Market Guide

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Important disclosures and certifications are contained on page 10 of this report.

Headwinds for Scandies

Headline inflation is easing but service inflation remains worryingly high

Headline inflation has continued to move lower in most regions driven by weaker energy-, freight rate- and goods price impulses. Meanwhile, importantly, core inflation remains sticky as evident from the continued rise in service inflation in most countries. These opposing forces pose a challenge for central banks when balancing the fight against elevated core inflation against a weakening growth backdrop – especially given the time lag from policy changes to when the impact has fully fed through to the real economy. In line with market expectations, we think the Fed has delivered its last rate hike for this hiking cycle. However, we think the current 65bp of rate cuts priced for the rest of the year is too aggressive. Declining headline inflation has eased the pressure on most central banks to deliver further rate hikes. Meanwhile, Norges Bank and Bank of England increasingly look challenged by the inflation outlook amid resilient growth and - in terms of Norges Bank – a weakening currency. Worries with respect to the banking sector remains a market theme but in our view this is a natural symptom of the sharp tightening of monetary policy over the past year.

USD positive, SEK negative and near-term headwinds for NOK

EUR/USD has recently faced renewed headwinds, pushing the cross back below 1.10. The move lower was not least aided by relative rates, relative growth surprises and the outlook for relative liquidity situations. Likewise, EUR/GBP has recently breached the 0.87 level, the lowest level since December 2022. Although headwinds have eased slightly, the NOK has suffered from continued large fiscal selling from Norges Bank. EUR/SEK has moved lower over the last weeks on central bank repricing. The JPY has been the big underperformer over the last month driven by a combination of higher global yields and a soft Bank of Japan.

We maintain our strategic case for a lower EUR/USD based on relative terms of trade, real rates and relative unit labour costs. Likewise, we see the prospect of the USD finding further near-term support despite the impending Fed pause. We remain bearish SEK over the medium term on the back of relative monetary policy, the bleak growth outlook globally and a relatively worse outlook for the Swedish economy compared to peers. We have a near-term negative stance on NOK given a mismatch in fiscal FX transactions and shaky global risk appetite. However, we still believe in a more bullish secular case for energy and by extension NOK over the coming 5 years, but highlight the risk that our bullish NOK view could take longer to play out.

A key assumption is that of a re-tightening of global financial conditions. Risks to this assumption primarily lie in the combination of a sharp drop in core inflation and a more resilient global economy than what we pencil in.

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USD strength in store

USD

- Inflation looks set to head lower in both the US and the euro area in the coming quarters although core inflation seems to be more sticky in the euro area. US economic data on growth, labour and inflation have generally moderated lately, but the underlying strength of the US economy seems intact. In the euro area, short-term macro momentum generally still looks positive but, there have been some weakening signs as of late. We expect this weakness to become more pronounced in H2 as the full impact of the last year's monetary policy tightening hits the real economy. Overall, we think the US economy will prove more robust compared to the European counterpart in H2.

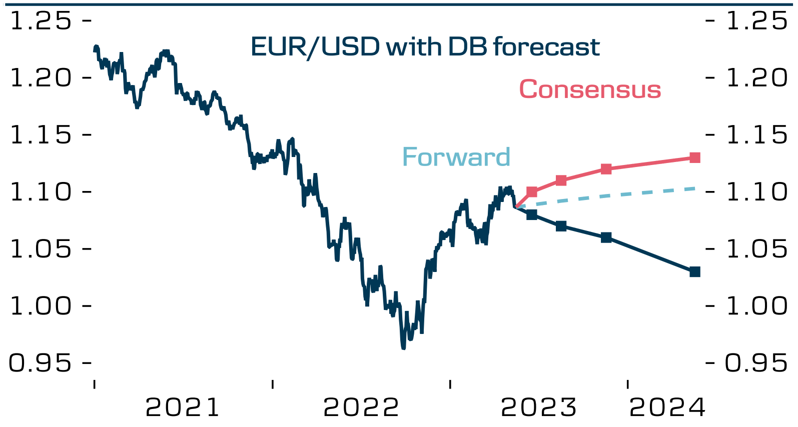
- In line with market expectations, we think the Fed has delivered its last rate hike for this hiking cycle. However, we think the current 3x25bp rate cuts priced for the rest of the year seem too aggressive. If we are right in this call, that will add some USD support in H2. For the ECB, we think there are three 25bp rate hikes left, bringing the policy rate up to 4%.

