

Market Guide

Stagflation risk boosts USD potential

Market overview

Possibly peak inflation worries with energy crisis looming

We have seen further signs of growth slowing and inflation rising hence lifting the overall stagflation risk. While US job growth has disappointed the details reveal a rising issue with labour supply which monetary policy cannot easily solve. Hence we still expect Fed to announce tapering at the November meeting and ultimately hike rates in H2 2022. Fears connected to the Chinese property market have eased amid rising confidence that the Chinese government will eventually step in to avoid a financial crisis. However, the recent turmoil adds new downside pressure on Chinese growth, which is already under pressure. Even if natural gas prices have come lower in recent weeks the energy crisis is increasingly spreading to the oil market with prices being supported by both substitution effects and an OPEC+ reluctant to lift supply.

USD and support to commodity currencies

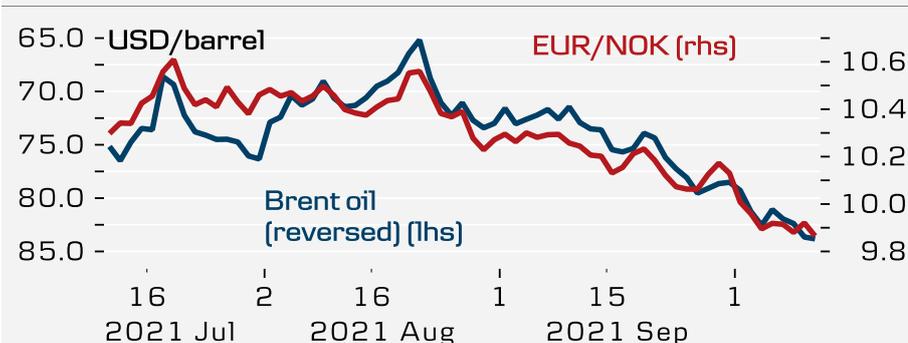
The hawkish stance from the Fed continues to support our expectation of a stronger dollar and weaker Scandinavian currencies in H2. However, NOK has recently experienced a rally supported by Norges Bank initiating its hiking cycle as well as a surge in natural gas prices. EUR/SEK has also moved lower on the back of contagion from the NOK, now trading in the 10.10-10.20 range. EUR/GBP has been more volatile lately, but continues to trade around 0.85. USD/JPY recently climbed to 113, the highest level since 2018, with a rally in oil prices and further rise in US yields as the drivers.

We lower our profile for EUR/USD to 1.10 in 12M (from 1.13) as a reflection of broader market themes increasingly turning pro-dollar: global liquidity conditions tightening, PMIs set to move lower and central banks facing rising inflation concerns. We expect both EUR/SEK and EUR/NOK to move higher from here targeting EUR/SEK at 10.50 in 12M and EUR/NOK at 10.40 in 12M. We expect EUR/GBP to move lower as the USD-positive environment is usually benefitting GBP and keep our forecast intact at 0.83 in 12M.

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Chart 1. Stronger NOK amid higher energy prices recently



Note: Past performance is not a reliable indicator of current or future results.

Sources: Federal Reserve, Bloomberg, Macrobond Financial

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USD – lower forecast to target 1.10 in 12M

- The US and the euro area economies are running at growth rates well above the trend as both regions remain in a mode of recovery, but the pace of expansion is slowing across regions, led by China.
- The Fed has begun discussions on the timing of rate hikes and tapering of asset purchases: Tapering is very likely to be announced during Q4. This will continue to shift the market’s attention towards USD on a theme of monetary divergence vis-à-vis EU.
- As a reflection of broader market themes increasingly turning pro-dollar with global liquidity conditions tightening, PMIs set to move lower and central banks facing rising inflation concerns we lower our profile for EUR/USD to 1.10 in 12M (from 1.13) in favour of USD strength.
- The risks to see EUR/USD above 1.20 include global inflation pressures fading, a pivot from Fed (e.g. in response to a slow US recovery) and/or renewed surge in global industry which could underpin a new leg higher for global reflation assets.

