Maybank

FX Flash

AUD - Downside Risks in the Near-term

Macro | FX Research and Strategy

Global

Hurdles for AUD Bulls Are High

AUD has made quite a bit of progress against the USD, despite the rate cut by RBA last Tue and Trump's threats to impose more tariffs on the rest of Chinese imports that have not been taxed yet (which amounts to around U$300bn). Softening US data builds the case of a Fed rate cut and that has provided the AUDUSD pairing an added boost. Still, AUD is one of the laggards amongst the G10 currencies, its losses against the USD is second only to JPY for the first week of June.

With Philip Lowe being open to more cuts as mentioned in a speech that was scheduled after the monthly RBA policy meeting last Tue, futures implied rate suggests almost another two cuts being priced by 2020. It is, however, hard to imagine AUD getting a lot lower as concerns on Australia's elevated household debt could keep the central bank from getting too bold in their rate actions.

AUDUSD touched a high of 0.7023 this morning, the resistance level there proved too strong for the AUD bulls to cross. With China's shipment from Australia on the decline, there is little to cheer in the latest trade report out of China for the AUD. The move higher in the AUD stands at risk of further unwinding towards the next support around 0.6920, marked by the 21-dma and then the next support around 0.6860, which is near low reached in May.

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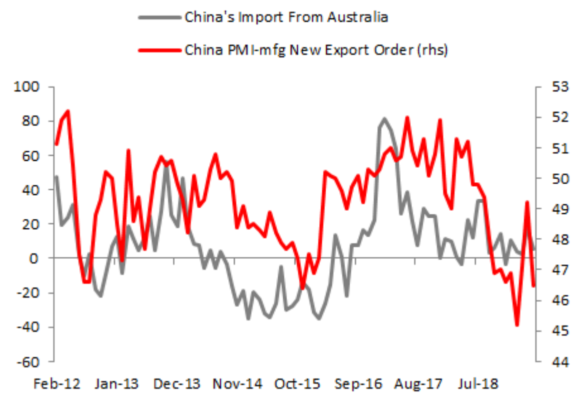
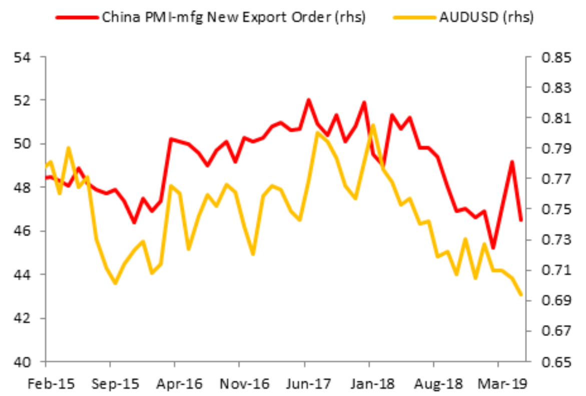
Shipment from Australia to China On a Decline...



Source: CEIC, Maybank FX Research & Strategy

Which typically is negative AUD



Source: *Bloomberg, Maybank FX Research & Strategy*

Yi Gang's Words Bring the RMB Lower
Recent words by PBoC Yi Gang that "no number is more important than other numbers" when he was asked if there was a line for the yuan to be defended, brought the USDCNH higher in an environment of thin-liquidity when Hong Kong was away for a longer weekend last Fri. Weakness in the RMB typically weighs on the AUD. Although his words could have been misconstrued, we see the move as a sign of underlying pent-up demand for USD against the CNH.

Positioning Ahead of the Labour Report This Thu
In addition, we have a labour report due out of Australia for May and we anticipate that market players may prefer to short the AUD ahead of the report as hiring indicators have not exhibited sufficient weakness to justify further rate cuts and the rate cut delivered last week was merely to "help make further inroads into the spare capacity in the economy". However, the central bank typically cut to insure against further deterioration in hiring momentum and that cut suggests that they might have seen what we have not. With recent activity data still rather sluggish, market players may prefer to bet on a weaker number this Thu.

Despite our caution on the AUD in the next few days, we see support at around 0.6860 to hold unless Australia's Bureau of Statistics delivers a shocking print on Thu. We take profit on our long AUD call at 0.7020 as it has been opened for a few weeks.

In the medium term, we still like to keep a slightly more optimistic view of the US-China trade war whilst acknowledging that the US-China trade

Recall that our base case is

"a "grey swan" type amid the re-escalation in "tit-for-tat" tariffs and non-tariff actions that diminish the prospect of a US-China trade deal anytime soon, resulting in a protracted period of tension, although "lines of communication" remains open. As US-China trade and tech war continues into 2H 2019 and as statistics on the "casualties of war" relating to growth, trade, corporate earnings, financial market stresses will start to pile up, these could eventually compel US and China to return to the negotiation table. Progression on talks taking both sides closer to a deal in late-2019/early-2020 is not impossible and this could help support sentiment and support our view for trade/tech-linked FX to recover"

as stated in our FX Monthly Issue 5. A protracted period of tension could mean that much of the tariffs imposed have been in the price of the AUD, along with the two rate cuts that market players expect to bolster the economy against further external headwind. CFTC data shows that the net non-commercial futures contracts for AUD are net -63291 as of data available on 7 Jun. In addition, with the rate cut priced and the next hiking cycle not likely anytime soon, **AUD could have become a funding currency for higher yielding EM or even DM FX and that would protect AUD from a lot more downside in a jittery environment.** In a situation where US-China trade war becomes a trade truce again or a trade compromise, that is also likely not negative for the AUD as well.

US Treasury Secretary Mnuchin has flagged out that "main progress" of the US-China trade talks should happen when Trump and Xi meet at the G20 Summit the end of Jun in Osaka (28-29 Jun). Trump has also warned that more tariffs could be imposed on the rest of the untaxed Chinese imports (which amounts to under U$300bn) after the event. Much is being geared up for this event. We continue to look for AUDUSD to trade within 0.68-0.72 for much of the next few weeks.

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