THINK economic and financial analysis

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G10 FX Talking: Dollar to stay strong

As the Federal Reserve tightens into a recession and yield curves invert further, expect the dollar to stay bid. We could easily see further gains of 5-7% across the board. In Europe, heightened scrutiny on policy choices could see GBP/USD nearing parity later this year

Source: Shutterstock

Main ING G10 FX forecasts

	EUR/USD	USD/JPY	GBP/USD
1M	0.95 ↓	146.00 ↑	1.07 ↓
2M	0.92 ↓	148.00 ↑	1.02 ↓
6M	0.92 ↓	148.00 ↑	1.02 ↓
12M	0.98 ↓	143.00 ↑	1.11 ↑

	EUR/GBP	EUR/CHF	USD/CAD
1M	0.89 ↑	0.95 ↓	1.38 ↑

2M	0.90	↑	0.93	↓	1.37	↓
6M	0.90	↑	0.91	↓	1.31	↓
12M	0.88	↓	0.90	↓	1.27	↓

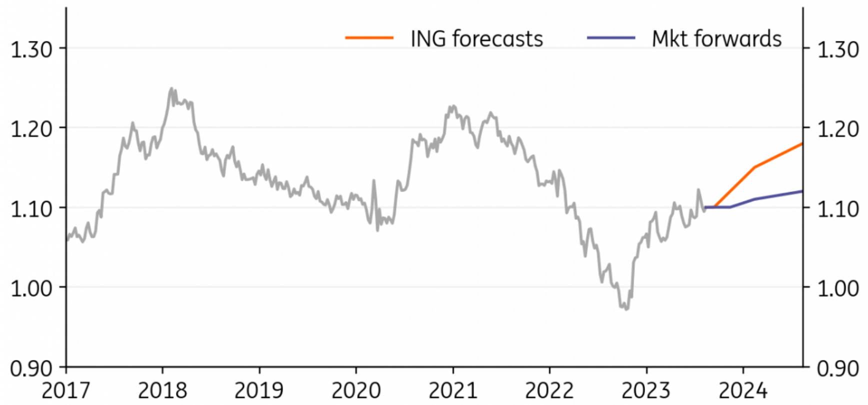
↑ / → / ↓ indicates our forecast for the currency pair is above/in line with/below the corresponding market forward or NDF outright

Source - all charts and tables: Refinitiv, ING forecast

EUR/USD: Volatility returns to April 2020 levels

	Spot	One month bias	1M	3M	6M	12M
EUR/USD	0.9705	Bearish	0.95	0.92	0.92	0.98

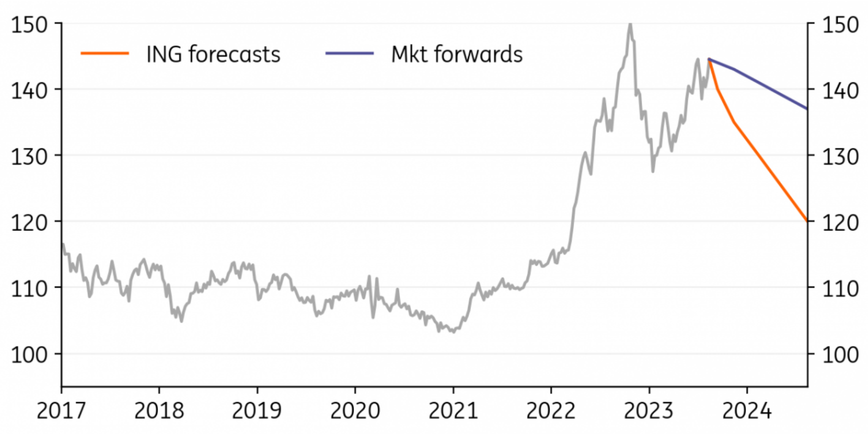
- EUR/USD realised volatility is now back to levels last seen in the early days of the pandemic. Tighter liquidity conditions as central banks raise rates and sell bonds typically do see volatility levels increase. This should be the story for this Autumn.
- Is the dollar about to top? From a risk management perspective, we would say 'no'. The Fed looks set to push ahead with tightening into a recession (rates peaking 4.25-4.50% early next year), which should keep the dollar broadly bid.
- The Eurozone is just entering three consecutive quarters of recession. As a pro-cyclical currency, this is not the time for the euro to shine. We see a 0.90-0.95 trading range developing.



