

FX Daily: Flight to safety continues to favour JPY

With no sign yet of a U-turn from Trump on tariffs, equity markets remain under heavy pressure. For FX, the flight to safety seeks those liquid currencies with large current account surpluses, notably the yen and the Swiss franc. The US current account deficit of 4% of GDP leaves the dollar vulnerable – unless this turns into a financial crisis



We expect the JPY and CHF to be favoured, EM currencies and commodity FX to be hit hard and for the dollar to probably trade somewhere in between

📌 USD: Too much baggage

Weekend press reports and TV interviews suggest US President Donald Trump is not yet ready to be swayed from his mission to reset the global trading system. Asian equities are off 6-10%, and this global trade war is proving the great leveller for global interest rates, where market interest rates are converging lower. Very much in focus is the Federal Reserve. The market now prices 110bp of Fed cuts this year and a low point for the easing cycle down at 3.00% next year. In a speech on Friday, Chair Jerome Powell was [giving little away](#) apart from saying that the tariffs will be "significantly larger than expected."

While the market does hear his remarks that tariff-induced inflation risks becoming more persistent, it is instead focusing on the stock market and growth prospects and making the call that the Fed will be forced to cut. The drop in long-term inflation expectations evident in the USD

[5Y5Y inflation swap](#) is probably driving that view. Needless to say, US and global growth forecasts are being slashed across the board.

In FX markets, the ongoing carnage in equity markets continues to favour defensive positioning. Liquidity is important here, but so is the balance of payments (BoP) picture in that your country does not want to be heavily dependent on foreign capital. Here, the dollar gets marked down on its 4% current account deficit and the view that foreign investors will pull capital or certainly raise FX hedge ratios on longer-term/stickier investments in the US. As to whether Washington policy is triggering a 'sell America' mentality, there are no clear signs of that yet. Yes, the US 5-year sovereign Credit Default Swap increased 5bp last week, but US Treasuries are not yet underperforming German Bunds. However, the US Treasury does auction \$119bn in 3, 10 and 30-year auctions Tuesday-Thursday this week, and any fat tail/poor bid-to-cover will be jumped on by investors and will prove a negative dollar event risk.

We are also watching to see whether, as one of our traders puts it, this political crisis turns into a financial crisis. For example, US high yield credit spreads are widening sharply, and there's a risk some skeletons are discovered in the financial closet. To that end, keep close watch of the EUR/USD three-month cross-currency basis swap. Any sharp widening in favour of the USD (i.e., the interbank market prepared to lend out euros in the swap market at below market rates to secure USD funding) would be a sign of trouble and could briefly send the dollar higher before the Fed is forced to step in.

In general, expect the JPY and CHF to be favoured, EM currencies and commodity FX to be hit hard and probably the dollar to trade somewhere in between.

Looking at the [calendar this week](#), the big focus will be on the February US CPI and PPI data on Thursday and Friday. Have the tariffs imposed on China and the steel and aluminium sector started to come through? Given the weight of the equity sell-off, the market may well trade higher inflation numbers as dollar negative on the back of the hit to real consumption. This week also sees NFIB small business optimism on Tuesday and the FOMC minutes on Wednesday.

DXY is heavily weighted towards Europe – a loser in a trade war. The yen only has a 14% weight. Overall, we think the dollar remains fragile and a 102-103 range may ultimately resolve in a breakdown to 100 – either if the Fed comes on board with easing or a 'sell America' mentality emerges. The wild card is the USD funding story.

Chris Turner

EUR: Caught in the middle

EUR/USD has retreated from its spike high to 1.1140 but remains in demand. As we discussed [last week](#), supporting factors for the euro are its role as a liquid alternative to the dollar and the fact that the euro runs a 3% current account surplus. Standing against the euro is the eurozone being an open, trade-driven economy. In focus this week will be what the Europeans do when it comes to retaliation. Trade leaders are meeting in Luxembourg today. From the sounds of it, Europe is going to be far more cautious and selective than the blunt 34% reciprocal tariff announced by China on Friday. Just quickly on China, we saw that the People's Bank of China fixed USD/CNY a little higher overnight – any fixing over 7.20 this week would drive USD/EM higher on the (likely mistaken) view that China is preparing to devalue the renminbi.

Back to the euro, this global trade war has seen the low point for the European Central Bank's easing cycle repriced closer to 1.50%. That said, EUR/USD two-year swap differentials have narrowed into levels last seen in early October and should serve to keep EUR/USD supported around 1.09 as this financial dislocation plays out. Again, 1.11/12 is major medium-term resistance, and we probably require some very negative US news to break that this week.

Chris Turner

📌 CEE: Not out of the woods yet

In the CEE region, we are waiting for the central bankers' response to the new global environment, and we are unlikely to hear much this week. However, we will see some new numbers that could help shape the view in the new conditions. Retail sales in Hungary were released this morning, and later today we will see industrial production in the Czech Republic.

Later, the National Bank of Romania will decide on rates, and we expect no change at 6.50%.

Tomorrow in Hungary, March inflation will be released and should be the main focus of the markets this week. We expect a drop from peak 5.6% to 4.9% year-on-year, slightly below market expectations, while core inflation should remain strong.

On Thursday, we will see the final GDP numbers in Romania for the fourth quarter of 2024 and final inflation numbers in the Czech Republic. Last Friday's release showed no change at 2.7%, and the details will tell us more about core inflation. And on Friday, current account numbers will be released across the CEE region.

CEE FX came under pressure again on Friday following a dovish repricing in the rates market. We see the rate differential tightening alongside negative sentiment from the equity market and some correction in EUR/USD downwards. We therefore do not believe that the CEE region is past the sell-off yet. In our view, the Polish zloty and Hungarian forint are particularly exposed. PLN due to positioning, valuations and a dovish turnover for the National Bank of Poland; the HUF due to usual sensitivity to global markets and highest exports to the US. European equity markets have been good navigators of EUR/HUF for us this year, and current levels point to a further move up to 410. Tomorrow's inflation print, however, will also be important. Elsewhere, we still retain our bias for PLN/CZK down, reflecting the different stages of the cutting cycle across the CEE region.

Frantisek Taborsky

📌 NOK: Vulnerable to the liquidity shock

After the Australian dollar, the Norwegian krone has been the worst-performing G10 currency over the last week. It has taken a big hit both from the fall in oil prices (an OPEC+ supply increase was a [big shock](#) here) and the fact that Norwegian interest rates have some of the furthest fall to given the previously hawkish stance of Norges Bank. What may well impact the NOK as well is declining liquidity. This generalised rise in volatility, increasing investors' value-at-risk metrics and forcing deleveraging, will impact FX liquidity. The NOK traditionally performs very poorly in illiquid environments, which could be the story this week.

Expect investors (those with the ability to establish new positions) to be looking at a pair like NOK/JPY. Were things to get really ugly this week in financial markets, NOK/JPY could make a break towards the 12.00 area.

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