

JULY 22

# Currencies Focus



## Summary

1. The DXY dollar index has appreciated more than 4% against most currencies over the past month. This is due rising fears of a global recession, and expectations that the Fed will hike rates more relative to most other central banks.
2. The euro suffered more than other currencies. Indeed, recession fears linked to reduced Russian gas exports lead to lower interest rate expectations for the ECB. The euro is close to parity at a 20-year low.
3. The Swiss National Bank surprised the market by hiking rates by 50bps. They gave some guidance towards more rate hikes. This led us to revise our targets for the EURCHF. We now target 1.02 (value of one euro) at a 3- and 12-months horizon.
4. The Bank of Japan clearly focuses its mandate on controlling the yield curve (interest rates for different maturities) rather than defending the yen. We lower our outlook for the JPY to 140 (value of one dollar) at 3 months and 130 at 12 months.
5. Downward revisions to global growth and uncertainties in China are weighing on the AUD and NZD. We are now slightly less bullish on these currencies. We change our target from 0.7 to 0.68 for the 3 and 12 months on the NZD (value of one NZD). For the AUD, we change from 0.76 to 0.74 (value of one AUD).
6. We lower our targets for the Indian rupee, the Mexican peso and the South African rand. We remain positive on the Brazilian and Chinese currencies.

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## OUR TARGETS OVER THE NEXT 3 AND 12 MONTHS

	Country	Spot 7/11/2022	Target 3 months	Target 12 months
Against euro	United States	EUR / USD 1.01	1.03	1.12
	United Kingdom	EUR / GBP 0.84	0.84	0.84
	Switzerland	EUR / CHF 0.99	1.02	1.02
	Japan	EUR / JPY 138.59	144	146
	Sweden	EUR / SEK 10.69	10.40	10.70
	Norway	EUR / NOK 10.27	9.60	9.60
Against dollar	Japan	USD / JPY 137.45	140	130
	Canada	USD / CAD 1.30	1.25	1.25
	Australia	AUD / USD 0.67	0.74	0.74
	New Zealand	NZD / USD 0.61	0.68	0.68
	Brazil	USD / BRL 5.35	5.00	5.00
	Russia	USD / RUB 62.70	100.0	90.0
	India	USD / INR 79.43	78.0	80.0
	China	USD / CNY 6.71	6.60	6.50

Source: Refinitiv - BNP Paribas WM



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## USD VIEW >> TARGET 12M VS EUR: 1.12

### 20-year low for the EUR

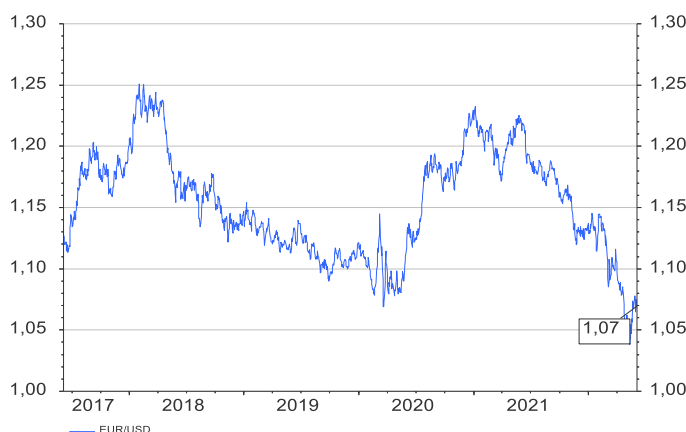
The euro lost around 4.5% against the dollar this month, hitting a 20-year low close to parity. Since mid-June, the downward revisions for the interest rate path in the eurozone and the risk-off mode penalized the single currency.

The possibility of an end of Russian gas exports could strongly weigh on the eurozone economic activity this winter. The Fed raised rates by 75bps in June as long-term consumer inflation expectations surprised to the upside.

For the ECB, we expect a 25bps hike at the end of the July followed by two 50bps hikes at each of the September and October meetings and then 25bps at the following meetings. The eurozone experienced a current account deficit of €5.8bn in April. This is the first deficit since 2011. Germany has thus experienced its first trade deficit since 1991, penalized by energy prices and supply chain disruptions. The French trade deficit reached a new record in May at €13.1 billion.

