A Modest Dollar Dump

After the Fed all but assured the market that a rate cut is coming at the end of the month, the Street will be hard pressed to find too many USD bulls.

Today's chart plots 34 currencies' returns against USD over the past five days versus their market beta on July 9, the day before Fed Chair Powell faced the House Financial Services Committee. (In this case, beta is defined as the standard deviation of each currency's daily returns for the past 60 days versus the same measure for DXY).

It's rare to get such a neat and tidy fit when comparing beta to returns. But so far, the riskier the cross is versus the dollar, the higher its return generally has been. This is strongly indicative of an indiscriminant shedding of USD positions in anticipation of an easing cycle.

We note, however, that despite this widespread risk appetite in currency markets, overall dollar weakness has been pretty restrained so far. At current levels, DXY is still higher than it's been for most of the past 12 months, and we wonder if rate cuts - nearly fully priced in since the end of May - will trigger an outright bear market in the dollar.

We expect other central banks to follow the Fed's dovish lead, and we remind readers that the reason the Fed has signaled a rate cut is coming is, in large part, due to a bleak global growth outlook, an environment which should impact the fundamentals of the some of the recent FX outperformers.

For now, however, the clear relationship between beta and spot returns portray a dollar that is truly on the back foot.
USD Crosses and Currency Beta

FX Returns vs FX beta since July 9th

SOURCE: BNY Mellon Markets, Bloomberg, data for 15 July 2019

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