Consultancy
Intelligence
Publishing

BRIEFING NOTE

November 22nd /// 2020

WEEK AHEAD: VACCINE vs LOCKDOWN?

WEEK AHEAD: VACCINE vs LOCKDOWN?

There is not much on the agenda next week, but that doesn't mean things will be quiet as the battle between longer-term vaccine hopes and the present lockdown reality continues to rage. The highlight on the economic calendar will be the latest PMIs, especially from the Eurozone, which will reveal how much damage the latest lockdowns have inflicted. In America, the latest Fed minutes might be viewed as outdated, so it will be all about infection numbers as more states tighten their restrictions. Finally, a Brexit deal could be imminent.

Conflicting narratives

The latest vaccine news sparked a wave of euphoria in global markets, but the enthusiasm didn't last long as surging infections and fading prospects of powerful fiscal stimulus kept the animal spirits on a leash. Investors are now trying to balance the brighter outlook for next year against the covid reality right now, with most of Europe in partial lockdown and America quickly moving in that direction.

The debate is whether all the 'good news' has been priced in at this point, leaving markets vulnerable to any negative headlines. Admittedly, much of the price action over the coming weeks will hinge on 1) whether the virus continues to spread uncontrollably in the US and 2) whether the Fed signals it will pull the QE trigger again in December.

What's striking is that while the stock market and commodities like crude oil were highly responsive to the vaccine news, the FX market barely reacted. Euro/dollar even moved lower afterwards, which is not what you would expect considering the greenback has been acting like a safe haven overall. This suggests markets saw the news as decreasing the likelihood of the Fed acting again with force, whereas the ECB has already pre-committed to another liquidity injection next month.

That said, Fed officials might not have much of a choice. Tightening restrictions across the US will inevitably hit growth even without a national shutdown, and Congress is unlikely to deliver substantial fiscal relief anytime soon. Plus, the Treasury is now trying to withdraw some of the emergency loan programmes that were available for small businesses, adding more pressure on the Fed to expand its own liquidity offerings.

The bottom line is that if markets sense more Fed easing is on the menu, that would argue for some upside in euro/dollar. Pointing in the same direction is a potential Brexit deal being wrapped up soon, which could boost both the pound and the euro at the dollar's expense. But even bearing this in mind, it is difficult to envision euro/dollar breaking above $1.20 as this region has been a line in the sand for the ECB lately. Hence, while the near-term risks around the dollar seem tilted lower, the downside looks relatively limited as well. The joker in all this is what happens with the upcoming European PMIs.

Eurozone PMIs: A lockdown horror show?

The week will kick off with a blast as the Eurozone's preliminary PMIs for November will hit the markets early on Monday. These will be the first numbers to reflect the new lockdowns, so things could get ugly. All the indices are projected to plunge, with France expected to bear the brunt of the pain as that's where the lockdowns are stricter.

The question now is whether the actual numbers will be even worse than the forecasts. Admittedly, Europe has been in a lockdown for several weeks now, so most of the bad news should be priced in at this stage. Plus, the forecasts are extremely grim already, so a massive disappointment does not seem very likely.

Still, this data set is the wild card for euro/dollar. A major disappointment could be the saving grace for the dollar that pushes euro/dollar lower, otherwise a combination of Fed easing and a Brexit breakthrough could push the pair towards $1.20 again.

Brexit deal finally in sight

The Brexit saga may be about to enter its final act, with both sides suggesting a deal is imminent. Of course, this is Brexit we are talking about, so nothing is certain until a deal is signed. The latest updates suggest 95% of the treaty has been completed, though gaps remain on the classic issues: competition rules, fisheries, and the policing of the deal.

It seems the negotiators have done all they can by themselves, and it is now up to the politicians to make the final compromises. Specifically, the EU expects the UK to compromise on competition rules before it concedes itself on fisheries. In other words, the ball is now in Boris Johnson's court – if he wants the deal, he has to soften his stance.

As for the pound, it has moved substantially higher lately in anticipation of an agreement deal, and if one is reached soon, it may have some more miles left in the tank. Speculators are still net-short the pound according to the weekly CFTC data, which leaves plenty of upside once the Brexit smoke clears. That said, if we enter December and a deal hasn't been reached yet, the optimism could evaporate very quickly.

The nation's PMIs for November are also out Monday.

FOMC minutes: Outdated already

In the US, the main release will be the minutes of the latest FOMC meeting on Wednesday, though any policy signals might already be seen as 'old news' by the markets. The Fed may have been unwilling to signal a new round of QE when this meeting took place in early November, with covid infections still running low and the outcome of the election undecided, but things could be very different now.

There's also a ton of economic data coming up. The preliminary Markit PMIs for November are out on Monday, before durable goods orders and the core PCE price index for October are released Wednesday, alongside the second estimate of Q3 GDP. None of these is usually a market mover.

The dollar may be more responsive to the factors outlined above, and how the US virus trend evolves. Any hints that a national lockdown is a realistic possibility when Biden takes over in January would only cement expectations for a more aggressive Fed.

