



EUROPEAN CENTRAL BANK

EUROSYSTEM

Market review

FXCG, 9 February 2017

Disclaimer: The views expressed in this presentation are those of the author and do not necessarily represent those of the ECB or the Eurosystem.

Market review and outlook

- Market developments since last FXCG meeting
- Currency outlook and key risks ahead

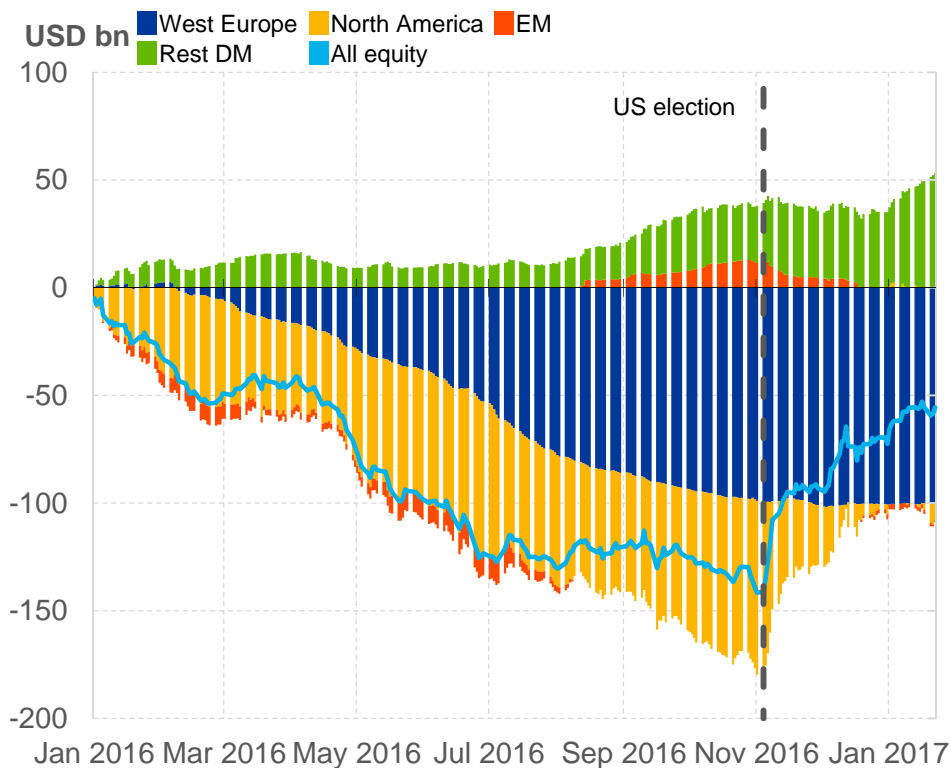
Lessons learnt

- US dollar funding at year end/quarter end