- We maintain the strategic case for a lower EUR/USD based on relative terms of trade, real rates and relative unit labour costs. Despite the impending Fed pause, we see the prospect of the USD finding further near-term support as we expect the Fed to hold rates steady into 2024. Furthermore, we think the outlook of the US economy looks less gloomy.

- We continue to forecast the cross at 1.03 in 6-12M.

- Among the biggest risks related to our forecast profile are a continuation of the relative asset demand of euro area assets, which has been a tailwind for the EUR this year. Furthermore, substantial weakness in US economy also poses a topside risk for the cross caused by e.g. bank sector uncertainties.

EUR/USD



	1M	3M	6M	12M
Danske Bank	1.08	1.07	1.06	1.03
Consensus	1.10	1.11	1.12	1.13
Forward	1.09	1.09	1.10	1.10

Hedging recommendations

Income: Sell USD via risk reversals.

Expenses: Purchase USD via forwards.

Source: Macrobond, Bloomberg, Danske Bank
Note: Past performance is not a reliable indicator of current or future results

GBP

Range bound

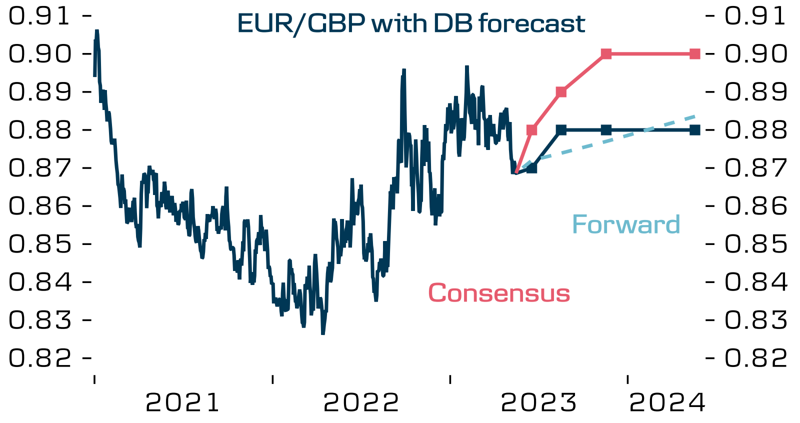
- The UK economy has held up better than expected, although the cyclical outlook remains weak. The latest labour market report showed a slightly higher unemployment rate at 3.9% and the first fall in total payrolled employees since February 2021. Wage growth remains north of 6% and continues to accelerate in the public sector. Both headline and core inflation came in higher than expected, with service inflation continuing to show persistence. Overall, we do not see the outlook for the UK to be substantially different from the Euro Area, although we expect the recession to reach UK sooner.

- At its latest meeting the Bank of England (BoE) hiked the Bank Rate by 25bp. We expect the BoE to hike the Bank Rate by a final 25bp in June bringing the policy rate to 4.75%, which is in line with market pricing. Combined with the, in our view, slightly dovish pricing on the ECB, we see relative rates as a positive for the cross.

- The past month, EUR/GBP has moved lower, briefly breaching below the 0.87 mark. The move lower follows economic conditions and momentum broadly holding up for the UK economy as well as relative rates lending support to GBP. Further out, EUR/GBP is, in our view, stuck between opposing forces. On the one hand, we expect relative rates and near-term broad EUR optimism to act as a tailwind for the cross. On the other hand, we see the global growth slowdown and the relative appeal of UK assets acts as a headwind. At present, we do not see the relative growth outlook or global investment environment to create significant divergence between EUR and GBP. We thus expect the cross to remain range bound around 0.87-88.

- The key risk that could see EUR/GBP trade substantially above our projection is a sharp sell-off in risk where capital inflows fade and liquidity becomes scarce.

EUR/GBP



	1M	3M	6M	12M
Danske Bank	0.87	0.88	0.88	0.88
Consensus	0.88	0.89	0.90	0.90
Forward	0.87	0.87	0.88	0.88

Hedging recommendations

Income: Sell GBP via FX forwards.

