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FX Tech Flash

Cautious of USD Bears Getting Ahead of Itself

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A Sympathetic Near Term Rebound for USD Not Ruled Out

USD's decline resumed after US payrolls report gave the nod, with NFP undershooting expectations (+75k vs. +175k expected) and hourly earnings disappointed (+0.2% m/m vs. +0.3% expected). We shared in our FX Weekly (last Fri) that *softer payrolls report could be the green light to validate markets' call for a rate cut soon - possibly to signal a cut at the upcoming Jun FOMC (19 Jun) and potentially delivering a 25bps cut as early as at 31 Jul*. Fed fund futures are now showing a 80% chance of a rate cut for Jul meeting (up from 47% in end-May). This week brings US PPI (Tue) and CPI (Wed). A softer print could further drag USD lower.

DXY was last seen at 96.75 levels. Bearish momentum on daily chart remains intact while stochastics is falling into oversold conditions. We see some risks of rebound in the near term. Resistance at 97 (100 DMA, 38.2% fibo retracement of 2019 low to high), 97.60 (21, 50 DMAs), 98.30. Key support at 96.5 (200 DMA). Break below 200 DMA puts next support at 96.30 (61.8% fibo) before 95.88 (76.4% fibo).

While bias to sell USD rallies remains intact, we are cautious of markets getting a bit ahead of itself especially on the aggressive expectations for large-sized Fed rate cut. In addition, sharp decline in UST 10Y yield to 2.05% last Fri may have found a short term bottom (also our 61.8% fibo retracement of 2016 low to 2018 double top). Unwinding of excessive UST longs could see UST yield retrace higher possibly towards 2.20/2.25% in the interim. This could see USD retrace some of its recent decline.

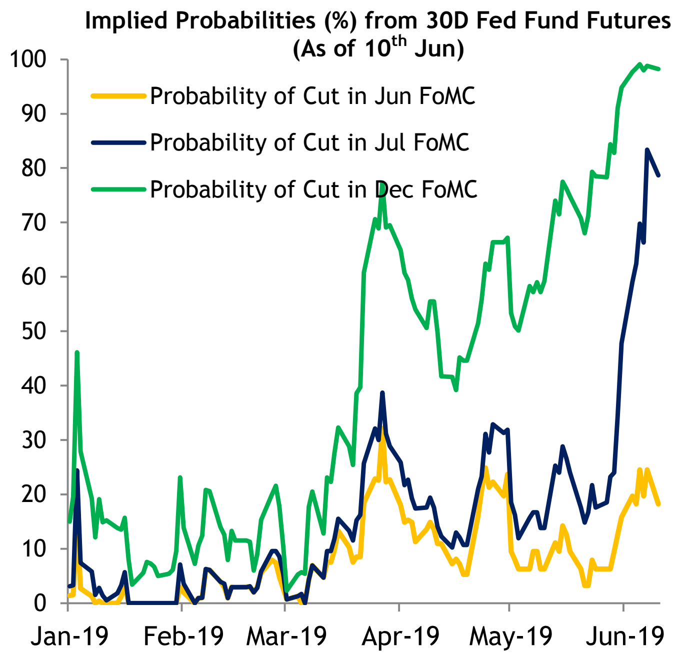
DXY (Daily Chart): Out of Trend Channel but 200DMA Supports

