Investment Research

Danske Bank

FX Forecast Update
Fed failed; USD strength set to prove more persistent

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Important disclosures and certifications are contained from page 22 of this report

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Forecast review part I

- **EUR/NOK.** The outlook for a stronger NOK suffered a clear blow last week, as the less committed easing message from the Fed's Jerome Powell has paved the way for more persistent USD strength. In our view, a strong USD and weak global cycle are likely to keep industrial metals and oil prices under pressure longer than we previously expected. This in turn constitutes an extended headwind for commodity FX and high beta currencies in general, including NOK. On the back of this, we lift our front-end forecasts to 9.80 in 1M (from 9.60) and 9.65 in 3M (9.50). We still expect Norges Bank to add further carry attractiveness to the NOK by hiking rates in September. Indeed as long as growth remains above trend, the NOK is simply too weak for the central bank to reach its inflation target (see *FX Strategy – Why is the NOK so weak?*, 28 May). However, global drivers remain the primary determinants and with the latest developments, we acknowledge reduced NOK potential in the medium to long term too. We forecast EUR/NOK at 9.60 in 6M (9.50) and 9.50 in 12M (9.30).

- **EUR/SEK.** We stick to our bearish medium-term view on the SEK based on a cyclical economic slowdown, domestically and abroad, and a subdued inflation outlook that we believe will re-challenge the Riksbank (the upcoming wage round will, in our view, not make it any easier to achieve its target). Global uncertainties and the sudden re-escalation of the trade war have weighed on the SEK recently and may continue to do for some time. However, next week's Swedish inflation data may prompt a small correction lower in EUR/SEK as our forecast is above that of the Riksbank. We remain comfortable with an upward-sloping medium-term trajectory for EUR/SEK and make only small adjustments to our forecast profile: we raise 1M to 10.70 (previously 10.50), 3M to 10.80 (was 10.70), 6M to 10.90 (was 10.80) and 12M to 11.00 (was 10.90).

- **EUR/DKK.** We see a case for Danmarks Nationalbank not fully tracking an ECB rate cut in September. This would reduce the negative carry on short EUR/DKK positions and send EUR/DKK lower. We forecast EUR/DKK at 7.4630 in 1M, 7.4575 in 3M, 7.4550 in 6M and 7.4550 in 12M.

- **EUR/USD.** The lack of a forceful response from the Fed to a weakening economy and lacklustre inflation expectations was a blow to our view of a short-term bounce in EUR/USD. In our view, a shallow rate cut cycle from the Fed would keep EUR/USD range bound in 3M, around 1.10 (revised down from 1.15). in 6-12M, we still look for a higher EUR/USD towards 1.13 in 6M (revised down from 1.17) and 1.15 in 12M (revised down from 1.17) on the erosion of USD carry, valuation, an improved outlook for the global economy and the odds of a trade deal.

- **EUR/GBP.** In the run-up to the Brexit deadline at end-October, we expect EUR/GBP to remain volatile and maybe more so than we previously thought likely. Financial markets are taking Boris Johnson's direct approach literally and, in the run-up to October, this could mean EUR/GBP will drift higher. Ultimately, we believe EUR/GBP could go as high as 0.97 (previously, we were thinking 0.91). Our base case continues to be a much, much less dramatic outcome at the end of October. We expect EUR/GBP to settle at 0.89-0.91 on the back of an extension and/or snap election. In the case of a decent deal or cancellation of Brexit, we believe EUR/GBP will turn towards 0-83-0.86. Although the outcome is anybody's guess, we believe it will improve after October.

- **USD/JPY.** Continued weakening of global demand is likely to take US yields to new lows and support JPY strength. We lower our USD/JPY forecast to 105.0 in 3M (previously 107.0) and weaken our expectation to a near-term rebound, lowering the 6M forecast to 105 (from 110). Strengthening global demand continues to be the base case on a 12M horizon, which shifts USD/JPY to 110.0 (unchanged forecast). The range of likely outcomes currently appears to be 105-110, with the short-term risk being largely negative.

- **EUR/CHF.** CHF is set to be under continued pressure from global risk-off sentiment following the less dovish Fed, global weakness and increasing trade tensions. While our medium-term bias remains for a higher pair on fundamentals, risks are, in our view, skewed towards even more CHF strength near term. The ECB being set to deliver a significant easing package at the September meeting is likely to put even more pressure on the SNB to follow suit, i.e. go further negative and possibly expand its balance sheet further. However, that, the SNB (1) revealed its distaste for balance-sheet expansion when abandoning the EUR/CHF floor in January 2015 and (2) may be closing in on a tipping point for where more negative rates could become counterproductive implies that markets could test the SNB's willingness and ability to deliver. This cocktail could send EUR/CHF well below 1.10. We lower our near-term forecast of EUR/CHF to 1.09 (from 1.11) in 1M and 1.10 in 3M (from 1.11) and stress that the risks to this are on the downside and dependent on the SNB's actions. We also lower our 6M and 12M forecasts to 1.12 and 1.14 (from 1.13 and 1.15, respectively).

- **USD/CAD**. The higher persistency of USD strength than we previously pencilled in marks a headwind for oil, global risk appetite and hence the CAD. Both headline and core inflation in Canada is trading just above 2%. However, inflation expectations have moved sharply lower recently, trading close to the 2016 low. With this in mind, the Fed cutting rates and the escalation in the trade war, we now pencil in two 25bp rate cuts from Bank of Canada over the coming 12M. Fundamentally, we still regard USD/CAD as overvalued with fair-value estimates in the low 1.20s. We forecast USD/CAD at 1.32 in 1M (from 1.30), 1.30 in 3M (1.28), 1.29 in 6M (1.27) and 1.27 in 12M (1.25).

- **USD/CNY**. Due to the recent escalation of the trade war, we have lifted our USD/CNY forecast to 7.05 in 1M (6.95), 7.10 in 3M (7.0) and 7.20 in 6M and 12M. We see a rising probability that the US and China will not reach a trade deal before the US election in November 2020 and that Donald Trump will raise tariffs further on imports from China worth USD300bn to 25%.

- **NZD/USD and AUD/USD** are set to be low, for longer. In New Zealand, leading indicators have shifted further down and now track annual GDP growth around 1.5%, in contrast to RBNZ's projection of 2.5-3.0%. Inflation prints have been slightly better but remain below target and the committee is likely to judge that downside risks to its inflation target remain in place given the global growth outlook. In Australia, housing market activity indicators are showing a tentative stabilisation but recent retail sales are showing consumption is weakening to a multi-year low. Both central banks are actively easing monetary policy in light of these developments.

The recent slightly hawkish comments from the Fed and re-escalation of the US-China trade war put both economies at risk and currency markets have been extremely speedy in pricing towards new multi-year lows, from what had previously been a positive outlook. Hence, since a month ago, the risk has shifted from upside to slight downside once again. We think the upcoming 1-6M outlook is worse than it appeared in June and July and we revise our expectations accordingly, while a more positive scenario in 12M puts a bottom in for the crosses. We revise **AUD/USD** to 0.67 in 1M (previously 0.70), 0.67 in 3M (previously 0.71), 0.70 in 6M (previously 0.715) and 0.70 in 12M (previously 0.715). Correspondingly, we set **NZD/USD** at 0.645 in 1M (previously 0.67), 0.645 in 3M (previously 0.675) and 0.67 (previously 0.68) in 6M and 12M. Nonetheless, these crosses are extremely sensitive to small changes in the perception of future Fed and trade policy and news on this front would materially and swiftly change spot pricing as well as the outlook. To see a rise to the highs of 2016-18, we would need to see a strong pickup in global activity; this remains very tentative though.

- **USD/RUB.** RUB continues to follow global risk sentiment, while the recent US sanctions did not have a significant impact on the Russian currency as Russia's local debt remains out of scope. In early August 2019, US President Trump signed an executive order imposing sanctions on Russia. It was the second round of sanctions by the US administration. The US banned loans or other assistance to Russia by international financial institutions and prohibited most loans from American banks to Russia's government. We slightly increase our 1M forecast to 65.60 (up from 65.40) and revise our forecast down for 3M to 66.00, 6M to 67.00 and 12M to 68.00 (down from 67.00, 68.00 and 69.00 respectively).

- **EUR/PLN.** The ECB's softening stance and the renewed trade dispute between China and the US sent EUR/PLN higher. We believe US-China trade tensions are likely to continue into 2020, which, in our view, would send the pair higher (the PLN has been relatively immune to the risk-off periods lately). As a result, we see a slight case for EUR/PLN to edge higher on a short-term basis to 4.32 (previously 4.28) in 1M but then as the Fed delivers on the cutting side in September, we see the pair going down to 4.25 in 3M, 4.23 in 6M and 4.23 in 12M.

