

EUR: Not much the ECB can do

It has been hard for President Draghi to talk down the EUR when its strength is driven by a solid domestic economy and the soft USD. Even at 1.25, EUR/USD is not out of sync with the short-term fundamentals. We target EUR/USD 1.30 this year. CEE FX remains in the sweet-spot.



EUR/USD broke above the 1.2500 level for the first time since December 2014 as the market looked through ECB's President Draghi's attempts to calm strong EUR expectations either via referring to the currency's "volatility creating uncertainty" or seeing "very few chances at all for a rate increase this year." See also [ECB Review](#).

Volatility is not strength

On the former, while clearly pointing at the recent EUR moves, we note that in terms of wording, referring to "volatility" is different and, in a sense, less interventionist than talking about euro "strength" or "abrupt" moves. While the headline news has recently been on the EUR/USD cross (and its appreciation) we note that the trade-weighted EUR materially lagged the EUR/USD strength (Fig 1) this year. This is because a non-negligible part of the EUR/USD upside was caused by the recent across-the-board USD weakness generated by the US administration comments (as is evident in Fig 1, the trade weighted EUR has actually been flat over the past days; or as per Fig 2 which shows EUR as an average G10 FX performer so far this year).



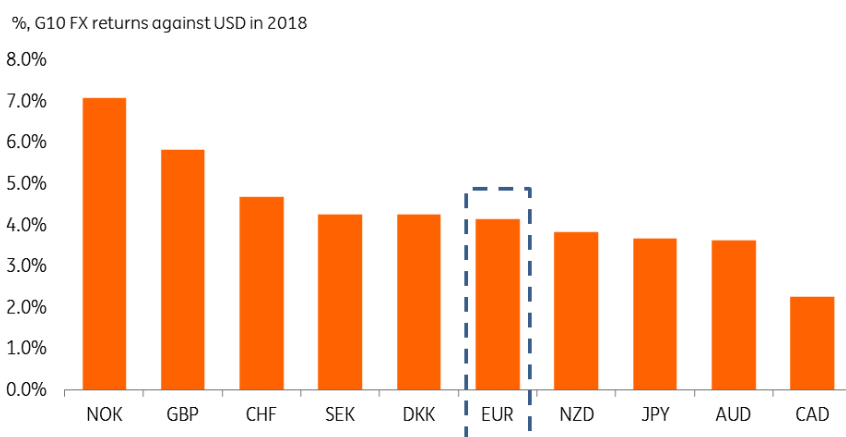
Source: ING, Bloomberg

It is not only about getting carried away by the ECB

Indeed, the above was (indirectly) cited by President Draghi as one of the three causes behind EUR strength:

1. Unquestionable improvement in the EZ economy
2. Heightened market sensitivity to perceived changes in the ECB communication
3. Dollar weakness (suggested implicitly, not explicitly) – as per above

However, so long as the ECB acknowledges that a non-negligible part of the EUR/USD strength is driven by weak USD as well as the very clear improvement in the Eurozone economy, the bar for the ECB to talk down the euro is high.



Source: ING, Bloomberg

EUR/USD still not overshooting

Note that based on our short-term financial fair value model, the EUR/USD is now fairly valued (on a short-term basis), even at around the 1.25 level. We thus don't see the current level as unsustainable or out of sync with short-term fundamentals. On a long-term basis, we reiterate OECD PPP EUR/USD fair value of 1.33.

No ECB rate hikes this year, but eventually helping the EUR in 2H18

We agree with Draghi's assessment on the deposit rate hikes. As per his comments, we don't look

for the ECB to start normalising the deposit rates this year. However, we still continue to see expectations of the eventual deposit rate normalisation as an important driver for EUR/USD in the second half of this year once forward-looking market participants start to meaningfully price in deposit rate hikes for 2019.

We also note that the market is currently pricing around 5bp of ECB deposit rate hikes for this year. This is not aggressive and in turn reduces downside risks to the EUR from the eventual dovish re-pricing of the 2018 ECB deposit rate outlook (i.e. from 5bp to 0bp). We reiterate our long-held target of EUR/USD 1.30 by the year end (see [EUR: Embrace the strong euro](#) from the [2018 FX Outlook](#)).

