

Currencies Focus

Summary

1. Central banks have been suggesting a gradual normalization of monetary policy in the face of persistent inflation. Central banks highlighted upside risks for inflation in 2022. Interest rate hikes are planned already this year for most developed central banks.
2. The EURUSD has been quite volatile, falling below 1.12 after the FED's minutes and then recently rising above 1.14 after the ECB suggested that they no longer rule out raising rates in 2022. We expect 4 rate hikes in both 2022 and 2023 in the US with the first one in March. In Eurozone, we now expect a first rate hike of 25bps in December 2022 and three others in 2023.
3. We are changing our targets on the following currencies: RUB, GBP and YEN. The rate differential should weigh negatively on the EUR vs GBP and the YEN vs USD. We now expect less appreciation for the RUB as geopolitical tensions could last.
4. We are bullish on oil-related currencies (CAD, NOK) and commodities (ZAR, NZD, AUD) in the context of a high economic growth and inflation mix in 2022-23.
5. Central banks in emerging countries have already raised rates in 2021 in the face of high single digit inflation. They offer an attractive carry trade and economic fundamentals should improve in 2022. We remain however bearish on the Indian rupee due a structural current account.

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OUR TARGETS OVER THE NEXT 3 AND 12 MONTHS

	Country	Spot 2/9/2022	Target 3 months	Target 12 months
Against euro	United States	EUR / USD 1.14	1.12	1.12
	United Kingdom	EUR / GBP 0.85	0.82	0.82
	Switzerland	EUR / CHF 1.06	1.06	1.08
	Japan	EUR / JPY 131.90	128	128
	Sweden	EUR / SEK 10.48	10.00	10.00
	Norway	EUR / NOK 10.06	9.75	9.60
Against dollar	Japan	USD / JPY 115.27	114	114
	Canada	USD / CAD 1.28	1.25	1.25
	Australia	AUD / USD 0.71	0.73	0.73
	New Zealand	NZD / USD 0.66	0.70	0.70
	Brazil	USD / BRL 5.35	5.50	5.25
	Russia	USD / RUB 76.13	76.0	74.0
	India	USD / INR 74.71	76.0	78.0
	China	USD / CNY 6.37	6.50	6.50

Source: Refinitiv - BNP Paribas WM



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USD VIEW >> TARGET 12M VS EUR: 1.12

First rate hike in March 2022

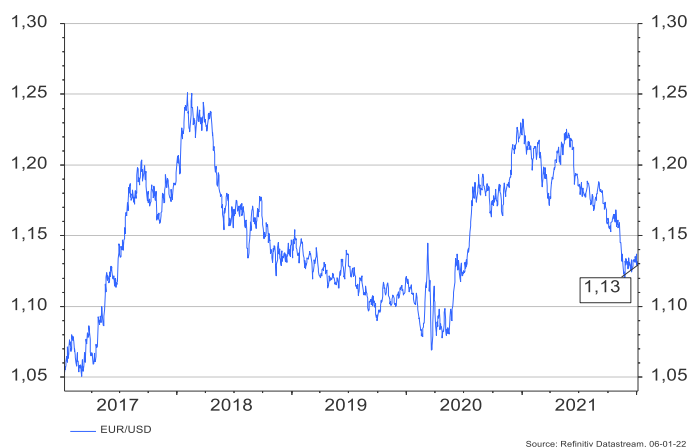
The EURUSD was quite volatile over recent weeks, first breaking 1.12 before rising again in recent days and crossing 1.14 after the ECB's hawkish tone.

The FED is expected to hike a first time in March. Historically, the first rate hike has often led to an appreciation of the EURUSD. We are thus confident that the dollar have some support.

In the eurozone, inflation reached 5.1% in January, well above the ECB's 2% target. Christine Lagarde recalled that many factors were cyclical but that price increases were a "serious concern". The ECB has not denied the possibility of raising rates this year. We now expect a first rate increase of 25bps in December 2022 and three more 25bps in 2023. In the context of a potentially more restrictive monetary policy by the ECB, we are monitoring the situation closely and do not rule out a revision towards a weaker dollar in the coming months if the ECB signals earlier rate hikes.