Expenses: Buy GBP via risk reversals. Alternatively consider hedging via forwards.

Source: Macrobond, Bloomberg, Danske Bank
Note: Past performance is not a reliable indicator of current or future results

SEK

We remain negative on the SEK

- Sweden may still best be described as a two-speed economy with weakness mainly found within households and the real estate sector, whereas manufacturers and the labour market continue to hold up. However, a very weak set of private consumption data for March was unfortunately associated with soft industrial orders and production data, a negative sign in a global slowdown especially if domestic demand does not provide a cushion and where latent fiscal muscles cannot be applied in an inflationary environment. We forecast a 1% contraction in 2023 as Swedish GDP growth is set to underperform European peers, a headwind for the SEK.

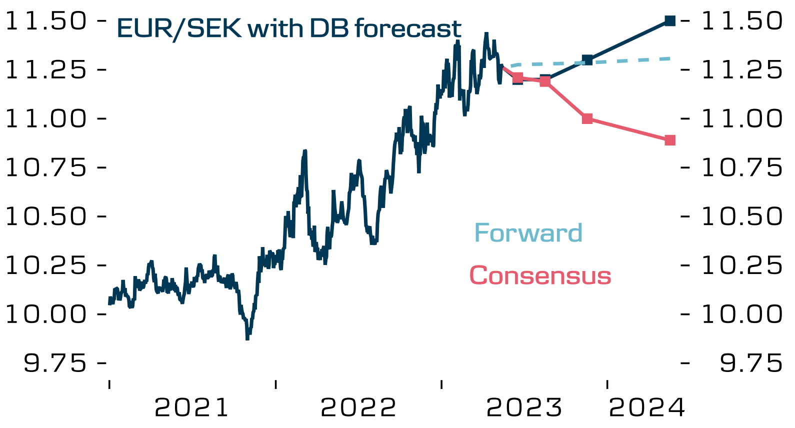
- Inflation has probably peaked and consecutive price changes seem to lose momentum. We predict a rather swift drop in inflation during the second half of 2023. We expect the Riksbank to raise policy rates by 25bp in June and 25bp in September. The risk to the forecast is tilted to the downside, which is in contrast to the ECB where we look for 3x25bp.

- Our short-term model for the SEK has had fair value close to 11.20 for the last few weeks, which is in line with our 1M (mid-May) target. Relative monetary policy is in the driver's seat and we deem it slightly supportive for EUR/SEK in a 3-6M perspective. In addition, the bleak growth outlook globally and for Sweden in particular is adding to SEK headwinds and remains a factor why we expect EUR/SEK to move higher over the 12M horizon.

- We expect EUR/SEK to move towards 11.50 over the coming year.

- Risks are two-sided and substantial not least related to inflation and central bank surprises.

EUR/SEK



	1M	3M	6M	12M
Danske Bank	11.20	11.20	11.30	11.50
Consensus	11.21	11.19	11.00	10.89
Forward	11.28	11.28	11.29	11.31

Hedging recommendations

Income: Utilise any rebound in SEK to sell SEK via FX forwards.

Expenses: Buy SEK via risk reversals.

Source: Macrobond, Bloomberg, Danske Bank
Note: Past performance is not a reliable indicator of current or future results

NOK

Headwinds the coming months

- The Norwegian economy continues to do better-than-expected and not least feared. Leading indicators are clearly pointing towards below-trend-growth in the coming quarters yet so far the labour market has only shown marginal weakness. The housing market has also done better-than-expected amid a tight supply side – albeit we still think house prices have yet to bottom. April core inflation surprised to the topside as imported inflation looks set to remain elevated for longer. Meanwhile, we do see signs of domestic inflation peaking with not least domestic goods inflation having come much lower.

