# G10 FX Talking: Policy tightening delays the dollar descent

In the G10 FX space, inflation data and central bank meetings will continue to dominate. Unless there is a sharp slowing in US activity and especially inflation data, expect the 22 March FOMC meeting to prove net hawkish and see the dollar retain most of its February gains


Source: Shutterstock

## Main ING G10 FX forecasts

| | EUR/USD | USD/JPY | GBP/USD |
|---|---|---|---|
| 1M | 1.07 ↑ | 135.00 → | 1.21 → |
| 3M | 1.10 ↑ | 130.00 ↓ | 1.27 ↑ |
| 6M | 1.12 ↑ | 125.00 ↓ | 1.28 ↑ |
| 12M | 1.15 ↑ | 120.00 ↓ | 1.24 ↑ |

| | EUR/GBP | EUR/CHF | USD/CAD |
|---|---|---|---|
| 1M | 0.89 ↑ | 1.00 ↑ | 1.35 → |

| | | | | | | |
|---|---|---|---|---|---|---|
| 3M | 0.89 | ↑ | 1.02 | ↑ | 1.33 | ↓ |
| 6M | 0.90 | ↑ | 1.03 | ↑ | 1.30 | ↓ |
| 12M | 0.90 | ↑ | 1.03 | ↑ | 1.26 | ↓ |

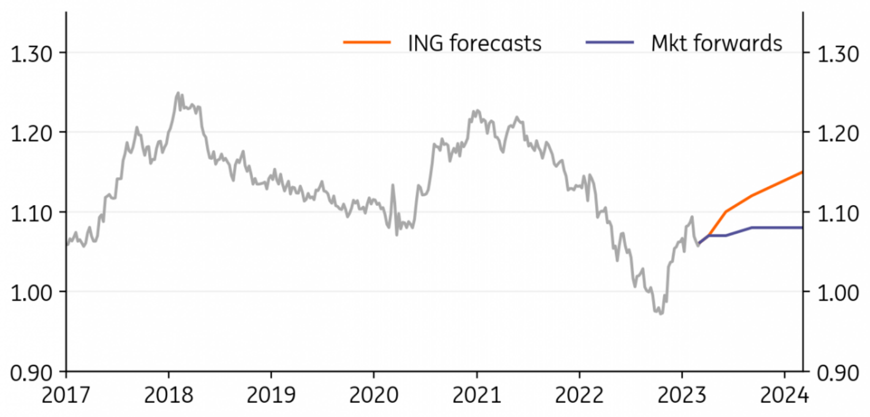
↑ / → / ↓ indicates our forecast for the currency pair is above/in line with/below the corresponding market forward or NDF outright

Source (all charts and tables): Refinitiv, ING forecast

### EUR/USD: Sticky inflation delays the dollar decline

| | Spot | One month bias | 1M | 3M | 6M | 12M |
|---|---|---|---|---|---|---|
| EUR/USD | 1.0647 | Neutral | 1.07 | 1.10 | 1.12 | 1.15 |

- February proved a counter-trend month for world financial markets, where sticky inflation and better activity data put to rest ideas of early Federal Reserve easing. Instead, investors priced another 50bp into the tightening cycle. The data over the last month probably means that the Fed will have to stay hawkish when it meets on 22 March, hiking 25bp and revising up the Dot Plots.
- 25bp hikes from the Fed in March, May and June mean tighter settings and inverted yield curves are with us a little longer and suggest the bulk of this year's dollar decline will come in 2H.
- A very hawkish European Central Bank (we look for 100bp of hikes) can help support the floor in what may well be a 1.05-1.10 range into the summer.