Yen's path versus dollar defies recovery trend, may cause headache for policymakers – Special Report

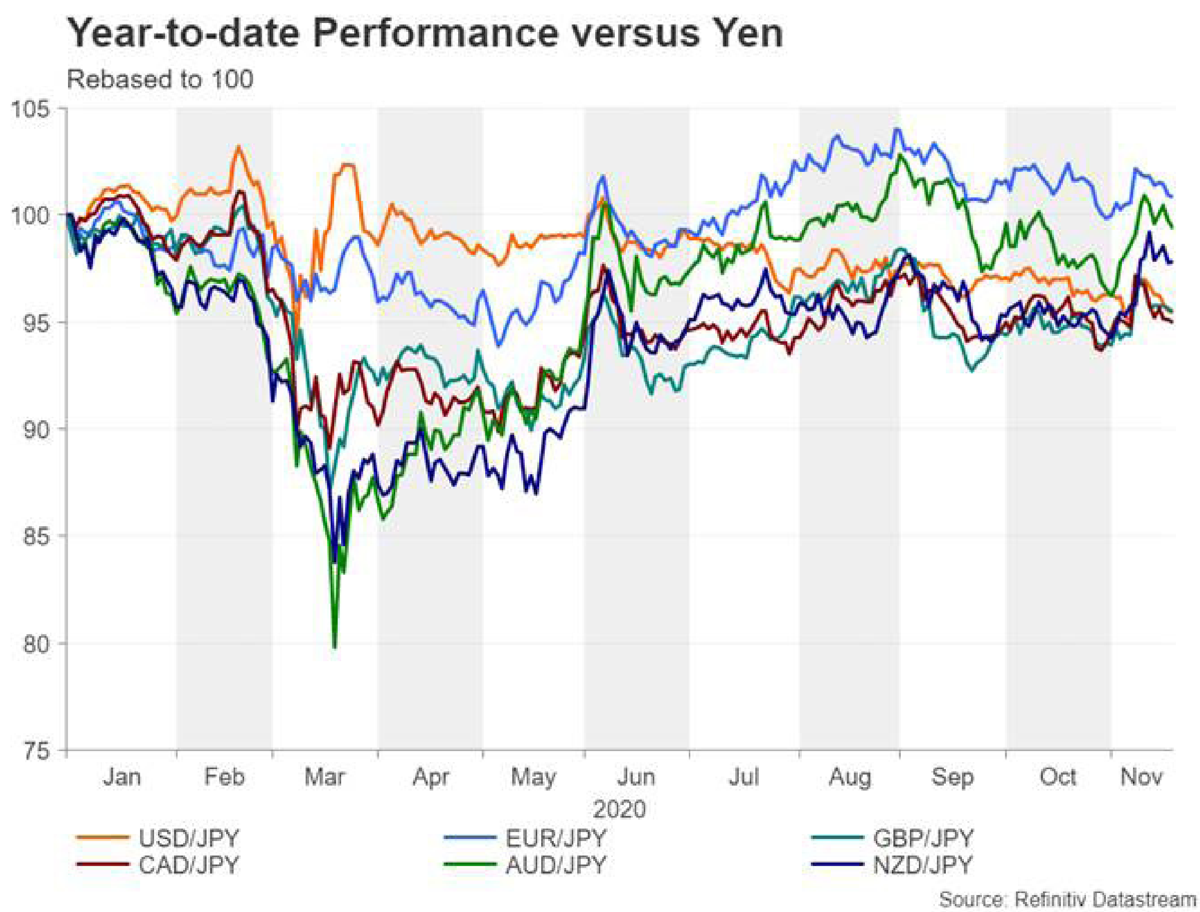
The Japanese yen has been on a steady downtrend against most of its major peers since March when it exploded higher during the virus-induced financial turmoil. Although only the euro and the Australian dollar have managed to erase their year-to-date losses, the gap for the remaining currencies isn't too great. The pound is down about 3.5% and the Canadian dollar still needs to recoup around 4.5%. So the US dollar's decline of a similar amount to the loonie shouldn't come across as particularly unusual, until you start to consider that the dollar isn't trending up. It's trending down!

Battle of the safe havens

Usually during global crises or downturns, the dollar has typically appreciated against its peers at the onset of the market panic but fallen against the yen. When confidence begins to return to the marketplace, the greenback tends to fall as other currencies recover, except against the yen, whose own safe-haven status supersedes the dollar's. The reason for that is what makes the two currencies an attractive destination for flights to safety in the first place.

The dollar is the world's most liquid currency, hence, why it remains the number one reserve currency of choice and why investors rush to own it when there is a funding squeeze. But investors generally only flee to the dollar in huge numbers when there is a crisis on a global scale. At all other times, it is the yen that draws the most demand from regular bouts of geopolitical risks, such as political uncertainty, trade tensions and Brexit.

