

## FX Daily: Riksbank needs to stay hawkish today

The Riksbank should hike by 50bp today, in line with expectations. We think it is necessary to sound hawkish to help restore confidence in the krona, despite a deteriorating economic and property market backdrop. Meanwhile, high-beta FX is on the rise this morning, but the rally may be premature given the scope for more hawkish Fed rate repricing



### ➔ USD: May be too early to jump back on short-dollar bets

After only moderately hawkish remarks by Federal Reserve Chair Jerome Powell on Tuesday, other Fed officials delivered more aggressive comments on the prospects for tightening yesterday. Christopher Waller, Lisa Cook, John Williams and Neel Kashkari all pointed at either the need for rates to go beyond 5.0% or reiterated the higher-for-longer narrative. All this prevented a recovery in risk sentiment yesterday and helped the dollar build a temporary floor. This morning, European and US equity futures point to a positive open, and high-beta currencies are in demand. This might be a sign that markets are seeing this moment as the peak in the Fed's hawkish communication and are now eyeing opportunities to re-enter short-USD pro-cyclical positions at more attractive levels.

However, there is still some room for USD rates to absorb further hawkish repricing in rates expectations, and the rebound in risk currencies may be premature. Markets are pricing in a 5.13% Fed peak rate as of this morning, so still not fully factoring in another hike beyond March. Around 50bp of easing in the second half of the year remains in the price, which reflects both disinflation and recession risks in the US. Probably, the aim of hawkish Fed speakers at this stage is to convince markets that a) rates can go at least to 5.25%; b) that rate cut speculation is misplaced.

It is fair to expect that more evidence from data will be required to convince markets of another 25bp after March. Jobless claims are the highlight of the day in the US today, and tomorrow's University of Michigan sentiment index is the last piece of data in the US for the week. We think that a more patient trading environment could return after this morning's risk-on mood and last until Tuesday's pivotal US inflation report. In FX, it appears too early for the dollar to re-enter a sustained downtrend: local stories may instead take centre stage.

*Francesco Pesole*

## ➔ EUR: German inflation tests ECB hawkish comments

German inflation numbers [released this morning](#) surprised on the downside. Headline CPI grew 8.7% year-on-year, lower than the forecasted 8.9%. The EU-harmonised print showed a deceleration from 9.6% to 9.2%, while consensus expectations were for a return to double-digit inflation.

This will probably test the ability of the European Central Bank to continue pushing back against the bullish reaction in the rates market after last week's ECB meeting. We'll hear from Governing Council members Francois Villeroy, Joachim Nagel, Pablo Hernández De Cos and Luis de Guindos today. EUR/USD may struggle to climb back to the 1.0800 handle just yet.

Elsewhere in Europe, keep an eye on Bank of England Governor Andrew Bailey as he testifies before parliament. Like in the eurozone, we have seen a good deal of hawkish commentary in the UK following last week's [BoE rate decision](#), and markets likely expect any policy comments today to fall on the hawkish side of the spectrum too. Weakness in the euro is endorsing the recent drop in EUR/GBP, and 0.8800 might be tested in the near term. Still, we don't see the pair's depreciation as sustainable given the grim economic outlook for the UK and no clear policy divergence.

*Francesco Pesole*

## ⬆️ SEK: A big day for the Riksbank

The Riksbank and its new Governor Erik Thedeen are facing a historic challenge. The Swedish economic outlook looks very bleak, with both GDP and high-frequency data pointing down and the housing market having already corrected 15%. On top of that, inflation remains above 10% and [the krona is close to all-time lows](#) against both the euro and in trade-weighted terms. Today's rate announcement and monetary policy report is of huge importance for the krona.

We expect, in line with consensus, a 50bp rate hike today ([here is our full preview](#)). This outcome is fully priced in, but more uncertainty lies around the forward-looking tone and rate projections. We think the Riksbank has all the interest in sounding hawkish at this stage, despite acknowledging the risks related to the housing slump and high inflation. Rate projections from November see a peak below 3%: we think today's revision will take it to at least the 3.25-3.50% region.

With wage negotiations in Sweden about to end and a tendency for Swedish data (especially CPI) to be rather volatile, patience should be the name of the game for the Riksbank now. Even in the face of a clearly worsening economic outlook, the Bank should focus on a) halting the slump in the krona; b) keeping inflation expectations in check. To us, this appears a necessary step to restore confidence in Swedish markets. Then, data will undoubtedly need to come to the rescue, but with no policy meetings until the end of April, there is definitely some time for the economic and inflation picture to improve.

We think a hawkish 50bp hike by the Riksbank can prevent another leg higher in EUR/SEK: a primary goal is to create a cushion for the pair to the all-time March-2009 11.68 highs. With markets currently attaching around 2.5-3% of risk premium to EUR/SEK due to concerns about the Swedish economy, SEK is not lacking room for recovery (our base case is still for a drop below 11.00 in EUR/SEK by the summer). We doubt this will happen in the near term though, and despite a convincing hawkish message by the Riksbank today, restoring confidence in the krona will require help from data. EUR/SEK may trade around 11.20-11.40 in the coming weeks, and that should already be a welcome development for the Riksbank.

*Francesco Pesole*

## ➔ CEE: NBR's turn to confirm end of hiking cycle

After the National Bank of Poland (NBP), today it is the turn of the National Bank of Romania (NBR) to confirm what [we believe](#) is the end of the hiking cycle. We don't expect any change in the key rate level, but a mildly cautious tone could be employed to balance the obvious easing of monetary conditions since the last meeting. On FX side, the record demand for ROMGBs is having a positive impact on the Romanian leu, which has been below the NBR's intervention level most of the time since the beginning of the year. Massive inflows into bonds have helped the RON to test levels below 4.90 EUR/RON several times. Plus, global conditions, led by falling gas prices and a higher EUR/USD, are positive for FX. On the local side, the FX implied yield remains attractive as well, fluctuating steadily in the 6.60-7.00% range for the 3M tenor, comparable to the Czech koruna and Polish zloty. However, given the NBR's solid track record of managing the RON, potential FX depreciation losses look limited, which gives a distinct advantage, especially against the Hungarian forint and Polish zloty. Thus, we continue to expect the RON to hold below the 4.90 EUR/RON level depending on further inflows into ROMGBs.

As expected, the NBP [left rates unchanged](#) yesterday and the statement did not bring much new information. So the main focus will be on Governor Adam Glapinski's press conference today at 3pm local time. The main questions will be on what inflation numbers the NBP expect for January and February, when inflation is expected to peak, and whether the governor still believes in the possible year-end rate cut he mentioned last time. The Polish zloty stabilised yesterday, but market rates have been volatile in Poland this week, probably also due to the NBP meeting, and the zloty remains fragile. The governor's words are thus likely to determine the zloty's direction. On the one hand, we see market expectations still significantly more dovish than our forecast, on the other, the whole IRS curve is higher by about 20-30bp over the last month. Thus, we expect the zloty to maintain the current 4.73-4.75 EUR/PLN range.

*Frantisek Taborsky*

## Authors

### Francesco Pesole

FX Strategist

[francesco.pesole@ing.com](mailto:francesco.pesole@ing.com)

### Frantisek Taborsky

EMEA FX & FI Strategist

[frantisek.taborsky@ing.com](mailto:frantisek.taborsky@ing.com)

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