Market Guide

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USD sell-off to prove temporary

Too soon for the Fed to pivot policy in a dovish direction

The narrative of a potential Fed policy pivot in a more dovish direction has dominated markets. While G10 central banks continue to tighten monetary policy both Norges Bank and Bank of Canada have slowed their hiking pace. Global demand continues to slow yet inflation remains at historically elevated levels across most regions. In the US, the latest inflation print fell substantially short of expectations triggering the largest single day drop in US 2Y rates since 2008. Meanwhile, the US labour markets remain strong and we still think it is premature to declare victory in its fight against above-target inflation. European natural gas prices have come sharply lower over the past months amid a drop in demand, mild weather conditions and inventories starting to fill up. Speculation of China abandoning its zero-covid policy has given a boost to the heavily battered Chinese equities and industrial metals.

USD coming under pressure

Price action in FX markets over the last month has been driven by not least the Fed-pivot narrative but also renewed focus on a Chinese reopening and lower energy prices have been important catalysts. EUR/USD has moved sharply higher and cyclically sensitive European currencies in the likes of NOK, SEK, HUF and PLN have rallied strongly. GBP has largely retraced its initial sharp move lower as the newly elected government is set to deliver a more firm stance on fiscal discipline. CNY has recovered some of its recent weakness.

Despite recent USD-headwind, we continue to forecast EUR/USD at 0.93 in 12M on the back of a substantial negative terms-of-trade shock to Europe vs US, tightening of global financial conditions and downside risk to euro area growth. We expect EUR/SEK to move higher over the coming months to 11.20 on the back of weak growth dynamics, relative monetary policy and the Riksbank's disregard for SEK weakness. On a 6-12M horizon, we see a recovery and sustainable support to risk assets and the SEK. We pencil in a rise in EUR/NOK over the coming 3 months driven by a slowdown in growth, a European recession and volatile asset markets but pencil in an eventual NOK rebound in 2023. We forecast EUR/GBP at 0.86 in 12M, but expect fragile risk environment, too aggressive market pricing on BoE and lower energy prices to weigh on GBP in the near-term.

A key assumption behind our FX forecasts is that of a stronger USD and tightening of global financial conditions. Risks to this assumption include global inflation pressures fading fast, renewed focus on China easing, a global capex uptick and/or industrial production increasing, which could underpin a new reflation leg higher.

USD

Rally in EUR set to fade over the coming year

- Global demand remains under pressure as high input prices and elevated inflation erodes purchasing power and corporate profits (except for a few select sectors, like energy). In addition, the coordinated tightening of global monetary conditions further adds to cyclical downside.

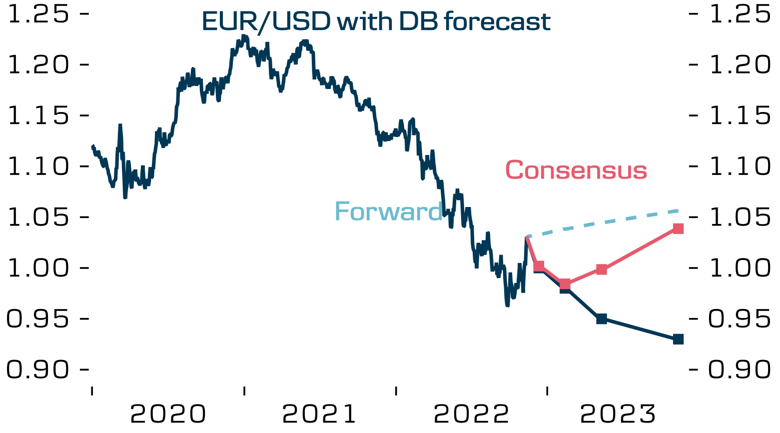
- Fed focuses on a scenario of substantial rate hikes and unwinding the held bonds. ECB will equally seek to raise rates, though more moderately. In our view, this is set to tighten financial conditions and to ensure inflation peaks out over 2023.

- Fundamentally, the US should continue to be a high(er) interest rate market and equities continue to appeal to foreign investors. This means the US is likely to attract capital, which generally helps the USD.