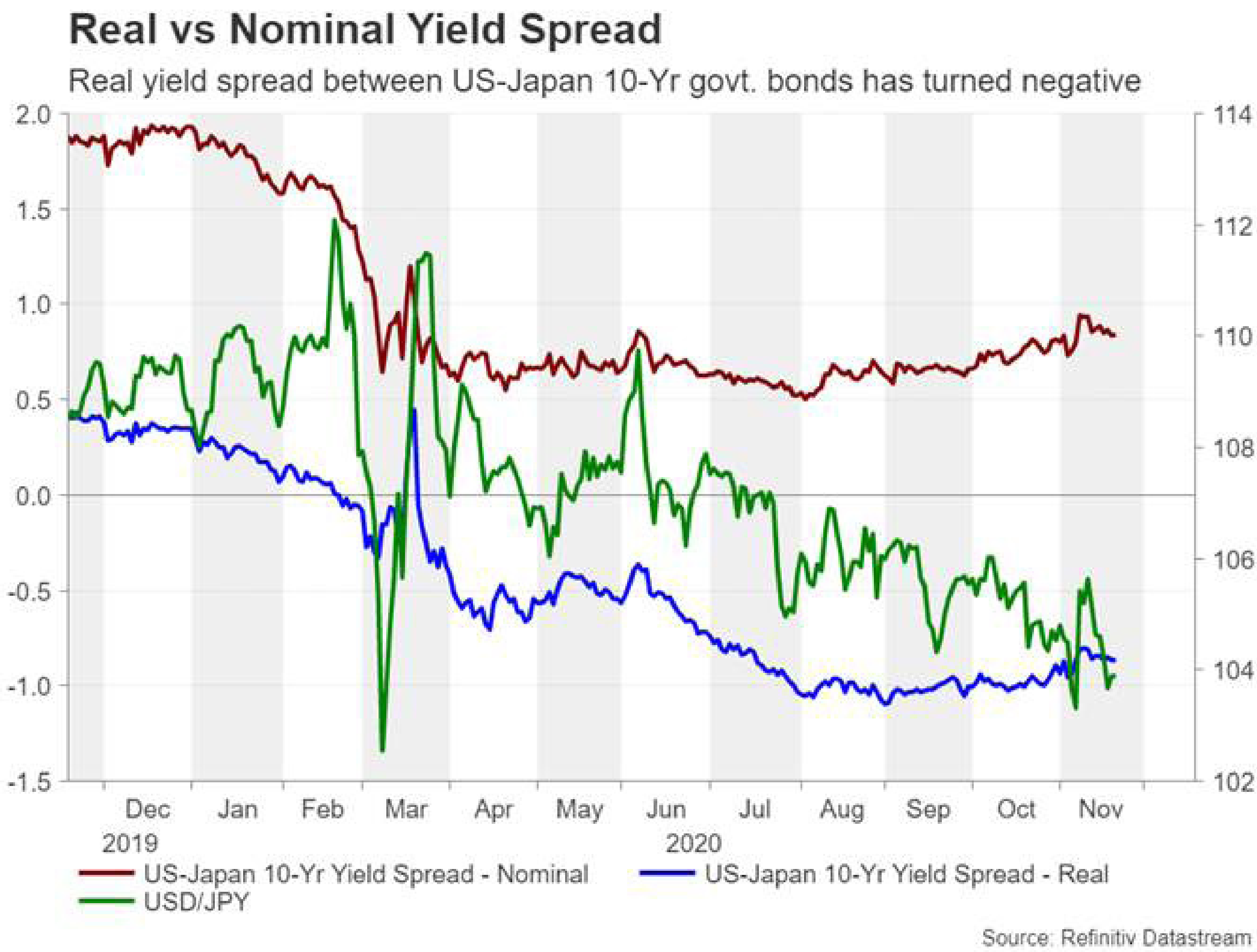
Japan is the world's biggest creditor nation, so the assumption is that when fresh turmoil erupts, investors will offload those assets – primarily government bonds – and convert them back into yen, pushing it higher.



USDJPY weakness defies rebound in risk appetite

However, following the unprecedented volumes of stimulus injected by governments and central banks around the world since March, market stress has eased substantially and a global economic recovery is well underway. The United States can even boast its recovery to be stronger and more resilient. There's also very little chance of the Federal Reserve cutting rates any lower, which means yield differentials are not expected to move in favour of the yen anytime soon. If anything, the spread on 10-year US-Japanese government bonds has been rising since August, which should be supportive of dollar appreciation.

So why does the dollar keep falling against the yen? The missing piece in the jigsaw here is real yields. On an inflation-adjusted basis, yields in the US collapsed below Japanese ones after the Fed slashed its key lending rate to near zero back in March and they've remained below Japan's ever since. But this doesn't totally solve the puzzle because even on an inflation-adjusted basis, US yields have been edging higher in recent weeks. The end to the US election uncertainty and the discovery of a COVID-19 vaccine have spurred risk assets while hurting safe-haven bonds. Thus, the dollar should have made more of an attempt to break its downtrend versus the yen than just briefly spike higher in risk-on episodes.



Japanese yields no longer the lowest in the world

One possible factor that is likely keeping dollar/yen skewed to the downside is the dramatic decline in capital outflows from Japan. This is partly down to the narrowing yield differentials, not just with the US but with all other countries whose central banks had scope to cut rates during the pandemic. Japanese investors have significantly reduced their allocations to overseas assets this year as they are no longer as attractive. To make matters worse, the pandemic has additionally disrupted mergers & acquisitions, leading to an overall sharp decline in foreign outflows from Japan.