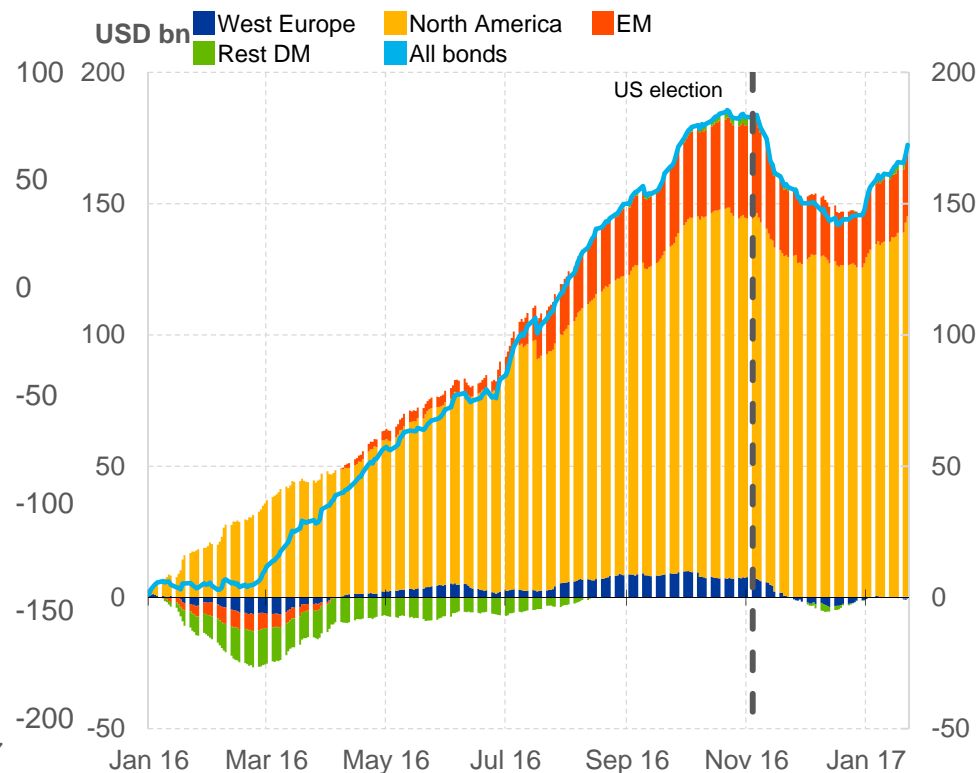
Global equity and bond fund flows

Substantial net inflows into US equity investment

Global equity fund flows



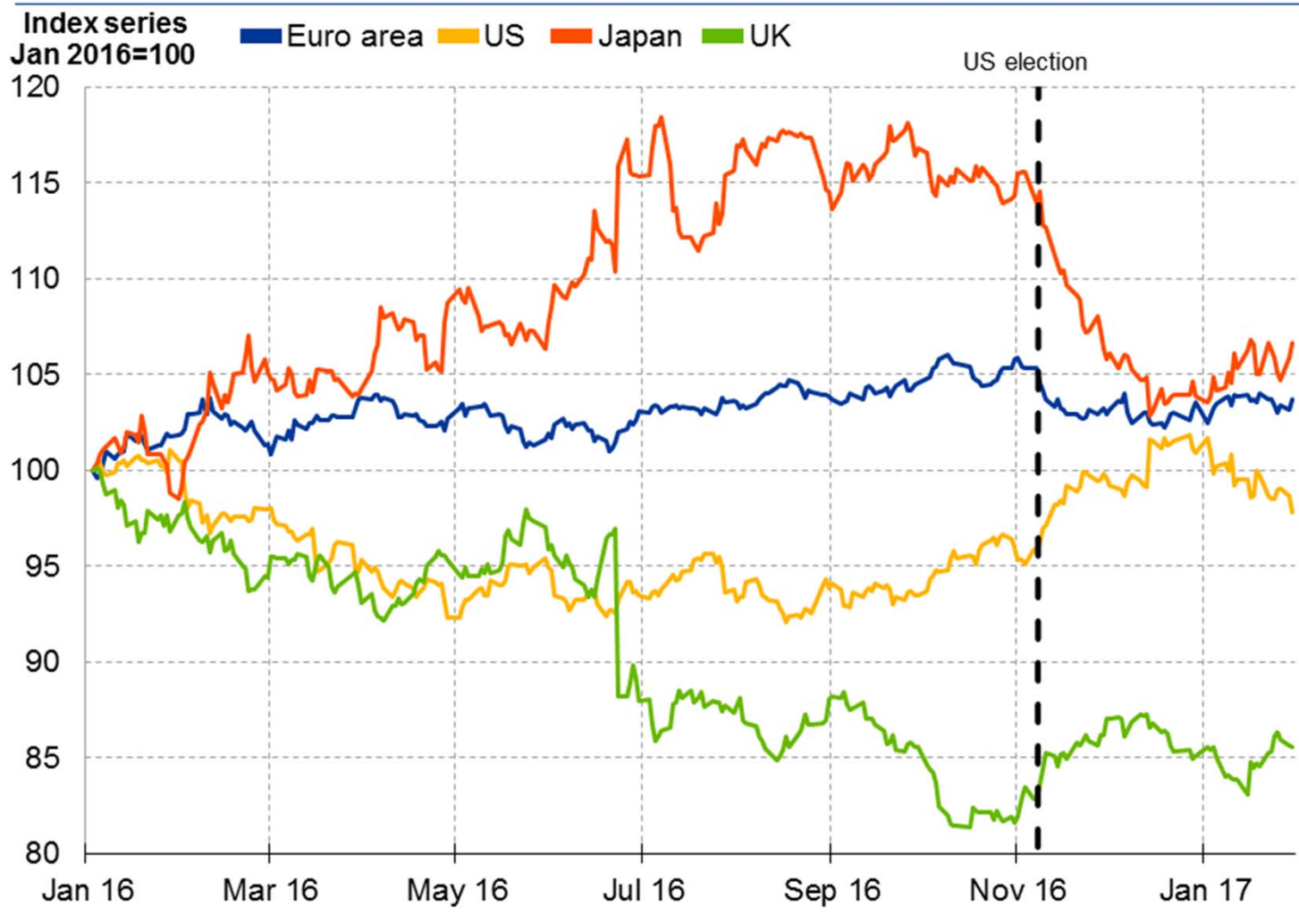
Global bond fund flows



Source: EPFR, ECB calculations

Effective exchange rates across major economies

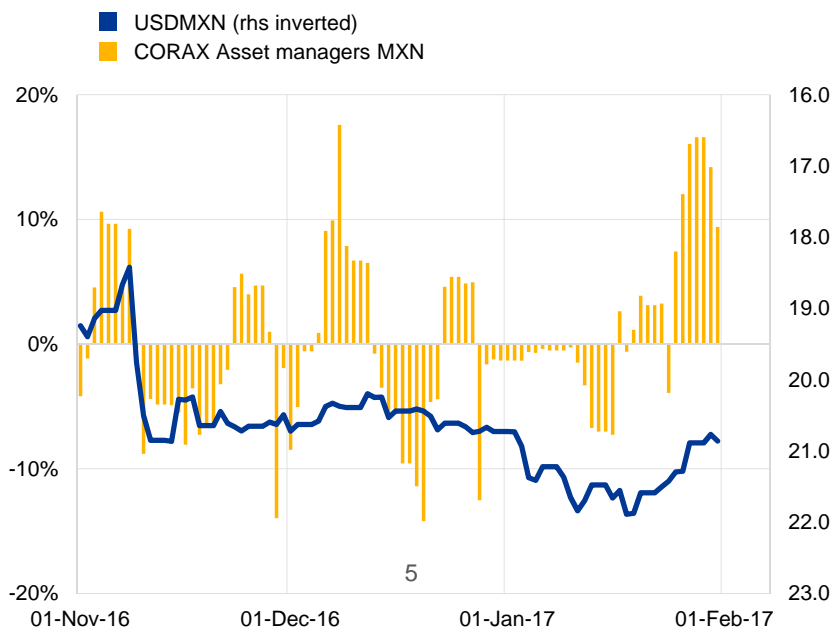
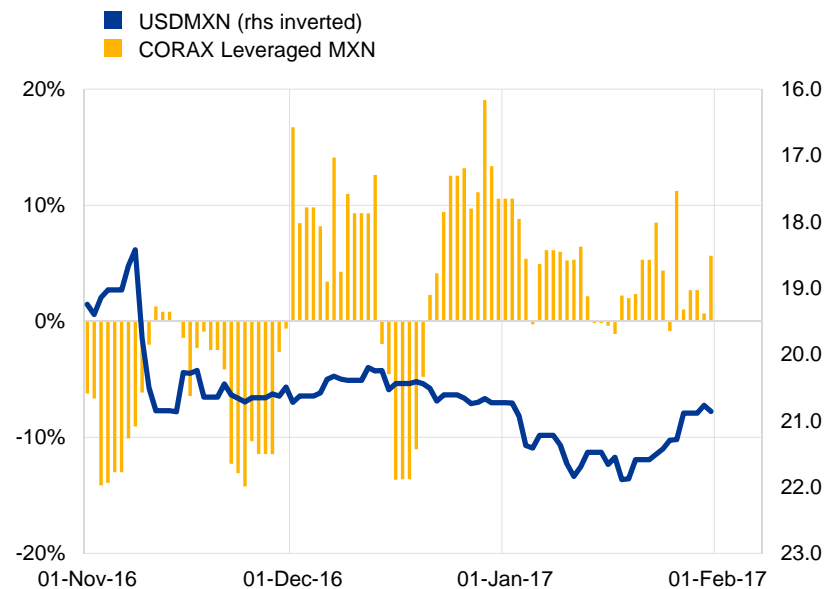
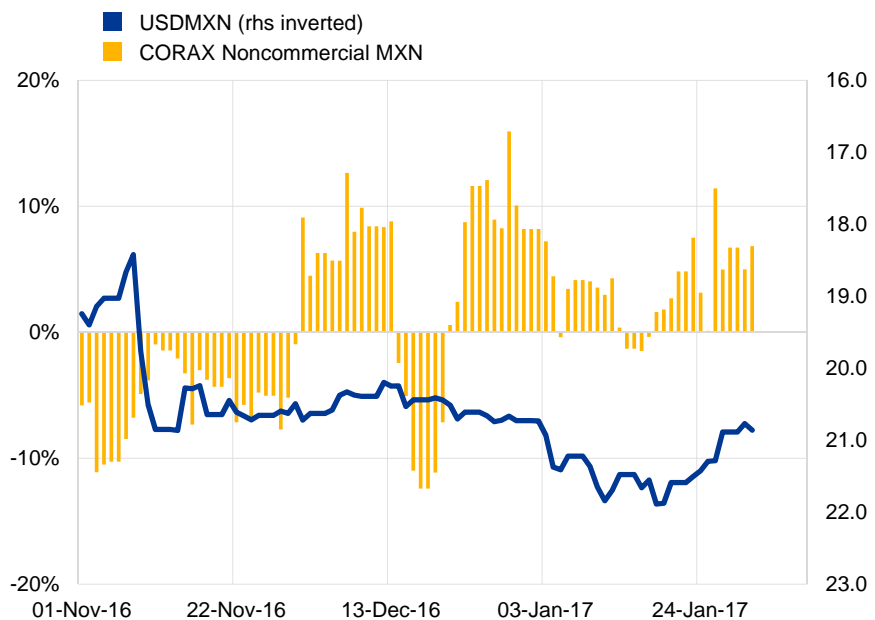
Effective exchange rates – indexed January 2016