The January Fed minutes suggested that the labor market was tight, and that inflation was highly concerning, implying a more aggressive monetary policy than previously expected. We thus expect the Fed to hike rates as early as March 2022 followed by three more in 2022 and 4 in 2023. The quantitative tightening (reduction of the balance sheet) should be announced in July and should be started in July. The yield differential should remain in favor of the dollar.

We keep our 3-month and 12-month outlook unchanged at 1.12.



GBP VIEW >> TARGET 12M VS EUR: 0.82

Hawkish Bank of England

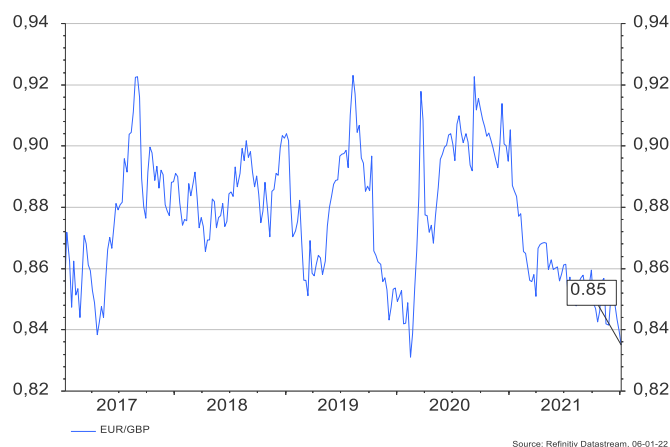
The EURGBP rose above 0.84 in early February after the ECB comments, despite a 25bps hike from the Bank of England.

The inflation rate in December reached 5.4% year-over-year and should peak around 7.25% in April 2022 driven mainly by energy prices. In 2022, the UK should have higher growth and inflation than the Eurozone. The Bank of England is ahead of schedule compared to the ECB in its restrictive policy and has hiked by 25bps its main rate in February. Four of the nine governors were in favor of a 50bps increase. We expect 50 bps of rate increases for 2022 as well as 2023. The Bank of England also announced the reduction of its balance sheet. **This will be favorable for the GBP and so we adjust our scenario.**

The January Business survey (PMI Composite index) came in at 53.4, with companies highlighting strong cost pressures. The balance of payments deteriorated in the third quarter explained by the current account deficit and FDI outflows. However, the portfolio flows were positive and the rate differential with the EUR will be supportive for the reduction of the UK's balance of payments deficit.

We change our EURGBP target to 0.82 (value of one euro) for our 3- and 12-month horizon, suggesting some appreciation for the GBP.

Regarding the GBPUSD, our 3- and 12-month targets are at 1.36. This suggests a slight appreciation of the GBP.



CHF VIEW >> TARGET 12M VS EUR: 1.08

Close to our 3-month target

The Swiss franc remained stuck around 1.04 in January before depreciating sharply following the ECB meeting. The EURCHF (value of one euro) rising above 1.05.

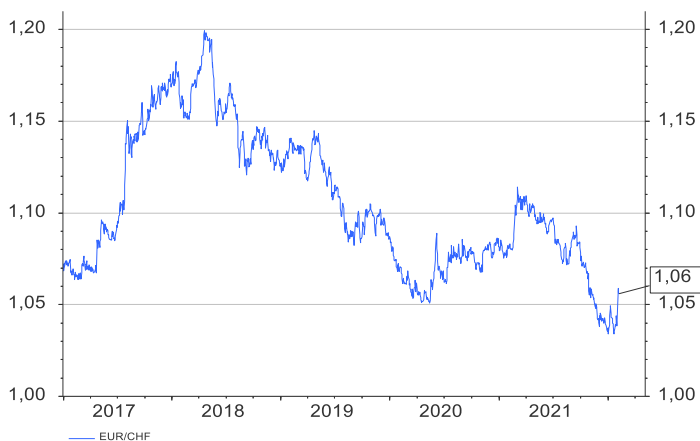
Switzerland's fundamentals remained very good in 2021 and the Swiss economy did not suffer from higher inflation like other developed areas. Inflation has indeed reached only 1.5% year on year in December.

The Manufacturing business survey (PMI index) in January remained high at 63.8 but is slightly lower compared to December (64.2). The order backlog remains robust.

The Eurozone economy should regain some momentum in 2022, especially with the recovery of services and tourism, and this will be a strong support factor for the euro. Moreover, with a more cautious ECB in terms of inflation risk and a Swiss repo rate of -0.75%, the Swiss franc could suffer more in 2022. The Swiss National Bank has given no indication of potential rate increases and considers the Swiss franc "highly valued". We therefore continue to expect the Swiss franc to depreciate in 2022.