USD/JPY: Tokyo pulls the trigger

	Spot	One month bias	1M	3M	6M	12M
USD/JPY	145.44	Neutral	146.00	148.00	148.00	143.00

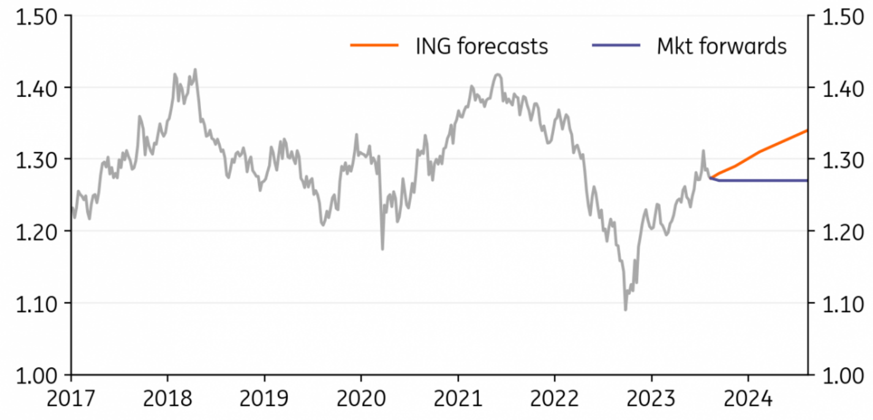
- In late September, Tokyo confirmed that it had intervened to sell USD/JPY (seemingly from the 145.70 area). The amounts were a large $20bn and shows that Tokyo means business. Importantly, US Treasury said it 'understood' the need for intervention. Does the G20 FX Communique get altered on October 12th?
- We doubt the BoJ FX intervention will define the exact top for USD/JPY. The macro factors driving the rally – hawkish Fed/energy crisis are still with us. And we see intervention as more of a campaign that might slow a move towards 150.
- Talk of a Plaza accord to reverse the dollar look premature too. The BoJ will need to hike to support this – unlikely before 2Q23.



GBP/USD: Policy mistakes get punished

	Spot	One month bias	1M	3M	6M	12M
GBP/USD	1.1076	Bearish	1.07	1.02	1.02	1.11

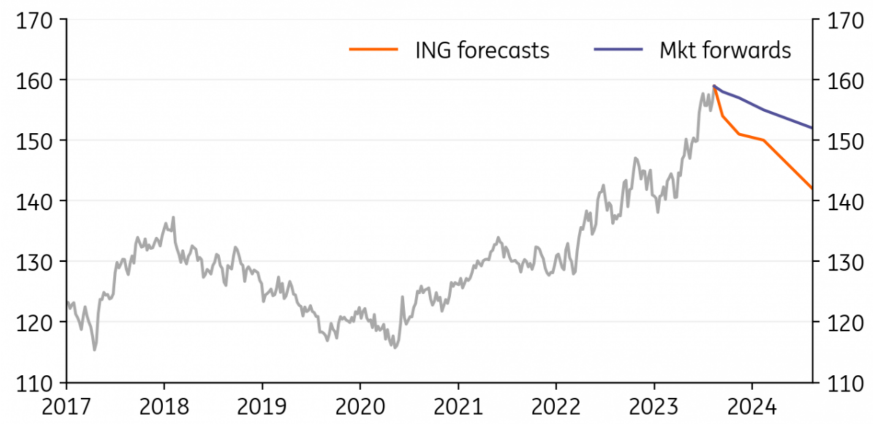
- It looks like the Fed will be pushing real interest rates deeper into more restrictive territory over coming months. That will tighten liquidity conditions still further and see that any policy mistakes get punished. The new UK government admitted such a policy mistake when reversing plans to scrap the top rate income tax bracket. The UK Gilt market was just not ready for huge supply.
- Key dates for the diary are October 14th and October 31st. The BoE intervened to buy Gilts, but said it would stop on Oct 14th. Does the Gilt market allow that to happen? And Oct 31st sees the medium-term fiscal plan released. Do the numbers add up?
- Cable does not seem out of the woods yet.