Source: Bloomberg and Bank of England

Emerging market FX

Mexican peso one of the favourite shorts in EMFX

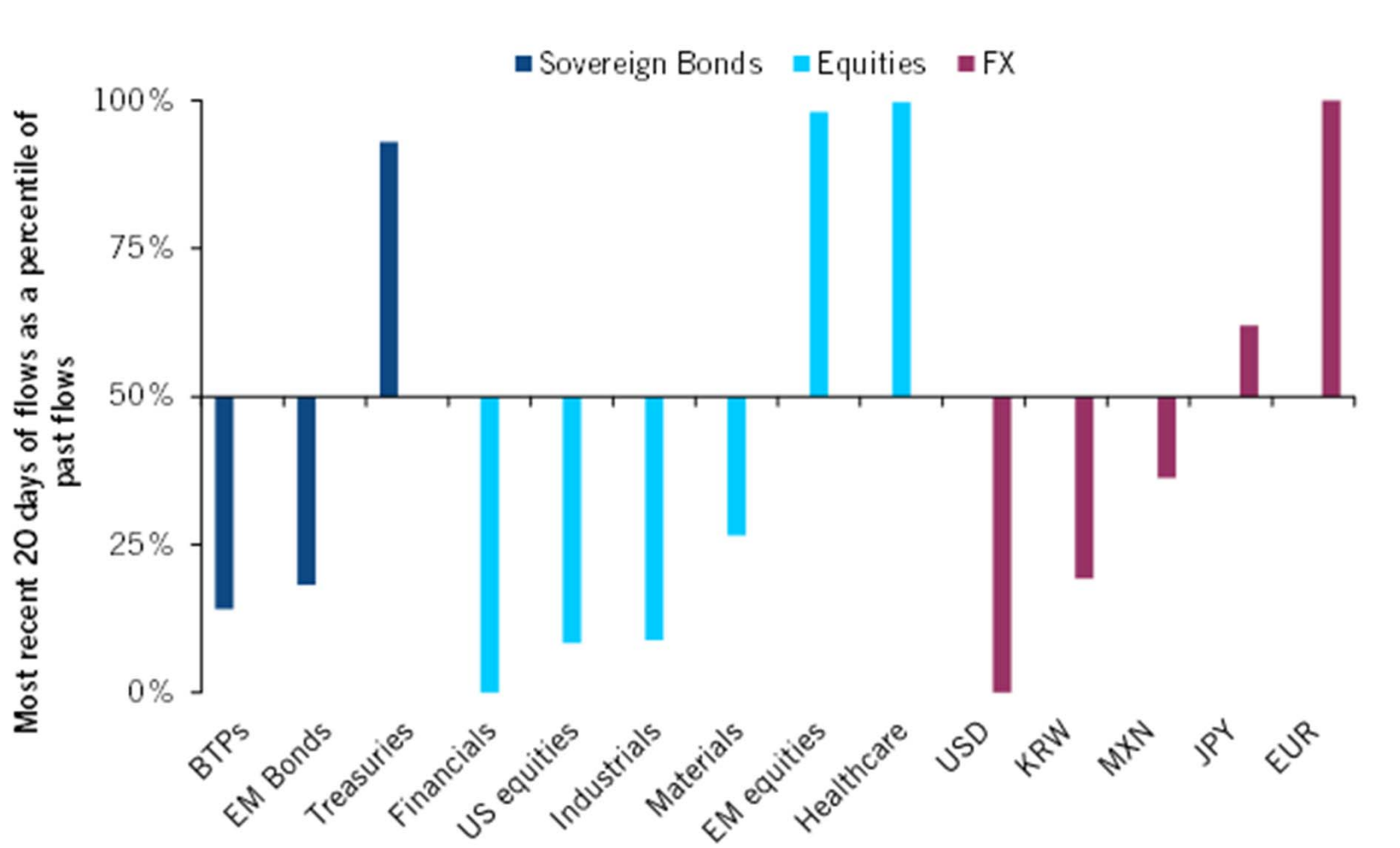


Source: Deutsche Bank

www.ecb.europa.eu

Flows across asset markets