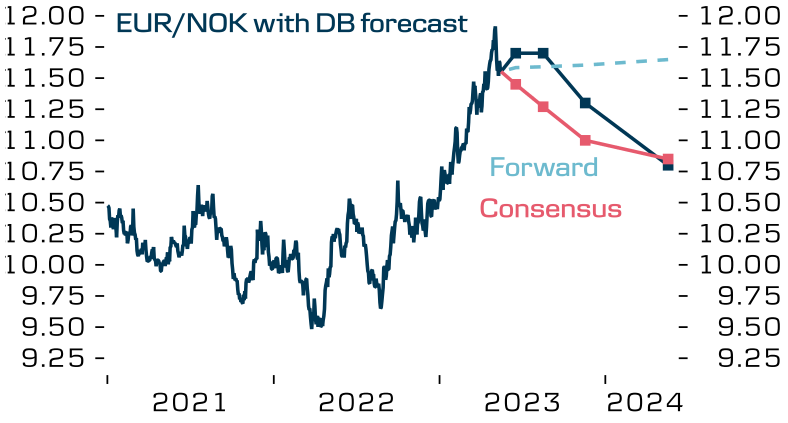
- In April, Norges Bank (NB) hiked the sight deposit rate to 3.25% whilst signalling that the balance of risk clearly has become skewed to the topside. This suggests that NB could not only hike policy rates in June but that the hiking cycle could extend into Q3 with hikes in September and/or August. If NOK does not strengthen or growth slow down significantly in the coming months we stand ready to add more tightening into our forecast profile for NB.

- We have a near-term negative stance on NOK given a mismatch in fiscal FX transactions and shaky global risk appetite amid slowing global growth, contractionary monetary and credit signals and bank sector concerns. We still believe in a more positive case for energy and by extension NOK for the coming 5 years but we highlight the risk that our NOK positive view could take longer to play out.

- We forecast EUR/NOK at 11.70 in 3M and 10.80 in 12M.

- Near-term risks are closely connected to the global investment environment and changes to the fiscal NOK FX sales amount.

EUR/NOK



	1M	3M	6M	12M
Danske Bank	11.70	11.70	11.30	10.80
Consensus	11.45	11.27	11.00	10.85
Forward	11.58	11.59	11.60	11.65

Hedging recommendations

Income: Sell NOK via knock-in forwards.

Expenses: Buy NOK via FX forwards. Consider hedging short-term income via risk reversals.

Source: Macrobond, Bloomberg, Danske Bank Note: Past performance is not a reliable indicator of current or future results

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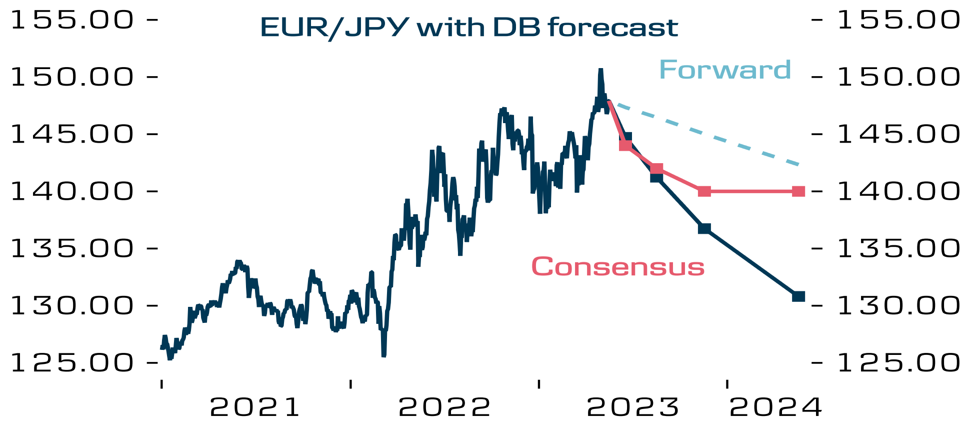
Others