- The large negative terms-of-trade shock to Europe vs US, a further cyclical weakening among trading partners, the coordinated tightening of global financial conditions, broadening USD strength and downside risk to the euro area makes us keep our focus on EUR/USD moving still lower (targeting 0.93) – a view not shared by the consensus.

- The key risk to shift EUR/USD towards 1.15 is seeing global inflation pressures fade and industrial production increase. The upside risk also include a renewed focus on easing Chinese credit policy and a global capex uptick but neither appear to be materialising, at present.

EUR/USD



	1M	3M	6M	12M
Danske Bank	1.00	0.98	0.95	0.93
Consensus	1.00	0.98	1.00	1.04
Forward	1.03	1.04	1.04	1.06

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

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GBP

Domestic policy to take a back seat

- The UK economy continues to weaken and all PMIs are now below 50 suggesting that the UK may already be in the early stage of a recession. The labour market remains tight, although we are seeing the first signs of easing. The cyclical outlook remains bleak for the UK economy, only further amplified by tighter monetary policy, higher energy prices and elevated inflation eroding purchasing power. Overall, we do not see the outlook for the UK to be substantially different from the Euro Area.

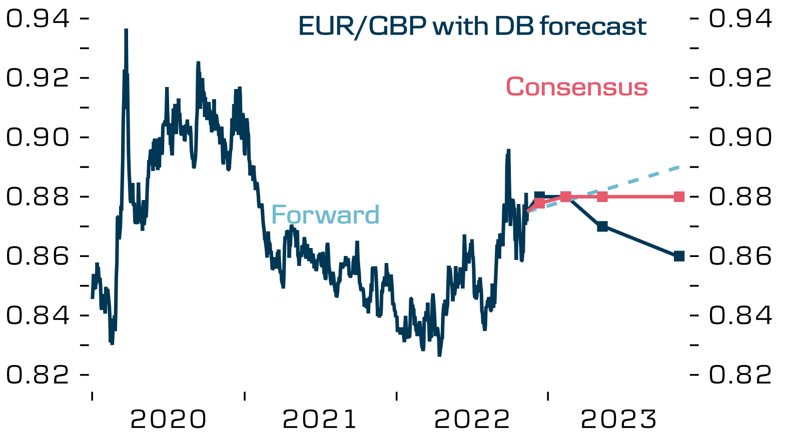
- We expect the Bank of England (BoE) to continue hiking policy rates until February next year, with risks skewed to more tightening. This is less than what markets are currently pricing. If markets start to price in fewer hikes for the BoE this would be supportive for EUR/GBP.

- Going forward, we expect domestic policy themes to be of less importance and volatility to continue to wear off. In the near-term, we expect fragile risk appetite, too aggressive market pricing on the BoE and lower energy prices to continue to prove a headwind for GBP. We thus forecast EUR/GBP at 0.88 in 1M.

- Further out, we remain cautiously optimistic that the cross will head lower as a global growth slowdown and the relative appeal of UK assets to investors are a positive for GBP relative to EUR.

- The key risk to see EUR/GBP moving above 0.90 is a sharp sell-off in risk where capital inflows fade and liquidity becomes scares. Other risks are the outlook for the UK economy deteriorating sharply compared to the Euro Area, lower energy prices and renewed escalations in EU-UK tensions.

EUR/GBP



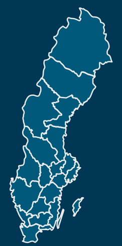
	1M	3M	6M	12M
Danske Bank	0.88	0.88	0.87	0.86
Consensus	0.88	0.88	0.88	0.88
Forward	0.88	0.88	0.88	0.89

Hedging recommendations

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

Expenses: Buy GBP via forwards.

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



SEK

Enters flow-ridden period

- Leading indicators are pointing to a sharp deterioration of growth from H2 2022. We see GDP contracting (-1.2%) and unemployment rising more than consensus, including the Riksbank and the government, in 2023 on the back of broad deterioration of households' purchasing power, higher interest rates and energy bills. In combination with a global recession, this is a clear negative for the SEK.