EUR/JPY: Downside bias remains

	Spot	One month bias	1M	3M	6M	12M
EUR/JPY	141.1600	Mildly Bearish	139.00	136.00	136.00	140.00

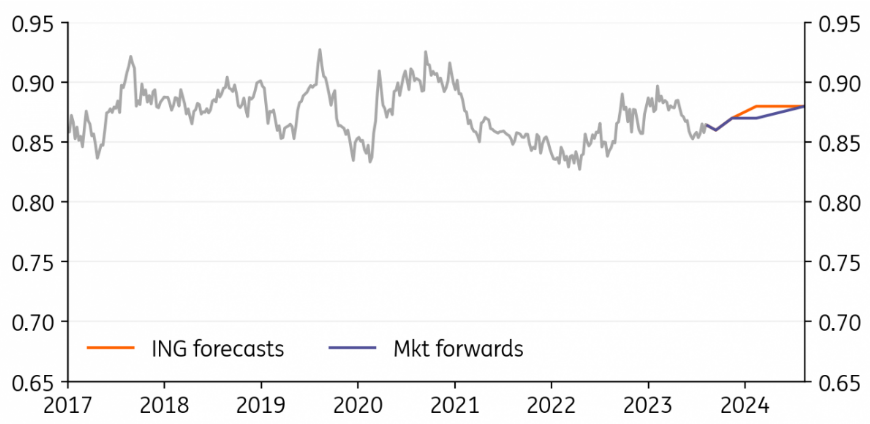
- EUR/JPY has been holding up quite well despite the global bear market in risk assets. Our bias would be that EUR/JPY struggles to sustain a break above 145 in an environment where central banks are actively looking to slow aggregate demand.
- For the ECB, we are looking for a 75bp hike in October, perhaps 50bp in December and another 25bp in 1Q23. The ECB will also have to think about QT in its APP portfolio, which may create problems for the Eurozone peripheral bond markets.
- Typically, the Japanese have been more interventionist than the Eurozone and on that basis – and given the forthcoming Eurozone recession - EUR/JPY risks look skewed lower next 6m.



EUR/GBP: Dangerous UK cocktail leaves GBP fragile

	Spot	One month bias	1M	3M	6M	12M
EUR/GBP	0.8763	Mildly Bullish	0.89	0.90	0.90	0.88

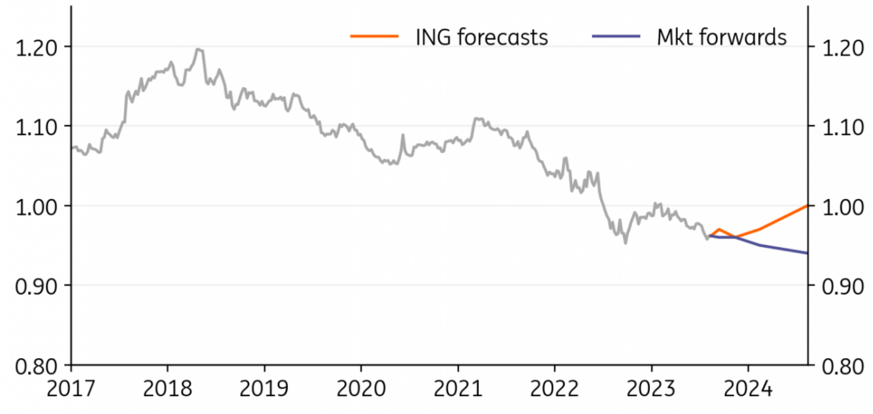
- Sterling has been driven by the fiscal credibility story. And it is interesting to note that the 10 year Gilt-Bund spread is struggling to narrow inside 200bp again – suggesting credibility is hard won and easily lost.
- The Chancellor's U-turn on the upper income tax bracket does little to assuage fiscal concerns. It only saves around £2bn compared to what could be £200bn of Gilt supply in FY23/24. Instead, the Chancellor will somehow need to find spending cuts or more likely tax increases – U-turn on energy windfall tax?
- Clearly this is a challenging picture and combined with a difficult global environment, sterling risks remain skewed lower.



