

FX Daily: High beta currencies look vulnerable in the short-run

The Nvidia-led equity rally may now have to face the reality of higher rates, and we suspect high-beta currencies are at risk of corrections. Today, the focus will remain on Germany's struggling economy, with the release of the Ifo survey. The implications for ECB policy remain limited, so the euro's relative resilience is probably justified



The Swedish krona has appreciated over 5% against the dollar and around 3.5% against the euro since the end of January

📈 USD: FX feeling the Nvidia effect

Federal Reserve speakers have echoed the content of the FOMC minutes since those were published. Communication has been understandably cautious on the inflation outlook considering the recent higher-than-expected CPI, particularly stressing the risks of cutting too early or too fast. Risk-sensitive assets would normally suffer from an easing pushback, but the narrative in equity markets is strictly one of tech-driven outperformance after very strong results from Nvidia.

One argument that we think makes sense at this stage is that once the Nvidia effect has faded, equity markets are left with increasingly stretched valuations as USD rates continue to rise. Both 2-year and 10-year treasuries have pared around half of the late October to late December gains,

trading around 50bp higher than their end-2023 levels. The S&P500 is up 6% year-to-date.

Our expectations are that the US data story won't be making a U-turn in the next couple of weeks. Indeed, we see a chance that February's data released in March starts to head in the right direction for Treasuries, but the 29 February PCE release should be strong and push rate cut expectations further away.

With all this in mind, we believe high-beta currencies are looking expensive in the very short run. The prospect of unstable risk sentiment and a dollar leg higher ahead of next week's PCE points to downside potential. Today, the US calendar includes the Conference Board's Consumer Confidence indicator, which is expected to have plateaued in February. We see room for a DXY stabilisation around 104.00 or a rebound already today as risk sentiment softens.

Francesco Pesole

EUR: German slump in focus

PMI releases have sent mixed messages. The eurozone's aggregate PMIs were better than expected, as discussed [here](#), this probably means that recession concerns are easing and that the Red Sea disruptions have not had much dampening effect on activity. At the same time, Germany is consolidating its role as the black sheep in the region.

German manufacturing PMIs plummeted to 42.3 in February, overshadowing a modest tick-up in the service sector. This morning, the Ifo survey is published, and we should probably brace for a soft reading there too. Germany makes up a third of the eurozone's economic output and is the largest trading partner for most EU members: the question FX analysts like us are trying to answer now is whether the euro has already largely priced in the German slump or if other factors have prevented it from taking the hit.

We think the former explanation is more accurate, although it requires an additional key point. The FX market is trading on global risk dynamics (as discussed above) and short-term rate differentials. The key question is therefore whether mounting evidence of German economic weakness should be associated with prospects of faster and earlier rate cuts by the ECB. President Lagarde and many of her colleagues tried to send the message that no, it shouldn't. Inflation – and above all wages – are the real focus, so the relative resilience of the euro should not be surprising and the risks of a decline in EUR/USD in the short term mostly related to USD upside potential, in our view.

This morning, the ECB publishes CPI expectation figures for January, which had come in at 3.2% and 2.5% a month prior. Two ECB hawks, Joachim Nagel and Isabel Schnabel are also speaking today.

Francesco Pesole

GBP: Strengthening domestic story

The UK has continued to experience some repricing higher in growth expectations, as PMIs inched higher again in February. If the ECB had to convince markets that rate cut expectations were overly optimistic, the Bank of England has the “privilege” of letting data do the talking.

In fact, recent comments by MPC members have not leaned to the hawkish side. Earlier this week, Governor Andrew Bailey endorsed expectations of easing this year and reaffirmed that inflation

does not need to fall back to target before the BoE can cut. The two most dovish MPC names, Ben Broadbent and Swati Dhingra said easing is likely and that there is a risk of overtightening.

The rebound in EUR/GBP from the excessively cheap 0.8500 low did not surprise us. But we have some doubts the pair can rally further in the near term, as markets may be more inclined to push 2024 ECB easing expectations back to 100bp (now 90bp) rather than pricing in three full cuts in the UK (now, 62bp). Still, our medium-term view remains bullish on the pair on the back of policy divergence.

Francesco Pesole

📉 SEK: A strong week, but will it last?

EUR/SEK broke decisively through the 11.20 area this week, which had been a decent support throughout February. The stronger-than-expected headline CPI in Sweden, some stickiness in long-term inflation expectations and the global equity rally have all contributed to a strong week for the krona.

Our short-term view on SEK is, however, not as rosy. We suspect the Riksbank turned dovish before the data really allowed it to, which is not a positive signal for SEK. The risk here is that policymakers are indeed feeling the pressure to relieve the economy from tight rate conditions and may start cutting before inflation has moved decisively lower, ultimately compressing the krona's real rate.

As discussed in the USD section, risk sentiment might struggle to keep fuelling rallies in high-beta currencies like SEK in the next couple of weeks. The end of FX sales means the downside could be rather slippery for the krona. We still see EUR/SEK rebound to the 11.30 area or higher before a longer-term decline can materialise.

Francesco Pesole

Author

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

chris.turner@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 www.ing.com.