Source: Refinitiv, Macrobond, ING

## USD/JPY: Bank of Japan event risks looms large

| | Spot | One month bias | 1M | 3M | 6M | 12M |
|---|---|---|---|---|---|---|
| USD/JPY | 135.83 | Neutral | 135.00 | 130.00 | 125.00 | 120.00 |

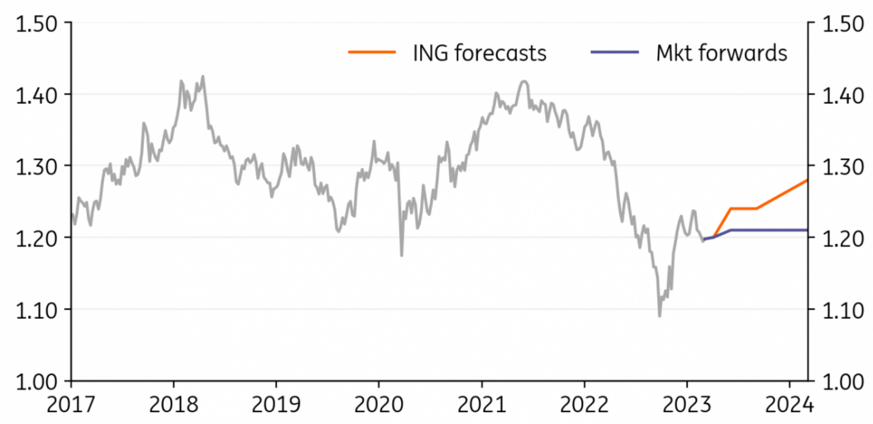
- The re-pricing of the Fed cycle and the steeply inverted US yield curve meant that US 10-year Treasury yields were dragged 60bp higher in February. Our strategy team sees outside risk to 4.25% over the coming weeks, but the year-end target is 3.00%. That should be bearish for USD/JPY – but more a story for later in the second quarter and through the second half of the year.
- That means USD/JPY could hang around these 135/137 levels through March, with outside risk to 140 if the Fed is very hawkish.
- Of acute interest will be developments in Japan. Outgoing BoJ Governor Haruhiko Kuroda holds his last policy meeting on 10 March. Incoming BoJ Governor Kazuo Ueda holds his first policy meeting on 28 April. Both could pose positive event risks for the Japanese yen.


Source: Refinitiv, Macrobond, ING

## GBP/USD: Bank of England tightening could be coming to a close

| | Spot | One month bias | 1M | 3M | 6M | 12M |
|---|---|---|---|---|---|---|
| GBP/USD | 1.2035 | Neutral | 1.20 | 1.24 | 1.24 | 1.28 |

- GBP/USD has been sluggish near 1.20, weighed down by the stronger dollar and GBP IRS rates failing to keep pace with the big, hawkish re-pricing seen in the USD and EUR curves. Unlike the Federal Reserve (+75bp) and European Central Bank (+100bp), we think the Bank of England may only have 25bp more of tightening left to do – taking Bank Rate to 4.25%. This is partly because more equivocal speeches from BoE officials and key survey data suggest tightness in the UK labour market is abating.
- Our game plan, therefore, sees GBP/USD staying soft through March on the strong dollar (1.1850 the potential and outside risk to 1.1650), before broader dollar weakness sees cable return to 1.23/1.25 this summer.
- A difficult equity environment could also challenge sterling.

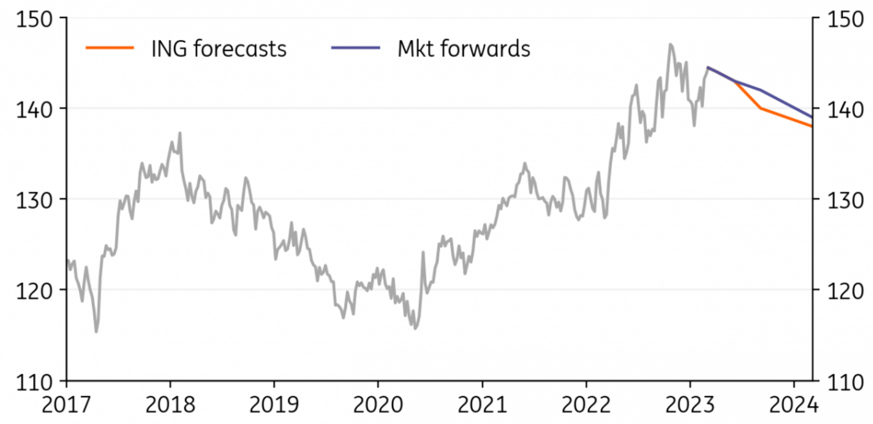



Source: Refinitiv, Macrobond, ING

## EUR/JPY: Looking more closely at the BoJ

| | Spot | One month bias | 1M | 3M | 6M | 12M |
|---|---|---|---|---|---|---|
| EUR/JPY | 144.6000 | Neutral | 144.00 | 143.00 | 140.00 | 138.00 |

