

## FX Markets in 2025 - ING's big calls

Donald Trump and the Republican party will control all the levers of US power in January. FX markets think they know what's coming. In this quick take on the Global FX market in 2025, we share our big calls on the trends which will dominate the developed and emerging market FX space



### 1 Dollar strength: Don't overthink it

There is a tendency in financial markets to do a lot of second-guessing. When the dollar briefly sold off on the Thursday after the US election some were wondering whether the smart money had concluded that Trump would be bad for the dollar. Our advice is not to overthink it and instead take the firm view that the new administration's plans for looser fiscal and tighter immigration policy, when combined with relatively higher US rates and protectionism, all make a strong case for a dollar rally.

Yes, the US economy may end up overheating – but 2025 should be the year when more air gets pumped into any potential dollar bubble. Inevitably there will be occasional setbacks to the dollar bull trend, be they a function of market positioning or open speculation on whether Trump's trade hawks want a weaker dollar. But the over-arching trend should be a dollar-positive one. And positive enough to see the dollar trade-weighted index break to the upside of a two-year range.

## Who could be in Trump's trade hitlist?

	Goods trade surplus with US (USDbn)	Current account balance (% of GDP)
China	301	1.6
Mexico	173	-0.2
Vietnam	122	5.8
Germany	90	6.4
Japan	77	4.6
Canada	67	-0.8
South Korea	66	4.0
Taiwan	60	14.7
Italy	49	0.9
India	48	-0.7
Ireland	31	13.5
Switzerland	21	7.1
Thailand	17	2.0
France	16	-0.7

Source: ING, Macrobond (4Q rolling data as of June 2024)

The US Treasury sets a threshold at USD 15bn for bilateral goods surplus with the US and 3% current account surplus as % of GDP as two of the three criteria when assessing potential macroeconomic and FX mis-practices in its key trade partners

## 2 European currencies will underperform

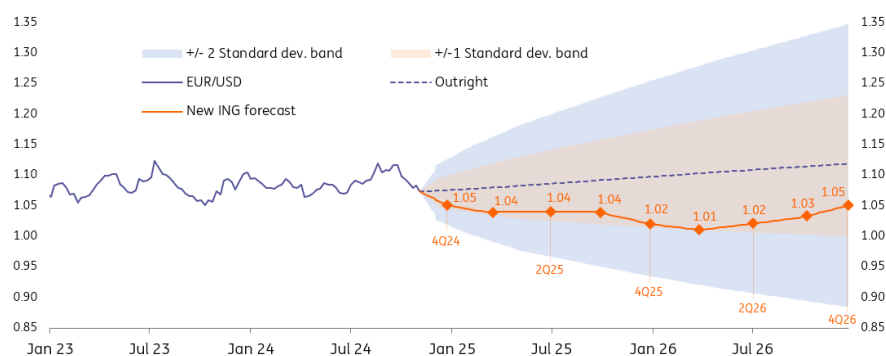
One of our key macro calls for next year is that the ECB will outpace the Fed in monetary easing as eurozone growth headwinds look set to intensify with Trump's protectionism while fiscal stimulus keeps the Fed cautious on rate cuts. Accordingly, we expect a further widening of the two-year USD:EUR swap rate gap to the 200bp area, which is consistent with EUR/USD trading below 1.05.

Trump's tariffs will be key, but we cannot ignore geopolitical risks in Ukraine and the Middle East, the low probability of any fiscal stimulus in the eurozone, and elections in EU countries potentially creating new frictions with Brussels. We doubt markets will lack reasons to add different degrees of risk premium into the euro on top of an already unsupportive rate differential.

As discussed when we published our [new EUR/USD forecast](#), we estimate a peak of risk premium around 4Q25-1Q26. Even if EUR can hold above parity before then, we see all the conditions for a structural shift from a 1.05-1.10 range to a 1.00-1.05 range in 2025.

We think Scandinavian currencies will also underperform due to exposure to European risk sentiment. SEK likely has more downside room than NOK, given a dovish Riksbank and greater exposure to global trade frictions. Sterling and the Swiss franc may act as relatively lower betas to the eurozone's troubles, and both stand to marginally outperform the euro.

## New EUR/USD forecast



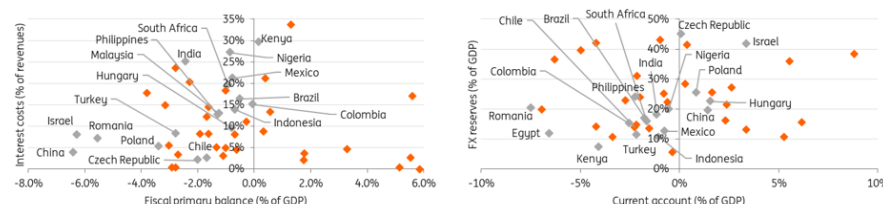
### 3 EMFX faces the toughest environment since 2020

Next year, emerging market currencies will face the twin headwinds of lower global trade volumes and higher US yields. When Trump took office in 2017, world trade was growing 5-6% YoY. By the end of 2019, after two years of tariffs, world trade was falling 2% YoY.