In the third quarter 2021, the balance of payments reached 2.6% of GDP thanks to strong FDI and a slowdown in capital outflows.

We maintain our 3-month target at 1.06 and our 12-month target at 1.08.



JPY VIEW >> TARGET 12M VS USD: 114

Less appreciation expected for the JPY

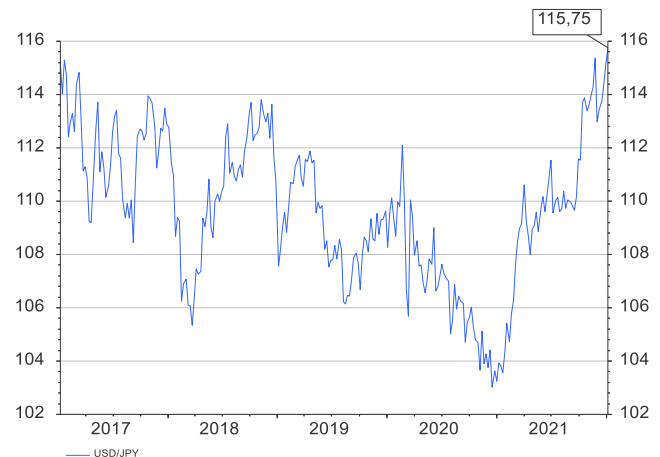
The Yen remained flat in January, stabilizing around 115. The Yen had risen in the middle of the month to around 113 in the face of rumors of a possible BOJ rate hike in the next few months. These speculations were dismissed at the meeting.

At its January 17th meeting, the Bank of Japan highlighted the economic recovery for 2022 and a higher inflation outlook. It should reach 1% for 2021, tending to 1.5% in 2022. Temporarily, the Bank of Japan indicates that it could reach 2%. However, it will not change its policy as long as the structural price increase is not above 2%, which suggests a continuation of its ultra-accommodating policy.

The USDJPY is correlated to the evolution of US interest rates relative to those in Japan. The expected monetary tightening in the US over the coming months should limit the appreciation potential for the Yen.

In November, the balance of payments contracted mainly due to the sharp rise in energy prices. It is still positive and should improve in 2022. However, on the portfolio flows side, Japanese pension funds are expected to further increase their allocation to US debt. The Yen is expected to move around its 50-day moving average around 114.

We change our 3-month and 12-month USDJPY targets at 114 (value of one dollar). This suggests a small appreciation of the JPY from current levels.



SEK VIEW >> TARGET 12M VS EUR: 10.00

Limited potential for the SEK

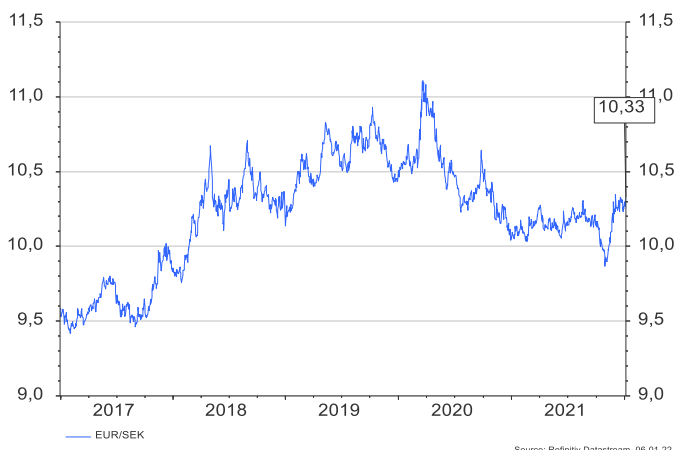
The EURSEK traded in a tight range in January between 10.2 and 10.5.

Inflation for November was 3.6% on a year-on-year basis, the highest in 28 years. The Swedish government announced on February 2 the end of all health restrictions. This should result in better economic data and should support the SEK.

At the February 9 meeting, the Riksbank remains committed to a first rate hike in 2024 and no balance sheet reduction in 2022. However, inflation remains high above 4% and house prices above 10%. The Riksbank could be more aggressive in its tone at upcoming meetings. The good health of the economy is illustrated by the high level of the business survey index (PMI) within the services (68.6) and the manufacturing (62.4). The Riksbank could revise its stance and could raise rates before 2024. Moreover, the quantitative tightening (reduction of the balance sheet) could begin sooner than expected.