- After December's surprise widening in the JGB yield target band, the market is now on alert for BoJ policy normalisation. Our analyst's view is that the next significant move may come in June once the BoJ has seen the spring wage agreements. That will not stop the market from speculating over further adjustments in policy at the 10 March or particularly the 28 April meeting.
- A possible adjustment could be to widen the +/- 50bp around 0% 10-year JGB yield target still further or shift to targeting yields shorter down the curve. Any such move would be JPY bullish.
- A downside bias on EUR/JPY also embeds the view of a fragile equity environment as policy rates are raised around the world.

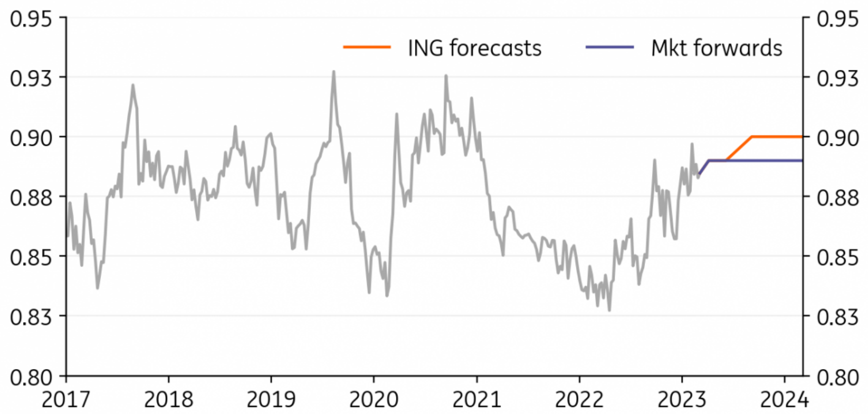



Source: Refinitiv, Macrobond, ING

## EUR/GBP: Warmer UK-EU relations are welcome

| | Spot | One month bias | 1M | 3M | 6M | 12M |
|---|---|---|---|---|---|---|
| EUR/GBP | 0.8847 | Neutral | 0.89 | 0.89 | 0.90 | 0.90 |

- Some welcome news over the last month is the improvement in UK-EU relations. The Windsor Framework agreement on Northern Ireland's trade represents a structural break from the UK antagonism seen since the Brexit vote in 2016. It is welcome, but not game changing for sterling in that the UK's trade relationship with the EU does not improve and the UK remains one of the weakest in the G7, beset by low productivity, weak investment and a shrinking labour force.
- As such, we think EUR/GBP will be driven more by short-term rate differentials (EUR supportive) and GBP could come under pressure as the BoE tries to outline a pause in its tightening cycle.
- Reopening the Brexit debate remains off the UK political agenda.




Source: Refinitiv, Macrobond, ING

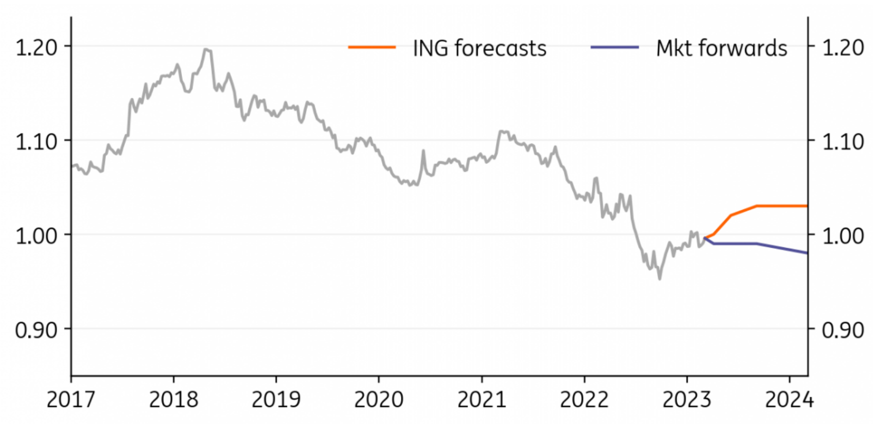
## EUR/CHF: Swiss National Bank will remains 'hands on'

| | Spot | One month bias | 1M | 3M | 6M | 12M |
|---|---|---|---|---|---|---|
| EUR/CHF | 0.9948 | Neutral | 1.00 | 1.02 | 1.03 | 1.03 |