In addition to tariffs, rising US bond yields will stress test the fiscal position of emerging markets and pressure those with large external financing needs. Our team looks for the US ten-year Treasury yields at 5.50% by the end of 2025. Those EM countries exposed to shorter duration in refinancing their debt or those that have high debt servicing costs relative to government revenues will prove vulnerable. In terms of external fundamentals, large current account deficits set against modest FX reserve coverage also present a risk in the event of capital outflows from emerging markets. The degree to which these countries withstand a 'Trump tantrum' in the Treasury market will be a key theme.

Fortunately, most emerging markets are running much narrower current account deficits than they have done during prior periods of bond market stress. And the countries at most serious risk in terms of debt servicing costs relative to government revenues are some familiar and poorly rated names such as Egypt and Pakistan. In particular, Kenya's heavily managed exchange rate could come under pressure next year given its poor country scorecard and the 13% real terms rise in the shilling this year. In terms of investment-grade sovereigns, India and Mexico have quite high debt servicing costs, too. But many of the big beasts in the EM world have high real interest rates, which offer their currencies some protection. We now look through the EM regions.

## EMFX Vulnerability Scorecard



Source: ING, IMF WEO October 24 outlook, FX reserves latest data

### 4 CEE: In harm's way

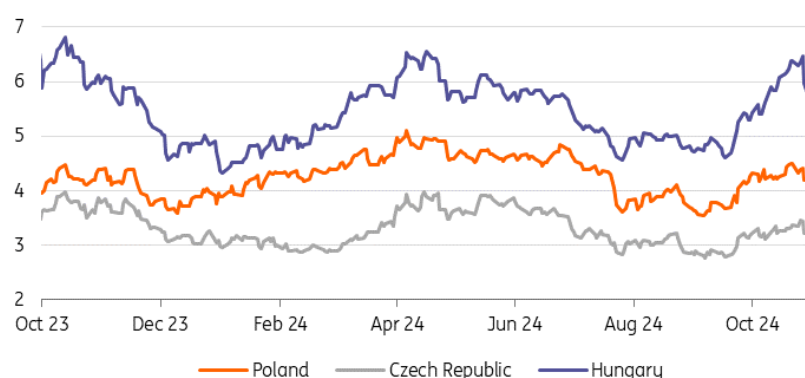
The region is fully exposed to the new post-US election conditions. Although the direct trade link

with the US is not as strong, it has roughly doubled in the last five years. However, the main exposure is through the trade link with Germany and the focus on automotive, which seems like the worst combination as we look to the future. The Czech and Hungarian economies are the most exposed here compared to the more diversified Polish economy. We believe that market expectations for a recovery next year in the CEE region are overly optimistic, and we will see further downside surprises.

At the same time, markets have priced out much of the easing in a pre-US election positioning adjustment. On the one hand, this helped to prevent a bigger sell-off in CEE currencies right after the US election result. On the other, there is now plenty of room for the market to price in more CEE rate cuts in an environment requiring more easing than before the US election. This should result in less supportive rate differentials for CEE currencies.

On the fiscal side, the CEE region is highly vulnerable, with financial markets increasingly focused on the rationale for high public finance deficits. Poland is already at the level of 5-6% of GDP for this year and next. Hungary is running high political risk with upcoming elections and tight polls. And the Czech Republic will see a general election in October next year, which may also change the fiscal direction somewhat. Overall, we see risks to CEE FX clearly on the downside for the coming months and more weakness for the region.

## CEE terminal rates are priced too high



Source: ING, Refinitiv

## 5 Asia: China will try to hold the line

Despite robust domestic fundamentals in strong growth and falling inflation, Asia FX will have to navigate the dual challenge of higher US interest rates and likely higher tariffs by the US in 2025, resulting in a stronger USD. At the centre of it all will be China. Tariffs will be negative for the country, but we don't expect a repeat of the first trade war for four main reasons:

1. There is no shock factor this time around; markets have been preparing for this possibility for over a year.
2. Global investor positioning is different from 2018. Markets are now heavily underweight China, and there is less money at risk of flight from there.
3. The Fed is now in a cutting cycle instead of a hiking cycle.
4. The PBOC now has currency stability as a key policy goal and will resist major movements in either direction.