Flows at the beginning of this year

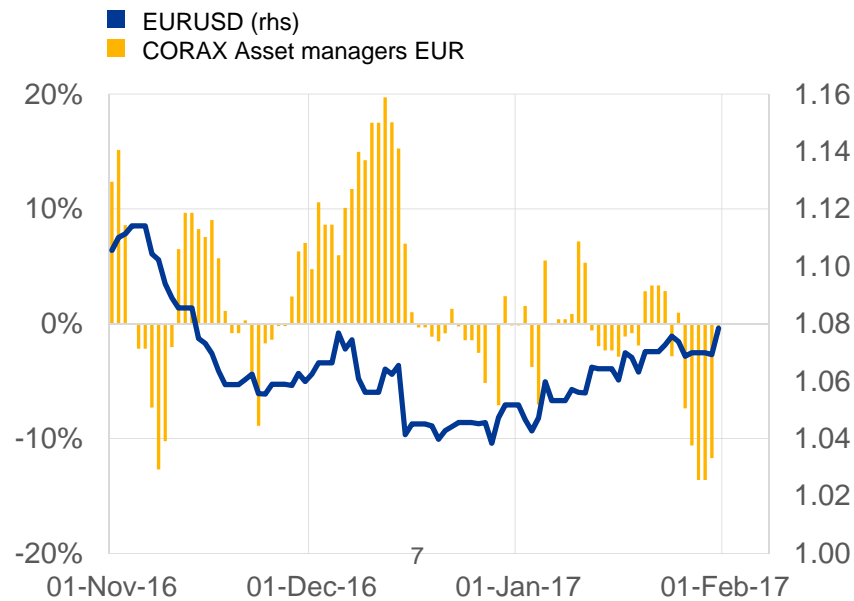
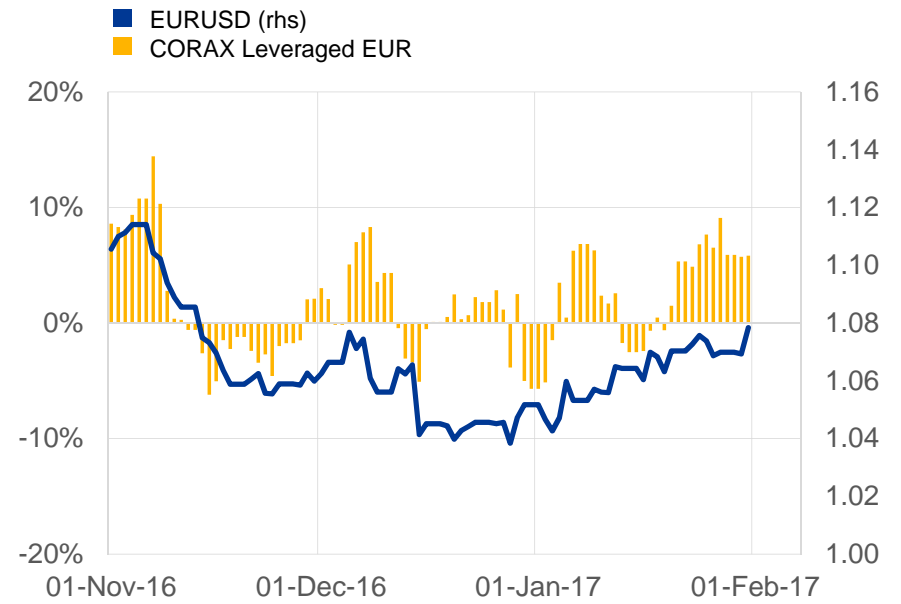
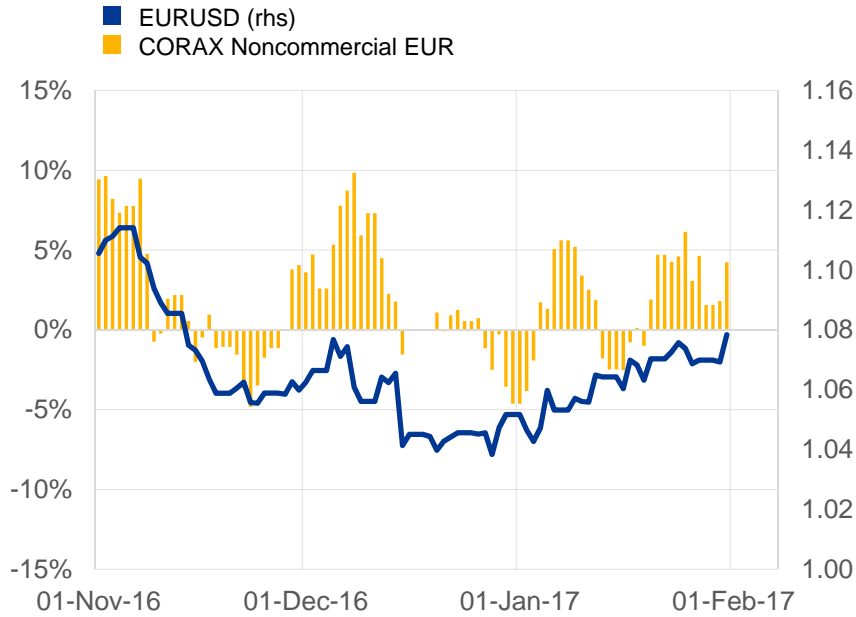


Source: State Street Global Markets, most recent 20 days of flows.

