

Forex News

EURUSD - US interest rate expectations remain decisive driver

EURJPY – the yen continues to strengthen – rumors about “helicopter money” increase uncertainty

EURCHF – Swiss franc remains relatively stable



Analyst:
Rainer Singer
rainer.singer@erstegroup.com

Brexit referendum had only short-lived impact on EURUSD

EURUSD responded to the surprising outcome of the Brexit referendum with a significant appreciation of the dollar. However, as sentiment in the financial markets stabilized relatively quickly again, US interest rate expectations promptly became dominant again; particularly in view of the fact that economic data indicated that the economy of the euro zone has (so far) suffered no damage.

Our expectation remains that the next US rate hike will be implemented in December, which should lend some support to the dollar towards the end of the year. After the recently released US labor market data, which were very strong, there remains a risk though that the Federal Reserve will act in September already. If the next payrolls report exhibits strong momentum again, a rate hike in September could be possible. However, given the Fed's cautious approach to date, we believe that this remains less probable than a December rate hike. Should it nevertheless happen, the dollar would probably strengthen earlier than we are currently expecting. Even in that case, the advance should be moderate though. The US presidential election campaign plays no noticeable role for the dollar at the moment, which may be due to the fact that Donald Trump is currently trailing significantly in polls. Should this change, the associated political uncertainty could weigh on the dollar to some extent. Per experience political factors in the US have no persistent impact on the exchange rate though. Thus the focus of currency markets should remain on economic developments and with that the outlook for interest rates, while any reaction of the exchange rate to political events is likely to be temporary.

EURUSD – since 2000



Source: Bloomberg, Erste Group Research

EURUSD – since July 2011



Source: Bloomberg, Erste Group Research



Analyst:

Gerald Walek

gerald.walek@erstegroup.com

JPY – the yen continues to strengthen – rumors about “helicopter money” increase uncertainty

As was to be expected based on leading indicators, Japan's economy stagnated in Q2 2016, after exhibiting surprisingly strong growth of +0.5% q/q in Q1 2016. Sentiment indicators currently point at least temporarily to a slight improvement of the situation in Q3 2016. For the year 2016 as a whole the IMF expects Japan to post GDP growth of +0.3%.

The most important event in July was the clear election victory achieved by prime minister Shinzo Abe's LDP. The markets interpreted this as a sign that additional fiscal and monetary policy measures would be in the offing in Japan. These expectations were stoked further by press reports about a meeting between former Fed chairman Ben Bernanke - who recently created a stir with a blog entry about the introduction of “helicopter money”¹ - and the governor of the BoJ shortly after the election. Essentially “helicopter money” would involve a ‘money-financed fiscal program’, in other words, fiscal stimulus financed by the central bank. Contrary to the approach pursued hitherto, this fiscal program would not lead to an increase in public debt, as it wouldn't be financed by issuing new government bonds, but with money the central bank would make directly available to the government. In its last meeting on 29. July, the BoJ eased monetary policy only marginally, but announced that it would conduct a review of its current monetary policy stance as well as the economic environment in September.

In the wake of the Brexit referendum, the yen has rallied strongly vs. the euro, to approx. the 110 level. In the process the yen has broken important support at the 120 level, which was followed by an acceleration of the decline, in line with our expectations. All important moving averages (20-, 50- and 200-day moving averages) remain downward sloping, which from a technical perspective points to a further strengthening of the yen vs. the euro. The 110 level provides very strong downside support, which should at least hold in the short term. If the BoJ were to decide to expand its monetary policy measures though, it could easily trigger yen depreciation and a counter-trend move interrupting the recent downtrend. The analyst consensus currently expects the cross rate to stabilize at a level of approx. EURJPY 112 by year-end.

EURJPY – since 2000



Source: Bloomberg, Erste Group Research

EURJPY – since July 2011



Source: Bloomberg, Erste Group Research

¹ <http://www.brookings.edu/blogs/ben-bernanke/posts/2016/04/11-helicopter-money>



Analyst:

Margarita Grushanina

margarita.grushanina@erstegroup.com

EURCHF – Swiss franc remains relatively stable

After appreciating strongly from 1.11 to 1.08 euro per Swiss franc in June, triggered by Brexit-related fears, EURCHF has leveled out between the 1.08 and 1.09 levels in recent weeks. Following of the Brexit referendum, the exchange rate was supported by SNB intervention in the foreign exchange markets. In the course of a press conference in June on the heels of the release of the SNB's monetary policy assessment, SNB chairman Thomas Jordan stated that there was no upper limit to the extent of the SNB's currency market interventions. He also reiterated that the SNB continued to be prepared to intervene in the foreign exchange markets and that the Swiss franc remained significantly overvalued.

