

Euro (EUR)

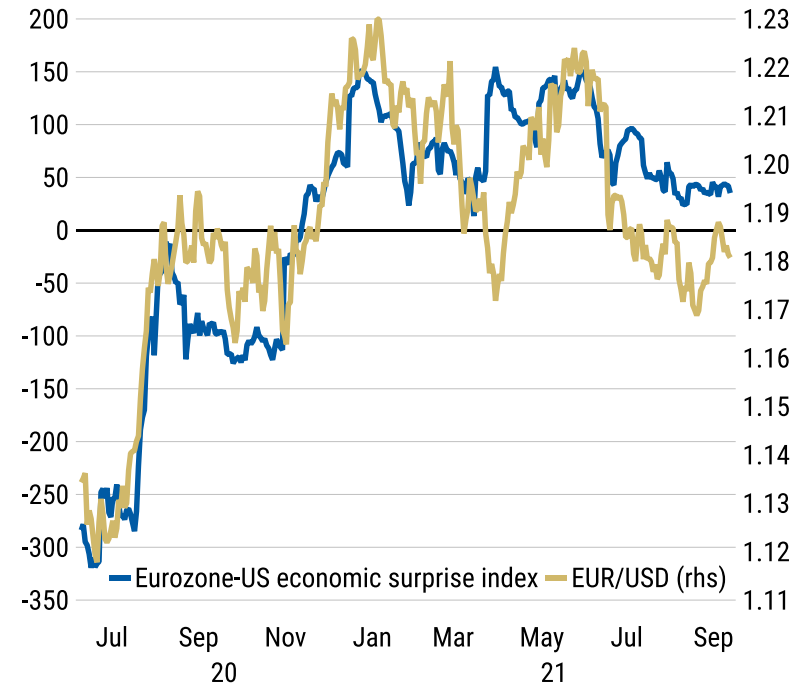
EUR | Staying Bearish Post-ECB

Higher US real rates relative to Europe - on policy and growth divergences - should push EUR/USD lower as the ECB's reaction function remains asymmetrically dovish

Dovish ECB versus hawkish Fed should weigh on EUR/USD via real yield differentials