Regarding the broad basic of payments, it was flat in the third quarter. The current account surplus was offset by the portfolio outflows.

We keep our EURSEK targets at 10.00 over the next 3 and 12 months (value of one euro). This suggests a moderate appreciation for the SEK.



NOK VIEW >> TARGET 12M VS EUR: 9.6

More strengthening ahead

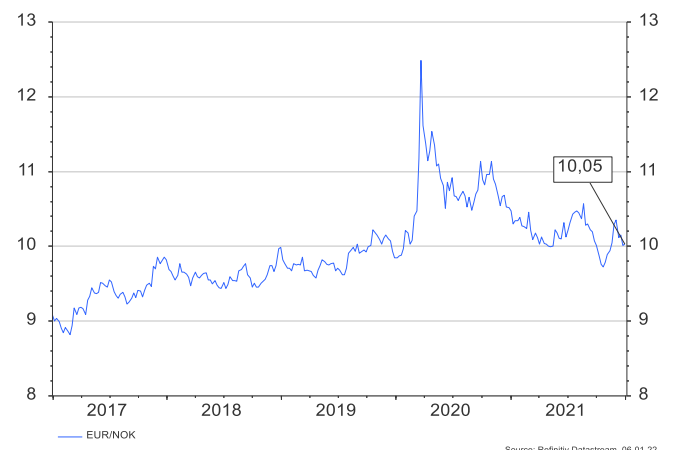
The EURNOK temporarily rose back above 10 following the central bank meeting.

At its January 19th meeting, the central bank announced that the repo rate was left unchanged at 0.5%. The Central Bank still expects a terminal rate of 1.75% by the end of 2024. Historically, the tightening in Norway generated an appreciation of the krone. We forecast that the rate differential with the ECB will result in an appreciation of the Norwegian Krone. Moreover, the NOK should remain supported by the high price for oil (Brent) in 2022.

The Broad Basic Balance of Payments stands at 6.9% of GDP in the quarter 2021 thanks to a widening current account surplus. The January manufacturing business survey (PMI) reached 56.5 in January, slightly down from December.

Interest rates are expected to rise faster than in most other developed countries. This should support the appreciation potential of the Norwegian krone.

We maintain our 3-month EURNOK target (value of one euro) at 9.75 and our 12-month target at 9.60. This suggests an appreciation of the NOK.



AUD VIEW >>

TARGET 12M VS USD: 0.73

Limited upside for the AUD

The AUD depreciated slightly over January. It was close to our target of 0.73 at the beginning of the month before falling back to 0.71 after the Fed meeting.

At the February 3rd meeting, the central bank of Australia announced the end of its bond purchases. Core inflation was much lower than in other developed countries, reaching 2.6% year-on-year in December. Faced with a tight labor market, with 4.6% unemployment, the market expects a first rate hike in June and a policy rate hike sequence to 0.75% this year from the current cash rate at 0.1%.

Monetary and fiscal support announced in China should benefit Australia's exports. The demand from Asia for coal and iron ore should remain strong in the coming months. The January business survey (Composite PMI index) was however somewhat disappointing reaching 46.7 amid the surge in Covid-19 cases and a fall in new orders for services.

Therefore, we maintain our 3-month and 12-month AUDUSD targets at 0.73 (value of one AUD). This implies a limited appreciation potential for the AUD over the coming year.

