LOONIE DROPS AS PRESSURES RESTRICT A BREAKOUT

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CAD

The loonie struggled to hold on yesterday as it fell half a percentage point against the greenback. Most of the loonie weakness came at the back-end of the session, despite oil rising to recent highs above $26. Prior to the slide in the Canadian dollar, the loonie lagged most of the G10 as the US dollar broadly softened. With the market still sitting net short on CAD, as per CFTC net non-commercial futures positions, it is highly likely that yesterday's USDCAD move was sentiment driven as the pair drove back up to the midpoint of its recent range on little news flow. The only headlines of note out of Canada came from Prime Minister Justin Trudeau, who said Canada is following a cautious approach to reopening borders including the one with the US. Both Canada and the US agreed to close the border to non-essential travellers in March, and extended measures to May 20th back in April. As that deadline approaches, many believe a further extension is likely as other nations in Europe, where the timeline is advanced by a few weeks, also keep restricted border access. A note by JP Morgan economist Silvana Dimino yesterday saw the bank revise down its growth forecast for Canada, owing largely to the "slower and uneven easing of Covid-19 restrictions across the provinces, largely in Ontario and Quebec which account for more than 50% of GDP". The bank now expects Q2 GDP to show a 45% annualised contraction and 2020 growth to show a 9% contraction, which is a -2% reduction from their previous estimates. While this doesn't explain why the loonie sold off yesterday, it adds to the negative pressures weighing on the currency which are restricting it from breaking out of its recent trading range despite a softening US dollar and firming oil prices. There is little scheduled for the loonie prior to tomorrow's BoC Financial System Review (FSR) and the release of MArch's manufacturing sales data.

USD

The dollar lost some momentum yesterday after US inflation printed lower than expected and US President Trump supported the idea of negative interest rate policy. Negative rates remained a topic of interest for markets, with Fed officials continuing to weigh in on the issue. The Fed's Neel Kashkari stated he does not want to say "never" with regard to NIRP, but the Fed should focus on other tools first, while the Dallas Fed's Robert Kaplan said he was opposed to them. However, recent comments by Fed officials haven't stopped fixed income markets toying with the idea of pricing in negative rates over the one-year horizon. President Trump, on the other, said in a tweet that the Fed should implement the policy. April inflation data were released, with the headline consumer price index falling 0.8% on the month, highlighting the severity of the demand shock facing the US economy. Today markets will keep a close eye on Fed Chair Jerome Powell's online conference today at 14:00 BST on current economic issues. Any comments on negative rates, as well as on general further stimulus measures, will be closely watched. With US fixed income markets increasingly reflecting speculation that official rates may fall further, the topic will remain a matter of intense focus for FX.

EUR

The euro ripped over almost a percentage point higher against the dollar yesterday, while also strengthening against Sterling. This morning, the EURUSD pair was trading relatively flat ahead of a speech from Federal Reserve Chair Jerome Powell. Today's data has included eurozone industrial production figures, which showed an 11.3% contraction in March, broadly consistent with expectations. European Central Bank Chief Economist Philip Lane and Vice President Luis De Guindos will both speak in the afternoon today at 12:00 BST and 16:00 BST respectively. Comments on whether or not the ECB will accept the jurisdiction of the German Court ruling will be watched, especially as ECB President Christine Lagarde did not touch upon the topic in her webinar last week.

GBP

Sterling has managed to recover a small fraction of the losses seen yesterday and overnight, after Gross Domestic Product data for the first quarter printed slightly better than expected. GDP fell 5.8% in March, or 2% across the whole of the first quarter. Both figures printed better than expected " the median forecast submitted to Bloomberg for March was a 7.9% contraction, while GDP was expected to have fallen 2.6% across the whole quarter. Although better than expected, the figures are shocking nonetheless only 9 days of March were spent in full lockdown, suggesting that a full month in lockdown would create a GDP contraction in the order of 20%. Food stockpiling from consumers may have also boosted March retail sales. Worse declines are likely in the second quarter, although the focus for markets is likely to turn to the shape of the recovery, as well as the risk that lockdown measures will need to be re-imposed at some point. Last night the Telegraph reported that the Government was considering a policy package to prevent an unsustainable increase in the public debt due to coronavirus mitigation measures, including tax increases and spending cuts. The Treasury's central forecast from the document is reportedly a deficit of £337 billion, or roughly 17% of GDP and roughly double the peak deficit after the 2009 financial crisis.