EUR/CHF continues to trade towards the top of a narrow range roughly defined by 0.9850-1.0050. We expect the Swiss national Bank has remained active in FX markets, probably selling FX reserves to limit the franc's depreciation. On 30 March we will see fourth quarter 2022 intervention data, which will probably be larger than the CHF739mn sold in the third quarter. Remember the SNB is trying to keep the real CHF stable as it fights above-target inflation.

On 23 March we should see the SNB hike the three-month policy rate 50bp to 1.50%. We look for one further 25bp hike in June.

Despite much wider rate differentials moving in favour of the EUR, we expect the SNB to keep EUR/CHF relatively stable.

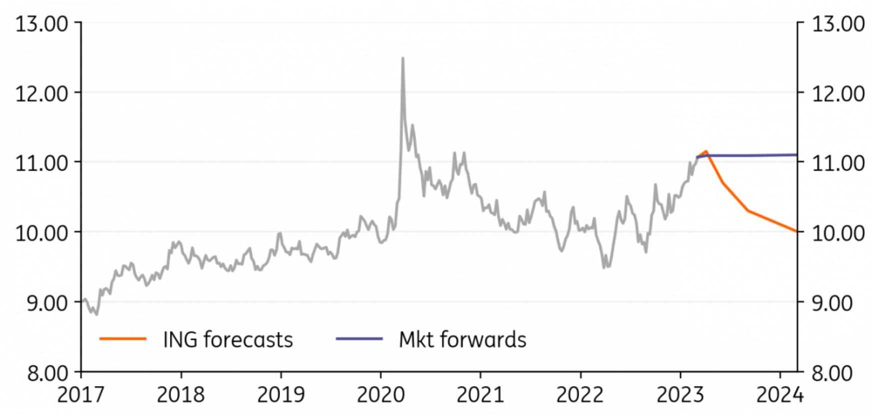



Source: Refinitiv, Macrobond, ING

### EUR/NOK: Illiquid NOK to stay volatile

| | Spot | One month bias | 1M | 3M | 6M | 12M |
|---|---|---|---|---|---|---|
| EUR/NOK | 11.0850 | Mildly Bullish | 11.15 | 10.70 | 10.30 | 10.00 |

- We expect Norges Bank to resume tightening with three back-to-back 25bp rate hikes in light of higher inflation and a more hawkish global environment. Markets have already priced this in, so the short-term impact on Norway's krone shouldn't be too significant.
- NOK is the least liquid currency in G10, and this means that the prospect of more tightening in global financial conditions will continue to exacerbate volatility in the krone. No sustained NOK recovery is possible without a material stabilisation in sentiment.
- At the same time, many negatives are in the price for NOK, and we saw NB slow the pace of FX purchases again in March (from NOK 1.9bn to NOK 1.7bn). Short-term pain and volatility remain likely, but we still favour a higher NOK in the medium term.

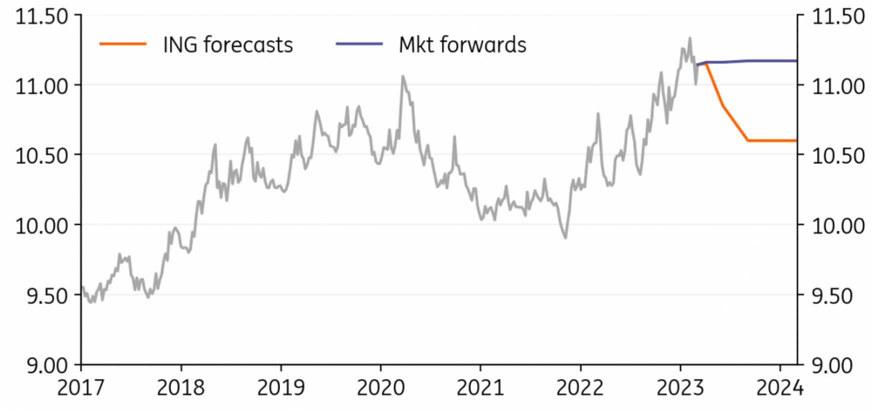



Source: Refinitiv, Macrobond, ING

### EUR/SEK: Be wary of Riksbank-led SEK rallies

| | Spot | One month bias | 1M | 3M | 6M | 12M |
|---|---|---|---|---|---|---|
| EUR/SEK | 11.1580 | Neutral | 11.15 | 10.85 | 10.60 | 10.60 |