NZD VIEW >>

TARGET 12M VS USD: 0.7

NZD with more upside

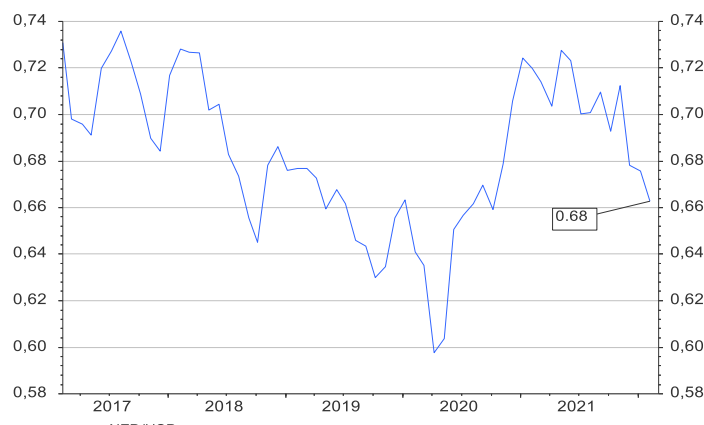
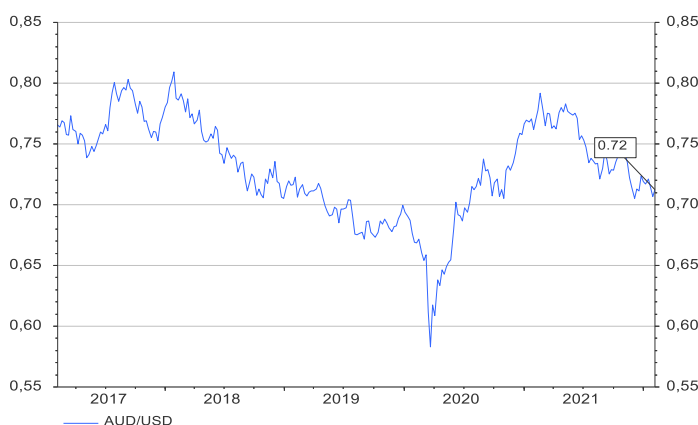
The Kiwi depreciated slightly in January following a more prudent message of the Fed regarding inflation.

The Reserve Bank of New Zealand continues to see the economy as above potential. The RBNZ raised rates by 25 bps to 0.75%. The RBNZ is expected to raise rates by 150bps in 2022 and another 50bps in 2023.

The high interest rate differential will give the NZD an advantage compared to other G10 currencies. At the last meeting in November, the central bank lifted rates by 25bps, seeing sufficient strength in the economy with low unemployment and house prices increase. The NZD should also benefit from better economic developments in China and a normalization of global trade.

In the third quarter of 2021, the broad basic balance of payments improved but remains negative at -2.24% of GDP. With bond yields higher than in other G10 countries, portfolio inflows should support the NZD.

We keep our 3-month and 12-month NZDUSD targets to 0.70 (value of one NZD). This implies a considerable appreciation potential for the NZD.



CAD VIEW >>

TARGET 12M VS USD: 1.25

Small upside for the CAD

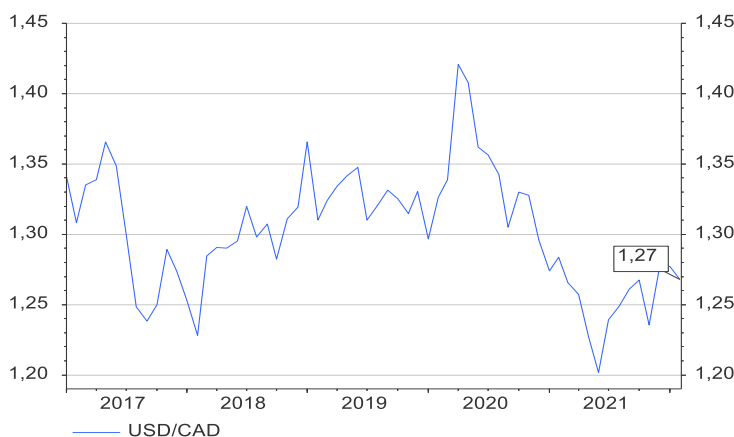
The USDCAD remained broadly stable in January oscillating between 1.28 and 1.25. A rate hike is imminent for both countries.

The Canadian central bank said that there is still a lot of uncertainty about inflation coming down and that rates will be raised in 2022 to cope with current inflation pressures (4.8% year-on-year). Markets expect a first increase in March followed by 3 more by the end of 2022. With monetary policy expected to be more restrictive in both the USA and Canada, we do not expect a significant rise in the interest rate differential. The 10-year rates of the two countries are quite close around 1.85%.

Oil prices (WTI) are quite high and sustained demand suggests that this will be the case over the coming year. This should support the CAD.

The balance of payments remained positive in the third quarter and reached 1.1% of GDP. It is supported by a surplus in the current account balance and positive portfolio flows.

We maintain our USDCAD (value of one dollar) target at 1.25 for the 3- and 12-month horizon. This suggests a moderate upside for the CAD over the next year.