The recent significant tightening of the inflation differential between Switzerland and the euro zone currently suggests that appreciation pressures on the Swiss franc should ease. We therefore expect a moderate weakening of the Swiss franc toward the EURCHF 1.10 level by the end of the quarter. In spite of the fact that the situation has calmed down somewhat, a variety of economic and political risks, including risks for the future of the European Union, remain in place. We currently expect that the Swiss franc will weaken slightly further over the coming year (Q2 2017: 1.12). However, a minimum exchange rate is no longer enforced. Should certain risks materialize (e.g. geopolitical conflicts, turmoil in the EU), the Swiss franc could once again appreciate rapidly and strongly.

EURCHF – since 2000



Source: Bloomberg, Erste Group Research

EURCHF – since July 2011



Source: Bloomberg, Erste Group Research

Exchange rate forecasts²

	current	Sep.16	Dec.16	Mar.17	Jun.17
EURUSD	1.13	1.12	1.10	1.12	1.14
EURCHF	1.08	1.10	1.11	1.11	1.12
EURJPY	current	Sep.16	Dec.16	Mar.17	Jun.17
Bloomberg Survey		123.0	112.0	113.0	113.0
Spot/Forward	113.3	124.0	124.0	124.0	124.0

Source: Bloomberg, Erste Group Research

Interest rate forecasts

	current	Sep.16	Dec.16	Mar.17	Jun.17
3M Euribor	-0.30	-0.25	-0.25	-0.25	-0.22
3M Libor US	0.81	0.66	0.94	1.19	1.44
3M Libor CH	-0.74	-0.75	-0.75	-0.75	-0.50

Source: Bloomberg, Erste Group Research

² By regulations we are obliged to issue the following statement: Forecasts are no reliable indicator for future performance