- **USD/TRY.** The TRY is stabilising on a global turn to monetary easing, while quick monetary easing by the TCMB limits the TRY's attractiveness in carry trades. However, domestic risk is still there. Because of global monetary relief, we adjust our USD/TRY outlook enhancing that the fragile domestic and geopolitical environment is still in place. Large FX debt redemptions by the Turkish private sector and more rate cuts later in 2019 are set to weigh on the TRY in 2019 and 2020. Thus, we remain bearish on the TRY in the long term, expecting the USD/TRY to reach the following levels: 5.60 in 1M, 5.70 in 3M, 5.90 in 6M and 6.00 in 12M (previously 5.70 in 1M, 5.90 in 3M, 5.90 in 6M and 6.20 in 12M).

- **Oil.** We expect oil prices to recover over the rest of 2019. We forecast Brent will average USD70/bbl in Q3 and USD75/bbl in Q4. In our view, OPEC+ cuts, a stabilisation of the global macro economy and eventually a weaker USD will underpin oil prices.

EUR/NOK – reduced potential for stronger NOK

- **Growth.** Back in June, the historically reliable Regional Network Survey indicated accelerating H2 mainland growth prospects of more than 3% y/y. Meanwhile, the past month's data releases have been on the weak side of expectations. Manufacturing sector surveys now suggest somewhat weaker growth ahead, as the impact of a slowing global industrial cycle seems increasingly to counter the positive domestic impulses from petroleum industries and oil investments. In addition, the fall in unemployment has slowed but this is at least partially due to rising bottleneck problems. Overall, however, we still expect above-trend growth in the year ahead driven by oil investments and consumption.
- **Monetary policy.** As expected, Norges Bank hiked the key policy rate by 25bp to 1.25% at the June monetary policy meeting. Meanwhile, as importantly, it clearly signalled that it intends to hike rates again as soon as September, with an additional high likelihood of another rate hike in 2020. While domestic releases have recently been somewhat on the soft side of expectations, we still expect Norges Bank to firm its September signal at the forthcoming interim August meeting. In addition, our base case remains two additional rate hikes in 2020.
- **Flows.** Foreign banks (proxy for speculative flows) have been net selling NOK over the past few weeks amid resurfacing trade war concerns and global risk off. Overall, we regard NOK positioning to be neutral.
- **Valuation.** From a long-term perspective, the NOK seems fundamentally undervalued. Our PPP model has 8.85 as 'fair'. A model incorporating relative productivity also suggests NOK potential after the year-long period of internal devaluation and NOK weakness.
- **Risks.** The biggest risk factors to our call are continued outperformance of the USD and a Fed not hiking rates while global growth remains weak. We could also be wrong in our above-trend call on Norwegian growth. In addition, any a breakdown in US -China trade negotiations would be NOK negative.

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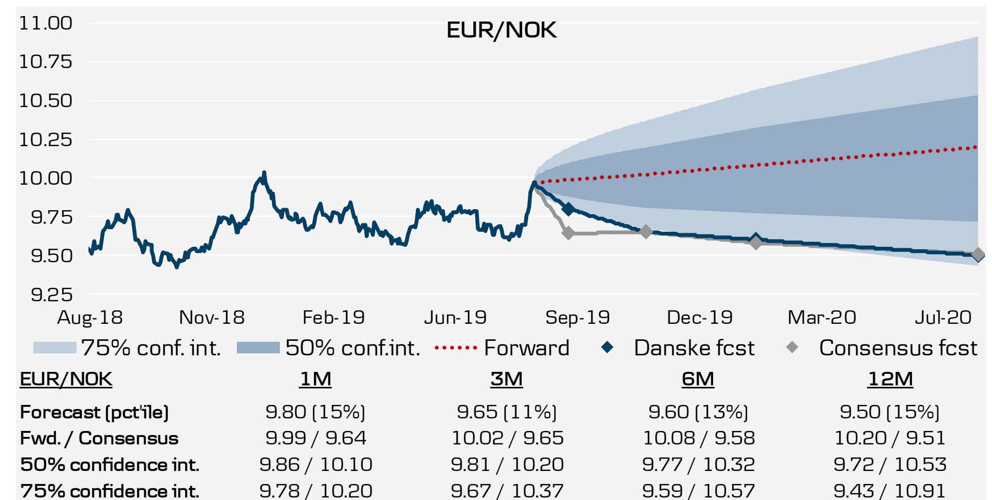
Forecast: 9.80 (1M), 9.65 (3M), 9.60 (6M), 9.50 (12M)



EUR/NOK	1M	3M	6M	12M
Forecast (pct'ile)	9.80 (15%)	9.65 (11%)	9.60 (13%)	9.50 (15%)
Fwd. / Consensus	9.99 / 9.64	10.02 / 9.65	10.08 / 9.58	10.20 / 9.51
50% confidence int.	9.86 / 10.10	9.81 / 10.20	9.77 / 10.32	9.72 / 10.53
75% confidence int.	9.78 / 10.20	9.67 / 10.37	9.59 / 10.57	9.43 / 10.91

Source: Danske Bank

- **Conclusion.** The outlook for a stronger NOK suffered a clear blow last week as the less committed easing message from the Fed's Powell has paved the way for more persistent USD strength. In our view, a strong USD and a weak global cycle is likely to keep industrial metals and oil prices under pressure longer than we previously expected. This in turn constitutes an extended headwind for commodity FX and high beta currencies in general, including NOK. On the back of this, we lift our front-end forecasts to 9.80 in 1M (from 9.60) and 9.65 in 3M (9.50).

  We still expect Norges Bank to add further carry attractiveness to the NOK by hiking rates in September. Indeed, as long as growth remains above trend the NOK is simply too weak for the central bank to reach its inflation target (see *FX Strategy – Why is the NOK so weak?*, 28 May). However, global drivers remain the primary determinants and with the latest developments, we acknowledge reduced NOK potential in the medium to long term. We forecast EUR/NOK at 9.60 in 6M (9.50) and 9.50 in 12M (9.30).

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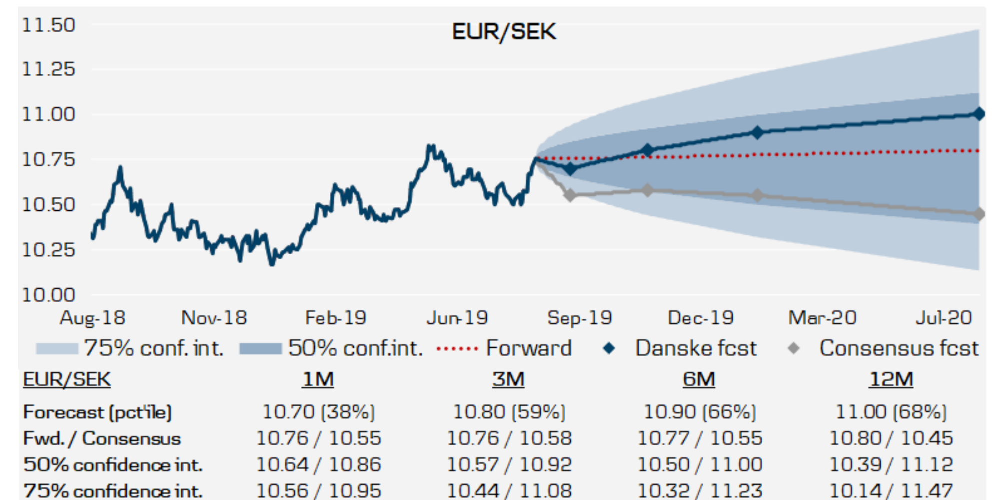
EUR/SEK – still on the increase

- **Growth.** The second-quarter GDP figure was a blow to the Riksbank, though in line with our estimate at 1.4% y/y (-0.1% q/q). It also fell short of market consensus and as such sent EUR/SEK sharply higher. In our view, domestic demand is an increasing headwind to growth and the SEK. Unfortunately, the global economic slowdown on the back of an escalating trade war is of no help either.
- **Monetary policy.** Despite soft messages and lingering cuts from the Fed and the ECB, the Riksbank stubbornly maintained its hiking bias in July, which in turn lent some support to the SEK. However, we think it is only a matter of time (September-October) before the Riksbank decides to postpone the next hike well into next year in an environment where both the Fed and the ECB have started to ease. Moreover, the growth outlook is likely to disappoint the Riksbank along with inflation (and wages). Hence, we expect no hike this year and probably not next year either, which would leave the policy rate in negative territory for longer. In our view, this will continue to weigh on the SEK especially versus the USD.
- **Flows.** The significant rate gap versus the US has held back commercial and investors' demand for the SEK and fuelled carry trades where SEK has been the funding currency. A more risk averse environment coupled with a smaller rate differential may lead to some unwinding of long USD/SEK positions. That said, the USD still stands out as the most attractive carry currency in the G10 space.
- **Valuation.** Fundamental factors can to some extent explain the recent years (real) depreciation of the SEK, although we would argue that ultra-easy monetary policy is the main culprit behind the weakening (see *FX Strategy – Hardships for the SEK*, 13 May).
- **Risks.** A pronounced risk-off environment has the potential to send the SEK down the drain (beyond 11.00 versus the EUR and beyond 10.00 versus the USD), though partially balanced by the scaling back of carry positions.