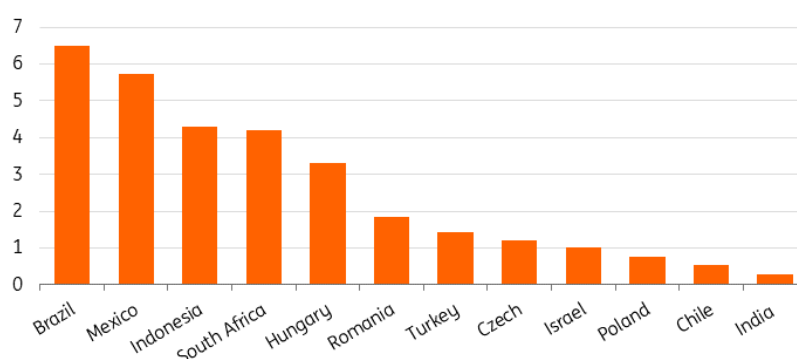
Our base case has the USD/CNY in a band of 6.90-7.35 next year, with potential further weakening in 2026 depending on economic and policy developments.

We think the Asian currencies with a higher sensitivity to CNY and larger trade surpluses with the US would face the highest depreciation pressure, and KRW stands out on both of these counts. IDR, at the other end of the spectrum, should be relatively less impacted.

We expect KRW to remain weak throughout 2025 for both external and domestic reasons. Korea's large and growing trade surplus with the US and high sensitivity to the renminbi puts it at high risk of volatility when tariff talk and their implementation escalate. The uncertainty around the possible renegotiation of the US-South Korea defence cost-sharing could add further pressure to the KRW. From a domestic growth standpoint, we think Korea has limited levers to utilise counter-cyclical macro policy measures to support growth. High household debt and the consequent financial stability risks limit aggressive rate cuts. A shift to expansionary fiscal policy is also unlikely, given the current government's priority of fiscal consolidation and lack of tax revenues.

As the tariff debate heats up and tariffs eventually get imposed on not just China but also the rest of Asia, perhaps in the second half of next year, IDR should benefit from being the only country in the ASEAN region where its share of US exports in total GDP has actually come down from 11% in 2016 to 8% by mid-2024. There have been significant positive developments on the local front as well, and political risks have receded. The reappointment of the incumbent finance minister, Sri Mulyani, should help contain concerns around fiscal slippage and likely mean that the fiscal deficit cap of 3% is retained. Lower dependence on foreign investors for fiscal deficit funding should be a positive for IDR. We see the IDR as a relative out-performer in the region.

## Real rates across the EMFX universe



Source: ING, Refinitiv

## 6 Latam: Real rates will be important

Much scrutiny will be on the Mexican peso, where the USMCA is up for review in the summer of 2026. Equally, the Brazilian real had a poor Trump 1.0, and government spending will remain in focus in 2025; Brazil has presidential elections the year later. While both currencies look vulnerable to incoming US trade policy, both do enjoy some protection from 5-6% real interest rates. Brazil also has a sizeable stock of FX reserves which it is ready to use.

We think Chile's peso will be one of the currencies more vulnerable in EM. Local real interest rates are close to zero after an aggressive easing cycle. A 2%+ current account deficit will not help, and

at 14% of GDP, Chile's FX reserves are low after a failed bid in 2022 to support the peso. Chile's currency suffered greatly during Trump 1.0, and 2025 may well be the year USD/CLP pushes close to 1100.

## 7 Yen-funded carry trade strategies to fall out of favour

Up until July this year, yen-funded carry trades had been very popular and successful. Since then, a massive unwind of short yen positions, along with uncertainty about the path for US politics and the global economy, have all kept volatility high. Uncertainty over the path for USD/JPY, Japan's domestic economy, BoJ rates, and the more challenging outlook for the high-yield target currencies (previously the Mexican peso) also make carry trade strategies so much harder to justify. Looking back at the performance of carry trade strategies during peak Trump 1.0 (March 2018-September 2019) and funding positions in the three highest yielding G10 currencies at the time (NZD, CAD and AUD) out of yen, would have delivered an annualised return of -3.3% with an 11% maximum drawdown. Not very attractive.

Yet, if there is to be any outperformance of the yen in terms of total returns, we think it will come against Europe. The Swedish krona is one of the lowest-yielding currencies with one of the most open economies. If the yen is to turn, we think it will do so against the krona, and we see a case for SEK/JPY correcting back to the 13.00 area.

If there is an ongoing interest in carry, we think that will remain in the Turkish lira. The US election demonstrated the TRY's resilience to global influences, and in fact, the lira was one of the few EM currencies in the region that managed to rally in the post-election environment. The Central Bank of Turkey is nearing the start of an easing cycle, which reduces potential carry, but should not decrease the CBT's determination to keep USD/TRY under control.

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