We expect a peak in US inflation around this time. This should help the Fed to slow the pace of interest rate hikes later this year. We do not expect Russia to stop gas exports but rather to limit the amount. This should be positive news and help the euro stabilize.

**We expect the euro to stabilize at 1.03 over the coming 3 months. We maintain our 12-month target at 1.12 (value of one euro).**



## GBP VIEW >> TARGET 12M VS EUR: 0.84

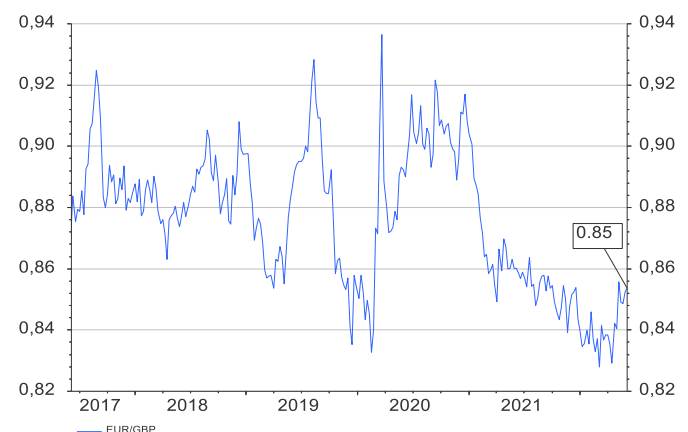
### No clear trend

The EURGBP was relatively stable around 0.85 (value of one euro) in June. The UK continues to face imported food and energy inflation which currently weaken the GBP. UK inflation reached a high of 9.1% and is expected to peak at 11% this autumn according to the Bank of England (BoE). Boris Johnson's resignation adds to the political and economic uncertainty. Recession risks have been rising.

The central bank (BoE) continued its rate hikes in June with a 25bp rate increase, the key rate is now standing at 1.25%. The market expects 150bps of additional rate hikes by the end of the year with potential 50bps hikes at upcoming meetings. Faced with a weak economy, the BoE may however deliver fewer rate hikes than expected and this could be a source of weakness for the GBP going forward. We do not expect any major trend for the GBP over the coming months.

The Composite PMI continues to suggest expansion with a level at 53.7 (60 reached in February and March). However, order books are down compared to previous months while consumer confidence is at its lowest since May 2020. The economy is slowing down significantly due to the income squeeze caused by inflation, and this should continue over the coming months.

**We maintain our 3- and 12-month targets at 0.84 (value of one euro) suggesting a sideways movement for the EURGBP over the next year.**



## CHF VIEW >> TARGET 12M VS EUR: 1.02

### Target revisions – sustained strength

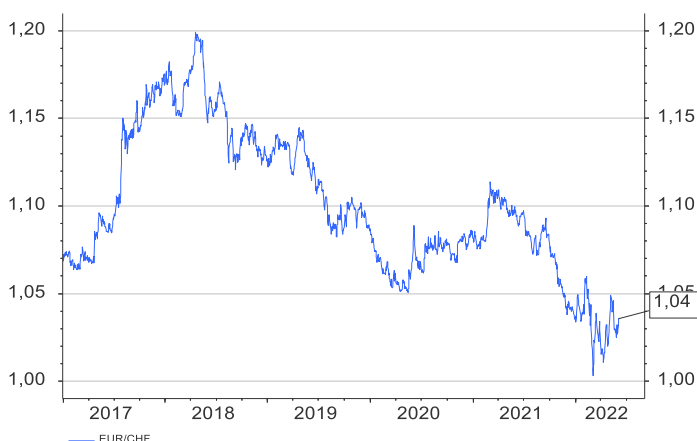
The Swiss franc broke parity with the euro after the Swiss National Bank (SNB) raised rates by 50bps at its latest meeting.

At an annualized rate of 2.9% in May, inflation in Switzerland is much lower than in the other G10 countries. The SNB has indicated that it wants to act now before inflation accelerates and weakens the economy. Further rate hikes are expected at upcoming meetings. The key rate now stands at -0.25% and should therefore soon turn positive again.