Forecast: 10.70 (1M), 10.80 (3M), 10.90 (6M), 11.00 (12M)



EUR/SEK	1M	3M	6M	12M
Forecast (pct'ile)	10.70 (38%)	10.80 (59%)	10.90 (66%)	11.00 (68%)
Fwd. / Consensus	10.76 / 10.55	10.76 / 10.58	10.77 / 10.55	10.80 / 10.45
50% confidence int.	10.64 / 10.86	10.57 / 10.92	10.50 / 11.00	10.39 / 11.12
75% confidence int.	10.56 / 10.95	10.44 / 11.08	10.32 / 11.23	10.14 / 11.47

Source: Danske Bank

- **Conclusion.** We stick to our bearish medium-term view on the SEK based on a cyclical economic slowdown, domestically and abroad, and a subdued inflation outlook that we expect to re-challenge the Riksbank (in our view, the upcoming wage round will not make it any easier to achieve its target). Global uncertainties and the sudden re-escalation of the trade war have weighed on the krona recently and may continue to do so for some time. However, next week's Swedish inflation data may prompt a small correction lower in EUR/SEK as our forecast is above that of the Riksbank. We remain comfortable with an upward-sloping medium-term trajectory for EUR/SEK and make only small adjustments to the forecast profile: we raise 1M to 10.70 (10.50), 3M to 10.80 (10.70), 6M to 10.90 (10.80) and 12M to 11.00 (10.90).

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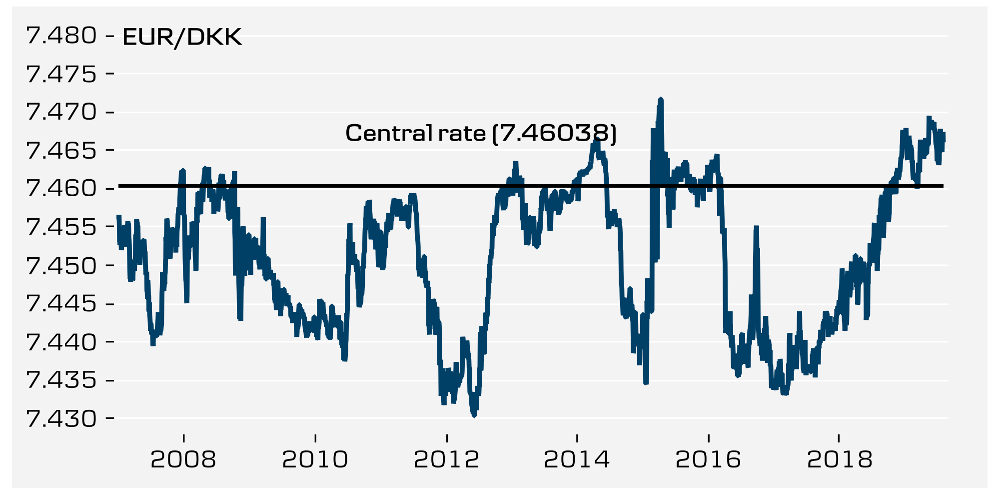
EUR/DKK – set to head back below the central rate

- **FX.** EUR/DKK continues to trade on the weak side of the central rate, while Danmarks Nationalbank has stayed on the sidelines in the FX markets since January. Near-term, EUR/DKK is likely to stay supported by trade war woes, weak equity markets and a large discount in FX forwards. However, after the September ECB meeting, the latter should narrow and send EUR/DKK lower. We forecast EUR/DKK at 7.4630 on 1M, 7.4575 on 3M and 7.4550 on 6M and 7.4550 on 12M.
- **Rates and forwards.** We look for the ECB to cut by 20bp in September, but Danmarks Nationalbank to go only halfway and cut by 10bp. This would bring the interest rate on certificates of deposit down to minus 0.75%. This in turn would narrow the wide discount in EUR/DKK FX forwards. The tricky part though is that we also expect the ECB to introduce a tiered deposit system, which may weaken the pass through of the ECB's rate cut to market rates and thus EUR/DKK FX forwards.
- **Flows.** The Danish current account surplus remains large but has moderated somewhat from the elevated level seen in past years. It still creates fundamental support for DKK. We expect a high savings rate and low investment activity to maintain this situation in coming years. Denmark has significant exposure to the US, as it earns around one-third of the surplus in the US.
- **Liquidity.** In H2, we expect the net position to rise to DKK220-270bn most days but in August we could see it touch the top end of this range. The Debt Management Office has sold a substantial amount of treasury bills, which has led to a temporary drain in liquidity compared with our previous forecast.

Forecast: 7.4630 (1M), 7.4575 (3M), 7.4550 (6M), 7.4550 (12M)



Source: Danske Bank

- **Conclusion.** We see a case for Danmarks Nationalbank not fully tracking an ECB rate cut in September. This would reduce the negative carry on short EUR/DKK positions and send EUR/DKK lower. We forecast EUR/DKK at 7.4630 in 1M, 7.4575 in 3M and 7.4550 in 6M and 7.4550 in 12M.

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EUR/USD – Fed set to keep USD strong for now

- **Growth.** The trade war escalation, geopolitical tensions, a downturn in global manufacturing and the slow adjustment of monetary policy by the Fed and ECB are all factors weighing on US and euro area economies. However, the US economy still looks relatively stronger. We do not see an imminent turn around for the better but a chance of stabilisation around the current weaker levels. Inflationary pressures remain muted in both economies and inflation expectations are at risk of becoming deanchored.

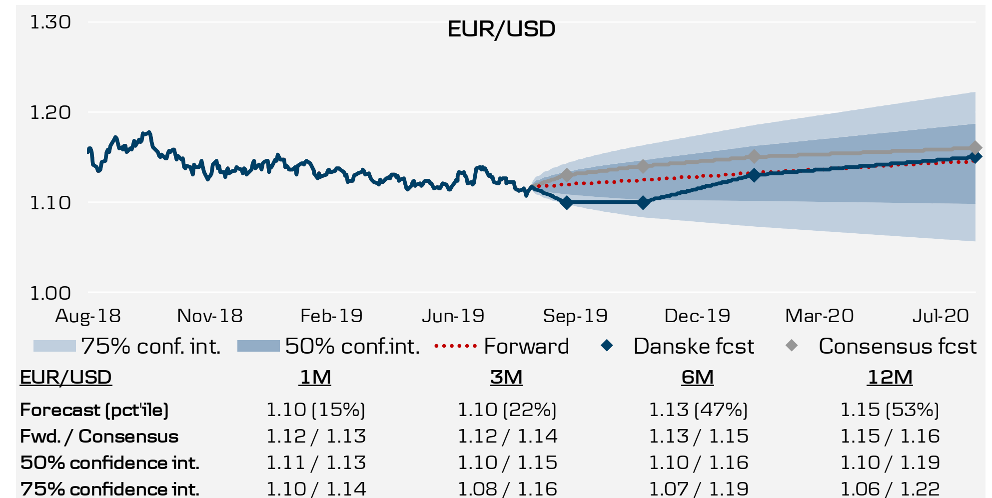
- **Monetary policy.** Both the ECB and Fed disappointed the market with the outcome of their July monetary policy meetings. The ECB signalled that rate cuts and QE are coming, while the Fed cut by 25bp and halted quantitative tightening. However, the market was looking for a more forceful reaction. We expect further adjustments of monetary policy in September. We look for the ECB to cut by 20bp, coupled with the introduction of a tiered deposit system and a restart of quantitative easing. We expect the Fed to cut by another 25bp. There is a risk that this scenario will disappoint market pricing again.