Erste Group Research

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Contacts

Group Research

Head of Group Research

Friedrich Mostböck, CEFA +43 (0)5 0100 11902

Major Markets & Credit Research

Head: Gudrun Egger, CEFA +43 (0)5 0100 11909

Ralf Burchert, CEFA (Agency Analyst) +43 (0)5 0100 16314

Hans Engel (Senior Analyst Global Equities) +43 (0)5 0100 19835

Christian Enger, CFA (Covered Bonds) +43 (0)5 0100 84052

Margarita Grushanina (Economist AT, CHF) +43 (0)5 0100 11957

Peter Kaufmann, CFA (Corporate Bonds) +43 (0)5 0100 11183

Stephan Lingnau (Global Equities) +43 (0)5 0100 16574

Carmen Riefler-Kowarsch (Covered Bonds) +43 (0)5 0100 19632

Rainer Singer (Senior Economist Euro, US) +43 (0)5 0100 17331

Bernadett Povaszai-Römhild (Corporate Bonds) +43 (0)5 0100 17203

Elena Statelov, CIAA (Corporate Bonds) +43 (0)5 0100 19641

Gerald Walek, CFA (Economist Euro) +43 (0)5 0100 16360

Katharina Böhm-Klamt (Quantitative Analyst Euro) +43 (0)5 0100 19632

Macro/Fixed Income Research CEE

Head CEE: Juraj Kotian (Macro/FI) +43 (0)5 0100 17357

Zoltan Arokszallasi (Fixed income) +43 (0)5 0100 18781

Katarzyna Rzentarzewska (Fixed income) +43 (0)5 0100 17356

CEE Equity Research

Head: Henning Eßkuchen +43 (0)5 0100 19634

Franz Hörl, CFA (Basic Resources, Real Estate) +43 (0)5 0100 18506

Daniel Lion, CIAA (Technology, Ind. Goods&Services) +43 (0)5 0100 17420

Christoph Schultes, MBA, CIAA (Industrials) +43 (0)5 0100 11523

Vera Sutedia, CFA, MBA (Telecom) +43 (0)5 0100 11905

Thomas Unger, CFA (Banks, Insurance) +43 (0)5 0100 17344

Vladimira Urbankova, MBA (Pharma) +43 (0)5 0100 17343

Martina Valenta, MBA (Real Estate) +43 (0)5 0100 11913

Editor Research CEE

Brett Aarons +420 956 711 014

Research Croatia/Serbia

Head: Mladen Dodig (Equity) +381 11 22 09178

Head: Alen Kovac (Fixed income) +385 72 37 1383

Anto Augustinovic (Equity) +385 72 37 2833

Milan Deskar-Skrbic (Fixed income) +385 72 37 1349

Magdalena Dolenc (Equity) +385 72 37 1407

Ivana Rogic (Fixed income) +385 72 37 2419

Davor Spoljar, CFA (Equity) +385 72 37 2825

Research Czech Republic

Head: David Navratil (Fixed income) +420 956 765 439

Head: Petr Bartek (Equity) +420 956 765 227

Renáta Ďurčová (Equity) +420 956 765 213

Jiri Polansky (Fixed income) +420 956 765 192

Dana Hajkova (Fixed income) +420 956 765 172

Jana Urbankova (Fixed income) +420 956 765 456

Research Hungary

Head: József Miró (Equity) +361 235 5131

Gergely Ürmössi (Fixed income) +361 373 2830

András Nagy (Equity) +361 235 5132

Tamás Pletser, CFA (Oil&Gas) +361 235 5135

Research Poland

Head: Magdalena Komaracka, CFA (Equity) +48 22 330 6256

Marek Czachor (Equity) +48 22 330 6254

Tomasz Duda (Equity) +48 22 330 6253

Mateusz Krupa (Equity) +48 22 330 6251

Karol Brodziński (Equity) +48 22 330 6252

Research Romania

Head: Mihai Caruntu (Equity) +40 3735 10427

Head: Dumitru Dulgheru (Fixed income) +40 3735 10433

Chief Analyst: Eugen Sinca (Fixed income) +40 3735 10435

Dorina Ilasco (Fixed Income) +40 3735 10436

Research Slovakia

Head: Maria Valachyova, (Fixed income) +421 2 4862 4185

Katarina Muchova (Fixed income) +421 2 4862 4762

Research Turkey

Umut Ozturk (Equity) +90 212 371 25 30

Oguzhan Evranos (Equity) +90 212 371 25 42

Treasury - Erste Bank Vienna

Saving Banks & Sales Retail

Head: Christian Reiss +43 (0)5 0100 84012

Equity Retail Sales

Head: Kurt Gerhold +43 (0)5 0100 84232

Fixed Income & Certificate Sales

Head: Uwe Kolar +43 (0)5 0100 83214

Treasury Domestic Sales

Head: Markus Kaller +43 (0)5 0100 84239

Corporate Sales AT

Head: Christian Skopek +43 (0)5 0100 84146

Fixed Income & Credit Institutional Sales

Institutional Sales

Head: Manfred Neuwirth +43 (0)5 0100 84250

Bank and Institutional Sales

Head: Jürgen Niemeier +49 (0)30 8105800 5503

Institutional Sales Western Europe AT, GER, FRA, BENELUX

Head: Thomas Almen +43 (0)5 0100 84323

Charles-Henry de Fontenilles +43 (0)5 0100 84115

Marc Pichler +43 (0)5 0100 84118

Rene Klasen +49 (0)30 8105800 5521

Dirk Seefeld +49 (0)30 8105800 5523

Bernd Bollhof +49 (0)30 8105800 5525

Bank and Savingsbanks Sales

Head: Marc Frieberthäuser +49 (0)711 810400 5540

Sven Kienzle +49 (0)711 810400 5541

Michael Schmotz +43 (0)5 0100 85542

Ulrich Inhofner +43 (0)5 0100 85544

Klaus Vosseler +49 (0)711 810400 5560

Andreas Goll +49 (0)711 810400 5561

Mathias Gindele +49 (0)711 810400 5562

Bernd Thaler +43 (0)5 0100 85583

Fabian Bütger +49 (0)151 53810580

Jörg Moritzen +49 (0)30 8105800 5581

Institutional Sales CEE and International

Head: Jaromir Malak +43 (0)5 0100 84254

Central Bank and International Sales

Head: Margit Hraschek +43 (0)5 0100 84117

Christian Kössler +43 (0)5 0100 84116

Bernd Thaler +43 (0)5 0100 84119

Institutional Sales PL and CIS

Pawel Kielek +48 22 538 6223

Michal Jarmakowicz (Fixed Income) +43 50100 85611

Institutional Sales Slovakia

Head: Peter Kniz +421 2 4862 5624

Monika Smelikova +421 2 4862 5629

Institutional Sales Czech Republic

Head: Ondrej Cech +420 2 2499 5577

Milan Bartos +420 2 2499 5562

Barbara Suvadova +420 2 2499 5590

Institutional Asset Management Sales

Czech Republic

Head: Petr Holecek +420 956 765 453

Martin Perina +420 956 765 106

Petr Valenta +420 956 765 140

David Petracek +420 956 765 809

Institutional Sales Croatia

Head: Antun Buric +385 (0)7237 2439

Željko Pavičić +385 (0)7237 1494

Ivan Jelavic +385 (0)7237 1638

Institutional Sales Hungary

Attila Hollo +36 1 237 8209

Borbala Csizmadia +36 1 237 8205

Institutional Sales Romania

Head: Ciprian Mitu +43 (0)50100 85612

Stefan Racovita +40 373 516 531

Institutional Solutions and PM

Christopher Lampe-Traupe +43 (0)50100 85507

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Erste Group Homepage: www.erstegroup.com