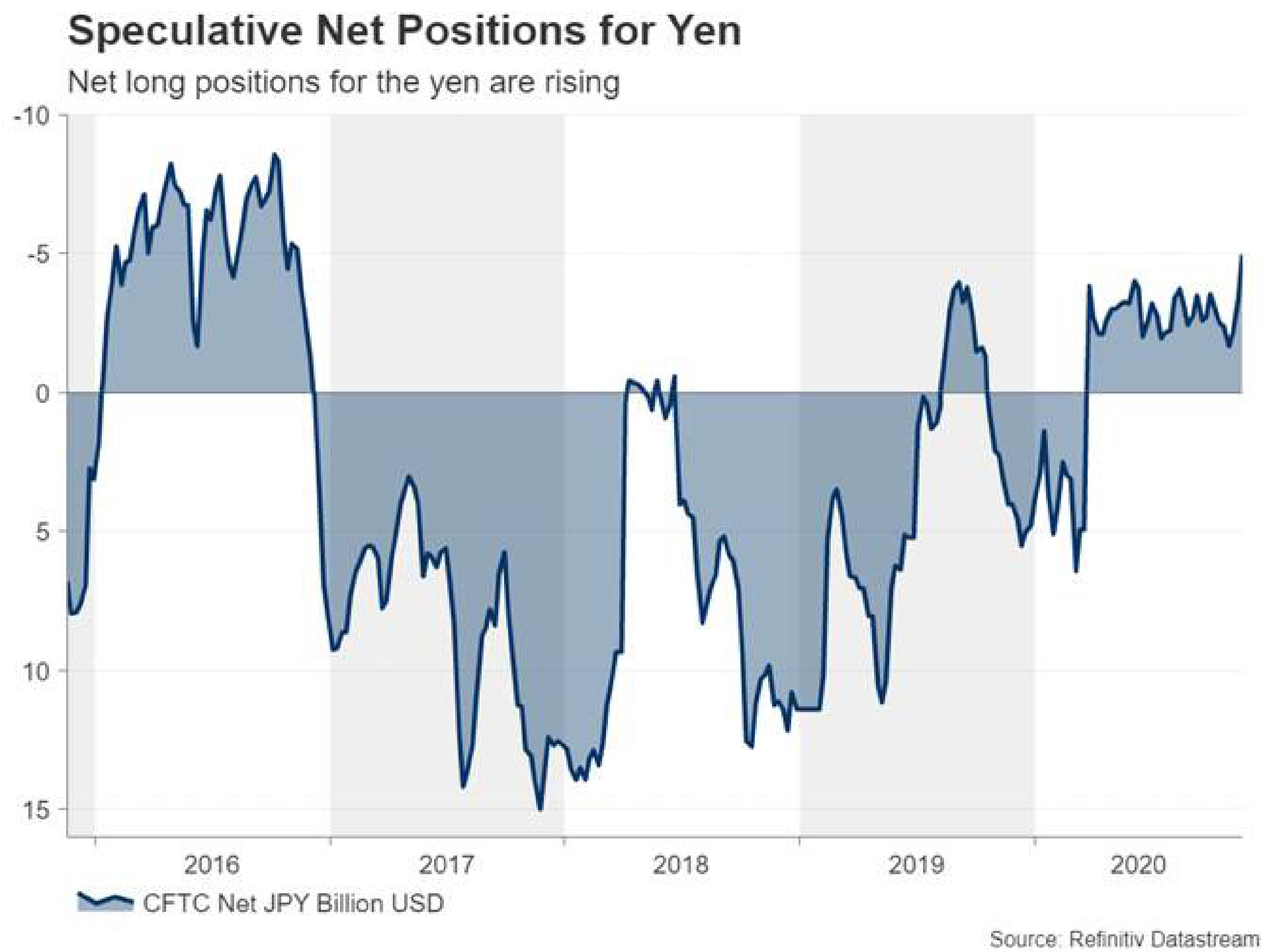
But the problems for dollar/yen don't end there. The soaring US fiscal deficit and expectations that the Fed will increase its asset purchases further, putting a cap on Treasury yields, make for a weaker dollar in the long run. Compounding this is the Fed's recent revamp of its policy framework. The decision to target average inflation over time rather than a fixed goal is likely to drive real yields even lower as the Fed lets price growth run above 2%.

Virus risks have not dissipated

In the meantime, of course, the uncertainty from the coronavirus outbreak hasn't entirely gone away. The stock market rally, fuelled by the abundance of liquidity, may give the impression that everything is almost back to normal, but it hides the ongoing pain for economies around the world, as a full recovery will likely not be possible until 2022 at the earliest.

