

FX Daily: A spoonful of sugar

Whether it's a song or a slightly ominous bank run scene, the Fed brought back memories of a famous 1964 film this morning. In essence, Powell's attempt to sweeten the pill for markets came at the cost of unclear communication, so the market's pricing and the dollar will remain a function of banking stress. Today, expect hikes in the UK, Switzerland and Norway



Mary Poppins statue at Leicester Square

➔ USD: Compromise comes at a price

The well-known verse “a spoonful of sugar helps the medicine go down” might have inspired Jerome Powell yesterday as he and his FOMC colleagues offered markets a few dovish hints while delivering a potentially painful 25bp rate hike. As discussed in our [meeting review note](#), those hints primarily consisted of the view that “some additional policy firming may be appropriate” - not “will be appropriate” as before - and on keeping the median dot plot estimate for 2023 unchanged at 5.1%.

The statement was paired with a well-telegraphed message of trust in the solidity of the US banking system, and Powell did offer modest pushback against rate cut expectations during the press conference. However, we doubt the dovish market reaction was either a surprise or an

unwanted development for the Fed.

Many had argued that one objective of the Fed yesterday was to avert a major setback in financial market sentiment, the market reaction would suggest this was achieved, and the drop in equities might actually be mostly a function of Secretary Janet Yellen dismissing speculation that the Treasury is planning to provide “blanket” deposit insurance to banks.

However, that came at a price: a considerably less clear Fed communication. No trade-off between price and financial stability is essentially possible only if financial conditions tighten (due to banking stress) enough to bring down inflation, or if regulators and other institutions effectively manage to restore market confidence without anything more than the financial stability tools offered by the Fed. This second scenario requires indeed that, as Powell stated, the US banking system is very solid. Markets are, so far, not trusting the ability of the Fed to treat inflation and financial stability independently. This looks unlikely to change soon, which means that rate expectations should remain strictly tied to developments in the banking crisis. And this brings us to the FX implications.

The dollar weakened on the back of the moderate dovish surprise by the Fed yesterday, and reluctance from the Treasury to consider an extension to the deposit insurance. At the same time, a new regional lender, PacWest is facing increasing turmoil on deposit outflows and First Republic's rating was cut from BB to B by Fitch. So, with a market not trusting the more ambiguous Fed communication and the US regional banking crisis far from resolved, it looks like investor bias on the Fed may stay on the dovish side. This should translate into a continued bearish bias for the dollar, primarily against European currencies should the stabilisation in European sentiment continue. Still, we see a high chance of seeing small USD upside corrections on the way, rather than a straight-line USD depreciation.

Francesco Pesole

EUR: Central bank meetings in Switzerland and Norway

EUR/USD is now officially eyeing the 1.1000 level. We discussed yesterday how that is a key benchmark level for the pair, and we think a break higher would likely mark a rather strong conviction call from the market that the Credit Suisse shock has been successfully absorbed by European markets. That may be a bit premature, and we flagged in the USD section above how the USD bearish bias surely doesn't prevent EUR/USD corrections on the way. In the current elevated volatility environment, those corrections can be quite pronounced, even if short-lived. Today's eurozone calendar includes consumer confidence data for March as well as a few European Central Bank speakers, although our focus in Europe today will mostly be on central bank meetings in Switzerland and Norway.

The Swiss National Bank faces a monetary policy decision in a very turbulent time, as it faces the challenging aftermath of the Credit Suisse rescue deal. Originally, this had appeared to be a no-brainer for the SNB – a 50bp rate hike – and consensus expectations are still pointing at such a move. Despite admitting this has become a much closer call recently, we think the past few days of tentative calm in markets will allow the SNB to deliver the half-point increase today. We must remember that policy meetings in Switzerland occur only once a quarter and that the latest inflation readings surprised on the upside.

We expect a hike in Norway as well, but by 25bp, as previously announced and widely expected.

Norges Bank will also publish the updated rate projections, which currently embed only another 10bp worth of tightening. We think NB could revise the peak rate higher on the back of higher inflation and despite the recent turmoil, if nothing else to counter the recent NOK weakness. We expect gains in both the Swiss franc and krone today.

Francesco Pesole

➔ GBP: BoE to hike

The ECB and Fed rate hikes mean that the chances of the Bank of England following suit with a 25bp move today are quite high, even more so following the surprisingly [high inflation readings](#) published yesterday. Here is our [full market guide](#) to today's BoE meeting.

Markets are now fully pricing in a 25bp scenario and will therefore look for some indications that the further 40bp currently embedded in the GBP OIS curve is warranted. The division within the BoE's MPC may be nothing but exacerbated by the recent market turmoil, the risk is that markets may receive very little guidance on future policy paths. Ultimately, the pound may rapidly default to being driven by external factors: primarily the banking situation and global risk sentiment. A test of 1.25 in cable in the coming days is looking quite likely.

Francesco Pesole

⬆️ CEE: Strong euro a welcome boost for region

Today's calendar in the region is basically empty and hence the main focus will be on the reaction to yesterday's Fed decision. Higher EUR/USD is good news for FX and the CEE region should thus continue to rally. On the other hand, the negative sentiment left by the Fed could put a bit of a damper on the positive push coming from EUR/USD.

However, today should not be all about the Hungarian forint and the Czech koruna as in the last few days. As we mentioned earlier this week, the Polish zloty and the Romanian leu just needed a stronger euro to strengthen, in our view. Unless negative market sentiment prevails today, the entire region could see decent gains. Still, the previous leaders, the forint and the koruna, should remain at the forefront of the region and move towards 385 EUR/HUF and 23.60 EUR/CZK. The Polish zloty could finally trade out of the March range of 4.680-4.720 EUR/PLN and test lower levels. The Romanian leu could look lower below 4.91 EUR/RON for the first time since the middle of February.

Frantisek Taborsky

Authors

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Frantisek Taborsky

EMEA FX & FI Strategist

frantisek.taborsky@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. (“ING”) solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.