STATE STREET

Flows across asset markets

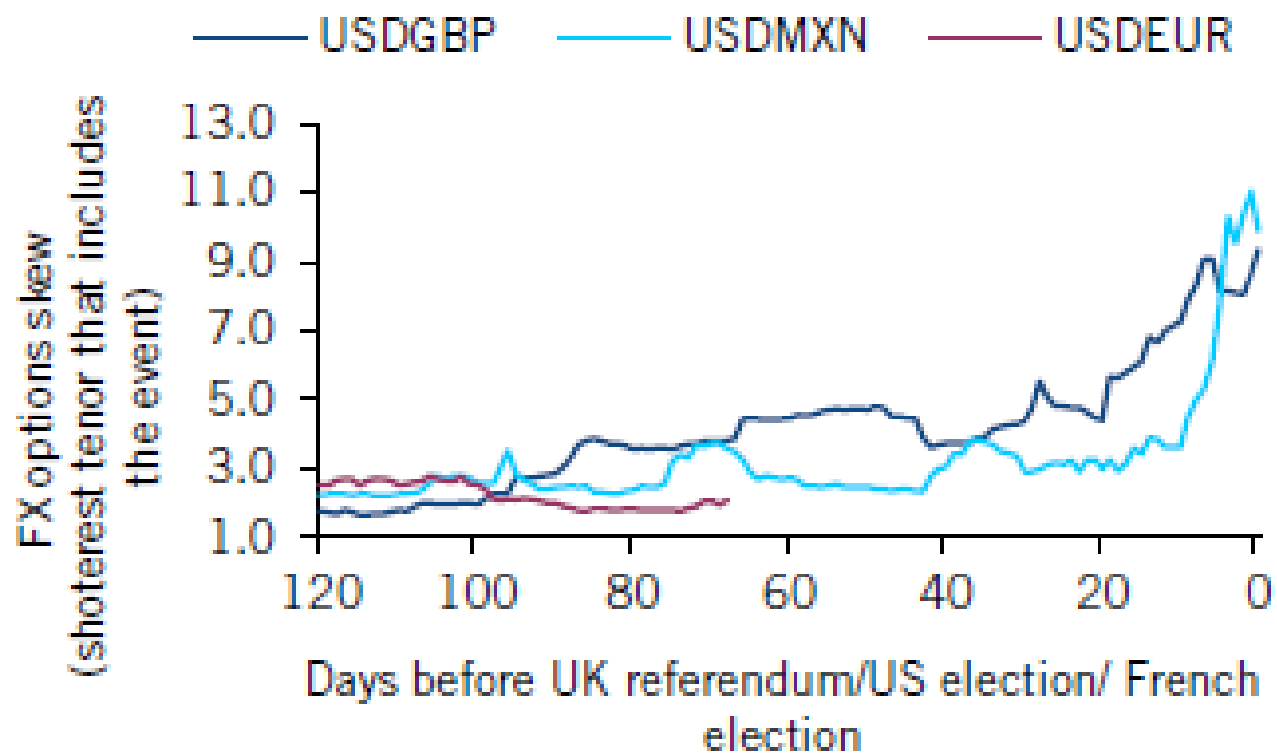
Overall investors have been net buyer of euro



Source: Deutsche Bank

Political events

FX options skew ahead of key votes



Source: State Street Global Markets, Bloomberg

STATE STREET

Discussion points

1. Could we see a global shift back from equities into bonds, which repercussion for the euro area? What would that mean for the FX market?
2. Has the risk rally discounted too much good news too soon?
3. Is the earlier consensus interpretation of the key macro trades still valid ?
 - a) Higher yields and a stronger US dollar?
 - b) What is the path forward for EM currencies?
4. Market focus going forward - Political, structural, cyclical drivers?
 - a) Event risks (French election, German election)?
 - b) Brexit ?
 - c) Central Bank policy meetings ?
5. How is the market positioned ? Which key indicators should be monitored?

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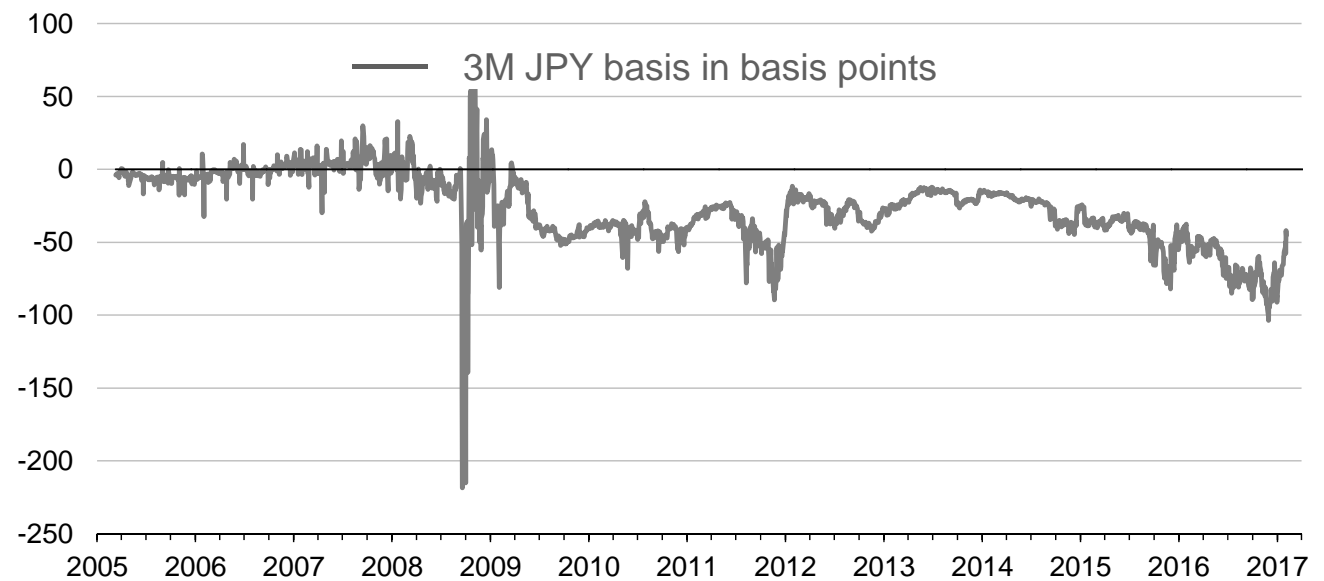
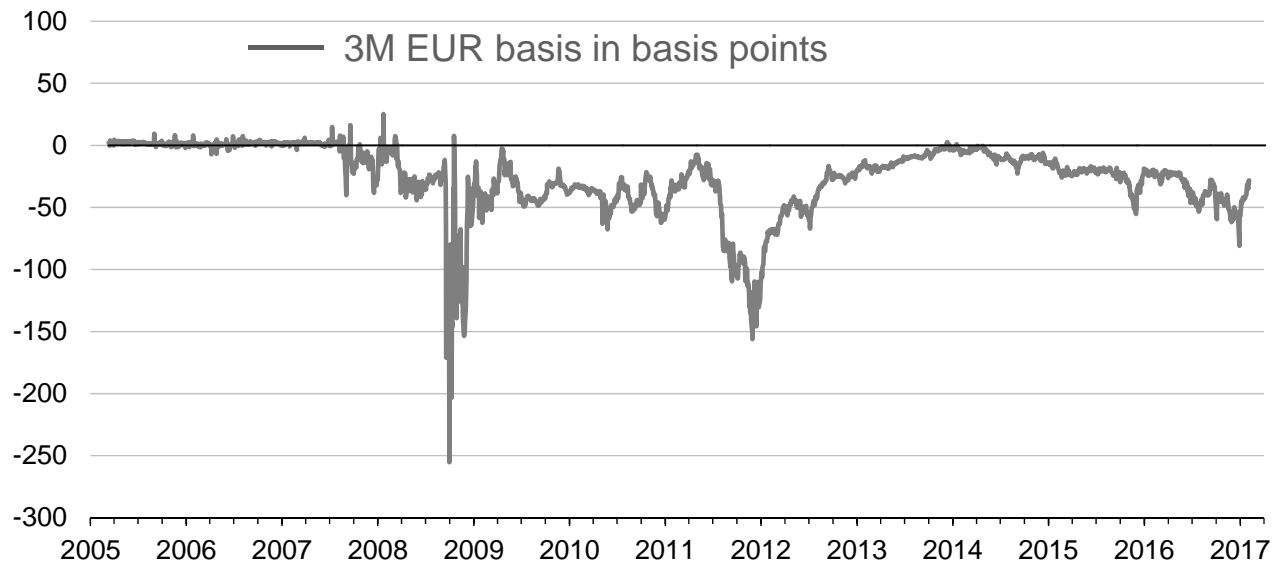
Lessons learnt