- The Riksbank had to sound hawkish to 'save' the krona, and we think they'll hike by a total of 50bp. Now, SEK appears to be rallying on more RB hawkish re-pricing but remember that excessive tightening and consequent pain for housing and the economy was the reason SEK had sold off in the first place.
- So, we continue to flag non-negligible upside risks for EUR/SEK in the near term, and a downtrend below 11.00 may still prove premature – unless data point to an improved growth outlook.
- We'll watch closely the outcome of wage negotiations and all Swedish activity data, which can tilt the balance for or against a black swan scenario for the economy. It won't be a smooth path, but we are still moderately bearish on EUR/SEK in 2H23.

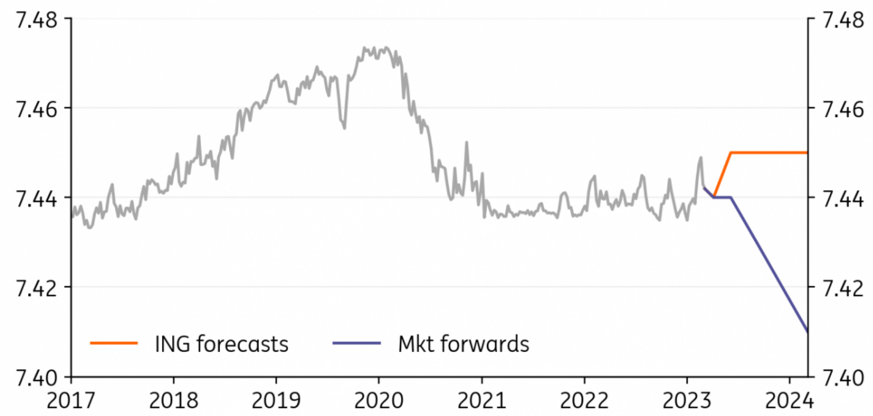



Source: Refinitiv, Macrobond, ING

## EUR/DKK: DN favouring rate gap over interventions

| | Spot | One month bias | 1M | 3M | 6M | 12M |
|---|---|---|---|---|---|---|
| EUR/DKK | 7.4432 | Neutral | 7.44 | 7.45 | 7.45 | 7.45 |

- Danmarks Nationalbank stopped FX intervention in February after widening the gap with the ECB with a 35bp hike at the start of the month. Back then, the Bank clearly signalled that the smaller hike was a consequence of rising FX intervention to defend the EUR/DKK peg.
- The ample room for further tightening by the ECB will offer many occasions to DN to deliver smaller increases and stabilise the EUR/DKK rate around 7.45 (or at least prevent large drops).
- We think another 35-40bp hike is possible after the 50bp ECB hike in March, even though a rise in domestic inflation risks tilting the balance back to FX intervention further down the road.




Source: Refinitiv, Macrobond, ING

### USD/CAD: BoC to stay put

| | Spot | One month bias | 1M | 3M | 6M | 12M |
|---|---|---|---|---|---|---|
| USD/CAD | 1.3587 | Neutral | 1.35 | 1.33 | 1.30 | 1.26 |