EUR/CHF: SNB looks set to guide EUR/CHF lower

	Spot	One month bias	1M	3M	6M	12M
EUR/CHF	0.9681	Mildly Bearish	0.95	0.93	0.91	0.90

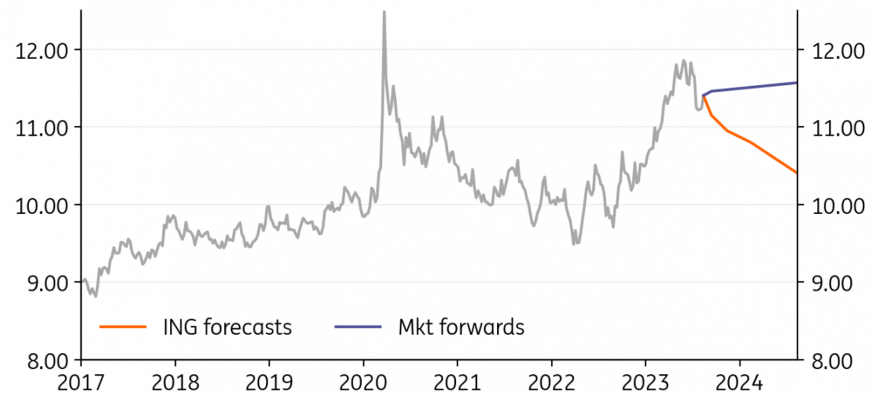
- In September, the SNB hiked 75bp to take the policy rate back to 0.50% and end the experience with negative interest rates. It also introduced an interesting reverse tiering on deposits, where any excess reserves would be remunerated at zero. ECB-watchers are taking great notice here.
- We still think the SNB is running a kind of monetary conditions framework, using both policy rates and the trade-weighted CHF to tighten conditions. With inflation amongst trading partners running 5-6% above Switzerland, the SNB will want a weaker EUR/CHF to keep the real Swiss franc stable.
- If we're right, SNB could be guiding EUR/CHF to 0.90 next year.



EUR/NOK: OPEC+ lifeline not enough

	Spot	One month bias	1M	3M	6M	12M
EUR/NOK	10.3500	Bullish	10.50	10.50	10.10	9.80

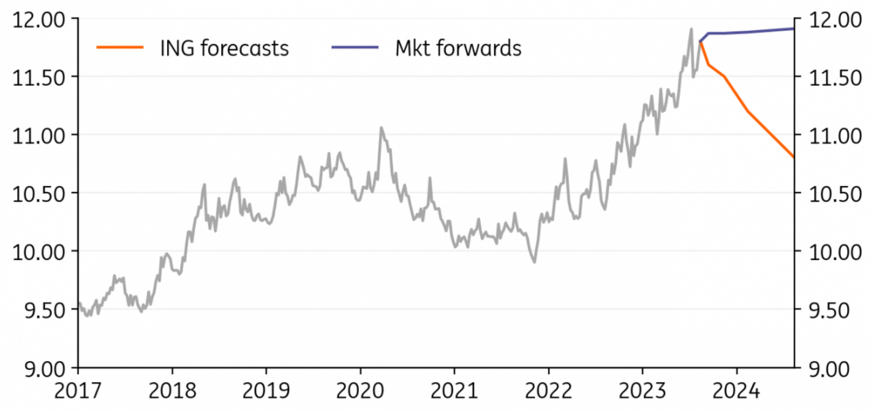
- NOK has dropped by more than 6% this past month, with its low-liquidity character leaving it highly exposed to the rocky risk environment.
- A decisive turn in the krone will need to wait for a recovery in risk assets, which may only occur in the new year. The OPEC+ output cuts may suggest a slightly better outlook for oil currencies (in the crosses) into year-end, but not enough to trigger a NOK recovery at this stage.
- Norges Bank should stick to the rate hikes it signalled at its latest meeting: 50bp in November, 25bp in December. There is some room for a hawkish surprise, but FX implications are small.