The Swiss economy continues to perform well with a very low unemployment rate of 2.2% and a growth rate expected by the SNB of 2.5%. The war had little significant effects so far on the Swiss economy. The strong currency limits imported inflation.

The manufacturing business survey (PMI) remains at a high level with 59.1 in June. The services survey is also well oriented with 58. It is down from 60 in May.

**The recent speech of the SNB suggests further rate hikes and a strong currency. We change our targets for the 3- and 12-month horizon to 1.02 (value of one EUR) from 1.03 and 1.08 respectively.**



## JPY VIEW >> TARGET 12M VS USD: 130

### New targets

The yen lost 1.1% in June and more than 17% since the beginning of the year. The yen is now at a 24-year low.

The interest rate differential continues to be the primary factor explaining the sustained weakness of the Yen. Bank of Japan (BoJ) Governor Kuroda reiterated the choice of an accommodative monetary policy to support the Japanese economy. The BoJ bought a record level of government bonds in June (YEN 16.2 trillion) in order to defend a yield of 0.25% on the 10-year government.

The Composite business survey (PMI) rose in June to 53.2 from 52.3, due in particular to the easing of restrictive measures in China. Businesses continue to point to strong inflationary pressures in input prices.

Over the next 3 months, the Japanese currency should stay weak in the face of high energy prices that are worsening its trade balance and a central bank that maintains an ultra-accommodating policy. **For the next 3 months, we therefore revise our target from 130 to 140 (value of one dollar).** Beyond this threshold, the BoJ could take measures to support the Yen. Over the next 12 months, the Fed should be able to slow the rate hike cycle, and this is expected to weaken the dollar against the Yen.

**We now target 130 (value of one USD) for the JPY over the next 12 months. This suggests a stronger Japanese currency compared to current levels.**



## SEK VIEW &gt;&gt;

## TARGET 12M VS EUR: 10.70

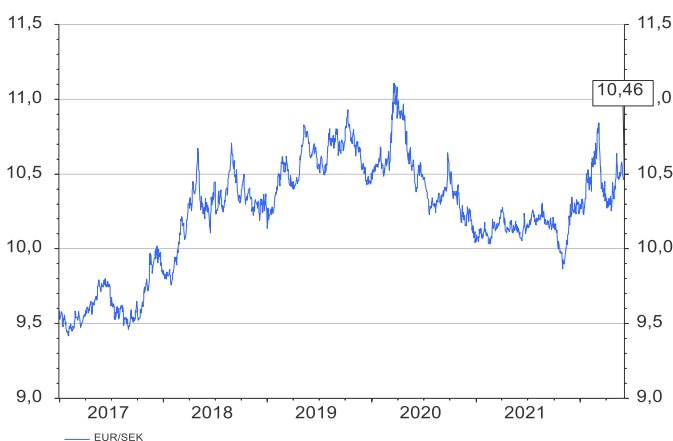
## Looking for a sideways move

The Swedish krona depreciated moderately against the euro over the last 30 days. The Riksbank raised rates by 50 bps at its June meeting, bringing the repo rate to 0.75%. The Riksbank is expected to raise rates by 50bps at each of its next two meetings this year. The Riksbank will also continue to reduce the pace of asset purchases in the second half of the year. Indeed, inflation reached 7.2% in May compared to 6.4% in April. Moreover, core inflation is expected to peak at 6.4% in the second half of 2022.

However, we believe that rate hikes will be more moderate than the market anticipates. Indeed, expectations of a terminal rate of 3.25% - 3.5% seem quite high. We expect a terminal rate closer to 2-2.5%. In the short term, we expect more appreciation of the SEK in the face of a widening rate differential with the ECB.

Economic activity remains strong. The Swedish Manufacturing business survey PMI dropped from 54.9 to 53.7 in June, driven down by delivery times, employment, and new orders. The June Services business survey (PMI) declined from 67.8 to 62.8.

