

Flash Note 28/03/2017

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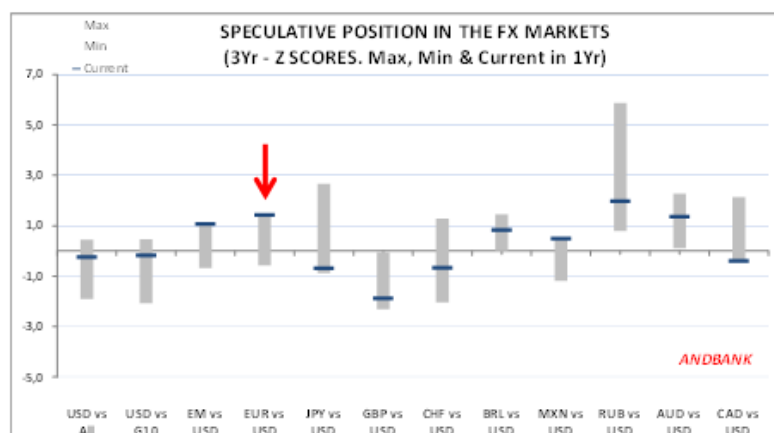
A breathing space for the euro

Flow Factors driving the EUR/USD

- In the aftermath of the first French presidential debate the EUR had some days of respite, **with net short spec positioning in EUR being trimmed aggressively (from US\$ -7.67bn to US\$ -2.66bn)**, or cut by 0.5 s.d. (basis of 3-y z-score) with respect last month positioning.
- EUR shorts are now the lowest in nearly 3 years, (or the positioning in Euros is now the longest seen in the last three years), reflecting the improvement in the data in Europe. **As a result, it will be necessary to see new positioning records in Euros to see additional appreciations.** We set the short-term range in the 1.05-1.10.
- Given our doubts about the sustainability of the economic jump (considering that the vast fiscal and monetary stimulus in China, that caused most of the “reflation trade”, have been gradually withdrawn since last summer), and if the investor’s structural pattern continues and decide to hold average exposure seen in the last three years (see the bar chart below), the stage is set for further structural falls in the Euro from this level.
- **Our Fundamental Value for the EUR/USD remains unchanged at 1.00**

Currency	Mkt Value of Net positions in the currency (Bn \$)	Change vs last week in the currency (Bn \$)	1-yr Max (Bn \$)	1-yr Min (Bn \$)	1-yr Avg (Bn \$)	Current Z-s score 3-yr
USD vs All	18,09	1,21	28,7	-6,9	12,1	-0,25
USD vs G10	19,33	1,35	28,4	-7,1	11,7	-0,18
EM	1,24	0,14	1,2	-1,7	-0,4	1,07
EUR	-2,66	2,78	-2,7	-19,0	-9,8	1,42
JPY	-7,50	0,27	8,6	-9,3	1,9	-0,68
GBP	-8,41	-0,27	-3,0	-8,4	-5,5	-1,88
CHF	-1,51	-0,39	1,4	-3,1	-0,5	-0,68
BRL	0,52	0,02	0,8	0,0	0,4	0,83
MXN	-0,09	0,05	-0,1	-2,3	-1,3	0,49
RUB	0,81	0,07	1,3	0,1	0,5	1,97
AUD	3,46	0,19	4,6	-1,2	1,8	1,36
CAD	-1,83	-3,42	2,3	-1,8	0,5	-0,40

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The Other Factors driving the EUR/USD

The Known positives for USD:

1. Rising positive carry on US dollar debt instruments.
2. The Fed has a tightening bias, while most other central banks still have easing bias.
3. Continued improvement in the US trade balance through greater domestic energy production. (4) The US\$10trn of unfunded positions leveraged with USD. Now that other currencies are signaling their easing stance more clearly, many of these leveraged positions could change their currency of funding (asking for € or ¥ loans and buying back the \$ to repay the loans).

The Known negatives for USD include:

1. The US president is a clear mercantilist, and mercantilists tend to dislike strong currencies. Trump's desire to relaunch manufacturing in the US cannot happen without a weaker dollar.
2. The US dollar is increasingly overvalued on a PPP against many currencies.
3. Almost everyone remains bullish on the US dollar.

Regards,

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