversal, a bearish seagull or similar.

#### Key items to watch

If one of these rise 1-2% a day, EUR/USD is likely to continue to move higher

- ZAR versus USD
- BRL versus USD
- TRY versus USD
- DAX
- European Autos, Banks and Travel

Source: Danske Bank

**Danske FX Trading Portfolio: open trades**

Trade	Opened	Entry	Closed	Current	PnL
Sell EUR/NOK spot (25% starter entry, 50pp add-on below 11.50)	25/03/20	11.8900		10.4718	8.7%
Sell 1yr EUR/USD strangle	17/04/20	1.1215/1.0739		1.1289	0.5%
Long 2M EUR/GBP ATMS 1:2 (0.8910-0.9070) call-spread	27/05/20	0.8910		0.89	0.0%

Source: Danske Bank

**Danske FX Trading Portfolio: recently closed trades**

Trade	Opened	Entry	Closed	Close level	PnL
Short USD/CNH 6M forward	04/12/19	7.0888	23/01/20	6.9443	2.0%
Sell EUR/NOK via 4M 10.17-10.32 risk reversal	01/11/19	10.1700	23/01/20	9.9743	1.8%
Short CAD/NOK spot	04/12/19	6.9169	23/01/20	6.8350	1.2%
Long NOK/SEK spot	04/12/19	1.0371	30/01/20	1.0490	1.5%
Long CNH/JPY via 3M forward	04/02/20	15.4886	07/02/20	15.6229	0.9%
Short EUR/JPY spot	24/02/20	120.4900	05/03/20	119.5200	0.8%
Long USD basket vs equal weighted SEK, CHF and JPY	04/12/19	100.0000	09/03/20	96.5000	-2.9%
Sell 3M 9.90-10.15-10.32 EUR/NOK seagull	05/02/20	10.1500	12/03/20	10.4718	-7.0%
Long 6M 120.4-126.0 ATMS EUR/JPY call spread	04/12/19	120.4000	16/03/20	118.6200	0.0%
Buy 3M ATMS 1.0740 EUR/CHF put	20/01/20	1.0740	16/03/20	1.0873	1.3%
Long EUR/HUF spot	04/12/19	330.9000	18/03/20	349.3000	5.5%
Buy 2M 11.4000-11.7212 NOK/JPY put spread	27/02/20	11.7212	30/04/20	10.3500	2.1%
Long EUR/SEK via bullish 2M seagull 10.72P/10.97C/11.27C	23/04/20	10.8850	04/05/20	10.3924	-0.4%
Short a 6M 0.8400-0.8800 ITM EUR/GBP put spread	04/12/19	0.8461	18/05/20	0.8919	2.3%
Long USD vs. AUD+SEK+JPY	25/05/20	100.00	02/06/20	97.50	-2.5%
Long EUR/USD via 3M seagull (1.0800C/1.1024C/1.0450P)	07/05/20	1.0788	08/06/20	1.1289	1.8%

Source: Danske Bank

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