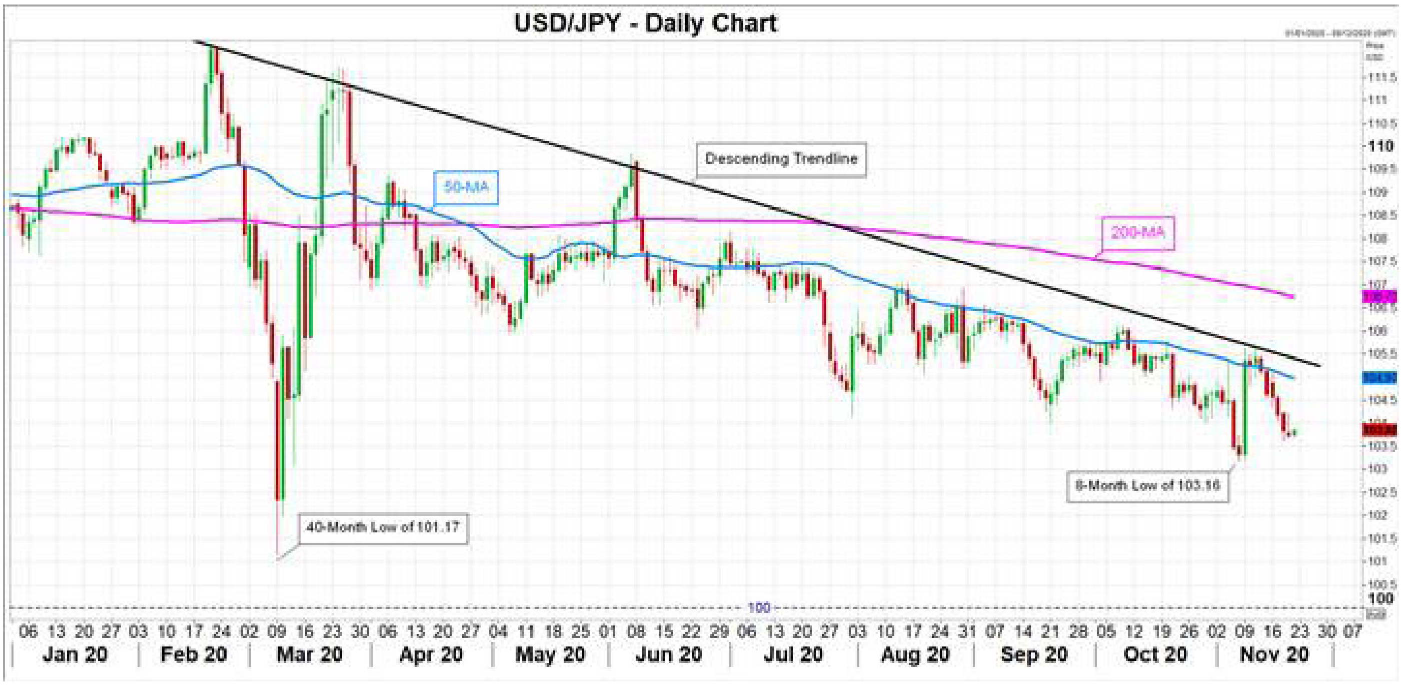
And while the vaccine news is what everyone had been waiting for, before mass distribution can begin, there is a cold dark winter to get through in Europe and America where virus cases are at record levels and deaths are rising alarmingly.

All these lingering risks can only imply investors still have plenty of reason to seek safety and are probably behind the recent increase in yen long positions (according to data from CFTC).



Bearish signals

From a technical perspective, dollar/yen is also looking increasingly bearish. The pair is trading below both its 50- and 200-day moving averages. More importantly, the fact that dollar/yen was unable to crack above its long-term descending trend line from the post-election and vaccine-led rallies signals that the greenback's bullish days are probably well and truly over.



Although that may not necessarily mean the yen is set for similar gains versus its other major peers, Japan's low inflation prospects and flat yield curve are now likely to work in favour of the currency than against it as was the case not that long ago.

The only caveat here is that Japanese policymakers are unlikely to let the yen appreciate beyond the 100 per dollar level. When the pair tumbled below 104 in the aftermath of the US election outcome, Japanese Prime Minister Yoshihide Suga didn't hesitate to ramp up his rhetoric about the importance of stable exchange rates. Hence, any further moves lower could potentially see the 100-101 region become a heavily congested area like it did back in 2016.

Technical Analysis – Tesla's stock shoots to new record high after joining S&P 500

Tesla's stock overshoot above a symmetrical triangle in the four-hour chart and unlocked a fresh record high of 508.26 after its entrance to the S&P 500 community, but failed to close above September's top of 501.50 on Thursday.

The Stochastics is seeking a turning point above their 80 overbought mark as the RSI seems to be slowing pace comfortably above its own 70 overbought level. In other indicators, the red Tenkan-sen is also reflecting some uncertainty about the positive momentum in the price as it remains close to the blue Kijun-sen.

That said, neither indicator has shown a convincing downside reversal yet, hence the basic scenario is for the stock to keep improving. Perhaps, a close above the 500 mark could add more fuel to the rally, pushing resistance up to the 550 number.

Alternatively, a backward flip may initially stall around the supportive red Tenkan-sen line at 456.40 before it extends to the upper surface of the triangle seen around 430. If the bears claim the latter, the next stop could be at the bottom line of the triangle and the 400 hurdle. Another step lower would increase the case of a down-trending market and resume a bearish outlook, especially If the 200-period exponential moving average (EMA) gives way too.

Summarizing, Tesla's stock is bullish in the short-term picture, though some stabilization should not be a big surprise as the market trades in overbought waters.