**We maintain our targets of 10.4 and 10.7 for the 3- and 12-month horizon. This implies a slight depreciation of the SEK the coming year.**



## NOK VIEW &gt;&gt;

## TARGET 12M VS EUR: 9.60

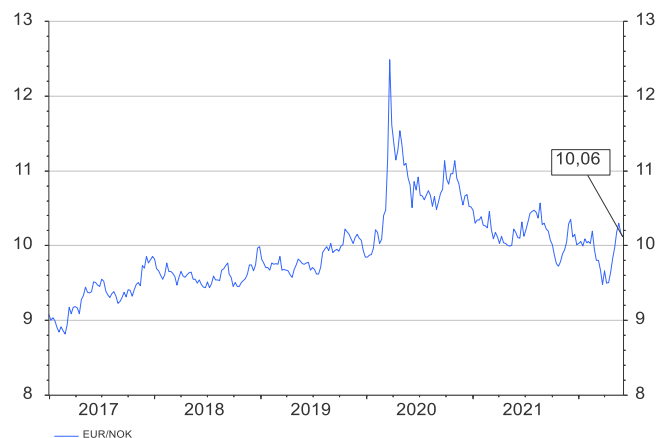
## Look for a rebound

The NOK depreciated nearly 1% against the euro, in response to risk aversion and falling crude oil prices. The central bank (Norges Bank) raised rates by 50bps at its meeting in early July, bringing the repo rate to 1.25%. The central bank indicated that a 25bps hike was the most likely scenario for the next meeting.

Crude oil, despite being down 15% from its peak, remains above \$100, a level not reached since 2014. This strongly supports Norway's current account balance, and supports our positive view on the NOK.

Norway is implementing a more restrictive monetary policy than the ECB and this will be an additional support factor for the Norwegian krone. Inflation is indeed high at 6.3% in June against 5.7% in May. The economy seems to be overheating with an unemployment rate of 3.2%, strong wage negotiations, and high real estate prices compared to pre-crisis levels.

**We maintain our 3- and 12-month targets at 9.6 suggesting a potential for NOK appreciation from current levels.**





## AUD VIEW &gt;&gt;

## TARGET 12M VS USD: 0.74

## Upside potential

The Australian dollar lost some ground over the last 30 days as the global economic slowdown did hurt commodity exports.

At its meeting in early July, the Reserve Bank of Australia (RBA) raised rates by 50bps to 1.35%. The RBA has raised rates by 125bps since May and has indicated that it will continue its normalization efforts. The market expects a further 175 rate hikes to come. The rate increases led to a drop in real estate prices, which had previously risen sharply since the beginning of the pandemic. This affects consumer confidence through the wealth effects. The terminal rate is expected to reach nearly 4% in 2023. This should continue to attract capital and supports our positive view on the currency for the next 3 and 12 months.

We are less bullish than last month due to lower economic growth prospects. Coal briquettes and iron ore, which account for nearly 40% of exports, have recently fallen significantly from their peak and reached in April.

**We therefore revise our 3- and 12-month targets from 0.76 to 0.74 (value of one AUD). This suggests upside potential for the AUD.**



## NZD VIEW &gt;&gt;

## TARGET 12M VS USD: 0.68

## Overheating economy

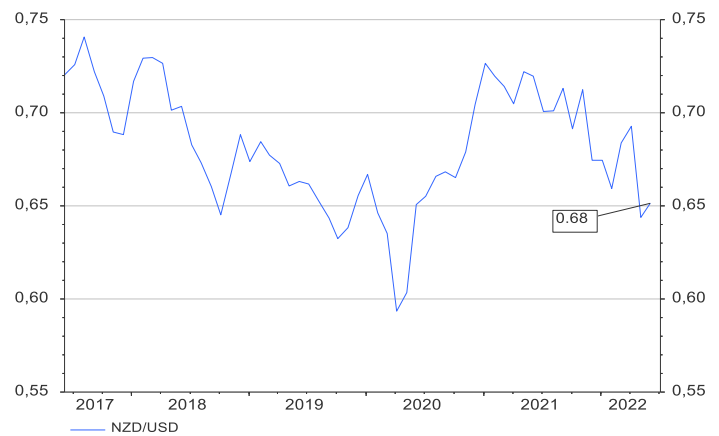
The Kiwi has depreciated by around 3% over the last month.

The New Zealand economy continues to show various signs of overheating which necessitates a continuation of the restrictive monetary policy (higher interest rates). The inflation rate has reached 6.9% and the unemployment rate is only 3.2%.