EUR/SEK: Riksbank's FX protest no help to krona

	Spot	One month bias	1M	3M	6M	12M
EUR/SEK	10.9500	Bullish	11.00	11.00	10.90	10.40

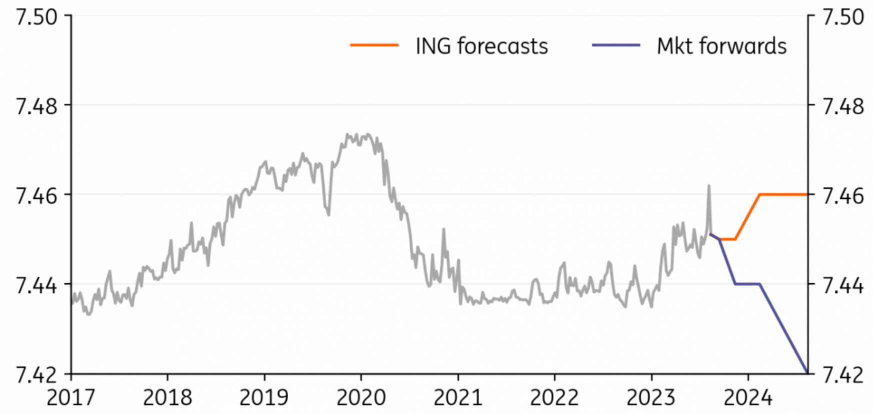
- Riksbank Governor Ingves recently said RB must keep comfortable distance to ECB with rate hikes. Not least because the RB is explicitly seeking a stronger SEK.
- In practice, rate hikes may still prove largely ineffective to strengthen SEK given the challenging risk environment. Slowing the pace of FX reserve-related SEK selling could actually do more to help SEK, but the RB has signalled reluctance in this sense.
- There is an elevated risk that EUR/SEK breaks above 11.00 before the end of the year as the energy crisis deepens and risk assets remain pressured. We look for a gradual 2023 recovery in SEK, but the timing remains highly uncertain.



EUR/DKK: DN back to FX interventions

	Spot	One month bias	1M	3M	6M	12M
EUR/DKK	7.4383	Neutral	7.44	7.44	7.44	7.45

- For the first time in 2022, Danmarks Nationalbank jumped back into the currency market, selling DKK 23bn in FX interventions to weaken DKK in September. This is half the size of the latest FX intervention (47bn in December 2021).
- For now, it looks like DN will stick to replicating the size of ECB rate increases and intervening to support EUR/DKK. However, we expect more EUR weakness into the winter and this may start to cast doubt over the sustainability of FX interventions.
- We still see a non-negligible risk that DN hikes rates by less than the ECB (10bp would be a start) in one of the coming meetings. This risk is likely higher if the ECB sticks to large hikes.