Technical Analysis – US 30 index range bound; skewed positive above 29,195

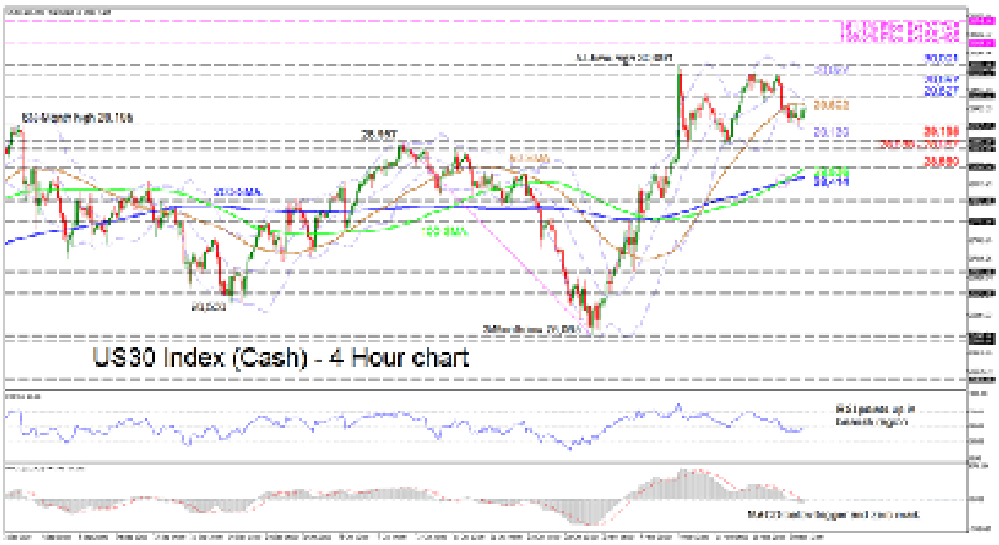
US 30 stock index (Cash) is facing the capping 50-period simple moving average (SMA) at 29,502, after improving a bit off the lower Bollinger band at 29,195. The index, ever since it logged a fresh all-time-high of 30,091 on November 9, has been trading in a ranging market between 28,838 and 30,091. That said, the flattening 50-period SMA and the conflicting signals in momentum within the short-term oscillators, promote a developing horizontal picture.

The MACD is in the negative zone slightly below its red trigger and zero lines, while the RSI is rising towards its 50 threshold. Nonetheless, the advancing 100- and 200-period SMAs are sponsoring positive price action and could play a crucial part in maintaining a bullish structure.

Pushing up, initial limitations may arise from the area surrounding the mid-Bollinger band, that being from the 50-period SMA at 29,502 until the 29,627 barrier. Climbing higher the tough resistance section of 29,957-30,091, involving the upper Bollinger band and the all-time-high, could try to suppress further advancing in the price. However, if buying interest surges, the index may aim for the 30,405 and 30,745 obstacles, which are the 150.0 and 161.8% Fibonacci extensions of the down wave from 28,957 to 26,065.

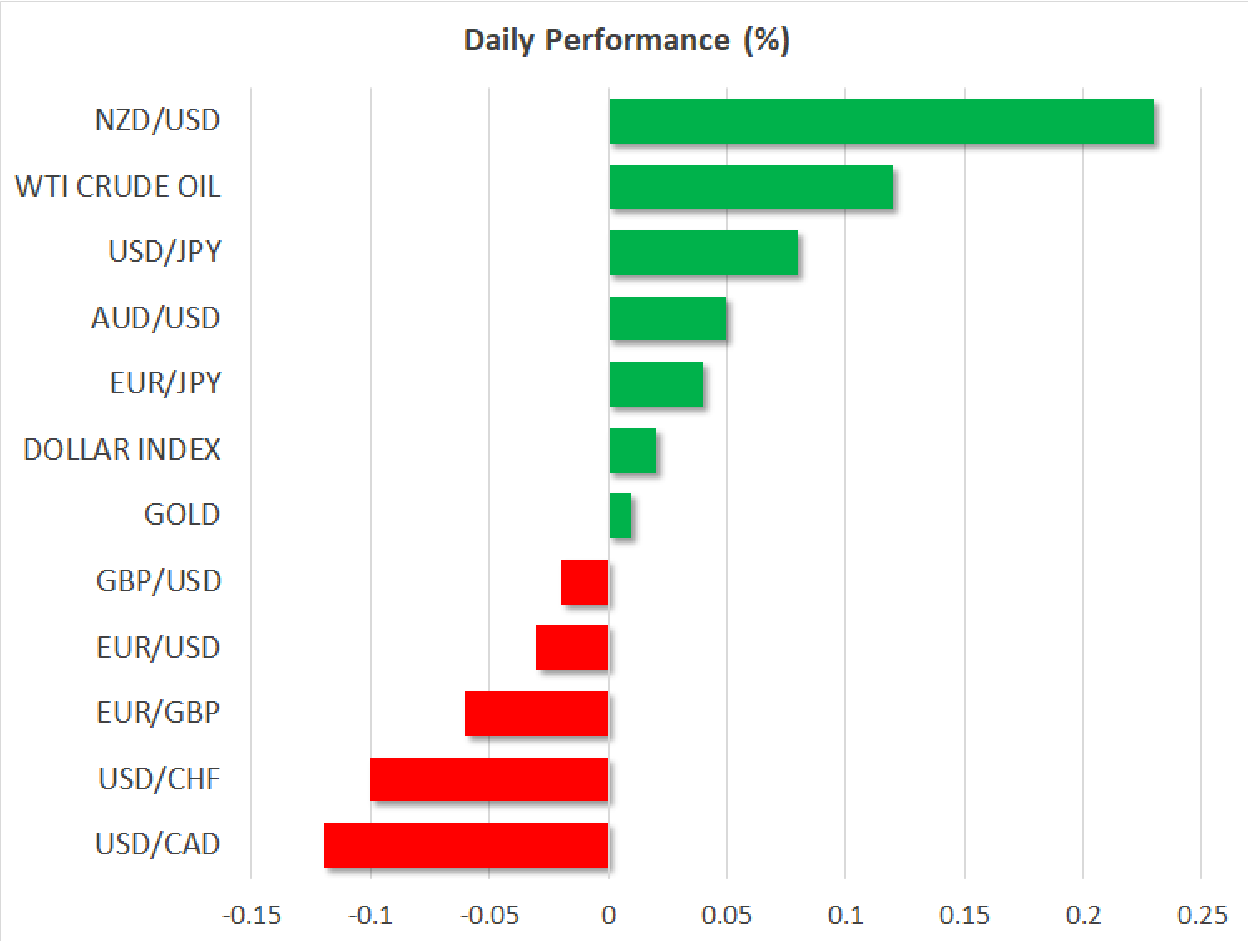
Alternatively, steering the price downwards may hit early support at the 29,195 level and the lower Bollinger band at 29,130. Next, the formed foundation of 28,838-28,957 may attempt to rescue the positive bias. Should this border fail to do so, the index may tumble towards the 28,560 boundary and the adjacent 100-period SMA at 28,536, ahead of the 200-period SMA at 28,414.