- US dollar funding at year end/quarter end

EUR and JPY cross-currency basis

Cross-currency basis: a puzzle

Why is it non-zero without a financial market crisis?

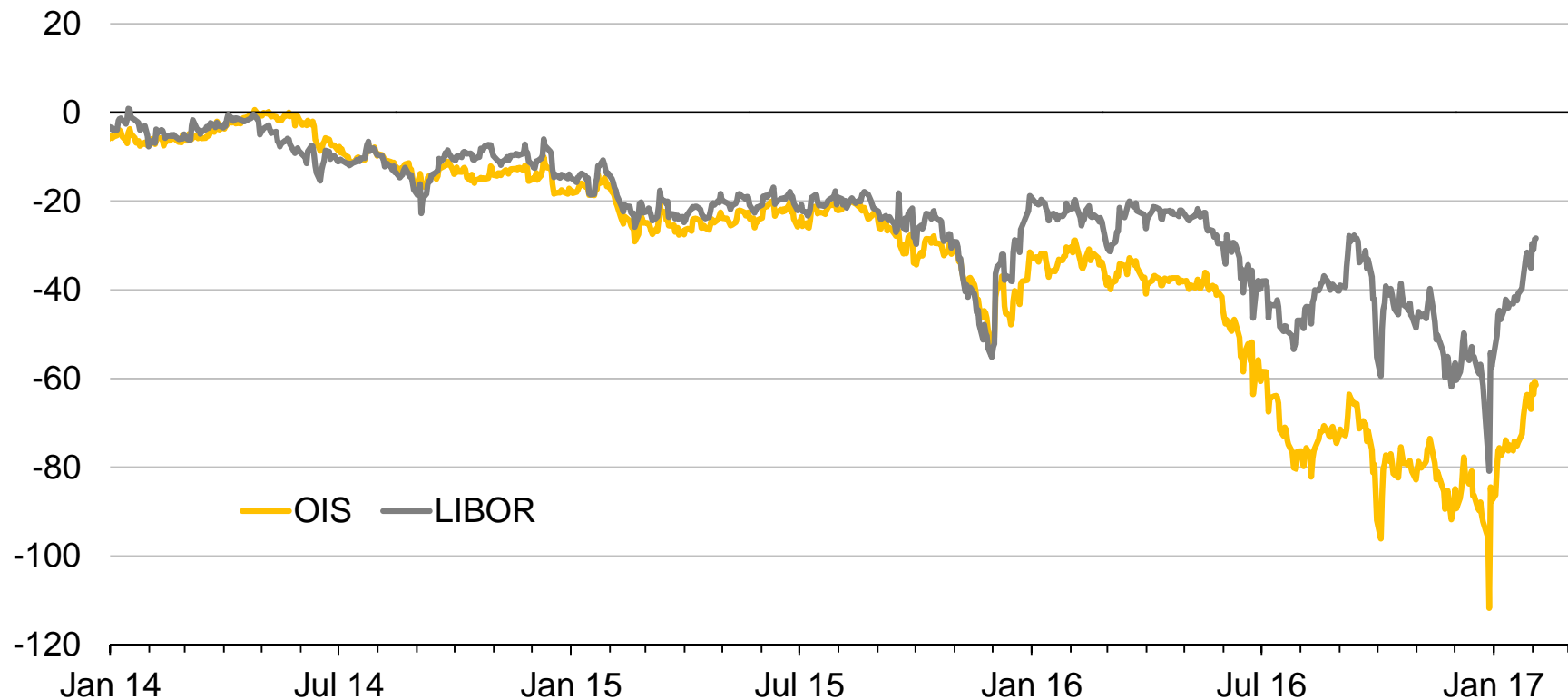


Sources: Bloomberg,
Commerzbank Research

The basis cannot be explained by counterparty risk OIS-based basis is even larger

3M EUR basis

Based on LIBOR and OIS rates; in basis points



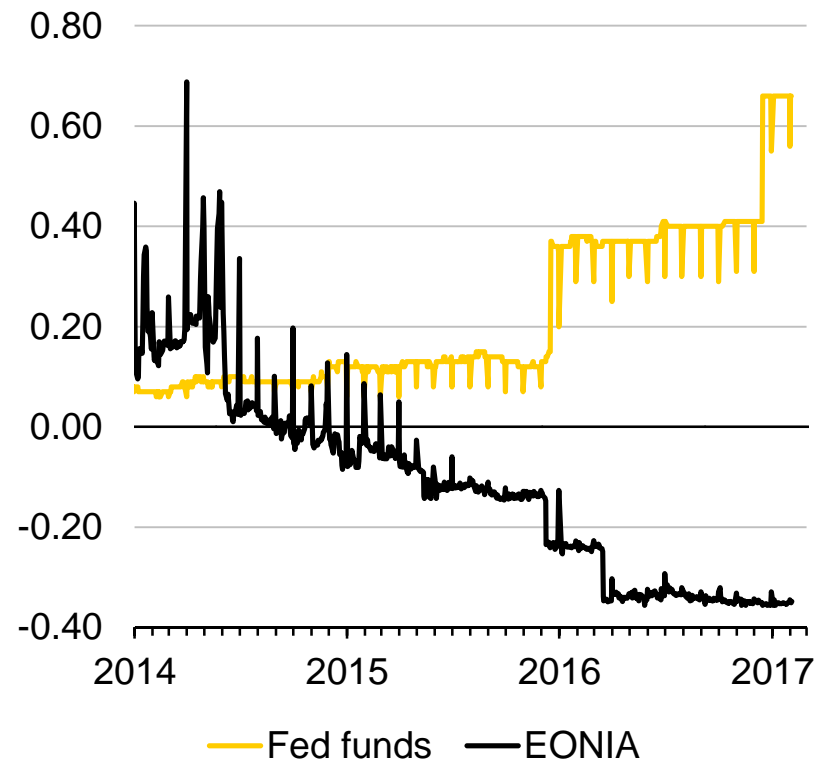
Sources: Bloomberg, Commerzbank Research

