

FX Daily: Tense markets, but dollar bear trend should win out

Continued focus on the health of the US regional banks has seen levels of money market stress edge higher. US policymakers will be looking at ways to patch things up, but the clear overall trend should be one of tighter credit conditions and weaker US growth. This should help take the steam out of inflation and send the dollar lower. For today, US NFP is in focus



⬇️ USD: The case for a weaker dollar is building

It has been a busy week of central bank policy meetings and also continued stress among the US regional banks. On the latter, there now seems to be growing scrutiny amongst regulators of the short-selling activity in these regional bank stocks and whether any market manipulation took place. US regulators, such as the Securities and Exchange Commission (SEC), have stopped short of instituting a ban on the short-selling of bank stocks (as we saw in 2008), but the point is that we have reached the stage when such policy action is being discussed.

The continued volatility in these bank stocks is keeping money market conditions tense. The 3-month USD FRA-OIS spread is nudging wider again, as is the 3m EUR cross-currency basis swap. Typically, this is a sign of market nervousness and is not conducive to the kind of benign dollar decline that floats developed and emerging currencies alike. What would help such a trend, however, would be softer US activity and price data which would allow the Federal Reserve to cut

rates. That brings us to today's US April NFP data.

Consensus expects a decent, but softer, 185k increase in the headline jobs data and average hourly earnings increasing at 0.3/4.2% month-on-month/year-on-year. Any softness in activity or price data would be supportive of market pricing of the first Fed cut in September and would be dollar bearish. Conversely, any above-consensus price data would add to recent sticky inflation releases such as the first quarter Employment Cost Indicator. This would see a bearish flattening of the US yield curve and send the dollar higher.

Looking at the bigger picture, however, it seems clear that tighter US credit conditions will only exacerbate the 2023 US slowdown and disinflation process and we suspect there will be plenty of dollar sellers should we see any surprise 1-2% rally in the dollar over the next couple of weeks. DXY has the lows of the year at the 100.75/85 area.

Chris Turner

➔ EUR: ECB muddies the water a little

Two-year euro swap rates fell by 12bp yesterday and EUR/USD softened after the ECB offered a slightly less hawkish than expected 25bp hike. The ECB's [statement](#) emphasised that past tightening has been transmitted 'forcefully' to euro area financing conditions and that the lags and the strength of that transmission remain uncertain. That buys the ECB some time and has been used by other central banks around the world too. However, ING's Carsten Brzeski's takeaway from the meeting was that the [door remains open](#) for further rate hikes. Indeed, we look for another 25bp hike in June.

We doubt such ECB equivocation will dent EUR/USD for too long. And in addition to what should clearly be supportive interest rate trends for EUR/USD this year should be much lower energy prices which have delivered a vast improvement in the euro's terms of trade. This is a complete reversal of conditions that were weighing on EUR/USD in the third quarter of last year. We suspect EUR/USD finds some good demand near 1.0900 now and we are just waiting for some softer US activity or price data to unlock a break of 1.1100.

Chris Turner

⬆ CHF: Swiss franc in demand

As we have been noting recently, we think the defensive (non-correlated) properties of the Swiss franc are in demand. Expect that to continue to be the case until the dust starts to settle in the US regional banking crisis. More locally, we have some Swiss data and a rare speech from Swiss National Bank President Thomas Jordan at 11CET.

On the local data front, we will see April FX reserve data. Swiss FX reserves have fallen about CHF200bn since the start of 2022 – partly due to valuation effects and partly due to the SNB intervening in FX markets to sell EUR/CHF. The latter is part of the SNB's strategy to keep the real CHF stable, which requires nominal CHF appreciation. With Swiss inflation (today released at 2.6% YoY for April) still dramatically lower than that in the eurozone, the SNB will continue to seek nominal CHF appreciation.

We favour EUR/CHF to grind down to the 0.9700 area – lows seen when the US banking crisis first broke.

Chris Turner

➔ NOK: Norges Bank might come to the krone's rescue

Yesterday, Norges Bank hiked rates by 25bp and signalled a similar move in June, in line with the latest rate projections (peak rate at 3.5%). We must remember that Norges Bank has turned increasingly hawkish explicitly to support the krone, and we heard again some currency protest by Governor Ida Wolden Bache. She reiterated that “if the krone remains weaker, a higher policy rate than envisaged earlier may be needed” and added that the recent krone weakness is larger than what can be explained by forecasting factors. We agree with the Governor, and NOK is indeed quite undervalued due to its low liquidity character and consequent sensitivity to risk sentiment.

However, Norges Bank tightening is falling short of supporting NOK, and while larger cuts to daily FX purchases look warranted in June, it now seems increasingly likely that NB will need to raise rates beyond the projected summer peak of 3.5%. We still expect volatility and vulnerability in the krone in the near term, but then a recovery in the second half of the year. EUR/NOK should be able to sustainably return below 11.00 by year-end.

Francesco Pesole

Author

Chris Turner

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

chris.turner@ing.com

Francesco Pesole

FX Strategist

francesco.pesole@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.