Overall, a nudge above the 50-period SMA may strengthen the neutral-to-bullish picture. Yet, ultimately a break either below 28,838 or above 30,091 could see a decisive direction unfold.



Stimulus fears after Mnuchin cuts off Fed emergency lifeline

- **Treasury Secretary asks Fed to return unused emergency funds, US futures slip**
- **But some relief as Senate Republicans agree to restart talks on new virus relief bill**
- **Fresh setback for Brexit talks after Barnier has to self-isolate as time running out**



Fed and White House clash over emergency programs

The Federal Reserve's powers for fighting the pandemic were severely curtailed on Thursday after Treasury Secretary Steven Mnuchin took the unusual step of not extending funding for many of the central bank's emergency lending programs that are financed by the federal government.

Mnuchin is hoping the funds can be used by Congress for other needs but many believe the move is designed to hinder the incoming Biden administration's ability to effectively respond to the latest escalation of the coronavirus in the United States.

Although a lot of the emergency facilities introduced at the height of the virus crisis in March, such as the Main Street Lending Program, have barely been used, the Fed believes their presence is crucial in maintaining calm in financial markets as they act as an important backstop for the economy.

Fed Chair Powell had recently hinted that those emergency programs, which are due to expire at the end of the year, were likely to be extended in December. But Mnuchin's decision to pull the plug on most of them now leaves the Fed racing to come up with alternative measures of support for the economy as there has been no let-up in the surge of new infections across the country.

Resumption of stimulus talks eases virus pain

The daily tally of new infections in the US hit another record yesterday, reaching 185,000 cases, with California announcing a night-time curfew. The growing list of restrictions may have already started to hurt the recovery as jobless claims unexpectedly rose last week and were also up from the prior week, signalling a stalling jobs market.

Renewed worries about the economy amidst all the vaccine euphoria has put a dampener on stocks this week. After a strong start, the Dow Jones and S&P 500 are on track to end the week flat. But the tech-heavy Nasdaq Composite is set for moderate gains as tighter restrictions have boosted stay-at-home and defensive tech stocks. Futures contracts for all three indices were last trading in the red, though the Nasdaq was outperforming again and almost flat.

There was some good news for the markets to digest this morning, however, as talks between Republicans and Democrats in the Senate on a new fiscal stimulus package have restarted. Given that previous efforts proved fruitless and a deal is unlikely before the new administration has been sworn in, reaction in the markets is fairly muted, though it is providing some support against all the negative virus headlines.

Relief that the ballot recount in Georgia for the presidential election has confirmed Joe Biden as the winner in the state may also be contributing in steadying the mood today as Trump's legal team appears to be running out of options in overturning Biden's victory.

Dollar stabilizes, pound upbeat on prospect of Brexit deal

European shares opened higher on Friday and major FX pairs were confined to narrow ranges. The New Zealand dollar was again the exception as it edged up 0.25%. The US dollar managed to regain some positive footing after yesterday's downside reversal. It was last up marginally against a basket of currencies.

The euro slipped slightly amid caution about the fate of the EU's virus rescue fund as the stand-off between Hungary and Poland and the rest of the bloc shows no sign of being resolved quickly.

The pound inched higher as hopes of a Brexit breakthrough remain high despite the talks in Brussels being temporarily suspended after a member of the EU's negotiating team tested positive for COVID-19, forcing Michel Barnier to self-isolate. EU leaders have reportedly been briefed today that a deal is very close, though differences persist on the main sticking points of fisheries, governance and level playing field. The next few days will be critical as it will be extremely difficult to extend the negotiations beyond the end of next week if a trade agreement is to be ratified by all parliaments by December 31.

GMT	COUNTRY	INDICATOR	PERIOD	UNIT	ACTUAL	REUTERS POLL	PRIOR
23:30	Japan	CPI, Core Nationwide YY	Oct 2020	Percent	-0.7	-0.7	-0.3
23:30	Japan	CPI, Overall Nationwide	Oct 2020	Percent	-0.4		0
0:01	United Kingdom	GfK Consumer Confidence	Nov 2020	Balance	-33	-34	-31
0:30	Japan	Jibun Bank Mfg PMI Flash	Nov 2020	Diff.Idx	48.3		48.7
7:00	Germany	Producer Prices YY	Oct 2020	Percent	-0.7	-0.7	-1
7:00	United Kingdom	Retail Sales MM	Oct 2020	Percent	1.2	0	1.5
7:00	United Kingdom	Retail Sales Ex-Fuel MM	Oct 2020	Percent	1.3	0.1	1.6
7:00	United Kingdom	Retail Sales YY	Oct 2020	Percent	5.8	4.2	4.7
7:00	United Kingdom	Retail Sales Ex-Fuel YY	Oct 2020	Percent	7.8	5.9	6.4
13:30	Canada	Retail Sales MM	Sep 2020	Percent		0.2	0.4
13:30	Canada	Retail Sales Ex-Autos MM	Sep 2020	Percent		0.2	0.5
15:00	Euro Zone	Consumer Confid. Flash	Nov 2020	Balance		-17.7	-15.5

Technical Analysis – NZDUSD rallies towards previous high of 0.6945

NZDUSD is trading not too far from the 0.6945 resistance level and momentum indicators suggest there is still some optimism for the pair to advance again. The near-term bias is looking bullish as the RSI is edging north in the bullish area, while the MACD is trying to extend its movement above its trigger line. Price action at the moment is above the Ichimoku cloud so the risks are to the upside.