- **Flows.** External balances as measured by relative current-account balances hint at EUR/USD upside in the medium term but history suggests a deficit like the US one can be sustained for prolonged periods, notably for a world reserve currency like the USD. The large eurozone capital outflows, which ECB policy has arguably spurred, have faded but with an end to negative rates nowhere in sight, a reversal is not on the cards near term.

- **Valuation.** The USD remains generally overvalued on most measures and our MEVA and PPP estimates for EUR/USD are in the 1.20s, suggesting the direction of gravity should still be higher medium term.

- **Positioning.** The market has started to add short EUR/USD positions again.

Forecast: 1.10 (1M), 1.10 (3M), 1.13 (6M), 1.15 (12M)



EUR/USD	1M	3M	6M	12M
Forecast (pct'ile)	1.10 (15%)	1.10 (22%)	1.13 (47%)	1.15 (53%)
Fwd. / Consensus	1.12 / 1.13	1.12 / 1.14	1.13 / 1.15	1.15 / 1.16
50% confidence int.	1.11 / 1.13	1.10 / 1.15	1.10 / 1.16	1.10 / 1.19
75% confidence int.	1.10 / 1.14	1.08 / 1.16	1.07 / 1.19	1.06 / 1.22

Source: Danske Bank

- **Risks.** If the Fed steps up easing more forcefully in the short-term, we could see a faster rebound in EUR/USD than we project.

- **Conclusion.** The lack of forceful response from the Fed to a weakening economy and lacklustre inflation expectations was a blow to our view of a short-term bounce in EUR/USD. A shallow rate cut cycle from the Fed would keep EUR/USD range bound around 1.10 in 3M (revised down from 1.15). In 6-12M, we still look for a higher EUR/USD towards 1.13 on 6M (revised down from 1.17) and 1.15 on 12M (revised down from 1.17) on the erosion of USD carry, valuation, an improved outlook for the global economy and the odds of a trade deal.

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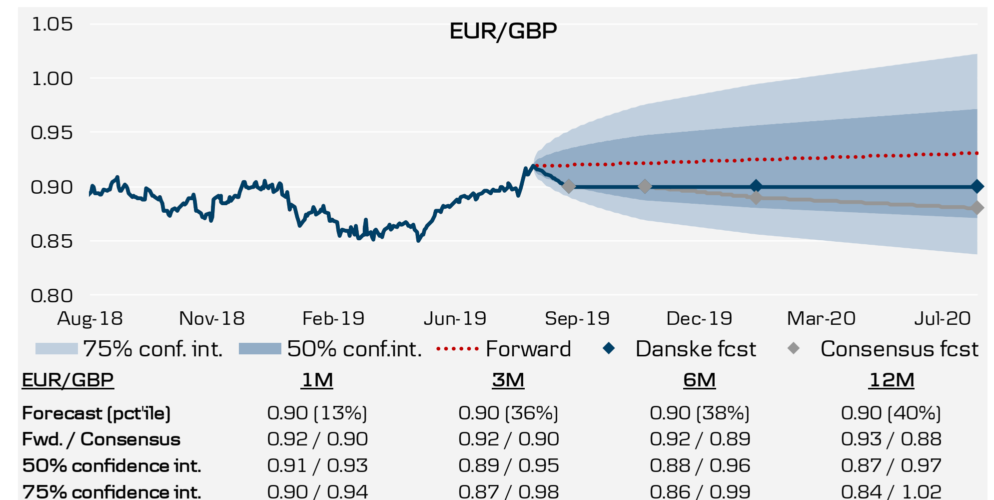
EUR/GBP – it's anybody's guess but we believe it'll improve after October

- **Recent history.** The GBP weakened somewhat after Theresa May stepped down. Additional weakening came on the back of declining domestic demand and with Boris Johnson having taken office, we have seen a further but mild weakening of the GBP. From best to worst, the GBP has net lost about 8% in a matter of three months.
- **Politics take centre stage, again.** Even if Boris Johnson wants to have Brexit settled, the arithmetic in the House of Commons does not change and it will be difficult to force a no-deal Brexit through. Our base case is another Brexit extension but this is not a high conviction call. Pivotally, we intend to monitor whether and if the dynamics in British politics change and we may see a snap election to get just that.
- **The range of possible EUR/GBP outcomes has widened.** Financial markets are taking Boris Johnson's direct approach literally and, in the run-up to October, that could mean EUR/GBP will drift higher – towards 0.97, say. Our base case remains an extension with EUR/GBP at 0.90 but the uncertainty is high.
- **Growth.** With the extension of Brexit, the period with uncertainty is prolonged, which will continue to be a drag on the economy. GDP expectations are running around 1% and downside risk is prevalent but as of today the numbers out of the UK remain decent.
- **Monetary policy.** The Bank of England continues to be quite passive. The communication is 'whatever happens, we will set interest rates to return inflation sustainably to target and provide what support we can to jobs and growth.' In practice, this means monetary policy is unlikely to change before either (1) we see a much stronger worsening in UK data or (2) a dramatic (or peaceful) Brexit is completed, after which policy may move in either direction.
- **Flows.** Investor positioning is heavily GBP short.

Forecast: 0.90 (1M), 0.90 (3M), 0.90 (6M), 0.90 (12M)



EUR/GBP	1M	3M	6M	12M
Forecast (pct'ile)	0.90 (13%)	0.90 (36%)	0.90 (38%)	0.90 (40%)
Fwd. / Consensus	0.92 / 0.90	0.92 / 0.90	0.92 / 0.89	0.93 / 0.88
50% confidence int.	0.91 / 0.93	0.89 / 0.95	0.88 / 0.96	0.87 / 0.97
75% confidence int.	0.90 / 0.94	0.87 / 0.98	0.86 / 0.99	0.84 / 1.02

Source: Danske Bank

- **Valuation.** GBP remains fundamentally undervalued: Our G10 MEVA model puts EUR/GBP at 0.78 (our Brexit-corrected MEVA estimate for the cross is around 0.83), while our PPP estimate is 0.76.
- **Risks.** There is a large Brexit premium (about 5-10%) which, if fully unwound, would strengthen GBP substantially.
- **Conclusion.** In the run-up to the end-October Brexit deadline, we expect EUR/GBP to remain volatile and maybe more so than we previously thought likely. Ultimately, EUR/GBP can go as high as 0.97 (previously, we thought 0.91). **Our base case continues to be a much, much less dramatic outcome at end-October. We expect EUR/GBP to settle at 0.89-0.91 on the back of an extension** and/or snap election. In the case of a decent deal or cancelation of Brexit, we believe EUR/GBP will turn towards 0-83-0.86.

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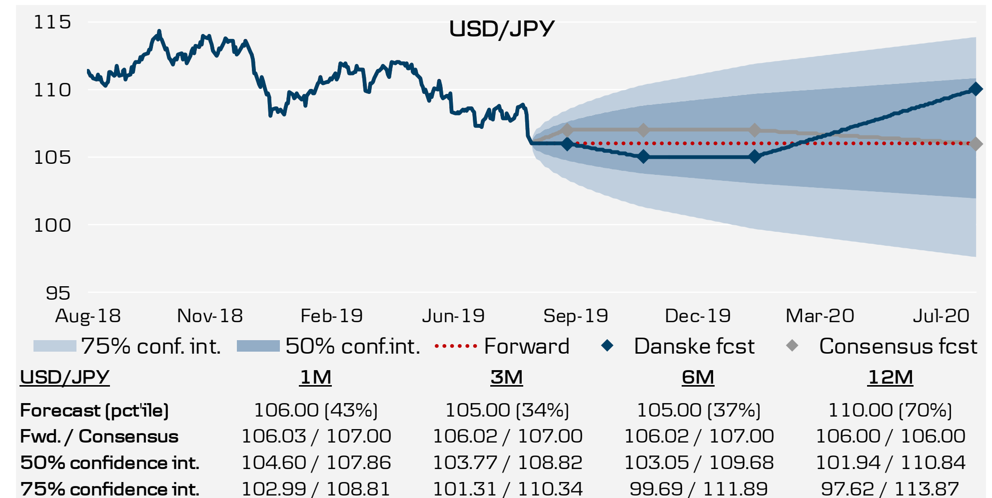
USD/JPY – JPY strength is not over – we now target 105.0 in 3M-6M

- **Recent history.** USD/JPY has been shifted around by major but quarterly trends in global sentiment. Lately, the combination of escalating trade skirmish, Brexit, a worsening of global demand and a more hawkish US central bank have added to JPY strength. Falling US yields and declining commodities has been a key driver of this.
- **Sentiment is the key driver.** We expect global sentiment to remain the key driver in the cross as risk-off, commodity sell-off and falling US rates run together and amplify each other to take USD/JPY lower. If central banks manage to stabilise sentiment and oil prices, we believe we would be likely to see JPY towards 110 in coming months. Continued weakening of global demand is likely to take US yields to new lows and support JPY strength.
- **Inflation and monetary policy.** We do not expect any changes in rates or the magnitude of the QQE this side of 2021. However, the probability that the flexibility around the 0% 10-year rate-target is expanded has risen following governor Haruhiko Kuroda and deputy governor Masayoshi Amamiya's comments recently in the wake of the market push for lower rates.
- **Terms of trade.** Commodity prices have come down, giving rise to a positive terms of trade shock, which supports JPY strength. Our expectation of improvements in commodity prices over the summer was short-lived, not least as the Fed has backtracked slightly on its dovish communication, leading to rising USD and falling commodity prices.
- **Flows.** Japan continues to be a significant capital exporter via its large current account surplus of above 3% of GDP, suggesting the currency relative to fundamentals is somewhat weak.
- **Valuation.** PPP is around 80, while our MEVA model suggests 104.
- **Positioning.** Investors are overall neutrally positioned in the cross.

