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20 November 2024
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Market Guide

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Danske Bank

Red sweep widens Atlantic FX gap

Republican sweep well-received by markets

Trump has secured another term in the White House with a Republican majority in congress. The Republican Sweep was well-received by markets sending rates and inflation expectations higher in the US and equities higher across the board with the outlook for more expansionary fiscal policy. On this side of the Atlantic, European rates and inflation expectations tracked lower following the election with the already struggling European economy set to face further headwinds from a hawkish trade policy. The election win further highlights the increasing divergence between the US and European economy in terms of structural growth, productivity and regulation. Geopolitics remain in focus for markets with the war in Ukraine and the Middle East continuing with heightened focus on implications from the incoming Trump administration.

The past month, the USD has been the clear outperformer following the Trump election win securing a Republican Sweep with EUR/USD breaking firmly below the 1.06 mark. In the UK, the Labour government spooked markets by delivering an expansionary budget largely funded by borrowing, which led to a sharp rise in UK yields and triggered a sell-off in GBP FX. EUR/SEK has edged higher the past month, trading north of the 11.60 mark. USD/JPY continues to edge higher on cautious commentary from the BoJ and US rates tracking higher.

Outlook: medium-term bullish on the USD and bearish on Scandies

The US election outcome reinforces our bearish outlook on EUR/USD, given anticipated pro-growth and inflationary policies in the US, along with our expectation of relatively stronger US growth dynamics compared to the euro area in the coming year. In the near term, however, we believe markets may have become overly hawkish on Fed pricing, and with downside risks to the cyclical US growth outlook, the USD rally could stall toward year-end. We remain medium- to long-term negative on NOK and think a continuation of the latest rally will prove but temporary in nature. For the SEK, we expect a short-term correction higher but expect a continued weak cyclical outlook, a stronger USD, and a Riksbank continuing to front run peers to remain medium-term headwinds for the SEK.

Risks to our forecasts primarily lie in a sharper economic downturn than what we pencil in. A much harder landing than what we pencil in would require sharp easing of global monetary conditions, which would likely entail a much weaker USD (after an initial squeeze higher) and much weaker cyclically sensitive currencies than in our base case. With the US Red sweep the risk of a re-acceleration of US inflation and hence USD real rates in the coming years has risen.

USD

We project a stronger USD over the next year

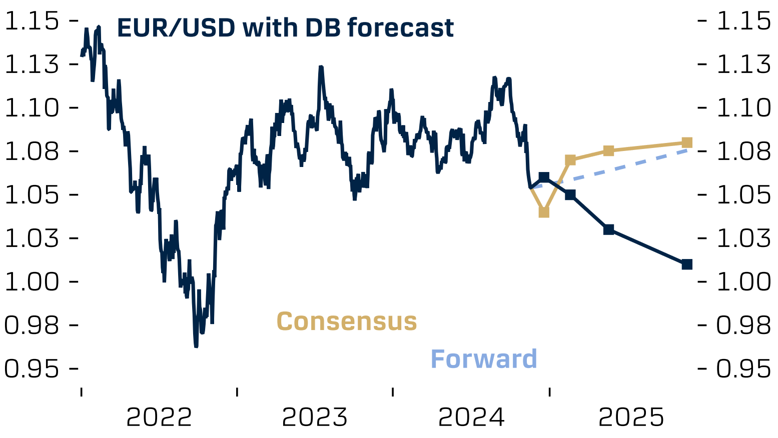
- The US economy is no longer overheated, and activity data has slowly begun to show signs of cooling, although the economy remains on a relatively strong footing. On the inflation front, a downward trajectory is likely to be maintained. Overall, recent macro data suggests that the Fed can gradually normalize monetary policy toward a more neutral stance. In the euro area, recent data indicates clear signs of weaker growth momentum and moderating labour market dynamics. Coupled with easing inflation data, with headline inflation declining below 2% for the first time in three years, the pressure on the ECB to move more quickly toward a neutral policy stance has increased.

- Following the 50bp Fed cut in September, the Fed reduced its rate-cutting pace with an anticipated 25bp cut in November. Strong US data since the September meeting has led markets to significantly reprice the outlook for further rate cuts, with around 35bp priced over the next three FOMC meetings. We expect the Fed to deliver a 25bp cut at each meeting through June of next year. Similarly, we anticipate the ECB to implement back-to-back 25bp cuts until summer 2025. If our expectations – which are below consensus for both the Fed and ECB – are correct, monetary policy alone could help stabilize EUR/USD toward year-end but is unlikely to have a notable impact over the longer term.