The Reserve Bank of New Zealand (RBNZ) is expected to raise rates by 50bps at its July meeting bringing the official cash rate to 2.5%. Wage pressures are high and call for a restrictive monetary policy. The terminal rate should be close to 4%.

Despite the risk of a decline in global demand, we see an appreciation potential for the NZD. We lower our targets somewhat compared to last month.

**We change our target from 0.7 to 0.68 (value of one NZD) for the 3- and 12- month horizon, reflecting the uncertainty on global demand. This still suggests significant upside potential for the NZD versus the USD from current levels.**



## CAD VIEW &gt;&gt;

## TARGET 12M VS USD: 1.25

## Appreciation potential

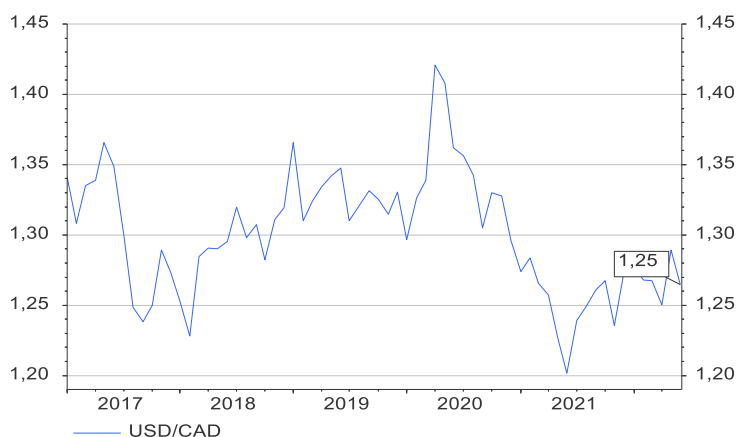
The Canadian dollar has lost some ground over the past 30 days, hurt by fears of a global slowdown.

The Bank of Canada (BoC) raised its rate by 50bps at its June meeting bringing the key rate to 1.5%. The central bank is expected to raise rates by 75bps in July and 50bps in September. It could then proceed with two 25bps hikes to bring the overnight rate to 3.25% by the end of the year. The BoC's monetary policy is one of the most aggressive in the G10 economies and should support the currency. Real bond yields are higher than in the United States.

The economy is close to full employment and an increase in rates is necessary to avoid a wage-price spiral. Inflation has reached 7.7% in May up from 6.8% in April.

The price of oil (WTI) has declined from its April peak of around \$120 per barrel and now stands at around \$101. This level is still high compared to recent years and is a supportive factor for the currency.

**We maintain our targets at 1.25 (value of one USD) for the CAD over a 3- and 12-month horizon, which suggests upside potential from current levels.**



## CNY VIEW &gt;&gt;

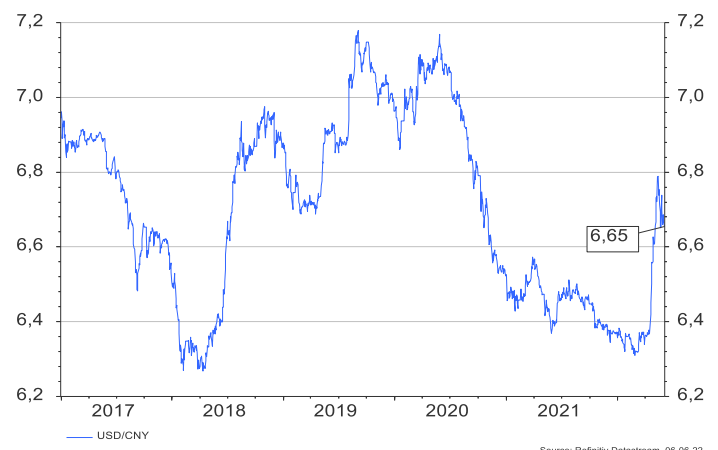
## TARGET 12M VS USD: 6.5

## Gradual recovery expected

There was no clear trend in the USDCNY over the past month. The People's Bank of China is one of the only central banks which could cut rates this year. In May, it cuts the loan prime rate by 15bps to 4.45%. Inflation is indeed quite low in China at 2.1% and the government is thus more focused on easing monetary conditions to boost growth. Although falling slightly, real rates are largely positive unlike many economies. This is a supportive factor for the CNY.