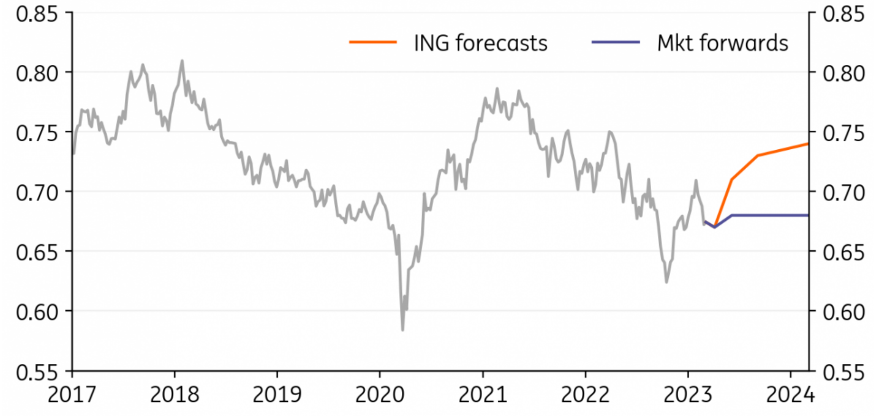
- The Bank of Canada stands as an outlier in the G10 central bank space, and despite the rise in Fed tightening bets, we expect no more hikes by the BoC given a worsening outlook for the property market and the broader economy.
- When adding an energy commodity bloc that is struggling to rebound and the very low exposure to the good China story, it seems likely that CAD won't be on the forefront of a risk rally.
- USD/CAD below 1.30 is still what we expect to see in the second half of 2023, but that should mostly reflect a broad improvement in risk sentiment and USD weakness rather than idiosyncratic CAD strength.


Source: Refinitiv, Macrobond, ING

### AUD/USD: Room to recover beyond the short-term

| | Spot | One month bias | 1M | 3M | 6M | 12M |
|---|---|---|---|---|---|---|
| AUD/USD | 0.6741 | Neutral | 0.67 | 0.71 | 0.73 | 0.74 |

- The Aussie dollar has been hit quite hard from the deterioration in global risk sentiment and geopolitical turmoil. Improvements in those two factors are needed to allow a rebound in AUD/USD, and that may only start to materialise from the second quarter onwards.
- But the Chinese growth story continues to place AUD in a rather advantageous spot to benefit from a broader stabilisation in risk sentiment. Iron ore prices have continued to rise and China's construction season in the second quarter should keep them supported.
- A slowdown in inflation creates problems for Reserve Bank of Australia hawks, but our base case is still that 4.10% will be reached, and that AUD/USD will climb back sustainably above 0.70 in the second half of 2023.

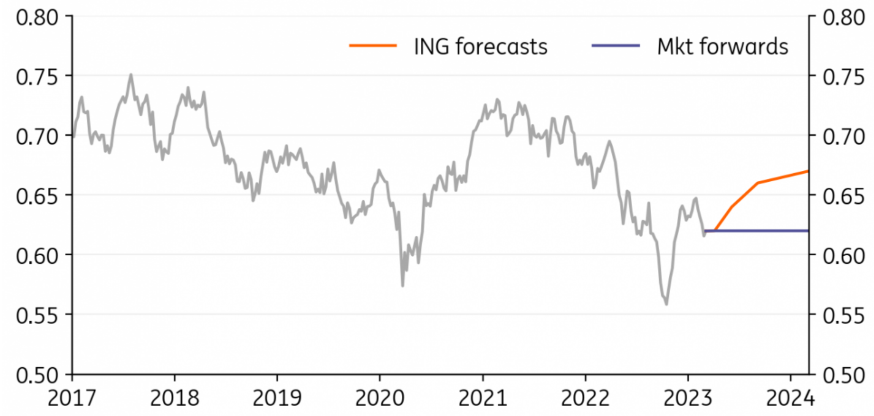



Source: Refinitiv, Macrobond, ING

## NZD/USD: Reserve Bank of New Zealand pivot may not come in April

| | Spot | One month bias | 1M | 3M | 6M | 12M |
|---|---|---|---|---|---|---|
| NZD/USD | 0.6192 | Neutral | 0.62 | 0.64 | 0.66 | 0.67 |

- As we expected, the RBNZ continued to delay their dovish pivot, despite lower-than-projected inflation and a disastrous cyclone adding to existing concerns around the economic outlook.
- There is a good probability that April won't see a pivot either, since we won't get CPI data before then, but only fourth quarter GDP. What will tilt the balance on the dovish side for the RBNZ, in our view, will be the disinflation process (which may well start earlier than they are projecting) and/or property market weakness rather than well-telegraphed evidence of a recessionary environment.
- We expect the RBNZ to end up short of their projected 5.50% peak rate, but that should not prevent NZD to touch 0.66 in 2H23.




Source: Refinitiv, Macrobond, ING

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