- We maintain a bearish medium-term view on EUR/USD, expecting the cross to gradually decline toward 1.01 over a 12M horizon. The US election outcome reinforces our bearish outlook, given anticipated pro-growth and inflationary policies in the US, along with our expectation of relatively stronger US growth dynamics compared to the euro area in the coming year. In the near term, however, we believe markets may have become overly hawkish on Fed pricing, and with downside risks to the cyclical US growth outlook, the USD rally could stall toward year-end.

- Significant weakness in the US economy poses a risk to our forecast, as does a marked improvement in the euro area economy, potentially supported by a rebound in the fragile global manufacturing sector.

EUR/USD



	1M	3M	6M	12M
Danske Bank	1.06	1.05	1.03	1.01
Consensus	1.04	1.07	1.08	1.08
Forward	1.06	1.06	1.06	1.08

Hedging recommendations

Income: We recommend hedging via risk reversals.

Expenses: We recommend purchasing USD forwards.

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

GBP tailwinds continue to prevail

GBP

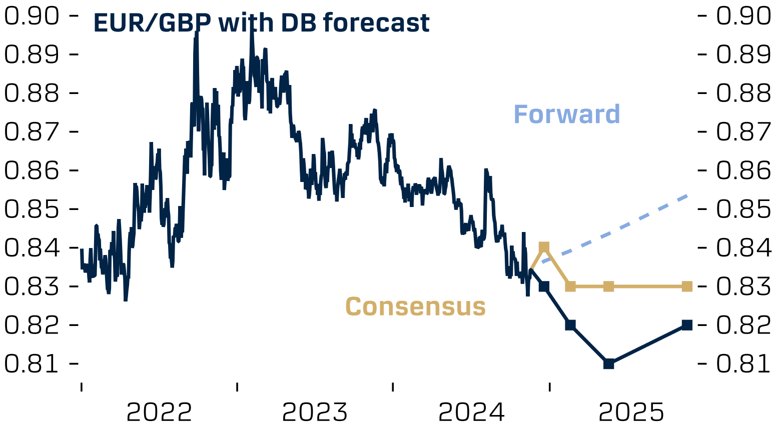
- After a strong start to the year, the UK economy slowed to 0.1% q/q in Q3, dragged by volatility in manufacturing and net trade. With underlying domestic demand holding up, we expect a rebound in growth in Q4. Inflationary pressures remain high, and we expect service inflation to remain sticky around 5% for the rest of 2024. A pickup in growth and still sticky underlying inflation is further amplified by the expansionary budget presented by the new Labour government in late October. The labour market continues its gradual loosening with vacancies moving lower and wage disinflation in both the public and private sectors.

- The Bank of England (BoE) decided to cut the Bank Rate by 25bp to 4.75% in November, in line with our expectation. The MPC delivered a hawkish twist to its guidance with the majority of the MPC signalling their inclination towards a gradual cutting cycle. Our base case of a continuous gradual easing cycle is further amplified by the expansionary fiscal measures presented by the government last month. We continue to expect the BoE to remain on hold in December and deliver the next 25bp cut in February. We see relative rates as a neutral for EUR/GBP in the near-term but a tailwind further out as we think markets underestimate the degree of easing in 2025.

- EUR/GBP jumped higher in late October after the Labour government delivered an expansionary budget largely funded by borrowing but has since fully retraced the move. GBP remains supported by the BoE's cautiously hawkish stance and UK growth outperformance relative to the eurozone. We expect these forces to keep weighing on the cross in the coming months, further amplified by continued tight credit spreads and a USD positive environment. Longer-term some of these tailwinds look set to fade and we expect not least a more dovish BoE to eventually weigh on GBP.

- The key risk to our forecasts in the near-term is centred around policy action from the BoE. If the BoE opts for a more front-loaded cutting cycle, this would act as a headwind for GBP. Other risks are closely related to the developments in the global investment environment, credit spreads and the relative growth outlook between the euro area and the UK.

EUR/GBP



	1M	3M	6M	12M
Danske Bank	0.83	0.82	0.81	0.82
Consensus	0.84	0.83	0.83	0.83
Forward	0.84	0.84	0.84	0.85

Hedging recommendations

Income: We recommend to hedge via risk reversals. Utilise a potential short-term rise in GBP by lifting hedge ratios

Expenses: We recommend to hedge via FX forwards.