Source: Bloomberg, Maybank FX Research & Strategy

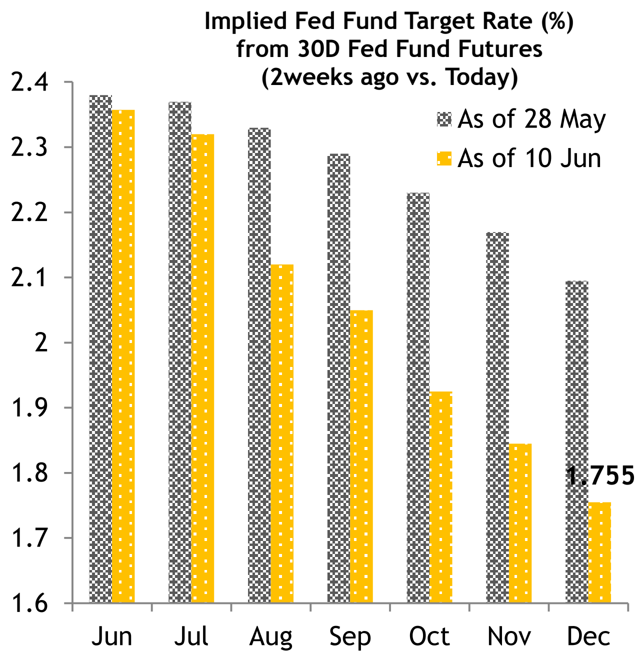
10Y UST Yield Finds Soft Support in the Interim? Chance for Rebound

Source: Bloomberg, Maybank FX Research & Strategy

Markets Pricing in Jul as Earliest Date for Fed Cut



Markets Looking for 2 Fed Cuts by End-2019



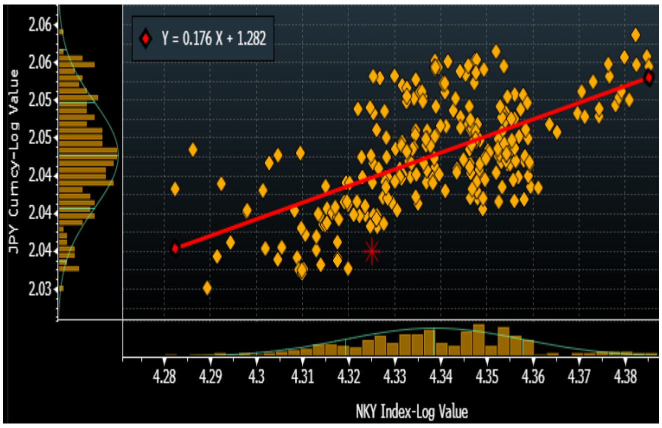
Source: Bloomberg, Maybank FX Research & Strategy

USDJPY Short Squeeze May Have More Room to Unravel

One way to express near term USD rebound would be via USDJPY especially given its positive correlation to equities and UST-JGB yield differentials. Confirmation of Trump suspending his plans for tariffs on Mexico was a welcome relief for fragile market sentiment. That saw equities reacted positively. And at the same time, USTs are in overbought conditions. Unwinding of UST longs could see UST yields rebound off its interim "soft-bottom". Subsequent re-widening of UST-JGB yield differentials could support USDJPY higher.

USDJPY Correlation at +0.67 with UST-JGB YD

USDJPY Correlation at +0.61 with NKY225



Note: Log values of USDJPY regressed with UST-JGB yield differentials (YD) and NKY225 on daily close over past 1year.
Source: Bloomberg, Maybank FX Research & Strategy

We continue to hold to our caution that USDJPY may have room for further upside squeeze. Pair was last seen at 108.65 levels. Bearish momentum on daily chart is waning while stochastics shows signs of turning from near-oversold conditions. A potential bullish divergence could also be in play, as seen from the MACD chart. Immediate resistance at 108.70 (76.4% fibo retracement of psot-20199 flash crash low to high). Decisive break above could see a move towards 109.20 (21 DMA)/ 109.40 (61.8% fibo). Support at 107.90, 107.50 levels.