CEE FX: The EUR/USD on steroids

By extension, the CEE FX has been benefiting from the EUR/USD rally. All PLN, CZK and HUF have been up by around 5% against USD so far this year. All three currencies are among the top seven EM FX performers, only surpassed by the previously battered currencies (likes of ZAR and MXN) or the commodity currencies such as COP.

This is in line with our view that 2018 will remain the sweet-spot for the CEE FX (as was the case the last year) and this currency segment should do well this year, benefiting from our view of EUR/USD reaching 1.30, as well as their solid domestic fundamentals, thus transforming into the EUR/USD on steroids.

Author

Alissa Lefebvre

Economist

alissa.lefebvre@ing.com

Deepali Bhargava

Regional Head of Research, Asia-Pacific

Deepali.Bhargava@ing.com

Ruben Dewitte

Economist

+32495364780

ruben.dewitte@ing.com

Kinga Havasi

Economic research trainee

kinga.havasi@ing.com

Marten van Garderen

Consumer Economist, Netherlands

marten.van.garderen@ing.com

David Havrlant

Chief Economist, Czech Republic

420 770 321 486

david.havrlant@ing.com

Sander Burgers

Senior Economist, Dutch Housing

sander.burgers@ing.com

Lynn Song

Chief Economist, Greater China

lynn.song@asia.ing.com

Michiel Tukker

Senior European Rates Strategist

michiel.tukker@ing.com

Michal Rubaszek

Senior Economist, Poland

michal.rubaszek@ing.pl

This is a test author

Stefan Posea

Economist, Romania

tiberiu-stefan.posea@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Jesse Norcross

Senior Sector Strategist, Real Estate

jesse.norcross@ing.com

Teise Stellema

Research Assistant, Energy Transition

teise.stellema@ing.com

Diederik Stadig

Sector Economist, TMT & Healthcare

diederik.stadig@ing.com

Diogo Gouveia

Sector Economist

diogo.duarte.vieira.de.gouveia@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Ewa Manthey

Commodities Strategist

ewa.manthey@ing.com

ING Analysts

James Wilson

EM Sovereign Strategist

James.wilson@ing.com

Sophie Smith

Digital Editor

sophie.smith@ing.com

Frantisek Taborsky

EMEA FX & FI Strategist

frantisek.taborsky@ing.com

Adam Antoniak

Senior Economist, Poland

adam.antoniak@ing.pl

Min Joo Kang

Senior Economist, South Korea and Japan

min.joo.kang@asia.ing.com

Coco Zhang

ESG Research

coco.zhang@ing.com

Jan Frederik Slijkerman

Senior Sector Strategist, TMT

jan.frederik.slijkerman@ing.com

Katinka Jongkind

Senior Economist, Services and Leisure

Katinka.Jongkind@ing.com

Marina Le Blanc

Sector Strategist, Financials

Marina.Le.Blanc@ing.com

Samuel Abettan

Junior Economist

samuel.abettan@ing.com

Franziska Biehl

Senior Economist, Germany
Franziska.Marie.Biehl@ing.de

Rebecca Byrne
Senior Editor and Supervisory Analyst
rebecca.byrne@ing.com

Mirjam Bani
Sector Economist, Commercial Real Estate & Public Sector (Netherlands)
mirjam.bani@ing.com

Timothy Rahill
Credit Strategist
timothy.rahill@ing.com

Leszek Kasek
Senior Economist, Poland
leszek.kasek@ing.pl

Oleksiy Soroka, CFA
Senior High Yield Credit Strategist
oleksiy.soroka@ing.com

Antoine Bouvet
Head of European Rates Strategy
antoine.bouvet@ing.com

Jeroen van den Broek
Global Head of Sector Research
jeroen.van.den.broek@ing.com

Edse Dantuma
Senior Sector Economist, Industry and Healthcare
edse.dantuma@ing.com