Forecast: 106.0 (1M), 105.0 (3M), 105.0 (6M), 110.0 (12M)



USD/JPY	1M	3M	6M	12M
Forecast (pct'ile)	106.00 (43%)	105.00 (34%)	105.00 (37%)	110.00 (70%)
Fwd. / Consensus	106.03 / 107.00	106.02 / 107.00	106.02 / 107.00	106.00 / 106.00
50% confidence int.	104.60 / 107.86	103.77 / 108.82	103.05 / 109.68	101.94 / 110.84
75% confidence int.	102.99 / 108.81	101.31 / 110.34	99.69 / 111.89	97.62 / 113.87

Source: Danske Bank

- **Upside risks.** Drivers set to take JPY back above 110 include (1) an inflation-driving Fed cut ,2() strong BoJ easing (currently very unlikely) and/or (3) improving global macro.
- **Downside risks.** Events that could take JPY below 105 include (1) declining commodity prices, (2) a continued deterioration of global demand, which looks likely as of today and (3) further negative news from the trade war.
- **Conclusion.** We lower our USD/JPY forecast to 105.0 in 3M (previously 107.0) and weaken our expectation to a near-term rebound, lowering our 6M forecast to 105 (from 110). Strengthening global demand continues to be the base case on a 12M horizon, which shifts USD/JPY to 110.0 (unchanged forecast). The range of likely outcomes currently appears to be 105-110, with short-term risk being largely negative.

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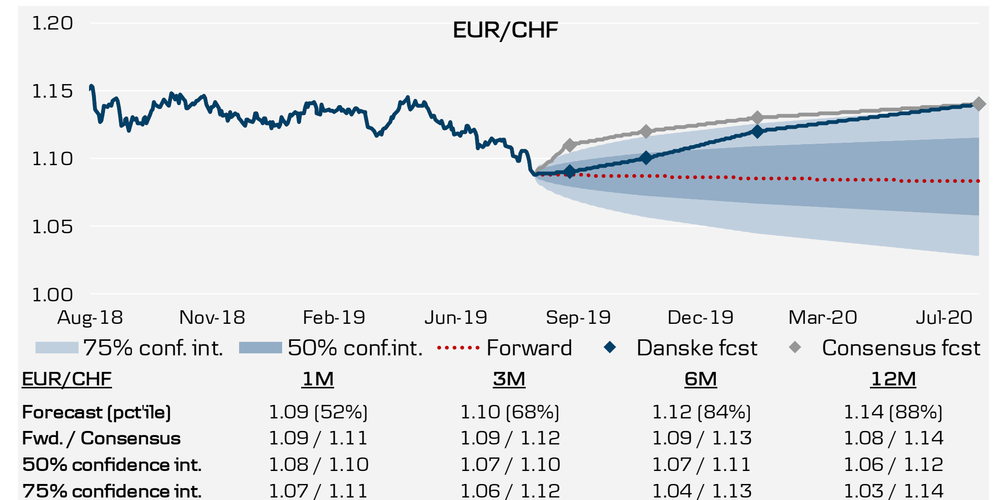
EUR/CHF – global risk-off and dovish ECB calls for SNB intervention

- **Growth.** Since the solid Q1 GDP print at 0.6% q/q, leading indicators have generally been moving downwards, meaning we expect less from the Q2 figures. While the KOF indicator improved slightly in July from a very low level, we now have both manufacturing and service PMIs well below 50 (at 44.7 and 48.2, respectively) telling a story of broader European weakness hitting the economy. That said, unemployment remains low at 2.3% (sa) for now and inflation continues to be around 0.5%, with little pipeline inflationary pressure in sight and downward pressure from a stronger CHF. Eurozone and global weakness, including the trade war, remain risks.
- **Monetary policy.** It is now a matter of how the ECB eases monetary policy, no longer if. We expect this to put pressure on the SNB to follow suit, i.e. go further into negative territory and possibly expand its balance sheet further. On top of this, the recent pressure on the CHF from global risk-off sentiment following the less dovish Fed, global weakness and increasing trade tensions could eventually force the SNB to intervene in coming weeks, although it has a distaste for balance sheet expansion given its current size. We see evidence of intervention by the SNB from the latest sight deposit data. Although this is small from an historical perspective, we will follow developments in the balance sheet closely, as intervention might be the only thing stopping EUR/CHF from falling deeply through the 1.10 level, which would cause further deflationary pressure and test the credibility of the SNB.
- **Flows.** Speculative positioning remains stretched CHF shorts.
- **Valuation.** Our longer-term valuation models suggest the cross should move higher in the medium to long term, with fundamental estimates in the mid 1.20s.
- **Risks**. While our medium-term bias remains for a higher pair on fundamentals, risks are in our view skewed towards even more CHF strength near term on global risk-off and central bank impotence.

Forecast: 1.09 (1M), 1.10 (3M), 1.12 (6M), 1.14 (12M)



EUR/CHF	1M	3M	6M	12M
Forecast (pct'ile)	1.09 (52%)	1.10 (68%)	1.12 (84%)	1.14 (88%)
Fwd. / Consensus	1.09 / 1.11	1.09 / 1.12	1.09 / 1.13	1.08 / 1.14
50% confidence int.	1.08 / 1.10	1.07 / 1.10	1.07 / 1.11	1.06 / 1.12
75% confidence int.	1.07 / 1.11	1.06 / 1.12	1.04 / 1.13	1.03 / 1.14

Source: Danske Bank

- **Conclusion.** EUR/CHF is set to see continued pressure from global risk-off sentiment after the less dovish Fed, global weakness and rising trade tension. While our medium-term bias remains for a higher pair on fundamentals, we believe risks are skewed towards even more CHF strength near term. The ECB being set to deliver a significant easing package at the September meeting is likely to put even more pressure on SNB to follow suit, i.e. go further negative and possibly expand its balance sheet further. However, the SNB (1) revealing its distaste for balance-sheet expansion when abandoning the EUR/CHF floor in January 2015 and (2) maybe closing in on a tipping point for where more negative rates could become counterproductive implies markets could test the SNB's willingness/ability to deliver. This could send EUR/CHF well below 1.10. We lower our near-term forecast for EUR/CHF to 1.09 (from 1.11) in 1M and 1.10 in 3M (was 1.11) and stress that risks are on the downside and dependent on the SNB's actions. We cut our 6M and 12M forecasts to 1.12 (was 1.13) and 1.14 (was 1.15).