- Relative monetary remains a key driver and captures the uptrend in EUR/SEK and USD/SEK. We expect the Riksbank will hike by 75bp in November, 25bp in February with a terminal rate at 2.75%. We expect they will stay at 2.75 throughout 2023. The Riksbank generally has a very relaxed approach to the krona, emphasized by them continuing selling SEK for the FX reserves.

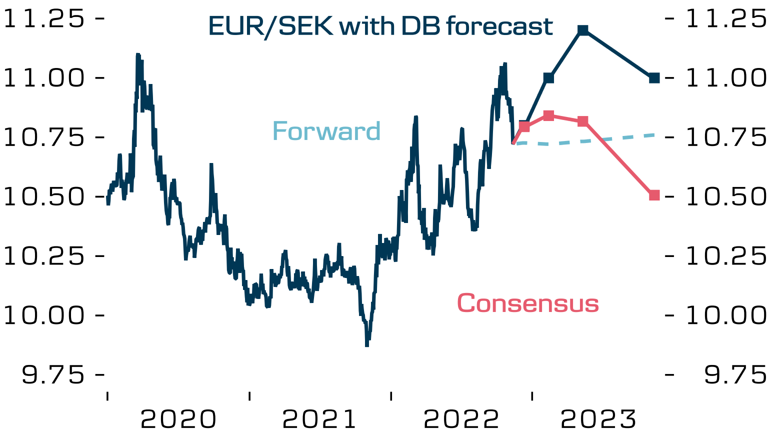
- We stick to our non-consensus view on a weaker SEK amid weak growth dynamics, especially for Europe, scope for another downturn in global equities and relative monetary policy. We therefore forecast EUR/SEK at 11.20 in 6M.

- Further out, we expect recovery and sustainable support to risk assets and the SEK and forecast EUR/SEK at 11.00 in 12M.

- In the coming weeks, focus on the tentative Christmas rally in risk assets, Philip Morris and PPM, where there is some - transitory - downside risk to our 1M estimate.

- The key downside risks to our forecasts are a dovish Fed pivot, sustained equities rebound, brighter growth outlook not least for Europe or a shift in Riksbank monetary policy stance including a shift in FX policies.

EUR/SEK



	1M	3M	6M	12M
Danske Bank	10.80	11.00	11.20	11.00
Consensus	10.79	10.84	10.82	10.51
Forward	10.73	10.72	10.73	10.76

Hedging recommendations

Income: Sell SEK via forwards.

Expenses: Buy SEK via forwards, alternatively via risk reversals

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

NOK

Paradoxically in the hands of Fed policy

- In general, data has come in slightly stronger-than-expected – yet still paint a picture of an economy clearly slowing. The housing market is beginning to exhibit weakness highlighting how the combination of higher policy rates and lower real disposable income is having an impact. October inflation surprised to the topside with core inflation hitting 5.9%. The details revealed a fairly broad-based rise yet we also see clear signs of inflation approaching a peak.

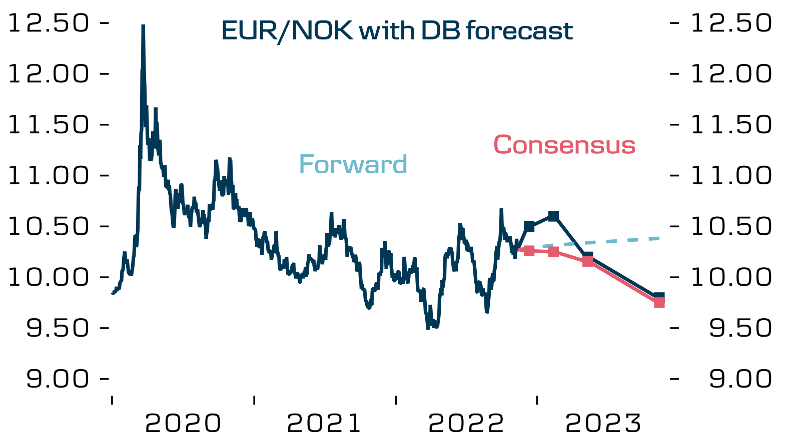
- While Norges Bank (NB) this summer front-loaded monetary tightening via three 50bp rate hikes, NB has now returned to a more "gradual" 25bp per meeting pace of rate hikes. In our base case NB will hike policy rates by a final 25bp in December brining the sight deposit rate to 2.75%. This is considerably below market pricing that pencil in an accumulative 80bp worth of hikes.

