8 January 2019
Article

US dollar unlikely to fall much more against G10 low yielders

Low yielding currencies such as the euro, Japanese and Swiss franc are likely to underperform high yielders and commodity currencies

Contents

- USD: Dollar downside vs G10 low yielders exhausted
- EUR: Topping out
- EMEA FX: Higher oil prices benefiting RUB, ILS and ZAR
- RON: NBR staying on hold

USD: Dollar downside vs G10 low yielders exhausted

After two straight days of material losses, the dollar has taken a breather. We see the upside of G10 low yielders (euro, Japanese and Swiss franc) against the US dollar as exhausted and look for commodity currencies (oil prices have likely troughed partly due to coming supply cuts) and higher yielding FX (benefiting from stabilising risk appetite) to outperform. The next key catalyst for further stock market gains is the evolution of US-China trade talks, with any positive headline news likely providing further support to battered risk assets. Today, President Trump delivers a televised address to the nation but any imminent resolution of the partial government shutdown seems unlikely. While not supportive for risk, what matters more at this point is the Fed's stance. Following Chair Jay Powell's speech on Friday, we don't expect the stream of Fed speakers to materially deviate from the cautious message on rates but relative optimism on growth will be non-negative for risk assets.

EUR: Topping out

We see the EUR/USD topping out against USD in terms of the near-term outlook. Today's dismal German November industrial production suggests that the risk of technical recession in Germany has increased, while the eventual restart of Fed tightening should also weigh on EUR/USD. Moreover, the upcoming EU Parliamentary elections in May and the Brexit woes are other non-positives for EUR vs USD. We project EUR/USD at 1.10 in coming months (before recovering in 2H19).

EMEA FX: Higher oil prices benefiting RUB, ILS and ZAR

While the central and eastern European FX remains fairly agnostic to the moves in oil prices, oil matters dearly for EMEA dollar-block currencies. As per our 2019 FX Outlook, our PCA analysis shows that within the EMEA space, the rouble, Israeli new shekel and South African rand are the key beneficiaries of rising oil prices (the first two via the direct oil channel, the rand via general moves in commodity prices) while the oil importing Turkish lira suffers the most. The rising oil price coupled with the risk of political noise ahead of the upcoming local elections in March should, in our view, tame the lira's upside and translate into underperformance vs the rouble.

RON: NBR staying on hold

Our economists expect the National Bank of Romania to stay on hold today, particularly in the context of the recent moves by the ruling Social Democrats, which have complicated efforts to manage monetary policy. The ROBOR-linked bank tax, announced last month, will tighten credit conditions, which means further NBR hikes could have an amplified impact. This suggests a large constraint for the NBR to hike and, in fact, opens the way for the NBR to cut the reserve requirement ratio to ease its stance. While this keeps the Romanian leu vulnerable, long EUR/RON positions remain unattractive as the spot is unlikely to outperform the very elevated forwards.

Petr Krpata, CFA
Chief EMEA FX and IR Strategist
+44 20 7767 6561
petr.krpata@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 NV 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. The producing legal entity 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 subject to limited regulation by the Financial Conduct Authority (FCA). 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.