Francesco Pesole
FX Strategist
francesco.pesole@ing.com

Rico Luman
Senior Sector Economist, Transport and Logistics
Rico.Luman@ing.com

Jurjen Witteveen
Sector Economist
jurjen.witteveen@ing.com

Dmitry Dolgin

Chief Economist, CIS
dmitry.dolgin@ing.de

Nicholas Mapa
Senior Economist, Philippines
nicholas.antonio.mapa@asia.ing.com

Egor Fedorov
Senior Credit Analyst
egor.fedorov@ing.com

Sebastian Franke
Consumer Economist
sebastian.franke@ing.de

Gerben Hieminga
Senior Sector Economist, Energy
gerben.hieminga@ing.com

Nadège Tillier
Head of Corporates Sector Strategy
nadege.tillier@ing.com

Charlotte de Montpellier
Senior Economist, France and Switzerland
charlotte.de.montpellier@ing.com

Laura Straeter
Behavioural Scientist
+31(0)611172684
laura.Straeter@ing.com

Valentin Tataru
Chief Economist, Romania
valentin.tataru@ing.com

James Smith
Developed Markets Economist, UK
james.smith@ing.com

Suvi Platerink Kosonen
Senior Sector Strategist, Financials
suvi.platerink-kosonen@ing.com

Thijs Geijer
Senior Sector Economist, Food & Agri
thijs.geijer@ing.com

Maurice van Sante

Senior Economist Construction & Team Lead Sectors

maurice.van.sante@ing.com

Marcel Klok

Senior Economist, Netherlands

marcel.klok@ing.com

Piotr Poplawski

Senior Economist, Poland

piotr.poplawski@ing.pl

Paolo Pizzoli

Senior Economist, Italy, Greece

paolo.pizzoli@ing.com

Marieke Blom

Chief Economist and Global Head of Research

marieke.blom@ing.com

Raoul Leering

Senior Macro Economist

raoul.leering@ing.com

Maarten Leen

Head of Global IFRS9 ME Scenarios

maarten.leen@ing.com

Maureen Schuller

Head of Financials Sector Strategy

Maureen.Schuller@ing.com

Warren Patterson

Head of Commodities Strategy

Warren.Patterson@asia.ing.com

Rafal Benecki

Chief Economist, Poland

rafal.benecki@ing.pl

Philippe Ledent

Senior Economist, Belgium, Luxembourg

philippe.ledent@ing.com

Peter Virovacz

Senior Economist, Hungary

peter.virovacz@ing.com

Inga Fechner

Senior Economist, Germany, Global Trade

inga.fechner@ing.de

Dimitry Fleming

Senior Data Analyst, Netherlands

Dimitry.Fleming@ing.com

Ciprian Dascalu

Chief Economist, Romania

+40 31 406 8990

ciprian.dascalu@ing.com

Muhammet Mercan

Chief Economist, Turkey

muhammet.mercan@ingbank.com.tr

Iris Pang

Chief Economist, Greater China

iris.pang@asia.ing.com

Sophie Freeman

Writer, Group Research

+44 20 7767 6209

Sophie.Freeman@uk.ing.com

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@ing.com

James Knightley

Chief International Economist, US

james.knightley@ing.com

Tim Condon

Asia Chief Economist

+65 6232-6020

Martin van Vliet

Senior Interest Rate Strategist

+31 20 563 8801

martin.van.vliet@ing.com

Karol Pogorzelski

Senior Economist, Poland

Karol.Pogorzelski@ing.pl

Carsten Brzeski

Global Head of Macro
carsten.brzeski@ing.de

Viraj Patel
Foreign Exchange Strategist
+44 20 7767 6405
viraj.patel@ing.com

Owen Thomas
Global Head of Editorial Content
+44 (0) 207 767 5331
owen.thomas@ing.com

Bert Colijn
Chief Economist, Netherlands
bert.colijn@ing.com

Peter Vanden Houte
Chief Economist, Belgium, Luxembourg, Eurozone
peter.vandenhoute@ing.com

Benjamin Schroeder
Senior Rates Strategist
benjamin.schroeder@ing.com

Chris Turner
Global Head of Markets and Regional Head of Research for UK & CEE
chris.turner@ing.com

Gustavo Rangel
Chief Economist, LATAM
+1 646 424 6464
gustavo.rangel@ing.com

Carlo Cocuzzo
Economist, Digital Finance
+44 20 7767 5306
carlo.cocuzzo@ing.com