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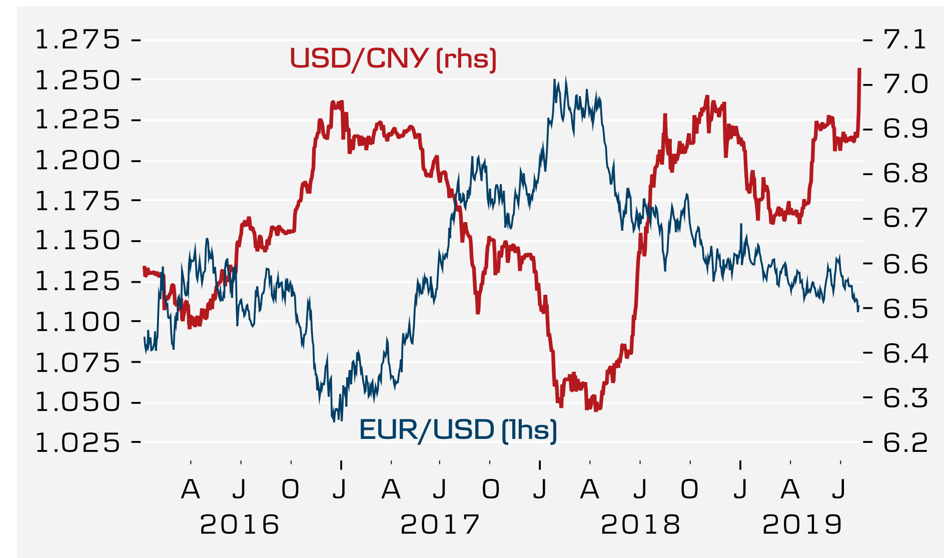
USD/CNY – more CNY weakness as trade war escalates

- **Growth.** Chinese PMI data points to a slowdown in growth but no hard landing. In recent months, the data has stabilised at a soft level. The recent escalation of the trade war puts more downside pressure on growth, which we expect to be partly compensated for by more Chinese stimulus. Our expectation of a moderate recovery in Q4 is now postponed into 2020. There is also a clear risk that Trump will add even more tariffs on China, which would leave a soft growth picture well into 2020. In our view, a trade deal before the US election in November 2020 is becoming less likely.
- **Monetary policy.** China has eased monetary policy since April last year by cutting the Reserve Requirement Ratio (RRR) and through measures to improve credit availability to the private sector. We look for a further cut in the RRR soon due to the trade war flaring up again and more targeted credit easing towards the small and medium sized companies.
- **FX policy**. CNY continues to be a managed peg against a basket of currencies. The PBoC allows the market to drive the CNY and intervenes less frequently than in the past. However, it aims to dampen volatility if moves in the currency are too sharp. Although the CNY has weakened significantly lately, we do not believe China will use it as a weapon in the trade war. Rather the weakening is due to heightened uncertainty and hedging flows. China wants to be seen as responsible and a devaluation would also hurt countries other than the US.
- **Flows.** FX reserves have increased moderately this year, showing little sign of outflows. However, anecdotal evidence suggests that China has tightened capital controls to stem outflows. In addition, portfolio inflows this year have been supported by an increase in the weight of Chinese equities in the MSCI Emerging Markets Index as well as inclusion of Chinese bonds in the Bloomberg Barclays index from 1 April.

Forecast: 7.05 (1M), 7.10 (3M), 7.20 (6M), 7.20 (12M)



Source: Danske Bank

- **Conclusion.** We expect the downward pressure on CNY to persist and keep our 3M target at 7.10. We have also lifted our 6M and 12M forecasts to 7.20, as we see less likelihood of a trade deal being struck before the US 2020 election. If we see the expected rise in EUR/USD in 12 months as we expect, it would help to cap the rise in USD/CNY.
- **Risks:** The risk is skewed on the upside for USD/CNY following the recent escalation, as it is increasingly difficult to see how the US and China can make ends meet to make a trade deal. There is a rising risk that Trump will go 'all in' and raise tariffs to 25% on all Chinese goods.
- **Valuation:** The CNY is at its long-term fair valuation. China's current account surplus has declined from the peak at 10% of GDP in 2007 to 0.4% of GDP in 2018.

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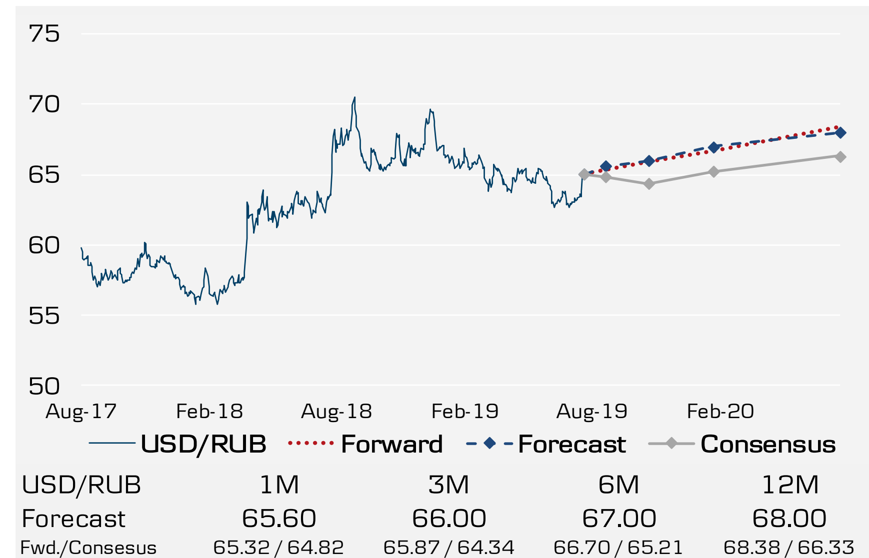
USD/RUB – global risk sentiment to overweight sanctions effect

- **Growth.** Q1 19 GDP final growth data was confirmed at 0.5% y/y versus brisk Q4 19 growth data of 2.7%. Despite a VAT increase and continuing tight monetary policy, household consumption was the major driver of GDP expenditure, while fixed investment and exports shrank. Yet, net imports fell even more than exports. We still expect 2019 GDP to expand moderately by 1.3% y/y, seeing significant downside risk to our forecast. We see some acceleration to 1.8% in 2020 due to notable monetary easing and the initiation of several investment projects by the state.
- **Monetary policy.** Russia's central bank (CBR) delivered a 25bp cut in July communicating its own intentions well in advance. Currently, inflation is tracking slightly above the target but we expect the central bank to cut the key rate by 25bp in September and probably in December 2019 as well, if both the ECB and the Fed continue to stay dovish.
- **Flows.** In line with other emerging market currencies, inflows into the RUB were recently halted by the Fed's hawkish cut. Combined with dovish CBR, the RUB's carry trade attractiveness has started diminishing. Yet, inflows into Russia's local debt by foreigners have been significant, fuelled by stable macro indicators.
- **Valuation.** Real rates in Russia remain positive despite the CBR's cuts. Looking at RUB technicals such as the relative strength indicator and Bollinger bands, we see that the USD/RUB has returned to 'fair value' territory after significant overbuying following the Fed's hawkish cut.

Forecast: 65.60 (1M), 66.00 (3M), 67.00 (6M), 68.00 (12M)



USD/RUB	1M	3M	6M	12M
Forecast	65.60	66.00	67.00	68.00
Fwd./Consesus	65.32 / 64.82	65.87 / 64.34	66.70 / 65.21	68.38 / 66.33

Source: Danske Bank

- **Conclusion.** The RUB continues to follow global risk sentiment, while the recent US sanctions did not have a significant impact on the Russian currency, as Russia's local debt remains out of scope. In early August 2019, US President Trump signed an executive order imposing sanctions on Russia. It was the second round of sanctions by the US administration. The US banned loans or other assistance to Russia by international financial institutions and prohibited most loans from American banks to Russia's government.
- **Risks.** The major downside risk for our forecast is geopolitical.

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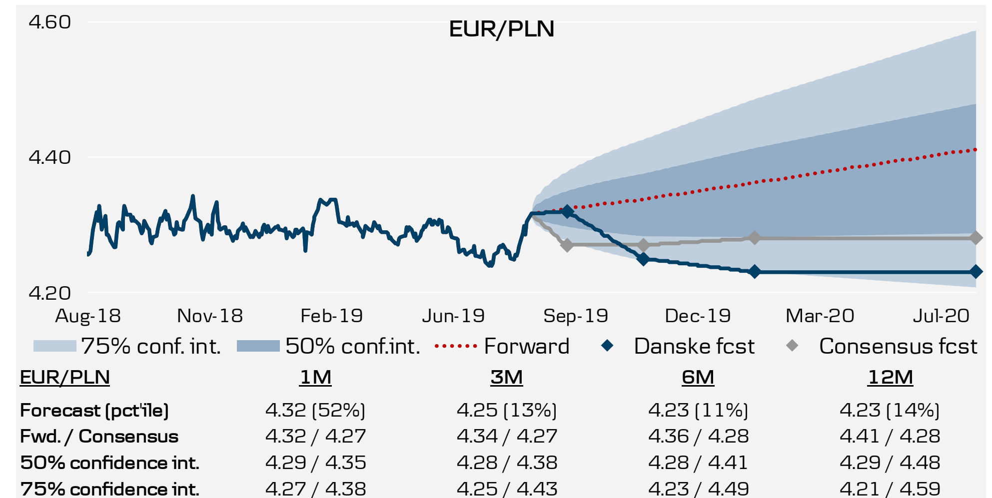
EUR/PLN – Europe's slowdown and softer ECB bites zloty