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

SEK

Potential SEK-strengthening near-term

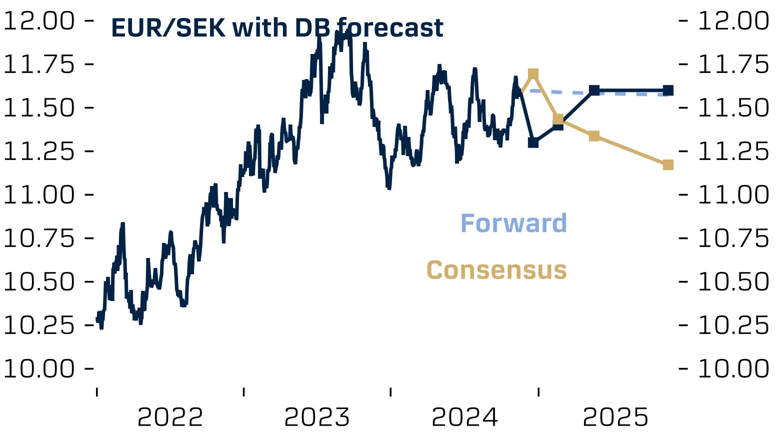
- Swedish macro has disappointed recently, and the long-awaited cyclical rebound has yet to materialize. The weak growth prospects have evidently started to unnerve the Riksbank somewhat, as it was cited as the main reason for them to 'go big' by cutting 50bp at the November meeting. Despite recent macro disappointments, we continue to pencil in a substantial growth recovery in 2025, where we also see the Swedish economy outperforming the eurozone. However, this is probably not enough to turn into an outright SEK tailwind as the global cyclical outlook with a continued US outperformance tend to be SEK negative.

- The Riksbank opted for 50bp in November, citing weaker-than-expected Swedish macro as the reason why. Despite current and still fragile growth prospects, we see the November move as a 'one-off' and expect them to revert to 25bp increments for the coming meetings, with the next cut already in December. We are also looking forward to the Riksbank's updated estimate of the Swedish neutral rate, which they have promised to discuss at the December meeting. This estimate will give further insights on what level the Riksbank sees for the terminal rate. In 2025, we pencil in three additional rate cuts (Jan, Mar & Jun), bringing the terminal rate to 1.75%.

- We remain strategically bearish on the SEK. However, we argue that the recent broad SEK selloff has been exaggerated. Our relative rates model has fair value for EUR/SEK at 11.25. Hence, the cross has reached stretched overbought levels, where historically spot has been prone to a significant correction. Additionally, the SEK enters its most constructive period of the year, with multi-year seasonality indicating a substantial downside in most SEK crosses through year-end. As such, we keep our 1M forecast intact. The medium-term outlook for the SEK remains challenging, though. US outperformance in terms of growth prospects and rates weigh on European currencies including the krona. Relative monetary policy is another headwind as the Riksbank front runs peers.

- A continued USD rally and/or a massive sell off in global equities account for the primary upside risks to our near-term forecast horizon.

EUR/SEK



	1M	3M	6M	12M
Danske Bank	11.30	11.40	11.60	11.60
Consensus	11.70	11.43	11.34	11.17
Forward	11.60	11.59	11.58	11.57

Hedging recommendations

Income: We recommend to hedge income via FX forwards. Utilise a potential short-term rise in SEK by lifting hedge ratios.
Expenses: We recommend to hedge expenses via risk reversals.