EUR/USD



	1M	3M	6M	12M
Danske Bank	1.15	1.14	1.12	1.10
Consensus	1.16	1.16	1.17	1.17
Forward	1.16	1.16	1.16	1.17

Hedging recommendations

- **Income:** Sell USD via participating forwards.
- **Expenses:** Purchase USD via forwards.

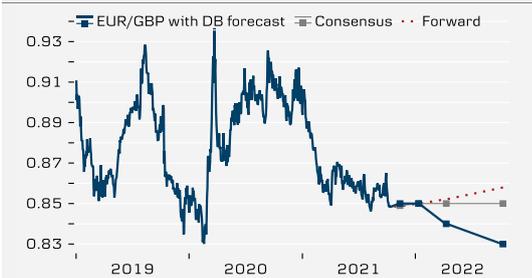
Source: Macrobond, Bloomberg, Danske Bank

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GBP – Bank of England to start tightening monetary policy

- We expect the UK recovery to continue although delta still creates uncertainty about the outlook. Stagflation risks seem higher in the UK compared to the euro area, as the UK is also hit by Brexit. That said, manufacturing accounts for a smaller share of the UK economy than in the euro area. Inflation is already high and is expected to increase further due to increasing energy prices. Inflation expectations have also risen.
- Like the Fed, the Bank of England (BoE) is about to start tightening monetary policy. QE bond buying is set to end by the end of the year and since our last update, investors have started to price in more aggressive rate hikes from the BoE.
- EUR/GBP has been more volatile lately, but continues to trade around 0.85. We remain bullish on GBP as the USD-positive environment is usually also benefitting GBP.
- We thus continue to target EUR/GBP at 0.83 in 12M.
- A risk to our forecast is a hit to global risk sentiment and/or if Bank of England keeps monetary policy accommodative for longer than currently expected. Stagflation may also become more pronounced in the UK compared to the euro area. EU-UK tensions remain a risk.

EUR/GBP



	1M	3M	6M	12M
Danske Bank	0.85	0.85	0.84	0.83
Consensus	0.85	0.85	0.85	0.85
Forward	0.85	0.85	0.85	0.86

Hedging recommendations

- **Income:** Sell GBP via participating forwards.
- **Expenses:** Buy GBP via forwards

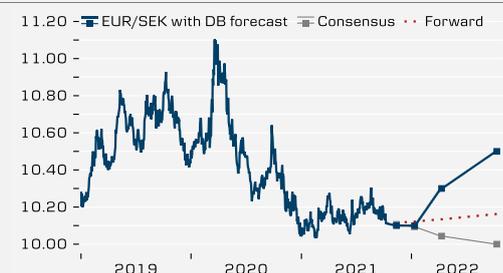
Source: Macrobond, Bloomberg, Danske Bank.

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SEK – near-term strength should fade out by year-end

- We have made a small upward revision in our GDP forecast and now expect growth just shy of 4% for the full year of 2021 with Q2/Q3 marking the peak in terms of GDP growth. There are increasing concerns regarding labour shortages, but we are still a bit off from previous highs reached in 2017-18.
- In the recent weeks the SEK has strengthened seemingly on the back of contagion from the NOK. However, we remain strategically bearish on the SEK due to deteriorating global growth momentum, fragile market environment, stronger USD and too aggressive medium-term pricing on the Riksbank.
- In the near term, the SEK could get some temporary support if the Riksbank inserts a hiking bias at the November meeting and if the seasonal pattern holds true. Therefore, we lower our EUR/SEK 1-3M forecast to 10.10 (from 10.20), while keeping 6M at 10.30 and 12M at 10.50.
- The upside risk to our forecast is the fact that EUR/SEK has been trading synchronized with risk sentiment and EUR/USD throughout the year. Meanwhile if the Riksbank not only inserts a distant hiking bias, but also revamps the policy outlook altogether on the back of recent pick-up in inflation, it poses a downside risk to our forecast.