- **Economic developments. The** Polish economy held up well in Q1 19, expanding 4.7% y/y versus 4.7% in Q4 18. However, there are signs of economic slowdown as PMI manufacturing continues to be in negative territory and construction output is shrinking for the first time in 2.5 years. On the consumption side, retail sales are still doing well supported by low unemployment and solid growth in real wages. We expect 2019 GDP growth rate to come to 4.2% y/y. This growth rate is still above the potential growth rate of the Polish economy, meaning the labour market is expected to tighten further.
- **Monetary policy.** Headline inflation (preliminary) climbed further in July to 2.9%, its seven-year high, compared with 2.6% in June. The rise in headline inflation is driven by a combination of higher energy prices and higher core inflation. The low interest rates appear to be accommodative as broad money has expanded more than 9% since January 2019. Furthermore, in light of the prospective fiscal expansion, the central bank governor continues to play down the need for tighter monetary policy despite the recent inflation shock. We think that core inflation will increase further to 2.0% towards the end of the year. However, given the dovish signals from global central banks, the market is pricing in a small chance of a 10bp rate cut in the latter middle of 2020, which seems dovish to us.
- **Risks.** Risks are skewed on the upside for EUR/PLN in the near term from possible escalation of the China-US trade war and US President Trump's trade attack on the EU. Weaker economic releases in Poland could lead to a more dovish repricing by the central bank.

Forecast: 4.32 (1M), 4.25 (3M), 4.23 (6M), 4. 23 (12M)



EUR/PLN	1M	3M	6M	12M
Forecast (pct'ile)	4.32 (52%)	4.25 (13%)	4.23 (11%)	4.23 (14%)
Fwd. / Consensus	4.32 / 4.27	4.34 / 4.27	4.36 / 4.28	4.41 / 4.28
50% confidence int.	4.29 / 4.35	4.28 / 4.38	4.28 / 4.41	4.29 / 4.48
75% confidence int.	4.27 / 4.38	4.25 / 4.43	4.23 / 4.49	4.21 / 4.59

Source: Danske Bank

- **Conclusion.** The ECB's softening stance and the renewed trade dispute between China and the US sent EUR/PLN higher. We see US-China trade tensions as likely to continue into 2020, which would send the pair higher (the PLN has been relatively immune to the risk-off periods lately). As a result, we see a slight case for EUR/PLN to edge higher on a short-term basis to 4.32 (previously 4.28) in 1M,but then as the Fed delivers on the cutting side in September, we see the pair going down to 4.25 in 3M, 4.23 in 6M and 4.23 in 12M.

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USD/TRY – global monetary easing set to offset the TCMB's cuts

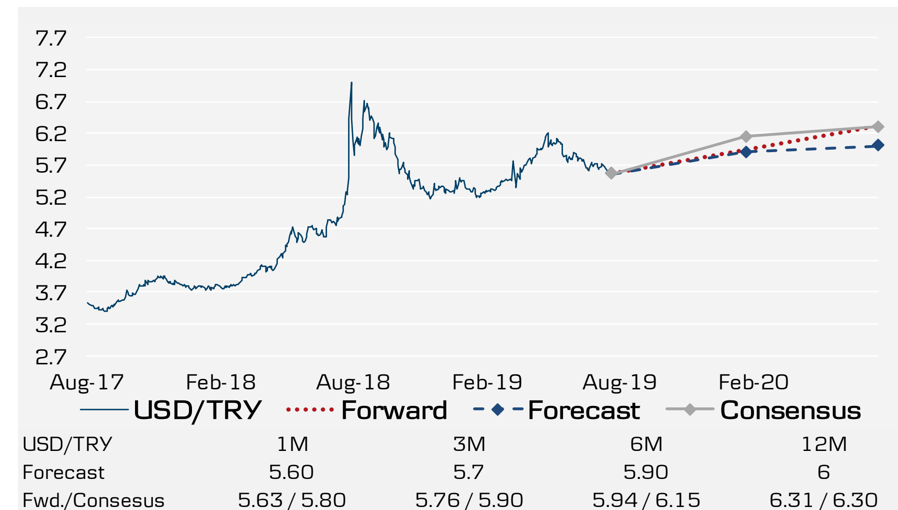
- **Growth.** The Turkish economy entered a recession in Q4 18 and GDP continued to contract in Q1 19, shrinking 2.6% y/y despite active fiscal stimulus. Given the election period is over for now, we expect the lack of fiscal stimulus in the future to restrain economic growth. We believe support will come from advancing monetary easing and exports on the weak TRY. We expect GDP to contract 2.0% y/y in 2019 and expand by 1.7% in 2020 and 3.0% y/y in 2021.

- **Monetary policy.** Turkey's central bank (TCMB) delivered a substantial cut of 425bp to the key rate setting it at 19.75% as inflation continued to fall. There is a clear change in TCMB's stance after its governor was changed earlier in 2019. We expect inflation to continue decreasing slowly, staying in double-digit territory throughout H2 19. Yet, we expect more cuts by the TCMB in 2019, as there is still enough room for positive real rate and the Turkish economy badly needs monetary stimulus on global monetary easing.

- **Valuation.** Inflows into Turkish assets continue to depend on both global risk sentiment and Turkish domestic factors. The increased fragility of domestic factors is weighing on economic performance expectations. According to technical analysis (Relative Strength Index), USD/TRY is becoming marginally oversold, which means that the TRY could see a correction in the near-term.

- **Risks.** Major downside risks to our TRY forecasts include more aggressive monetary easing than markets are pricing, renewed political pressure on the TCMB, further escalation of the trade war and geopolitical confrontation with the US on Russia's air defence system.

Forecast: 5.60 (1M), 5.70 (3M), 5.90 (6M) and 6.00 (12M)



USD/TRY	1M	3M	6M	12M
Forecast	5.60	5.7	5.90	6
Fwd./Consesus	5.63 / 5.80	5.76 / 5.90	5.94 / 6.15	6.31 / 6.30

Source: Danske Bank

- **Conclusion.** The TRY is stabilising on a global turn to monetary easing, while quick monetary easing by the TCMB is limiting the TRY's attractiveness in carry trades. However, domestic risk is still there. As a result of global monetary relief, we adjust our USD/TRY outlook, enhancing that a fragile domestic and geopolitical environment is still in place. Large FX debt redemptions by the Turkish private sector and more rate cuts later in 2019 are set to weigh on the TRY in 2019 and 2020. Thus, we remain bearish on the TRY in the long term.

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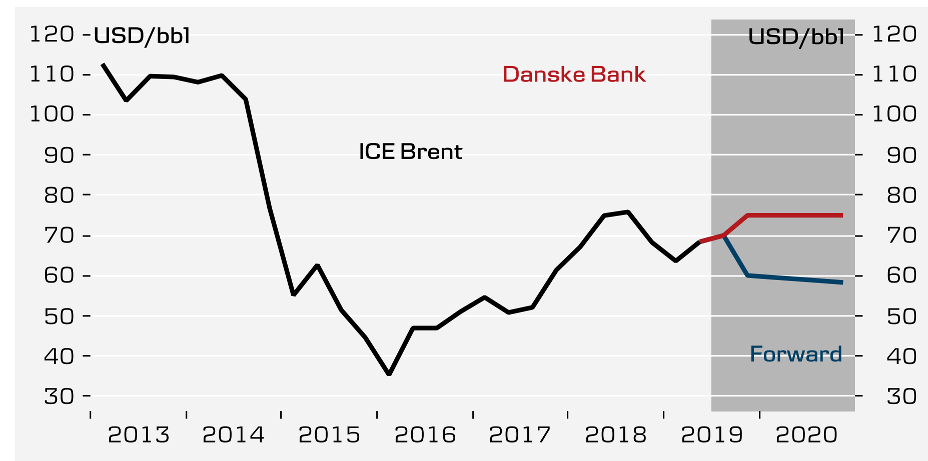
Oil – ‘risk off’ spills over to the oil market

- **Macro.** Supply remains tight in the oil market, as OPEC+ has extended output cuts and production levels in Iran and Venezuela remain depressed by sanctions. However, lacklustre demand due to the escalation of the trade war and weak global manufacturing activity is keeping the oil market balance fairly stable. We see this situation extending in the short and medium-term.
- **Forward curve.** Backwardation in the Brent crude oil market forward curve has narrowed following the fall back close to USD60/bbl in the spot price, while the price on longer dated contracts has started to trend lower. Backwardation should widen as spot prices recovery in H2 in accordance with our forecasts.
- **Positioning.** Speculative investors are close to stretched long positioned in WTI and we have seen only a small effect on positioning following the recent sell off in the oil market.
- **Risks.** In the short-term, the main risks to our oil prices forecasts are on the upside from a further rise in tensions between the US and Iran and on the downside further escalation in the trade war and deterioration in the global economy coupled with a still strong USD.