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

NOK

Further NOK-rally will prove temporary

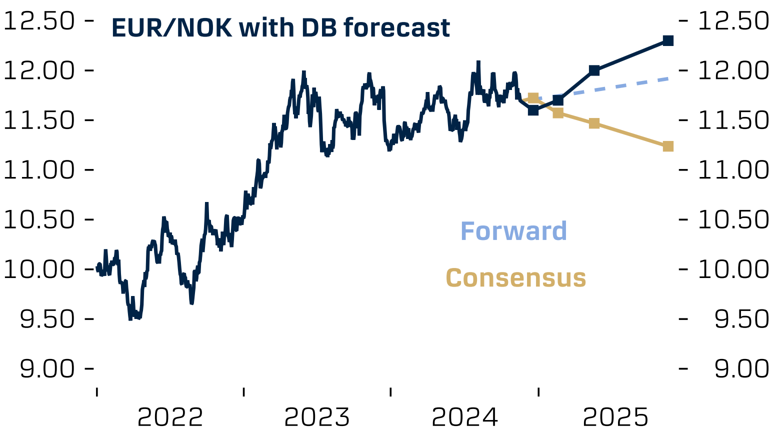
- The growth story in Norway remains that of "muddling through". Over the last two years we have had close to zero growth in the mainland economy and despite inflation – and presumably rates next year – coming lower the stabilisation in savings rates still seem to limit the potential for a sharp consumption driven rebound in mainland GDP. Also, the decline in new orders for the petroleum industries also suggest that one of the primary growth engines look set to lose steam in 2025. The outlook for construction, retail and manufacturing also remains weak, leaving the public side of the economy as the key cushioning factor amid somewhat more expansionary budgets than previously assumed. Inflation continues to move lower, and we expect core inflation to move close to 2% y/y in the beginning of 2025.

- Norges Bank (NB) delivered a hawkish surprise at the September meeting by pushing back against market expectations of a 2024 rate cut. While we think it is fair for markets to price some probability of a 2024 rate cut, we think NB has revealed its preferences which suggest that continued downside surprises to inflation is unlikely to be enough to trigger rate cuts. Instead, we need to see capacity utilisation metrics turn over. We pencil in the first rate cut in March 2025 and eventually think NB will deliver more rate cuts than currently signalled in both 2025 and 2026.

- Despite the NOK rallying since the US elections amid a very weak EUR performance and NOK rates following USD rates more closely (wider rates spreads), we remain medium- to long-term negative on NOK and see any further rally as temporary. Any announcement from NB to cap the size of the FX reserve seems like the most probable catalyst for driving more near-term NOK strength. We highlight how the combination of surging unit labour costs and falling unit profits is not sustainable over time without a rise in unemployment and/or a weaker exchange rate. Given the fiscal setup in Norway we think the potential for much higher unemployment is capped which should add renewed downside pressure on NOK in the coming years.

- Risks are connected to the global investment environment, US monetary policy, possible NB announcement on FX intervention and the Middle East.

EUR/NOK



	1M	3M	6M	12M
Danske Bank	11.60	11.70	12.00	12.30
Consensus	11.72	11.57	11.47	11.24
Forward	11.71	11.74	11.80	11.92

Hedging recommendations

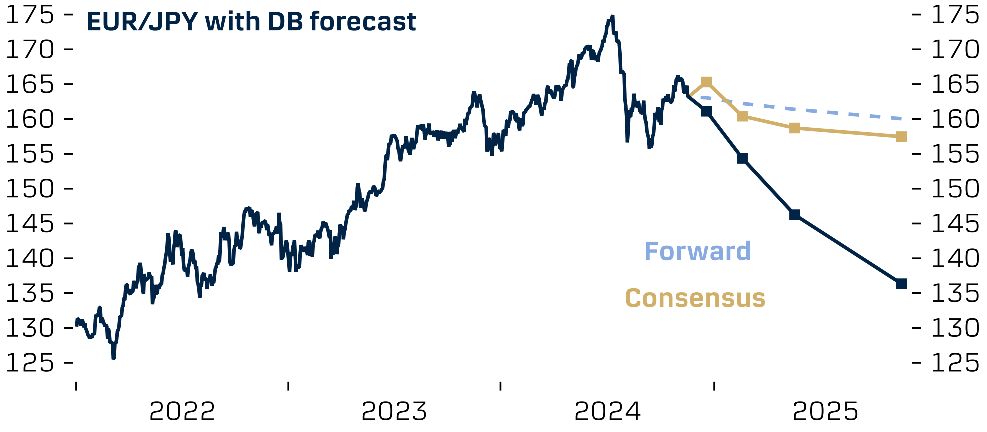
Income: We recommend to hedge NOK income via FX forwards and take advantage of potential short-term gains in NOK to further increase hedging.

Expenses: We recommend to hedge NOK expenses via risk reversals.