EUR/SEK



	1M	3M	6M	12M
Danske Bank	10.10	10.10	10.30	10.50
Consensus	10.11	10.09	10.04	10.00
Forward	10.12	10.12	10.13	10.16

Hedging recommendations

- **Income:** Sell SEK via forwards.
- **Expenses:** Buy SEK via risk reversals.

Source: Macrobond, Bloomberg, Danske Bank.

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NOK – set for another move lower in Q4

- Mainland activity levels have surpassed the pre COVID-19 peaks. Meanwhile, while a sizeable gap to the pre-crisis trend remains there are increasing signs of capacity utilisation problems lifting domestic cost pressures.
- NOK has recently experienced a rally supported by Norges Bank initiating its hiking cycle as well as a surge in natural gas prices.
- Despite this recent strengthening, we increasingly see the NOK potential exhausted as NOK rates pricing looks stretched and as NB will have to lower its daily NOK purchase for both Q4 and 2022.
- We thus maintain a negative view on NOK but lower the EUR/NOK profile forecasting 10.40 in 6M (from 10.60) in light of higher-than-anticipated oil and gas prices.
- The biggest risk to our forecasts is global commodity prices. Should oil and gas prices continue higher while global risk appetite remains positive then we would expect EUR/NOK to trade below our forecasts. On the other hand, marked risk-off could trigger a larger-than-projected setback.

EUR/NOK



	1M	3M	6M	12M
Danske Bank	10.00	10.20	10.40	10.40
Consensus	9.92	9.99	9.94	9.85
Forward	9.88	9.90	9.94	10.02

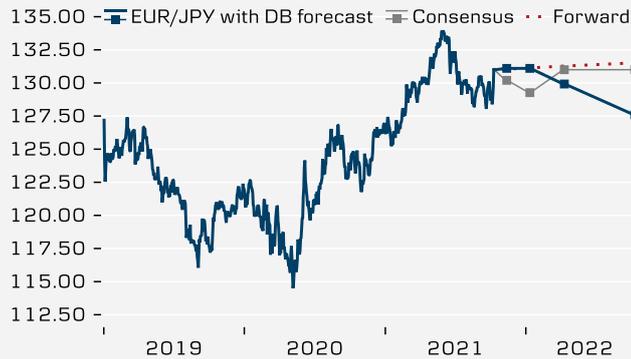
Hedging recommendations

- **Income:** Sell NOK via forwards.
- **Expenses:** Buy NOK via risk reversals.

Source: Macrobond, Bloomberg, Danske Bank.

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EUR/JPY



	1M	3M	6M	12M
Danske Bank	131.10	131.10	129.92	127.60
Consensus	130.20	129.27	131.00	131.00
Forward	131.04	131.14	131.27	131.52

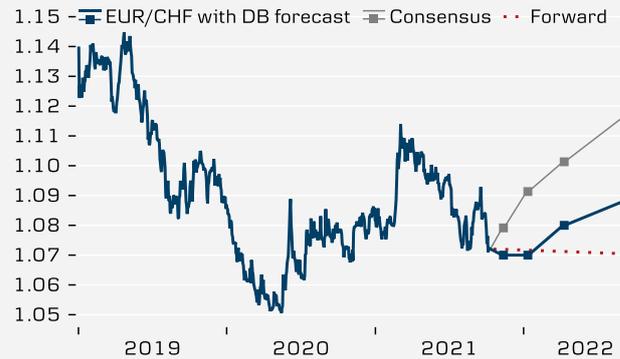
Hedging recommendations

- **Income:** Sell JPY via participating forwards.
- **Expenses:** Buy JPY via forwards.

Source: Bloomberg, Danske Bank.