Moderating eurozone growth and improving US data would be EUR-negative

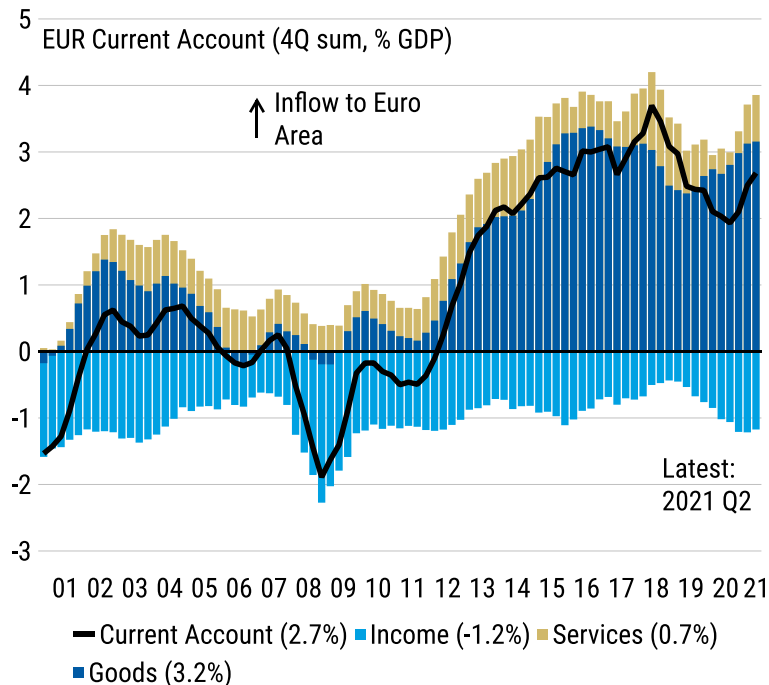


Source: Macrobond, Bloomberg, Morgan Stanley Research

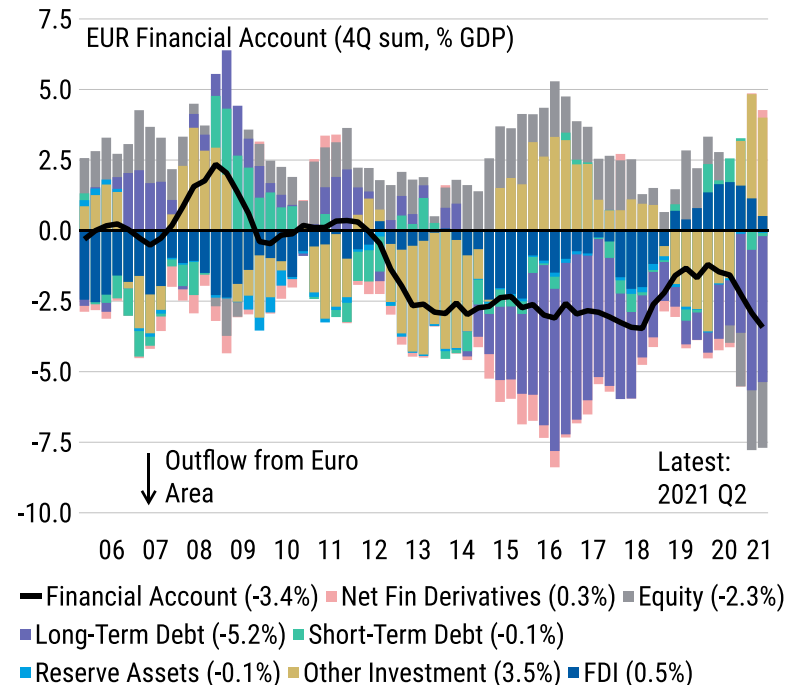
EUR | Current and Financial Accounts

The eurozone's current account surplus rose to 2.7% of GDP in 2Q21 as the goods and services surplus increased. Outflows into foreign long-term debt remain