Dysfunctional money markets

Strong monthly seasonality

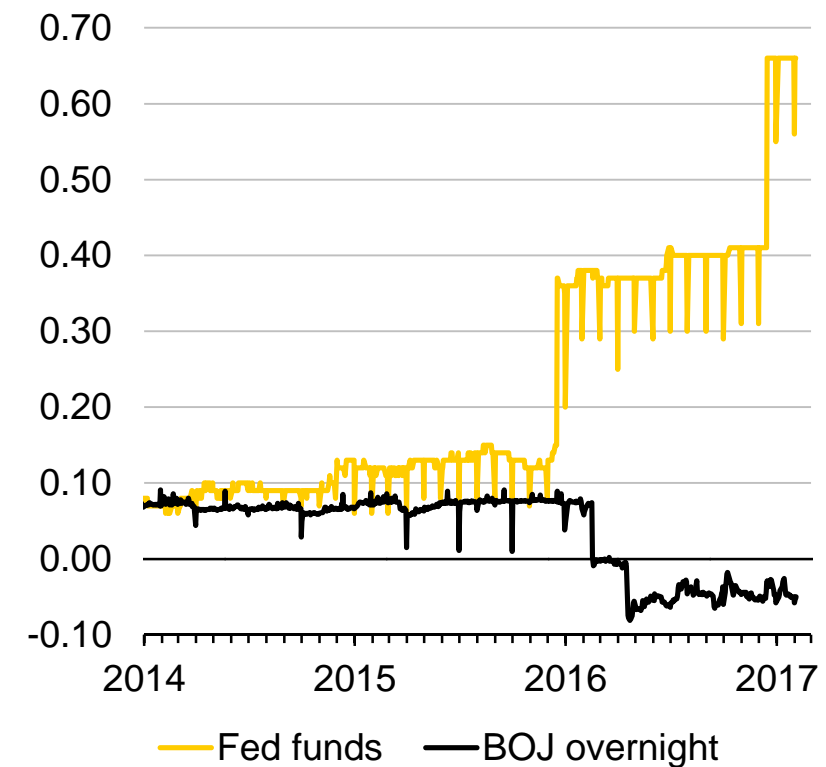
EONIA vs. Fed funds rate

Percent



BoJ overnight rate vs. Fed funds rate

Percent



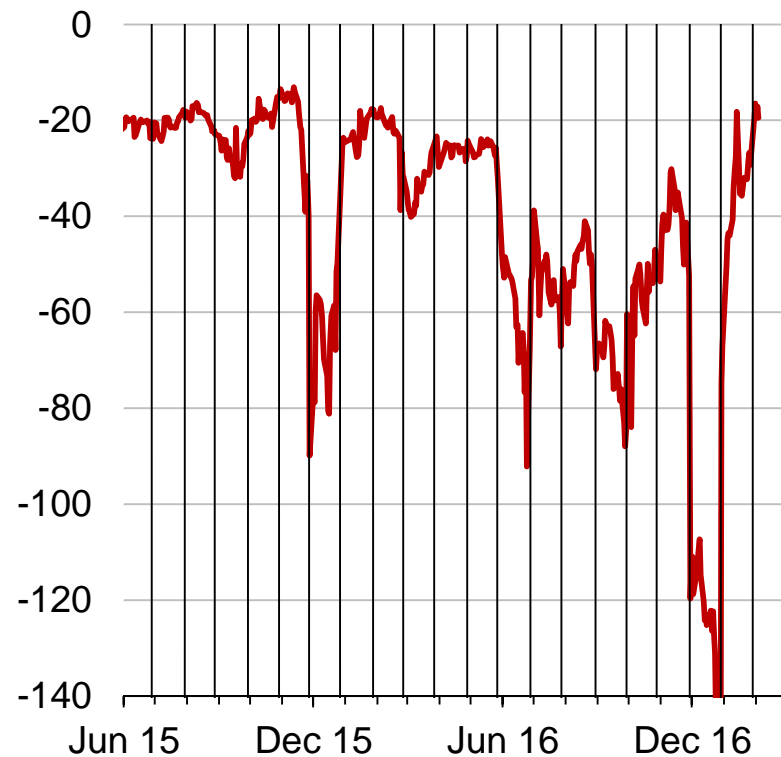
Sources: Bloomberg, Commerzbank Research

Dysfunctional FX forward markets

Strong monthly/quarterly seasonality

1M EUR basis

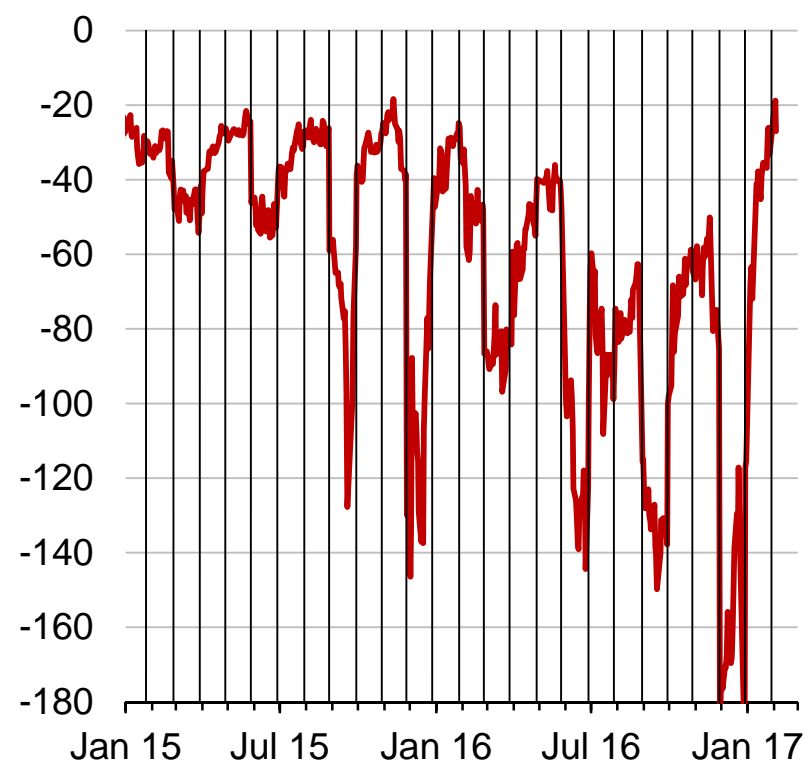
Basis points; vertical lines indicate month-change in settlement