CNY VIEW >>

TARGET 12M VS USD: 6.5

Moderate depreciation expected

The CNY was stable in January fluctuating in a narrow range between 6.32 and 6.38.

China cut policy rates on January 19th. The People's Bank of China lowered the 1-year loan prime rate from 3.8% to 3.7% and the 5-year rate from 4.65% to 4.6%. The January manufacturing business survey index (PMI) fell to 49.1 from 50.9. This was probably due to rising Covid cases, weaker external demand and longer delivery times. Backlogs were also falling. Further monetary easing can be expected over the coming months. This could lead to a higher spread between US and Chinese rates. This factor is a headwind for the CNY.

In the short-term, The currency remains supported by a strong balance of payments with increasing portfolio flows thanks to recent monetary easing. The People's Bank of China will also be keen to avoid more appreciation of the currency in order to support exports.

In 2021, exports increased by 31% year-on-year in USD terms. However, with the recovery of industrial production in other countries and the shift in consumption from goods to services, there is a short-term downside risk for Chinese export growth.

We maintain our 3- and 12-month targets for USDCNY at 6.50. This suggests a weakening of the CNY over the coming year.



Emerging Markets VIEW >>

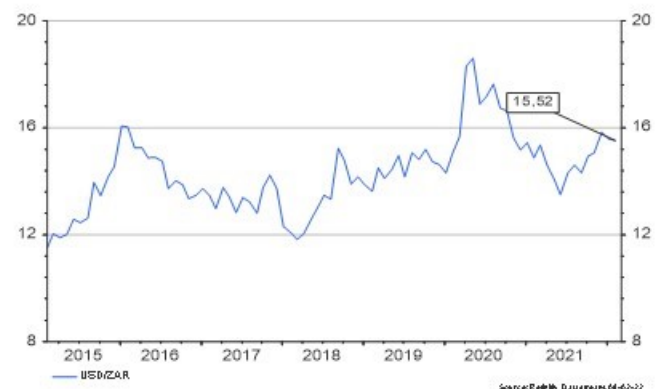
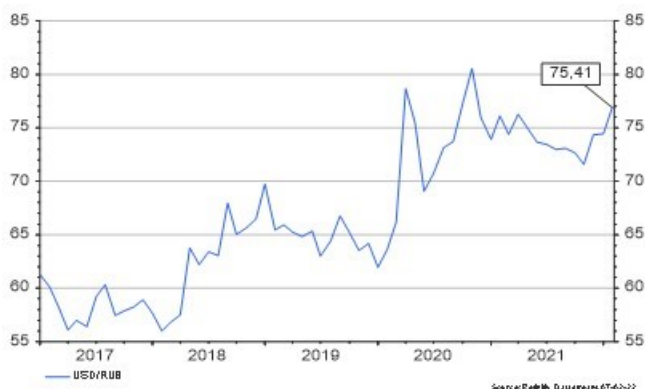
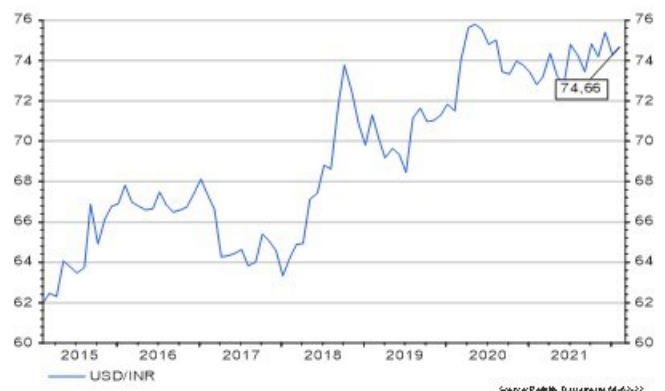
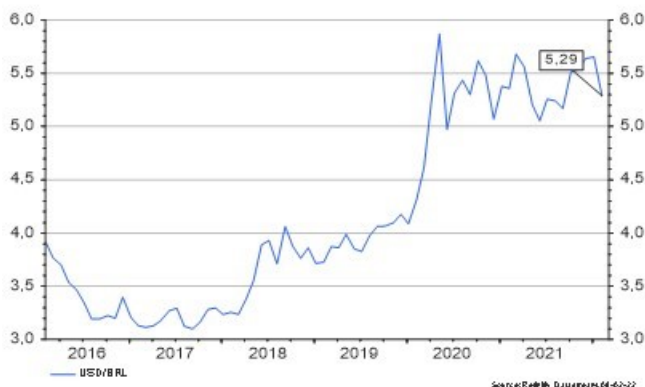
Monetary policy shift to fight inflation