Should the pair make another run higher, it's likely to meet resistance at 0.6945 as this level has strongly capped prices on Wednesday. A successful break above this key resistance area would open the way for the 0.6970 barrier ahead of the 0.7060 hurdle, registered in June 2018.

If the soft positive momentum fails to hold and prices turn lower, the red Tenkan-sen line at 0.6905, which overlaps with the 20-period simple moving average (SMA) is the nearest support that could halt steeper declines. A potentially more important support, though, is the 40-period SMA which stands near the 0.6876 level.

In the bigger picture, NZDUSD would need to make a sustained climb above 0.6970 for the outlook to become convincingly bullish.

Technical Analysis – GBPJPY puts breaks on decline after trendline rejection

GBPJPY drifted higher and above all its daily simple moving averages (SMA) on the back of encouraging vaccine news and Brexit hopes last week, though the support-turned-resistance ascending trendline was there once again to block the way above 140.00.

The area around the blue Kijun-sen line managed to stabilize the downfall from the trendline around 137.33 and the price is currently trying to return above the 50% Fibonacci of the 142.69 – 133.00 downleg.

In momentum indicators, the Stochastics favour upside corrections as they are set for a bullish reversal around their 20 oversold level. On the other hand, the RSI, close to its 50 neutral mark, is more cautious about any positive moves but as long as it holds above the supportive trendline, it can't rule them out either.

Should the bulls clear the nearby 137.86 hurdle, the 61.8% Fibonacci of 139.00 could provide immediate resistance. If not, the pair may advance towards the ascending trendline seen at 140.30, a break of which could next expose the price to the 141.94 – 142.69 key restrictive zone.

Alternatively, a drop below 137.00 and the 20-day SMA may reach the 200-day SMA currently around the 23.6% Fibonacci of 135.30. Another step lower could strengthen selling pressure towards the 133.00 bottom, violating the upward pattern in the two-month picture.

In brief, GBPJPY is on the defensive following its latest decline. A break below 137.00 is expected to generate additional losses, while a bounce higher may see the retest of the ascending trendline if the 139.00 number gives way.

Technical Analysis – GBPUSD bounces off 1.3200; bullish in short-term

GBPUSD has gained little on Thursday and it managed to hold above the 20- and 40-period simple moving average (SMA), with the technical indicators feeding prospects for a possible positive short-term trading; the RSI holds above 50, while the MACD continues to strengthen in bullish territory above its trigger line.

A move higher could take the pair until the double top at 1.3310, a challenging point over the last week. Higher resistance could next be found around the 1.3475 barrier, taken from the peak on September 1.

Alternatively, if the 20- and 40-period SMAs proves easy to get through, the spotlight would turn to the 1.3200 round number, which is the 23.6% Fibonacci retracement level of the up leg from 1.2854 to 1.3310.

In the short-term picture, GBPUSD turned positive after violating the rebound off the 1.2854 support level. Should the market continue the upward pattern, the outlook may turn brighter above 1.3310.

Technical Analysis – USDCAD comes to a standstill as momentum fades

USDCAD's dictating bearish picture seems to be taking a breather after a bounce off a newly formed 10-month low of 1.2927. The slowing bearish pace of the 50- and 100-day simple moving averages (SMAs) and the flattening out in the 50-day SMA are assisting the stalled, negatively-skewed structure.

The short-term oscillators currently display conflicting signals in directional momentum. The MACD, in the negative region, is above its red trigger line, while the stochastic oscillator maintains a negative bearing. That said, the flat RSI is hovering slightly below its 50 threshold.

In a positive scenario, early resistance may develop from the 1.3172 high and the nearby 50-day SMA at 1.3185, followed by the 100-day SMA at 1.3245. Should buyers persist to oppose the predominant negative bearing, they may meet constraints from the 1.3298 level before the critical region of highs of 1.3389-1.3420. Moving higher, their efforts may then be challenged by the resistance zone of 1.3458-1.3504, and the 200-day SMA of 1.3540 overhead.

If selling interest intensifies, initial friction to downside moves may come from the key limiting low of 1.2993, followed by the support section of 1.2927-1.2950. Deteriorating under this base, the price may dip towards the 1.2884 obstacle from back in September 2018. Steeper declines may then have sellers meet the 1.2782 trough from October 2018 ahead of the 1.2728 low achieved in May of 2018. If the bears persist, they could take the price as low as the 1.2622 boundary.

Summarizing, a controlling neutral-to-bearish bias has gripped the pair below the SMAs. A break below 1.2927 may strengthen the negative structure, while a thrust above 1.3420 could boost confidence in the pair.

Consultancy
Intelligence
Publishing