EUR/JPY



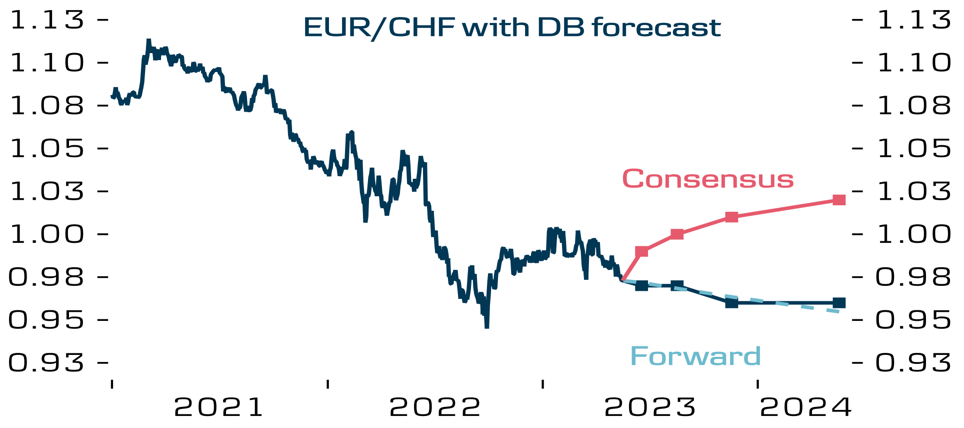
Hedging recommendations

Income: Sell JPY via risk reversals.

Expenses: Buy JPY via forwards.

Source: Macrobond, Bloomberg, Danske Bank
Note: Past performance is not a reliable indicator of current or future results

EUR/CHF



Hedging recommendations

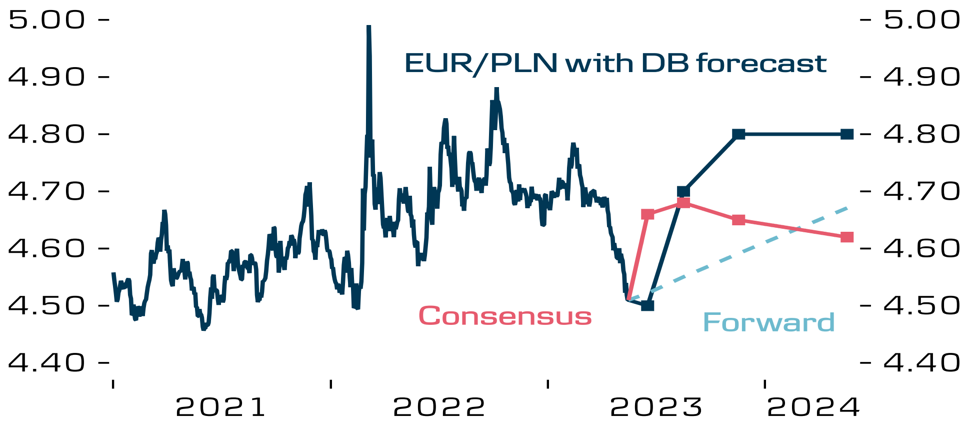
Income: Sell CHF via risk reversals.

Expenses: Buy CHF via forwards.

Source: Macrobond, Bloomberg, Danske Bank
Note: Past performance is not a reliable indicator of current or future results

Others

EUR/PLN



Hedging recommendations

Income: Sell PLN via forwards, alternatively via KI-forwards.

Expenses: Buy PLN via risk reversals.

Source: Macrobond, Bloomberg, Danske Bank
Note: Past performance is not a reliable indicator of current or future results

FX Forecast Table

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Exchange rates vs EUR

G10	Spot	+1m	+3m	+6m	+12m
				Last Update:	16/05/2023
Exchange rates vs EUR					
EUR/USD	1.09	1.08	1.07	1.06	1.03
EUR/JPY	147.84	145	141	137	131
EUR/GBP	0.87	0.87	0.88	0.88	0.88
EUR/CHF	0.97	0.97	0.97	0.96	0.96
EUR/SEK	11.26	11.20	11.20	11.30	11.50
EUR/NOK	11.55	11.70	11.70	11.30	10.80
EUR/DKK	7.45	7.4450	7.4450	7.4450	7.4500
EUR/AUD	1.63	1.64	1.65	1.66	1.63
EUR/NZD	1.74	1.74	1.75	1.77	1.75
EUR/CAD	1.47	1.46	1.46	1.45	1.41
EM	**Spot**	**+1m**	**+3m**	**+6m**	**+12m**
EUR/PLN	4.50	4.50	4.70	4.80	4.80
EUR/HUF	369.48	370	380	400	420
EUR/CZK	23.65	23.4	23.4	23.8	23.8
EUR/TRY	21.48	21.4	21.7	22.6	23.5
EUR/ZAR	20.80	20.5	20.2	19.9	19.3
EUR/CNY	7.58	7.55	7.54	7.53	7.36
EUR/INR	89.52	89.0	88.3	88.0	86.0

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