Current account breakdown



Financial account breakdown

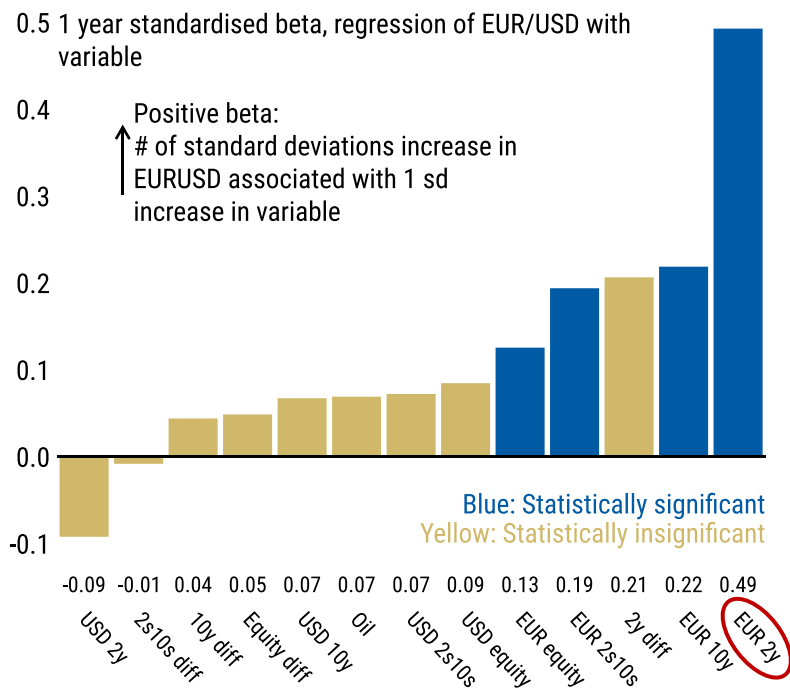


Source: Macrobond, Morgan Stanley Research

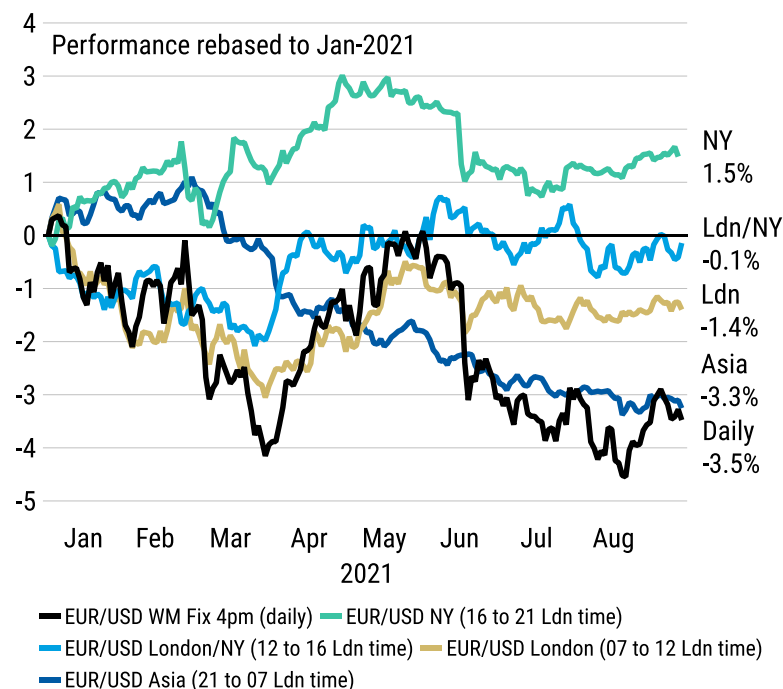
EUR | Betas and Time Zone Performance

Short-term yields are the most significant driver of EUR/USD. The divergence in the ECB and Fed reaction functions should help EUR/USD weaken

Sensitivity of EUR/USD to different market variables



EUR/USD performance across time zones

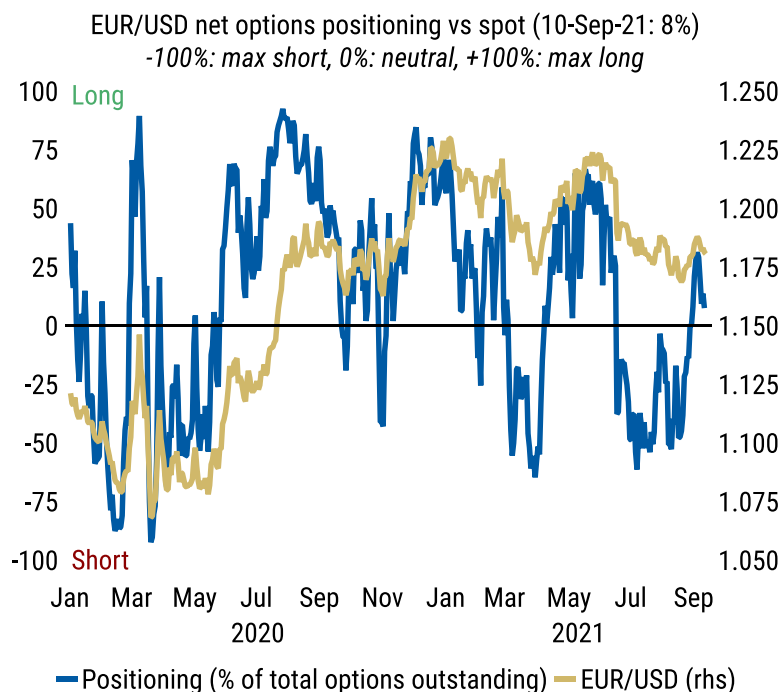


Source: Macrobond, Bloomberg, Morgan Stanley Research

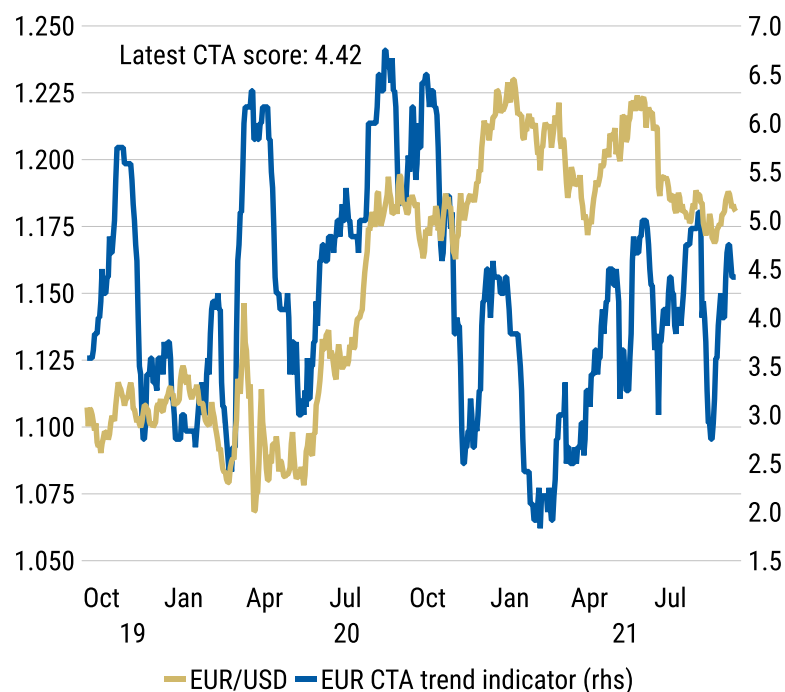
EUR | Market Positioning and Sentiment

Short-term positioning is neutral EUR while asset managers remain most long EUR in the futures market. Our EUR/G10 momentum CTA indicator is at neutral levels