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EUR/CHF



	1M	3M	6M	12M
Danske Bank	1.07	1.07	1.08	1.09
Consensus	1.08	1.09	1.10	1.12
Forward	1.07	1.07	1.07	1.07

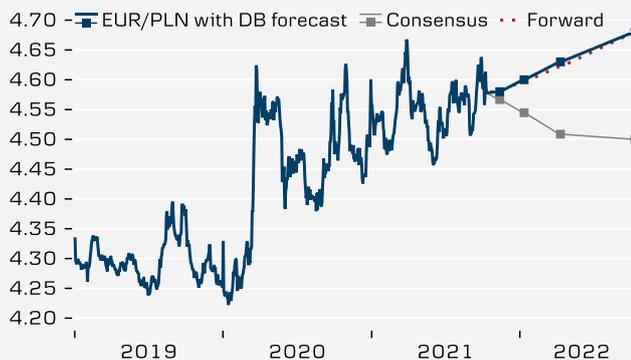
Hedging recommendations

- **Income:** Sell CHF via forwards.
- **Expenses:** Buy CHF via participating forwards.

Source: Bloomberg, Danske Bank.

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EUR/PLN



	1M	3M	6M	12M
Danske Bank	4.58	4.60	4.63	4.68
Consensus	4.57	4.54	4.51	4.50
Forward	4.58	4.60	4.62	4.68

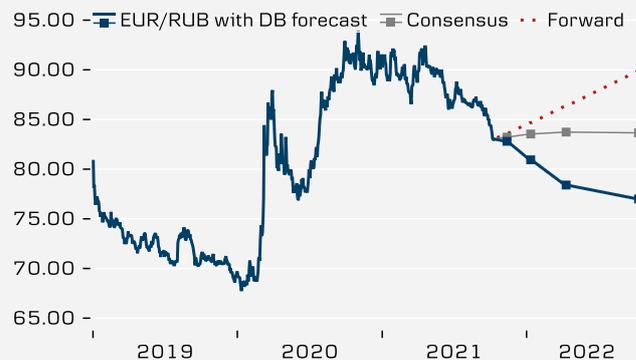
Hedging recommendations

- **Income:** Sell PLN via forwards.
- **Expenses:** Buy PLN via forwards.

Source: Bloomberg, Danske Bank.

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EUR/RUB



	1M	3M	6M	12M
Danske Bank	82.80	80.94	78.40	77.00
Consensus	83.22	83.54	83.73	83.66
Forward	83.58	84.67	86.36	89.86

Hedging recommendations

- **Income:** Sell RUB via forwards. We expect RUB to strengthen and one may consider option-based strategies.
- **Expenses:** Buy RUB via forwards.

Source: Bloomberg, Danske Bank.

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Danske Banks' FX forecasts

Last Update: <u>12/10/2021</u>					
G10					
	Spot	+1m	+3m	+6m	+12m
Exchange rates vs EUR					
EUR/USD	1.156	1.15	1.14	1.12	1.10
EUR/JPY	131.0	131	131	130	128
EUR/GBP	0.848	0.85	0.85	0.84	0.83
EUR/CHF	1.073	1.07	1.07	1.08	1.09
EUR/SEK	10.11	10.10	10.10	10.30	10.50
EUR/NOK	9.86	10.00	10.20	10.40	10.40
EUR/DKK	7.4407	7.4400	7.4400	7.4450	7.4450
EUR/AUD	1.565	1.60	1.63	1.62	1.62
EUR/NZD	1.659	1.67	1.68	1.67	1.67
EUR/CAD	1.439	1.45	1.47	1.47	1.46
EM					
	Spot	+1m	+3m	+6m	+12m
EUR/PLN	4.579	4.58	4.60	4.63	4.68
EUR/HUF	360	360	362	364	365
EUR/CZK	25.4	25.4	25.3	25.1	25.0
EUR/RUB	83.0	83	81	78	77
EUR/TRY	10.41	10.4	10.5	10.5	10.6
EUR/ZAR	17.27	17.3	17.1	17.4	18.2
EUR/CNY	7.45	7.53	7.52	7.50	7.48
EUR/INR	87.3	87.4	87.2	86.2	85.8

Source: Bloomberg, Danske Bank

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