Forecast: USD70/bbl (Q3), USD75/bbl (Q4), USD75/bbl (2020)



Source: Danske Bank

- **Conclusion.** We expect oil prices to recover over the remainder of 2019. We forecast Brent will average USD70/bbl in Q3 and USD75/bbl in Q4. We expect OPEC+ cuts, a stabilisation of the global macro economy and eventually a weaker USD to underpin oil prices.

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Danske Bank FX forecasts vs EUR

G10	Spot	+1m	+3m	+6m	+12m
				Last Update:	05-08-2019
Exchange rates vs EUR					
EUR/USD	1.116	1.10	1.10	1.13	1.15
EUR/JPY	118.3	117	116	119	127
EUR/GBP	0.919	0.90	0.90	0.90	0.90
EUR/CHF	1.087	1.090	1.100	1.120	1.140
EUR/SEK	10.752	10.70	10.80	10.90	11.00
EUR/NOK	9.969	9.80	9.65	9.60	9.50
EUR/DKK	7.466	7.4630	7.4575	7.4550	7.4550
EUR/AUD	1.649	1.642	1.642	1.614	1.643
EUR/NZD	1.712	1.705	1.705	1.687	1.716
EUR/CAD	1.476	1.452	1.430	1.458	1.461
EM	**Spot**	**+1m**	**+3m**	**+6m**	**+12m**
EUR/PLN	4.315	4.32	4.25	4.23	4.23
EUR/HUF	328	320	328	320	315
EUR/CZK	25.783	25.60	25.60	25.50	25.30
EUR/RUB	72.597	72.16	72.60	75.71	78.20
EUR/TRY	6.208	6.16	6.27	6.67	6.90
EUR/ZAR	16.648	16.34	16.28	16.95	16.68
EUR/BRL	4.319	4.33	4.10	4.11	4.03
EUR/CNY	7.856	7.76	7.81	8.14	8.28
EUR/INR	78.705	80.30	75.90	77.97	79.35

Source: Bloomberg, Danske Bank

Danske Bank

Danske Bank FX forecasts vs DKK

G10	Spot	+1m	+3m	+6m	+12m
				Last Update:	05-08-2019
Exchange rates vs DKK					
USD/DKK	6.69	6.78	6.78	6.60	6.48
JPY/DKK	6.31	6.40	6.46	6.28	5.89
GBP/DKK	8.127	8.29	8.29	8.28	8.28
CHF/DKK	6.867	6.85	6.78	6.66	6.54
SEK/DKK	0.694	0.70	0.69	0.68	0.68
NOK/DKK	0.749	0.76	0.77	0.78	0.78
EUR/DKK	7.4663	7.4630	7.4575	7.4550	7.4550
AUD/DKK	4.527	4.55	4.54	4.62	4.54
NZD/DKK	4.362	4.38	4.37	4.42	4.34
CAD/DKK	5.057	5.14	5.22	5.11	5.10
EM	**Spot**	**+1m**	**+3m**	**+6m**	**+12m**
PLN/DKK	1.730	1.728	1.755	1.762	1.762
HUF/DKK	2.28	2.33	2.27	2.33	2.37
CZK/DKK	0.290	0.292	0.291	0.292	0.295
RUB/DKK	0.103	0.103	0.103	0.098	0.095
TRY/DKK	1.203	1.212	1.189	1.118	1.080
ZAR/DKK	0.448	0.457	0.458	0.440	0.447
BRL/DKK	1.720	1.722	1.818	1.812	1.852
CNY/DKK	0.950	0.962	0.955	0.916	0.900
INR/DKK	0.095	0.093	0.098	0.096	0.094

Source: Bloomberg, Danske Bank

Danske Bank

Danske Bank FX forecasts vs SEK

G10				Last Update:	05-08-2019
	Spot	+1m	+3m	+6m	+12m
Exchange rates vs SEK					
USD/SEK	9.63	9.73	9.82	9.65	9.57
JPY/SEK	9.09	9.18	9.35	9.19	8.70
GBP/SEK	11.70	11.89	12.00	12.11	12.22
CHF/SEK	9.89	9.82	9.82	9.73	9.65
EUR/SEK	10.75	10.70	10.80	10.90	11.00
NOK/SEK	1.08	1.09	1.12	1.14	1.16
DKK/SEK	1.44	1.43	1.45	1.46	1.48
AUD/SEK	6.52	6.52	6.58	6.75	6.70
NZD/SEK	6.28	6.27	6.33	6.46	6.41
CAD/SEK	7.28	7.37	7.55	7.48	7.53
EM					
	Spot	+1m	+3m	+6m	+12m
PLN/SEK	2.49	2.48	2.54	2.58	2.60
HUF/SEK	3.28	3.34	3.29	3.41	3.49
CZK/SEK	0.42	0.42	0.42	0.43	0.43
RUB/SEK	0.15	0.15	0.15	0.14	0.14
TRY/SEK	1.73	1.74	1.72	1.63	1.59
ZAR/SEK	0.65	0.66	0.66	0.64	0.66
BRL/SEK	2.49	2.47	2.63	2.65	2.73
CNY/SEK	1.369	1.380	1.383	1.340	1.329
INR/SEK	0.137	0.133	0.142	0.140	0.139

Source: Bloomberg, Danske Bank

Danske Bank FX forecasts vs NOK

G10	Spot	+1m	+3m	+6m	+12m
Exchange rates vs NOK					
USD/NOK	8.93	8.91	8.77	8.50	8.26
JPY/NOK	8.43	8.40	8.35	8.09	7.51
GBP/NOK	10.85	10.89	10.72	10.67	10.56
CHF/NOK	9.17	8.99	8.77	8.57	8.33
SEK/NOK	0.93	0.92	0.89	0.88	0.86
EUR/NOK	9.97	9.80	9.65	9.60	9.50
DKK/NOK	1.34	1.31	1.29	1.29	1.27
AUD/NOK	6.04	5.97	5.88	5.95	5.78
NZD/NOK	5.82	5.75	5.66	5.69	5.53
CAD/NOK	6.75	6.75	6.75	6.59	6.50
EM	**Spot**	**+1m**	**+3m**	**+6m**	**+12m**
PLN/NOK	2.31	2.27	2.27	2.27	2.25
HUF/NOK	3.04	3.06	2.94	3.00	3.02
CZK/NOK	0.39	0.38	0.38	0.38	0.38
RUB/NOK	0.14	0.14	0.13	0.13	0.12
TRY/NOK	1.61	1.59	1.54	1.44	1.38
ZAR/NOK	0.60	0.60	0.59	0.57	0.57
BRL/NOK	2.31	2.26	2.35	2.33	2.36
CNY/NOK	1.269	1.264	1.236	1.180	1.147
INR/NOK	0.127	0.122	0.127	0.123	0.120

Source: Bloomberg, Danske Bank

Danske Bank

Danske Bank FX forecasts vs USD

G10	Spot	+1m	+3m	+6m	+12m
				Last Update:	05-08-2019
Exchange rates vs USD					
EUR/USD	1.116	1.10	1.10	1.13	1.15
USD/JPY	106.0	106	105	105	110
GBP/USD	1.215	1.22	1.22	1.26	1.28
USD/CHF	0.974	0.99	1.00	0.99	0.99
USD/SEK	9.634	9.73	9.82	9.65	9.57
USD/NOK	8.932	8.91	8.77	8.50	8.26
USD/DKK	6.690	6.78	6.78	6.60	6.48
AUD/USD	0.677	0.67	0.67	0.70	0.70
NZD/USD	0.652	0.65	0.65	0.67	0.67
USD/CAD	1.323	1.32	1.30	1.29	1.27
EM	**Spot**	**+1m**	**+3m**	**+6m**	**+12m**
USD/PLN	3.866	3.93	3.86	3.74	3.68
USD/HUF	293	291	298	283	274
USD/CZK	23.101	23.27	23.27	22.57	22.00
USD/RUB	65.053	65.60	66.00	67.00	68.00
USD/TRY	5.561	5.60	5.70	5.90	6.00
USD/ZAR	14.917	14.85	14.80	15.00	14.50
USD/BRL	3.889	3.94	3.73	3.64	3.50
USD/CNY	7.04	7.05	7.10	7.20	7.20
USD/INR	70.50	73.00	69.00	69.00	69.00

Source: Bloomberg, Danske Bank

Danske Bank

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