The manufacturing business survey (PMI) rose to 51.8 in June from 48 in May, reflecting improvements in supply chains and fewer mobility restrictions. Delivery times have decreased for the first time in two years, while order books are growing again. The recovery could be gradual in the second half of the year.

**We remain confident that the CNY will gradually stabilize and appreciate over the coming year thanks to better economic newsflow. We therefore maintain our 3-month target at 6.6 and 12-month target at 6.5.**



## Emerging Markets VIEW >>

### Bullish on BRL and MXN

The Fed's rate hike is limiting the appeal of some emerging currencies and partly explains the decline of the currencies of India, Mexico and South Africa in the first part of the year.

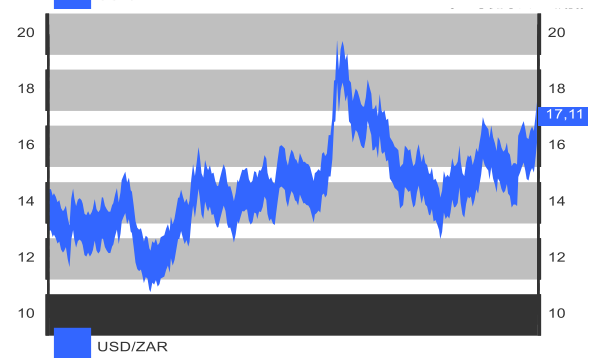
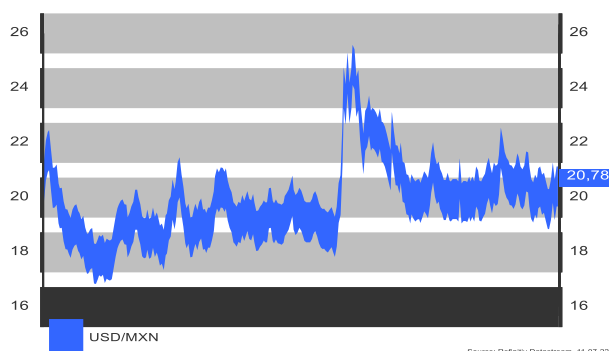
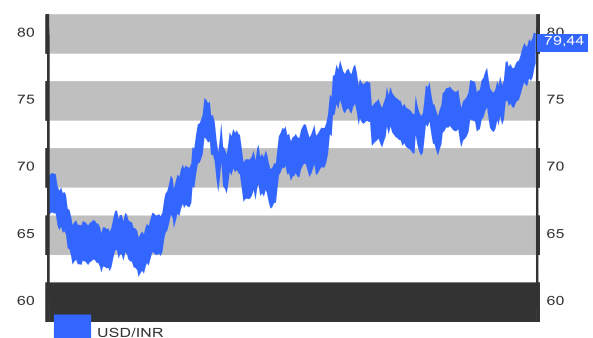
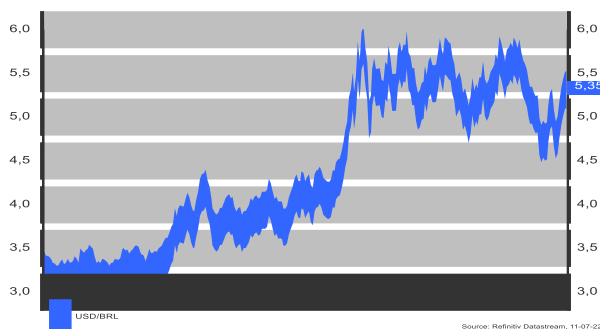
The Brazilian currency (BRL) has depreciated quite a bit over the past 30 days on the back of the Chinese slowdown and risk aversion. The prices of most metals and agricultural commodities that Brazil exports have remained high. The price of iron ore, which represents 12% of Brazilian exports, has fallen back below \$120. This is a drag for the BRL. As annual inflation is being close to 12%, the interest rate was increased to 13.75%. Monetary policy is restrictive, and the high level of rates should support the BRL in the medium term. Brazil offers positive interest rates, and the carry trade is favorable for the currency. We are therefore positive on the BRL from current levels. **We keep our targets unchanged at 5 (value of one USD) for 3-month and 12-month.**

Inflation in Mexico reached 7.6%, a 21-year high. The bank of Mexico raised its rates by 75 bps and the key rate is now at 7.75%. Mexican debt should thus offer positive real rates which should support the currency.