Options positioning



CTA trend indicator



Source: DTCC, Macrobond, Bloomberg, Morgan Stanley Research

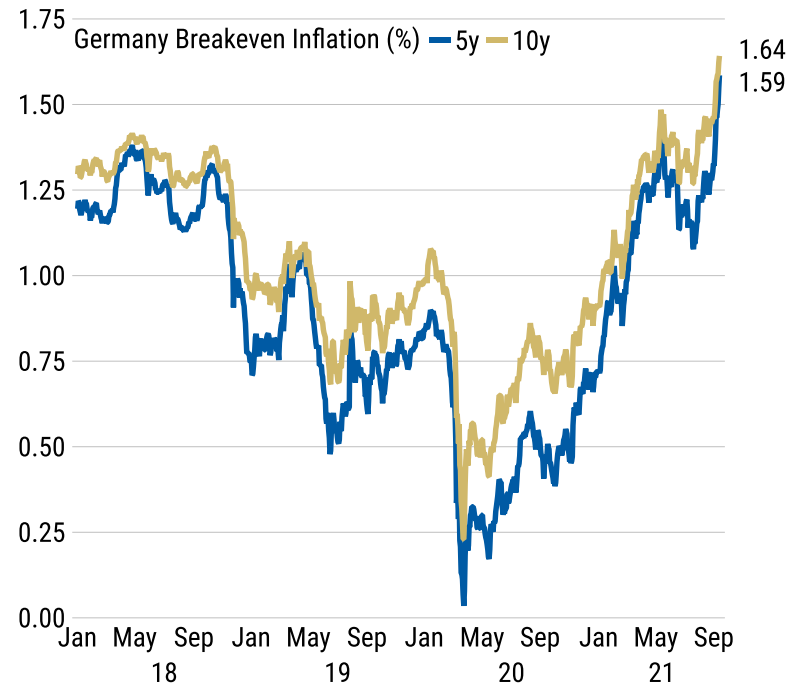
EUR | Rates Market Backdrop

Rising European breakeven rates have driven the US-Europe real rate decoupling since early August. Diverging growth expectations should help drive the second leg

Real yields



Breakeven inflation rates

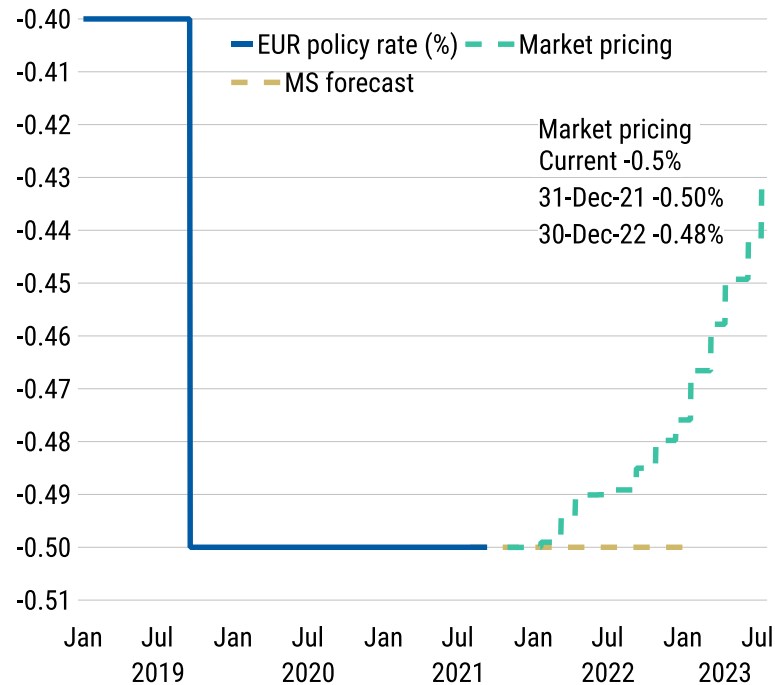


Source: Macrobond, Bloomberg, Morgan Stanley Research

EUR | Monetary Policy

Market timing of the first ECB rate hike remains years away in mid-2025 despite the ECB's decision to moderately slow its PEPP purchase pace