- NOK is notoriously sensitive to the global growth and commodities outlook. Consequently, changes in the market narrative of both a potential Fed policy shift (pivot) or China abolishing its zero-covid policy have had and will continue to have big impacts on NOK. With the latest US CPI disappointment, the near-term topside to EUR/NOK look somewhat diminished. That said, we still think it is too early to turn outright bullish on NOK – irrespective of a more secular positive story brewing for the Norwegian currency. We have lowered our reverse "v-profile" slightly.

- We forecast EUR/NOK at 10.60 in 3M and 9.80 in 12M.

- A severe global recession and a sharp sell-off in risk could send EUR/NOK substantially above our projection. On the other hand, a persistent move higher in oil and natural gas prices combined with an improved growth outlook could send EUR/NOK lower than earlier-than-projected.

EUR/NOK



	1M	3M	6M	12M
Danske Bank	10.50	10.60	10.20	9.80
Consensus	10.26	10.25	10.16	9.75
Forward	10.28	10.31	10.34	10.38

Hedging recommendations

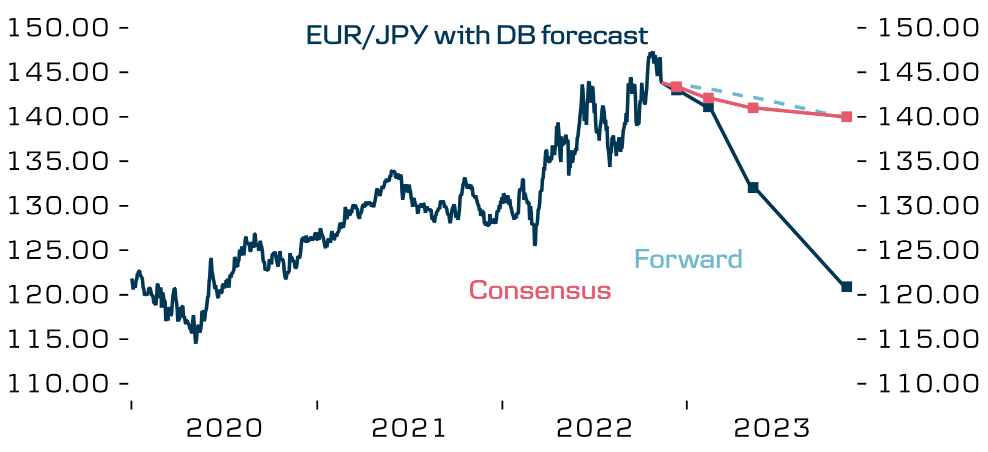
Income: Sell NOK via forwards heading towards year-end. Consider lowering the hedge ratio later this year wrt. 2023 income.

Expenses: Buy NOK via risk-reversals in the coming months. Consider lifting the hedge ratio later this year.