USDJPY (Daily): More Room for Upside on Break bove 108.70

Source: Bloomberg, Maybank FX Research & Strategy

Reiterate Bias to Lean against USD Strength

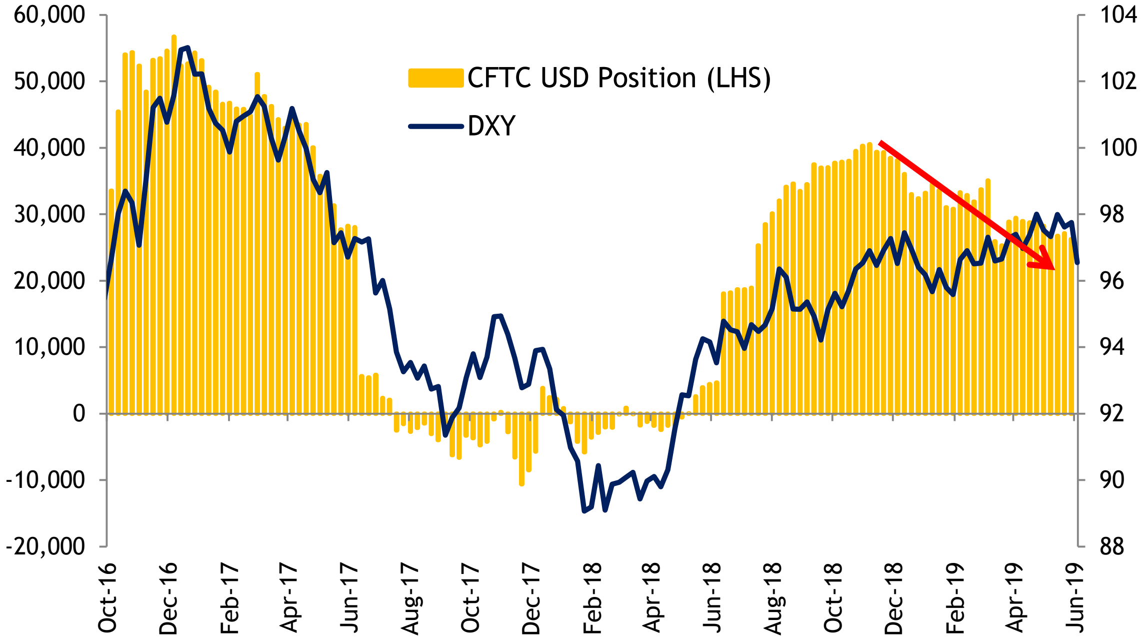
Notwithstanding the caution for a sympathetic USD bounce in the near term, we reiterate our call looking for DXY strength to ease. True that market typically buys USD on fears of no trade deal, etc. But we argued that trade tensions can also hurt US growth, jobs creation and financial markets. Potentially the Fed may even need to ease monetary policies at some stage. In this environment where US growth/activity outlook starts to dim, flight to quality flows/ equity sell-off should favor JPY and CHF while EUR could somewhat retain its relative resilience. As a result DXY strength could be curbed. And this has so far been evident from recent data which saw ISM Mfg, ADP employment, NFP payrolls and wage growth coming in softer than expected as well as recent Fed speaks.
Fed Chair Powell said that that Fed is prepared to respond if it decides that Trump's trade conflicts are threatening the US economy (7 Jun).

On Mon (3 Jun), Bullard (voting member) said that a downward policy rate adjustment may be warranted soon to help re-center inflation and inflation expectations at target and also to provide some insurance in case of a sharper than expected slowdown. He added that even if the sharper-than-expected slowdown does not materialise, a rate cut would only mean that inflation and inflation expectations return to target more rapidly.

Barkin (non-voting member) said he is "frankly nervous" about the fragility of businesses' mindset on their investment postures due to uncertainty in the air (relating to increased tariffs).

Late-May, Vice Chair Clarida discussed the possibility of Fed rate cut. he said the Fed was "very attuned to the risks to the outlook and if they crystallised it could be a reason for more accommodative monetary policy". He added that if incoming data were to show a persistent shortfall in inflation below 2% objective or to indicate that global economic and financial developments present a material downside risk to baseline outlook then these are developments that the FoMC would take into account in assessing the appropriate stance".

USD Long Positions Are Finally Unwinding



Source: Bloomberg, CFTC, Maybank FX Research & Strategy

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