

FX Daily: Hawkish Riksbank can lift the krona today

We expect a 50bp hike by Sweden's Riksbank today, and despite the domestic economic woes, signals that rates will peak at close to 4.0%. This can trigger a krona rally today. Elsewhere, we'd be wary of chasing the dollar rebound seen yesterday, given the raising bets on Fed rate cuts after fresh US banking concerns



📌 USD: Be careful chasing the dollar rebound

The release of quarterly earnings in the US continues to paint a better picture for American corporates, with big tech companies beating estimates yesterday. However, concerns about the US banking sector have returned after First Republic's shares dropped 49% following the larger-than-expected drop in deposits and announced restructuring plans. Ultimately, a risk-off mood has prevailed, despite the overall contagion effect having been significantly more contained than in previous instances in March: the 3-month FRA-OIS spread ticked higher to 32bp, but is a far cry from the 50bp and 60bp peaks seen last month.

In FX, this still translated into a fully-fledged flight to safety, with the yen outperforming and the dollar recovering ground yesterday. High-beta currencies came under pressure, particularly the Norwegian krone, which is the least liquid currency in G10 and inevitably very vulnerable to

adverse swings in risk sentiment.

The dollar's rebound followed its natural correlation with risk aversion yesterday, although we signal how in multiple instances when concerns about the stability of the US banking system rose in the past month-and-a-half it was the dovish repricing in Fed rate expectations that had a more tangible short-term impact on the dollar. We would therefore warn against chasing a dollar rally that is fuelled by idiosyncratic negative news on a US bank, especially in the run-up to the FOMC meeting.

The dollar hasn't really connected with the dovish repricing in Fed rate expectations, with rate cut expectations that have risen steadily since the end of last week. From 55bp of easing priced in by year-end on Friday to 75bp this morning. We suspect that some help to the dollar momentum shown yesterday would need to come from good US data over the remainder of the week. Ahead of the more important GDP and PCE figures tomorrow and Friday, we'll take a look at durable goods orders and wholesale inventories today.

All in all, we think the balance of risk is tilted to the downside for the dollar today, as some stabilisation in sentiment would pave the way to at least partly re-link with falling Fed rate expectations. DXY may slip back to the 101.00/101.50 range by the end of the week.

Francesco Pesole

📈 EUR: Narrow rate differential still points higher

EUR/USD continues to hover around the 1.1000 mark, and we think it can find some fresh support above that level if some risk sentiment stabilisation offers a chance to reconnect with a favourable rate differential. The eurozone calendar is quite empty and the predominance of news coming from the US on the banking and equity sector leaves EUR/USD even more driven by the dollar leg.

As discussed in [yesterday's FX Daily](#), the 2-year EUR-USD swap spread has narrowed further thanks to the combined effect of rising dovish bets on the Fed and the reinforcement of hawkish pricing in the EUR curve. The spread is currently at -66bp, the narrowest since 2020 when it peaked at -53bp.

Elsewhere in Europe, the National Bank of Hungary walked the talk yesterday ([here is our full meeting review note](#)), beginning its dovish pivot with a rather symbolic step. We believe the 450bp technical cut in the top end of its rate corridor might be followed by cuts in the effective rate in the coming months, based on the re-tuned forward guidance. However, a more cautious approach by the central bank means good news for the Hungarian forint.

Francesco Pesole

📈 GBP: Room to climb back

The pound moved broadly in line with other pro-cyclical European currencies yesterday, and we see room for a recovery as the dollar's good momentum may struggle to last. As is the case for EUR/USD, GBP/USD can count on an improved rate differential, which has recently moved back into positive territory (2-year swap rate as reference) by around 25bp and is at its highest since October 2022.

We see room for Cable to re-test the recent 1.2543 highs by the end of the week in a less

unfavourable risk environment, and thanks to the pre-Bank of England meeting hawkish narrative which is still offering decent support to the pound.

Francesco Pesole

SEK: Riksbank hike can help SEK

The Riksbank will raise interest rates again this morning, and the consensus is centred around a 50bp hike to bring the policy rate to 3.50%. This is also our call ([here is our full preview](#)) and what markets are fully pricing in, so the market impact will mostly be driven by: a) the new economic projections and b) any forward-looking language.

When it comes to the projections, core CPI inflation forecasts will need to be revised higher, since it has overshoot the Bank's previous projections, although the really important bit for the market will be the updated rate path projections. Here, we think that the Riksbank will be wishing to sacrifice a bit of credibility to maintain a very hawkish tone, and we expect them to signal a peak rate close to or at 4.0% and no rate cuts for the whole projection period.

This should, in practice, prove unfeasible. Even one more rate hike – despite being our base case – would be very easy to deliver given ongoing economic strains in Sweden, and rate cuts will likely need to be delivered next year. However, the Riksbank needs to focus on its short-term goal, which at the moment is to support its currency and send a signal of trust in its economy and financial system by staying resolutely hawkish.

The decent performance of SEK compared to peers in the past few days suggests that markets had started to position for a hawkish Riksbank today, but EUR/SEK still trades in modest overvaluation (around 0.5%) according to our short-term fair value model and we think the Riksbank can push the pair to the 11.20 mark with a convincing hawkish message today. We remain doubtful that the pair can fall much further in the near term given lingering headwinds to the krona (global risk sentiment, concerns about the Swedish housing and economic situation).

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