

FX Daily: Unorthodox correlations

With the yen bearing the brunt of the risk rally, the dollar saw some delayed benefits from the re-tuning in Fed rate expectations and enjoyed a modest recovery yesterday. Today, all eyes will be on CPI data from Germany and Spain. Elsewhere, USD/MXN could break below 18.00 today as Banxico hikes and oil stays supported



➔ USD: Dollar takes a breather as yen takes a hit

Yesterday's moves in the FX market provided another confirmation that we cannot apply the traditional frameworks to the interaction between currencies and other assets. If diverging monetary policy paths (at least as perceived by the market) in the US and Europe are gradually reconstructing the link between USD/European FX and front-end rate differentials, the interactions between safe-havens, high-beta currencies and swings in the equity market continue to prove rather unorthodox.

An important point is that the dollar's safe-haven status was perhaps dented by the fact that the banking turmoil has primarily been a US story. Furthermore, another safe-haven currency, the Swiss franc, got caught up with idiosyncratic banking stress, leaving the yen to benefit widely from the initial shock – especially considering its high inverse correlation with Federal Reserve rate expectations. This helps us understand the underperformance of JPY since the start of this week and especially yesterday. Improving sentiment asymmetrically hits the yen given it is

accompanied by an unwinding of dovish Fed bets: the USD/JPY level might rebound to the 135.00 area, even though we favour another decline in the pair beyond the short term.

The bloc of pro-cyclical currencies remains extremely homogeneous. Markets have fallen out of love with the Aussie dollar as [lower inflation](#) points to a stronger chance of a pause in rate hikes and the New Zealand dollar is now looking like a more attractive option in the region. Oil-sensitive currencies may continue to enjoy decent momentum as we see more upside risks to oil prices. The Canadian dollar is also benefiting from the general improvement in American (North and Latam) sentiment but lacks a domestic tightening story, so its rally may start to run out of steam sooner than other peers (like MXN and NOK). We think the Mexican peso has more room to rise, as discussed in the MXN section below. We see Norway's krone as more attractive than Sweden's krona in the near term.

Back to the dollar, we think the small recovery seen yesterday could be one of many along a gradual decline path, but would favour some consolidation around current levels today. Today's calendar sees the third release of fourth-quarter GDP figures, plus speeches by the Fed's Thomas Barkin, Susan Collins and Neel Kashkari.

Francesco Pesole

➔ EUR: First CPI readings in focus

Preliminary March inflation readings in Spain and Germany will be closely watched today. The German figures will obviously draw greater interest, and consensus expectations are for a deceleration from 8.7% to 7.3% in the headline rate. Spanish numbers will be published earlier this morning and we must remember that they did trigger some market shake-up recently. Expectations are for a flat core rate at 7.6%, but a sharp deceleration in headline inflation from 6.0% to 3.7%.

With the European Central Bank explicitly data-dependent despite an implicit hawkish bias, this week's inflation figures are set to be an important driver of the market's rate expectations. There are currently two 25bp rate hikes fully priced in by September in the OIS curve, and the bar for another hawkish repricing is set quite high. However, ECB speakers have leaned on the hawkish side of late and the EUR OIS curve is not discounting banking stress in the same way the USD OIS curve is.

The EUR/USD rally took a break around 1.0840 and we could see it hover around those levels today, but we still favour a break above 1.0900 and ultimately a test of 1.1000 in the near term.

Francesco Pesole

⬆️ MXN: 25bp hike by Banxico, and maybe a break below 18.00

We think the Mexican peso's bullish momentum may have further to run. Today, Banxico will announce monetary policy and we expect a 25bp rate hike to 11.25%. This is a consensus view and markets are almost fully pricing in this outcome, so most of the focus will be on forward-looking language.

Recent banking turmoil would suggest policymakers will hold a more cautious stance on the future path of monetary policy. However, market pricing suggests investors have already scaled back expectations for additional Banxico tightening beyond today's hike. If anything, leaving the door

open for more tightening if needed as the Bank reiterates its resolution to fight inflation might see some positive impact on the peso.

Beyond the central bank risk event, we think MXN remains attractive in an environment where markets favour currencies with high carry and positive exposure to rebounding crude prices. A break below 18.00 in USD/MXN may be on the cards soon, potentially today on a hawkish surprise by Banxico.

Francesco Pesole

CZK: Koruna welcomes hawkish Czech National Bank

The CNB board decided yesterday to keep the key interest rate at 7.00%, in line with expectations. Also, unsurprisingly, six of the seven members were in favour of the decision, while one voted for a 25bp rate hike. The board also confirmed that it would "continue to prevent excessive fluctuations of the koruna". The governor during the press conference commented on market expectations of a peak in interest rates at current levels and a significant rate cut this year (roughly 125bp in cuts priced in before the meeting). However, according to the governor, a rate hike cannot be ruled out and rate cut expectations are premature at this point.

The Czech koruna visibly welcomed the CNB's hawkish tone and moved below 23.60 EUR/CZK for the first time since the sell-off in global markets two weeks ago. The central bank has confirmed that it is ready to intervene if needed, but current levels are far from where the CNB was last active. On the other hand, the central bank's statement is clearly supportive for the koruna and implies that the currency is safe in the event of a global sell-off. Moreover, with the prospect of higher rates for a longer period of time, a solid FX carry is also certain. Overall, the koruna thus offers decent risk/reward and we expect it to strengthen further.

Frantisek Taborsky

Author

Frantisek Taborsky

EMEA FX & FI Strategist

frantisek.taborsky@ing.com

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

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.