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

Others

EUR/JPY



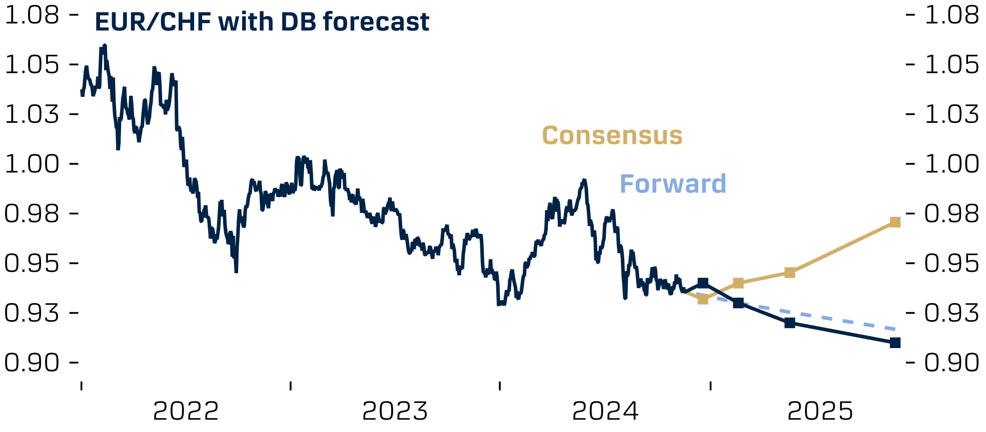
Hedging recommendations

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

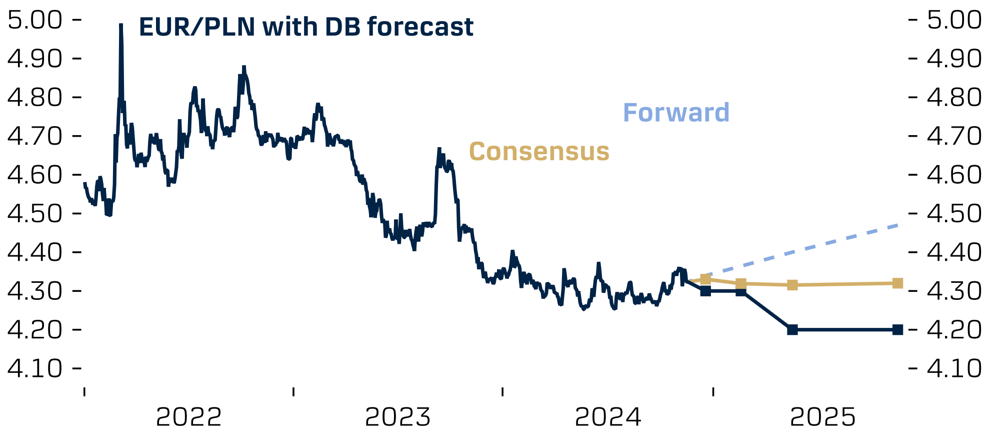
Income: Sell CHF via risk reversals.

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: We recommend to hedge via knock-in forwards.

Expenses: We recommend to hedge via FX forwards.

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

FX Forecast Table

Exchange rates vs EUR

G10				Last Update:	20-11-2024
	Spot	+1m	+3m	+6m	+12m
Exchange rates vs EUR					
EUR/USD	1.06	1.06	1.05	1.03	1.01
EUR/JPY	165	161	154	146	136
EUR/GBP	0.83	0.83	0.82	0.81	0.82
EUR/CHF	0.94	0.94	0.93	0.92	0.91
EUR/SEK	11.58	11.30	11.40	11.60	11.60
EUR/NOK	11.64	11.60	11.70	12.00	12.30
EUR/DKK	7.4595	7.4575	7.4575	7.4550	7.4550
EUR/AUD	1.62	1.61	1.62	1.61	1.60
EUR/NZD	1.79	1.77	1.78	1.78	1.74
EUR/CAD	1.48	1.47	1.47	1.46	1.45
EM					
	Spot	+1m	+3m	+6m	+12m
EUR/PLN	4.33	4.30	4.30	4.20	4.20
EUR/HUF	409	400	410	420	430
EUR/CZK	25.3	25.3	25.2	25.0	25.0
EUR/TRY	36.5	37.0	37.8	38.6	41.0
EUR/ZAR	19.1	19.2	18.9	18.2	17.5
EUR/CNY	7.66	7.65	7.61	7.52	7.47
EUR/INR	89.1	89.6	88.8	87.7	86.9

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Report completed: 20 November 2024, 09:25 CET

Report first disseminated: 20 November 2024, 10:00 CET