The market is still pricing 155bps to come. Over the next year, the outflows caused by the pandemic should come back and support the MXN. The economic recovery is still unclear due to the rise in energy and raw material prices, which is increasing the country's current account deficit. **We change our 12-month target from 19 to 19.5 and we keep the 3-month at 20.5 (value of one dollar).** It suggests appreciation from current levels.

In South Africa, the currency has lost around 7% over the past 30 days. Recent flooding and power outages have impacted economic activity, reduced exports and weakened the currency (ZAR). However, high commodity prices, although below their peak, are a supporting factor for the future. The country is expected to record a positive current account balance in 2022 before turning negative again in 2023. **We change our 3-month ZAR target from 15 to 15.5. We also modify our 12-month target to 16 from 15.** This still suggests an appreciation but more moderate.

The Indian currency (INR) is close to an all time low against the dollar. The Indian rupee is under pressure due to the context of rising energy and food prices, and rising debt costs. India is vulnerable to capital outflows. Imported energy inflation weakens its economy. The Reserve Bank of India (RBI) raised rates by 50bps at the last meeting from 4.4% to 4.9%, with inflation expected to reach 6.7% this year versus 5.7% before. High energy prices and the difficult post-pandemic recovery continue to worsen the trade balance, leading us to revise our targets. **We change our 3-month and 12-month targets to 78 and 80 respectively (from 76 and 78).**



	Country	Spot 7/11/2022	Trend	Target 3 months (vs. EUR)	Trend	Target 12 months (vs. EUR)	
	United States	EUR / USD	1.01	Negative	1.03	Negative	1.12
	United Kingdom	EUR / GBP	0.84	Neutral	0.84	Neutral	0.84
	Japan	EUR / JPY	138.59	Negative	144	Negative	146
	Switzerland	EUR / CHF	0.99	Negative	1.02	Negative	1.02
	Australia	EUR / AUD	1.50	Positive	1.39	Neutral	1.51
	New-Zealand	EUR / NZD	1.65	Positive	1.51	Neutral	1.65
	Canada	EUR / CAD	1.31	Neutral	1.29	Negative	1.40
	Sweden	EUR / SEK	10.69	Positive	10.40	Neutral	10.70
	Norway	EUR / NOK	10.27	Positive	9.60	Positive	9.60
Asia	China	EUR / CNY	6.76	Neutral	6.80	Negative	7.28
	India	EUR / INR	80.10	Neutral	80.34	Negative	89.60
Latam	Brazil	EUR / BRL	5.40	Positive	5.15	Negative	5.60
EMEA	Russia	EUR / RUB	63.22	Negative	103.00	Negative	100.80

	Country	Spot 7/11/2022		Trend	Target 3 months (vs. USD)	Trend	Target 12 months (vs. USD)
	Eurozone	EUR / USD	1.01	Positive	1.03	Positive	1.12
	United Kingdom	GBP / USD	1.19	Positive	1.23	Positive	1.33
	Japan	USD / JPY	137.45	Neutral	140.00	Positive	130.00
	Switzerland	USD / CHF	0.98	Neutral	0.99	Positive	0.91
	Australia	AUD / USD	0.67	Positive	0.74	Positive	0.74
	New-Zealand	NZD / USD	0.61	Positive	0.68	Positive	0.68
	Canada	USD / CAD	1.30	Positive	1.25	Positive	1.25
Asia	China	USD / CNY	6.71	Neutral	6.60	Positive	6.50
	India	USD / INR	79.43	Neutral	78.00	Neutral	80.00
Latam	Brazil	USD / BRL	5.35	Positive	5.00	Positive	5.00
	Mexico	USD / MXN	20.78	Neutral	20.50	Positive	19.50
EMEA	Russia	USD / RUB	62.70	Negative	100.00	Negative	90.00
	South Africa	USD / ZAR	17.05	Positive	15.50	Positive	16.00
	USD Index	DXY	108.02	Neutral	105.92	Negative	98.40

Source: Refinitiv - BNP Paribas WM

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