USD/CAD: Loonie's attractiveness going wasted

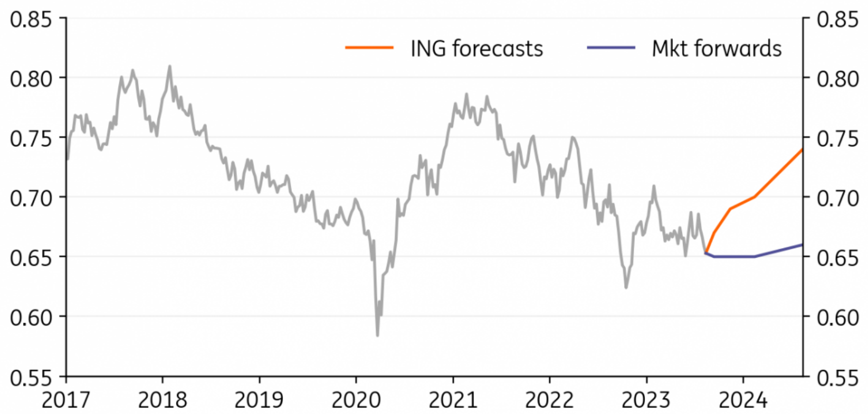
	Spot	One month bias	1M	3M	6M	12M
USD/CAD	1.3722	Mildly Bullish	1.38	1.37	1.31	1.27

- We haven't changed our view that the loonie should emerge as a key outperformer once sentiment stabilises, thanks to low exposure to Europe and China, positive impact from high energy prices and a hawkish Bank of Canada (which recently reiterated its commitment to fighting inflation despite economic pain).
- Still, CAD's high beta and USD strength will keep USD/CAD in the 1.35/1.40 region into the new year, in our view, regardless of the BoC matching the Fed's tightening.
- The recent output cuts by OPEC+ are surely a good signal for oil-sensitive currencies, and may somewhat limit the downside risks for CAD even if risk assets remain weak.

AUD/USD: Downturn should continue

	Spot	One month bias	1M	3M	6M	12M
AUD/USD	0.6323	Mildly Bearish	0.62	0.61	0.65	0.68

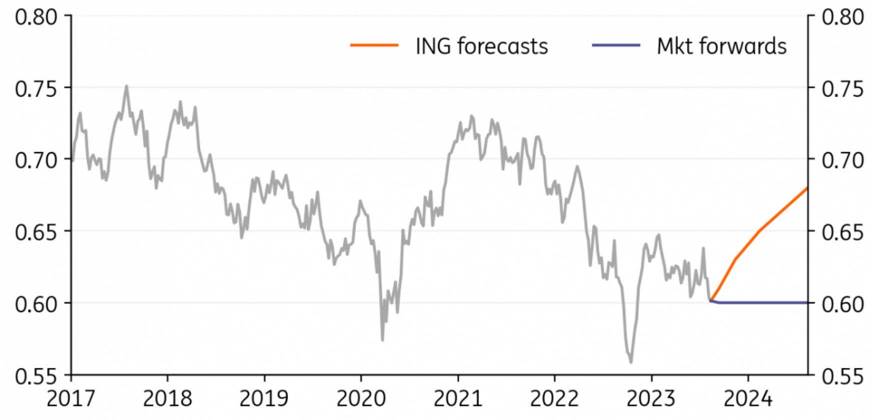
- We remain bearish on AUD/USD into year-end, as risk sentiment fragility, China's economic (and currency) woes and a strong USD all point to continuous weakness in the pair.
- We currently forecast a bottom around 0.60-0.61 around year-end before a rebound that should accelerate in the second half of 2023. A break below 0.60 this year is entirely possible though.
- The RBA surprised on the dovish side in October as it delivered a "small" 25bp hike. Indeed, policymakers in Australia have greater flexibility given policy meetings are scheduled for each month; but our base case is that 25bp increases will become the norm. The FX implications, for now, should remain quite secondary.



NZD/USD: Eyeing 0.50?

	Spot	One month bias	1M	3M	6M	12M
NZD/USD	0.5603	Mildly Bearish	0.55	0.55	0.58	0.60

- The RBNZ has stirred away from any dovish signal as it hiked by another 50bp in October and signalled more tightening is on its way. Another 50bp increase is largely expected at the November meeting.
- Like for AUD – and many other developed currencies – the role of monetary policy remains secondary compared to global risk dynamics.
- NZD/USD is looking at the 0.50 2009 lows as the next key support: that would be a 12% drop from the current levels and seems too stretched in our view. However, a move to the 0.52-0.53 area cannot be excluded should risk assets fall further.



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