Policy rate



Months to first rate hike

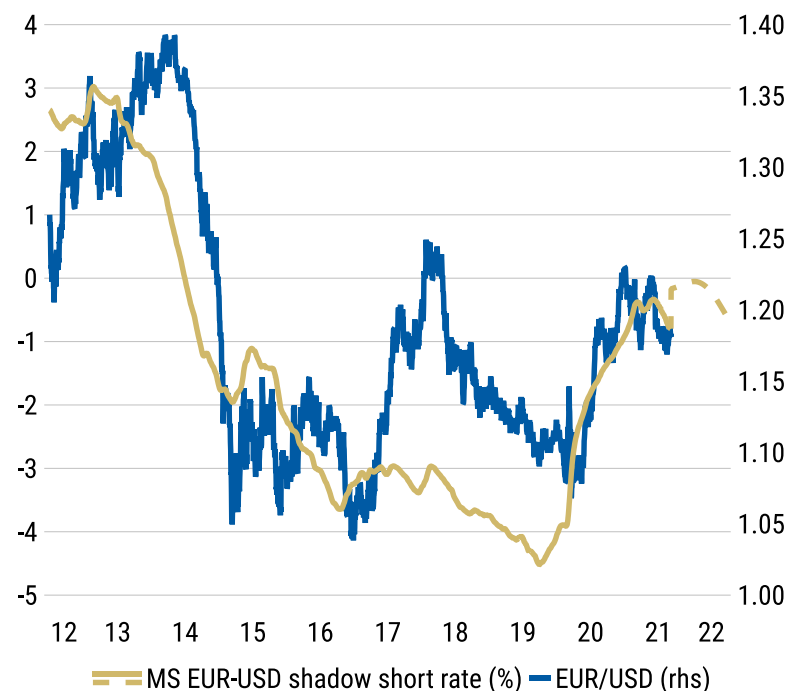


Source: MS STIRT Desk, Macrobond, Bloomberg, Morgan Stanley Research forecasts

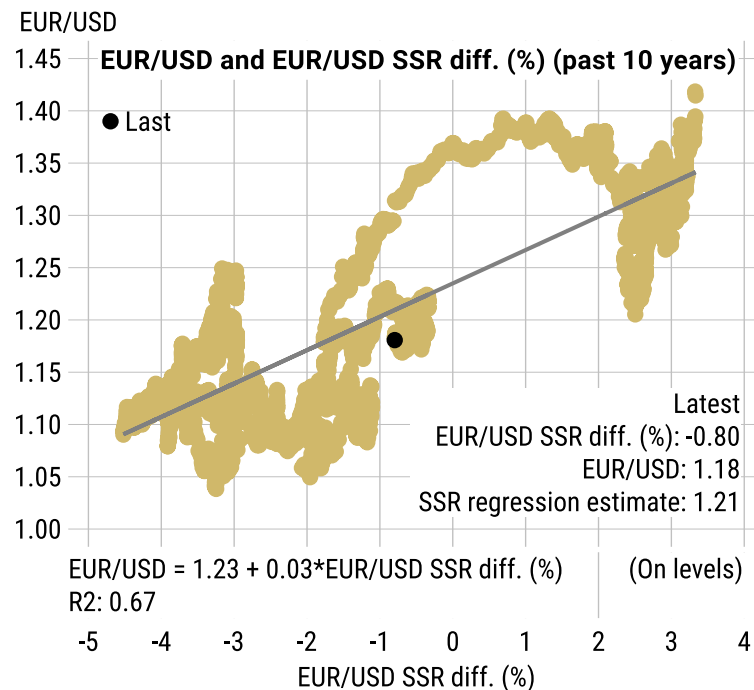
EUR | Shadow Short Rate

EUR/USD is trading marginally below what current shadow short rate differentials would suggest (1.21)

SSR differential vs. spot history



SSR differential vs. spot regression



Source: Macrobond, Bloomberg, Morgan Stanley Research
 Note: Dashed lines represent Morgan Stanley Research forecasts