Sources: Bloomberg, Commerzbank Research

1M JPY basis

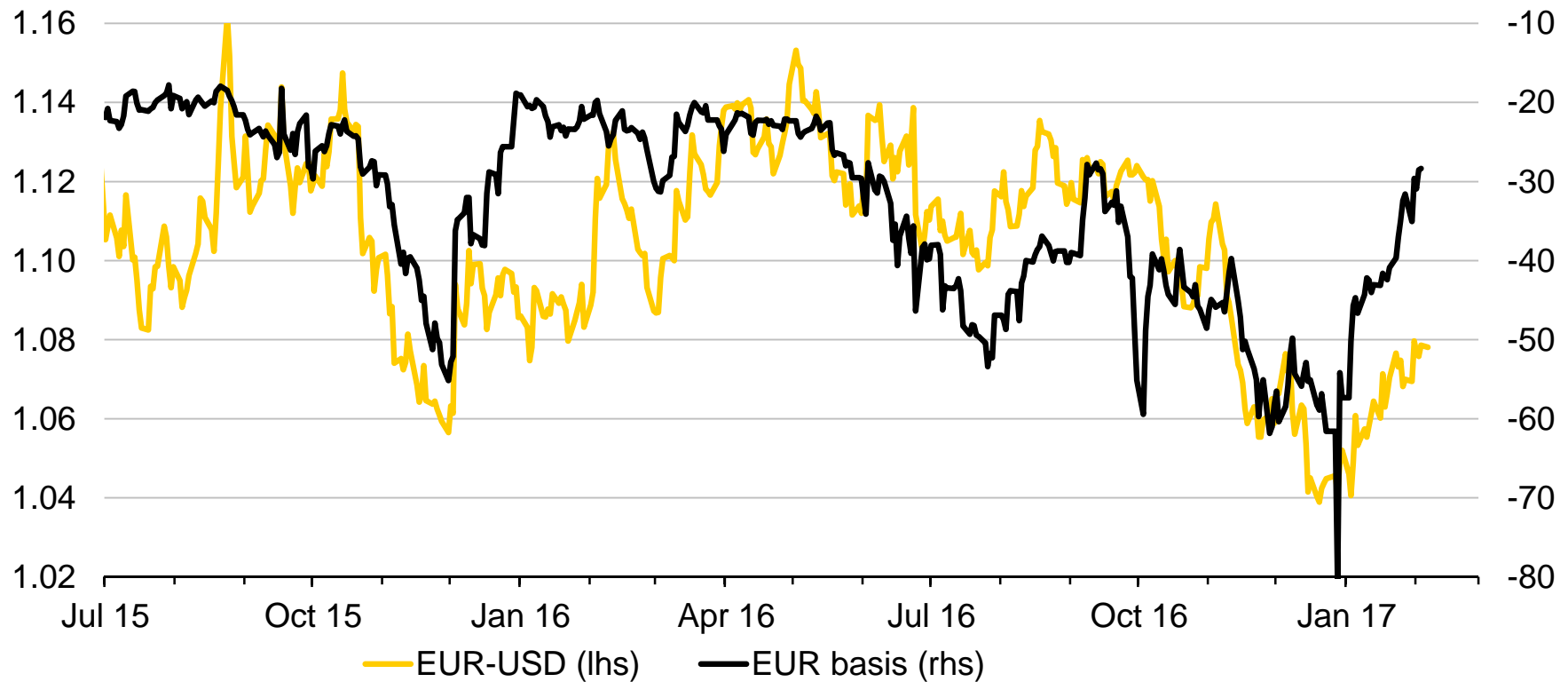
Basis points; vertical lines indicate month-change in settlement



Co-movement of EUR-USD and EUR basis

EUR-USD spot and 3M EUR basis

Basis in basis points



Sources: Bloomberg, Commerzbank Research

LIBOR-OIS spread (LOIS) Counterparty risk or dysfunctionality indicator?

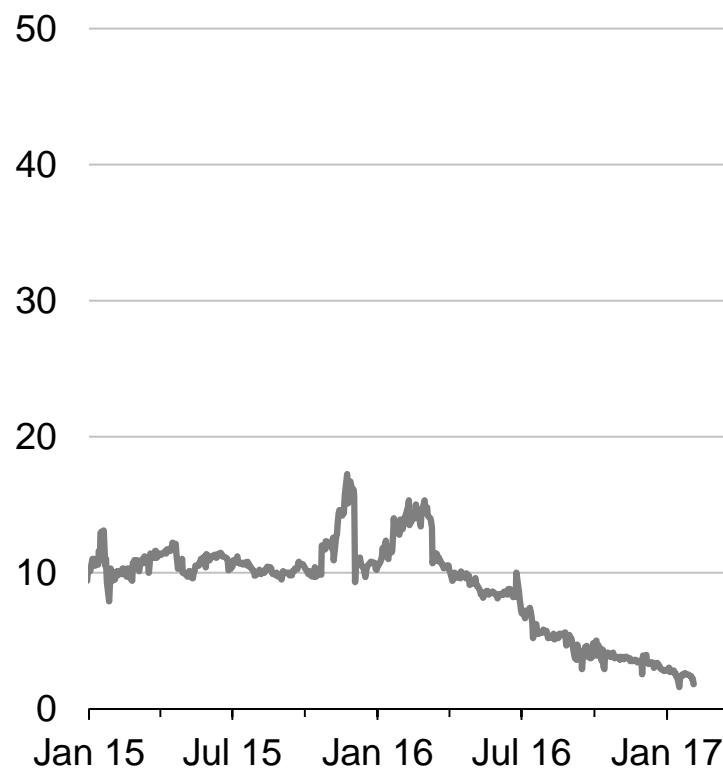
USD 3M LOIS

Basis points



EUR 3M LOIS

Basis points



Sources: Bloomberg, Commerzbank Research

Discussion points

- What are the lessons learnt?