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

Others

EUR/JPY



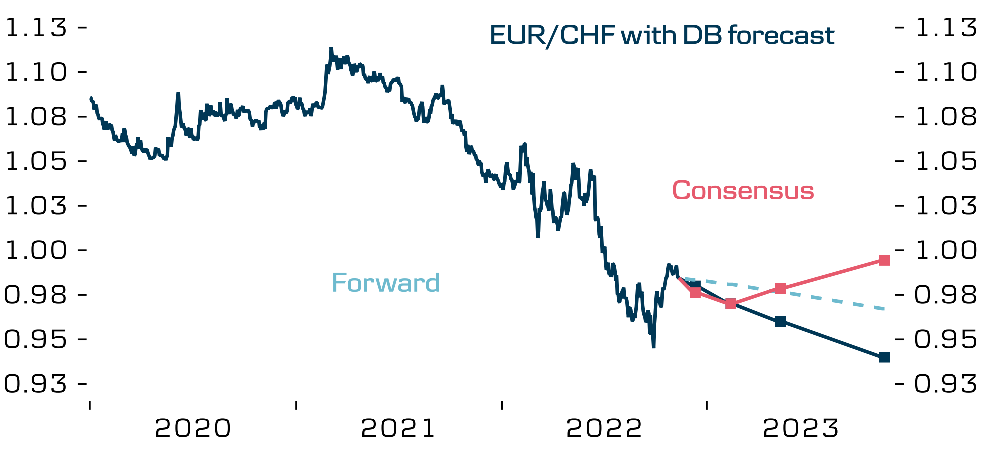
Hedging recommendations

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.

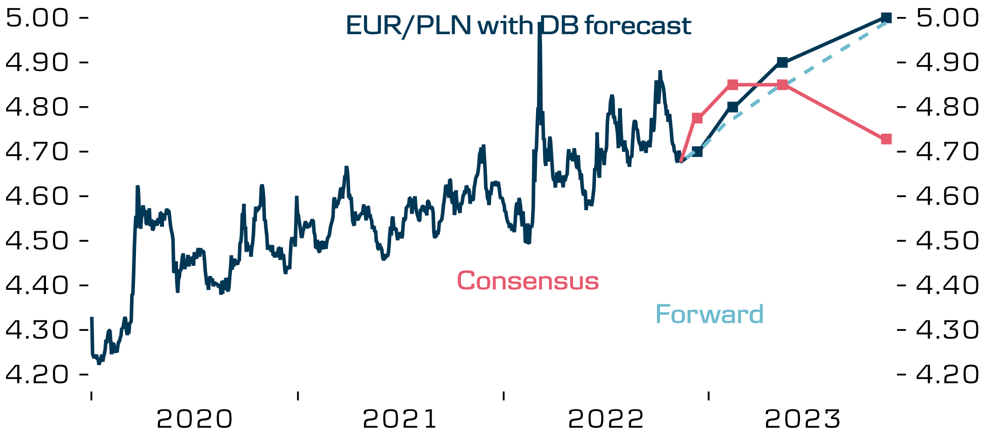
Expenses: Buy CHF via forwards.

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

Danske Bank

Others

EUR/PLN



Hedging recommendations

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

Expenses: Buy PLN via forwards.

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

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FX Forecast Table

Exchange rates vs EUR

Last Update: 14/11/2022

G10	Spot	+1m	+3m	+6m	+12m	End 2023
Exchange rates vs EUR						
EUR/USD	1.03	1.00	0.98	0.95	0.93	0.93
EUR/JPY	144.97	143	141	132	121	114
EUR/GBP	0.88	0.88	0.88	0.87	0.86	0.84
EUR/CHF	0.98	0.98	0.97	0.96	0.94	0.92
EUR/SEK	10.80	10.80	11.00	11.20	11.00	11.00
EUR/NOK	10.35	10.50	10.60	10.20	9.80	9.60
EUR/DKK	7.44	7.4400	7.4400	7.4450	7.4500	7.4500
EUR/AUD	1.54	1.52	1.51	1.48	1.45	1.43
EUR/NZD	1.69	1.67	1.66	1.64	1.60	1.58
EUR/CAD	1.37	1.36	1.35	1.32	1.29	1.25
EM	Spot	+1m	+3m	+6m	+12m	
EUR/PLN	4.70	4.70	4.80	4.90	5.00	4.78
EUR/HUF	408.30	410	415	430	440	430
EUR/CZK	24.31	24.3	24.3	24.2	24.1	24.0
EUR/TRY	19.18	18.6	18.6	19.0	20.5	23.3
EUR/ZAR	17.86	17.0	16.7	16.2	15.8	15.8
EUR/CNY	7.29	7.25	7.20	7.08	7.07	6.65
EUR/INR	83.80	82.0	81.3	80.8	80.0	76.7

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Date of first publication

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