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AUD Rally Looks Set To Continue As Markets Eye Latest Jobs Report

AUD risk is elevated as we head into the upcoming jobs report, scheduled for 9:30pm ET. Expectations are low, offering a balance of risk that opens up the potential for greater upside and a possible extension of the near-4% month-to-date rally. The AUD's pro-risk profile has allowed for meaningful sentiment-driven gains over the past few weeks as markets have begun to move away from a definitively defensive posture, fading conflict-related fear in order to participate in the move toward a resolution.

The medium-term chart reveals a clear bullish trend off of last April's panic washout low that delivered a short-lived break under 0.60. The subsequent recovery has been impressive, reaching a fresh multi-year high above 0.70 in late January with renewed strength that opens up the potential for a push to new highs on the way to 0.72. The longer-term chart frames out a clear bullish retracement of the 2021-2025 decline, and offers major technical levels around 0.72 (61.8% retracement), 0.75 (76.4% retracement), and 0.80 (full retracement).

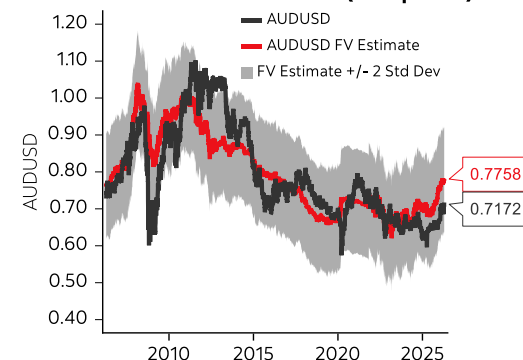
In terms of drivers, the majority of recent AUD movement has been—and continues to be—driven by sentiment. The fade in conflict-related fear is important and still leaves ample for sentiment-driven upside. The shift in the broader market's tone will also allow for a realignment between spot AUD and estimates of its fundamental fair value.

Estimates of AUDUSD's fair value based on 2Y yield spreads between the Australia and the US offer levels closer to the mid-0.77s. The AUD has shown periods of historical deviation from its fair value estimate and appears able to maintain a sizeable differential at certain extremes. The narrowing of the differential is equally important, offering the potential for a complete elimination and shift to the alternative side.

In the current instance, the AUD is still trading below its FV estimate despite notable gains in both spot exchange rates and yield spreads. We see scope for medium-term gains toward the FV estimate in the mid-0.77s but also feel it important to highlight the possibility of an extension to levels well into the upper end of the band around the range.

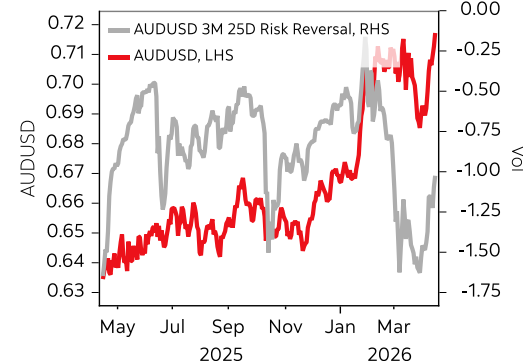
We are bullish above 0.72 and see high risk of a swift rally to the next target at 0.75.

AUDUSD vs. FV Estimate (2Y Spread)



Source: Macrobond, Scotiabank FICC Strategy

AUDUSD vs. 3M 25D Risk Reversal



Source: Macrobond, Scotiabank FICC Strategy

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