

TECHNICAL STRATEGY NOTE: FX STRATEGY

EM'S TESTING RESISTANCE LEVELS

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EURUSD: CONSOLIDATING IN THE MIDDLE OF THE BEAR CHANNEL



Source: BBG, Nedbank CIB

- With the central banks backing off from a more restrictive monetary policy stance, it is time to look at some longer-term charts to see what potential moves we can expect from currencies.
- Since the 2008/09 GFC, the EURUSD has been in a bear market.
- This trend accelerated in 2014 as the USD monetary base started to shrink as USD FX reserves started to decline, and this fuelled the USD rally. In 2016 and 2017, the central banks added lots of liquidity, causing the USD to fall; this, while the interest rate differential was favouring a stronger USD.
- The stronger USD, stemming from the tighter global financial conditions in 2018, caused a lot of damage in markets.
- The market is now waiting for the central banks to reverse this trend again by adding liquidity and stimulus, as was the case after the "Shanghai accord" in early 2016.
- We are fully aware that it is real rates that matter to asset prices and the economy, but it is quite concerning that markets require a liquidity boost with nominal rates in the US at just 2.25% and at zero in other parts of the world.
- We expect the EUR to rally into the 1.16s to complete wave 2 before the next bear trend starts. See the next slide for more details.

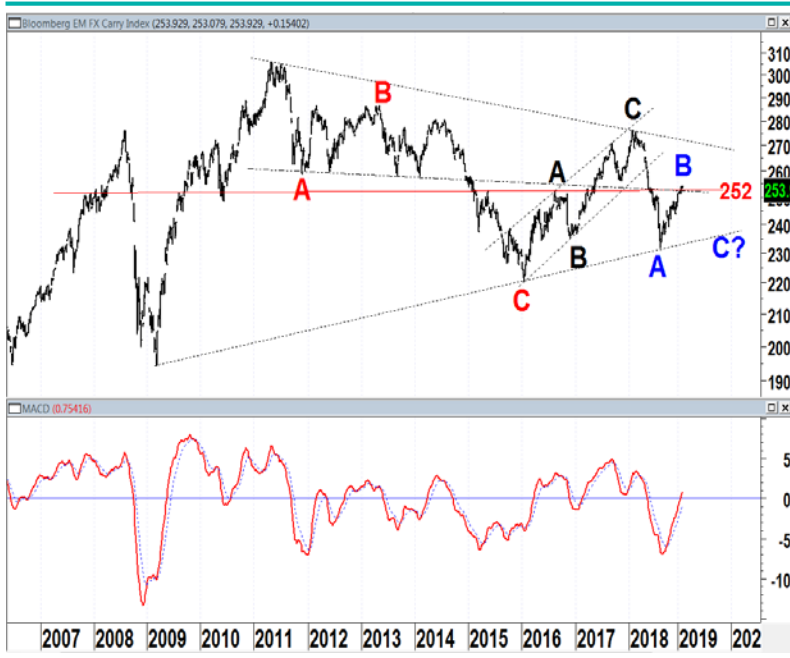
EURUSD: THE PRICE ACTION SINCE 4Q18 IS NOT A BULL TREND



Source: Reuters, Nedbank CIB

- We were concerned last week that the break below the blue dotted line at 1.1330 would trigger a final wave to the downside. We expected this bear move to be short-lived; we had a few days in mind, not just a few hours.
- The fact that this break was false is bullish, and with the current fundamental news, a rally to the higher 1.16s is on the cards.
- This rally is, in our opinion, the C wave of a big consolidation phase that has been playing out since 3Q18 to complete wave 2 of the bear trend.
- The overlapping nature of the off-the-4Q18 low is also a signal that it is a corrective rally and not a trend.

BLOOMBERG EM FX CARRY INDEX: TESTING IMPORTANT RESISTANCE



Source: BBG, Nedbank CIB

- There are many calls to upgrade EMs to a buy signal. The EMs have already rallied since early September 2018 to test the mid-point line of a pattern that has been developing since before the GFC.
- We would like to see over the next week or two whether the bull trend can maintain its momentum above the necklines at 252 before calling the market higher to the trendline through the 2011 and 2018 highs at 270.
- The rand weakened from 2011 with the other EMs; the only time the correlation was not high was from 2012 to 2014, when the other EMs consolidated but the rand remained in a bear trend. After that period, the correlation has remained very high.
- It is without a shadow of doubt bullish for the carry trade that the funding cost (policy rates) will not be under pressure. But as we have written numerous times before, at these super-low interest rates, the quantum of money is as important as the price of money.
- The global economy will remain under pressure this year and fewer dollars will be created via global trade, and this will be negative for the carry trade. Time will tell which force – cost or quantum – will get the upper hand. Please refer to tomorrow's publication "FX Insight" for more insight on our view on the sustainability of the EM carry trade.

USDZAR: TESTING A MAJOR SUPPORT LINE



Source: Reuters, Nedbank CIB

- In 2016 and 2017, the rand rallied with all the other EMs as the ECB and BoJ added major liquidity. Central bank balance sheets grew USD3.5tn over that period.
- In 2018, growth in central bank balance sheets slowed and the EM currencies sold off quite aggressively.
- The EM FX carry index above is testing an important neckline, and the USDZAR has corrected to test the top of the previous channel at 13.31 (blue line).
- If the EM carry index could break decisively above the 252 level, the USDZAR could break below 13.31, targeting 13.12. An extended target will be 12.58, where wave C will be equal in length to wave A.
- We expect the USDZAR to bottom out in the lower 13s.