At its February 2nd meeting, the Brazilian Central Bank raised interest rates by 150 bps to 10.75%. This is the eighth straight increase since March and is the result of the inflation rate exceeding 10% in 2021. The central bank is expected to raise rates again in March by 100 bps and is on the verge of concluding its restrictive policy. As a commodity and oil exporter currency, the BRL should remain supported in 2022. However, the rise in US rates will lower the yield differential with Brazil. The elections in October are another source of uncertainty for the currency. **We keep our 3-month target at 5.5 and the 12-month target at 5.25.**

The Russian currency (RUB) depreciated by 3% in January amid tensions with Ukraine. The RUB hit a low of 79 against the USD before rallying strongly in the last few days of the month. We are more confident about the 12-month horizon, with tensions expected to ease during the coming months and demand for oil remaining strong in 2022. Regarding the monetary policy, in December, the Bank of Russia raised rates by 100bps and the key rate now stands at 8.5%, with inflation still exceeding expectations. **We are adjusting our 3-month target to 76 reflecting the short-term bearish momentum and the 12-month target to 74.**

We remain cautious on the Indian currency (INR). In India, the current account deficit remains a concern. The trade deficit is near a record at 9% of GDP. The global merchandise trade has been slowing the last few months due to elevated freight rates and shortage of semiconductors. Investors expect 150bp of hikes in 2022 which would bring the repo rate at 5.5%. At the February 9th meeting, the Reserve Bank of India left the repo rate unchanged at 4%. **We are still cautious on the currency and maintain our target at 76 for our 3-month horizon and 78 for our 12-month horizon. This suggests a depreciation of the INR.**

The South African currency (ZAR) appreciated in January and is approaching our target. At its January meeting, the central bank raised rates by 25bps to 4%. In total, the South Africa Reserve Bank is expected to raise rates by over 200bps in 2022 to fight inflation which is around 6%. The demand for commodities will remain sustained in 2022 and it should support the ZAR. **We maintain our 3-month and 12-month targets at 15 suggesting an appreciation for the ZAR.**



	Country	Spot 2/9/2022	Trend	Target 3 months (vs. EUR)	Trend	Target 12 months (vs. EUR)	
	United States	EUR / USD	1.14	Positive	1.12	Positive	1.12
	United Kingdom	EUR / GBP	0.85	Positive	0.82	Positive	0.82
	Japan	EUR / JPY	131.90	Positive	128	Positive	128
	Switzerland	EUR / CHF	1.06	Neutral	1.06	Negative	1.08
	Australia	EUR / AUD	1.62	Positive	1.53	Positive	1.53
	New-Zealand	EUR / NZD	1.74	Positive	1.60	Positive	1.60
	Canada	EUR / CAD	1.46	Positive	1.40	Positive	1.40
	Sweden	EUR / SEK	10.48	Positive	10.00	Positive	10.00
	Norway	EUR / NOK	10.06	Positive	9.75	Positive	9.60
Asia	China	EUR / CNY	7.28	Neutral	7.28	Neutral	7.28
	India	EUR / INR	85.49	Neutral	85.12	Negative	87.36
Latam	Brazil	EUR / BRL	6.12	Neutral	6.16	Positive	5.88
EMEA	Russia	EUR / RUB	87.11	Positive	85.12	Positive	82.88

	Country	Spot 2/9/2022		Trend	Target 3 months (vs. USD)	Trend	Target 12 months (vs. USD)
	Eurozone	EUR / USD	1.14	Negative	1.12	Negative	1.12
	United Kingdom	GBP / USD	1.35	Neutral	1.37	Neutral	1.37
	Japan	USD / JPY	115.27	Neutral	114.00	Neutral	114.00
	Switzerland	USD / CHF	0.93	Negative	0.95	Negative	0.96
	Australia	AUD / USD	0.71	Positive	0.73	Positive	0.73
	New-Zealand	NZD / USD	0.66	Positive	0.70	Positive	0.70
	Canada	USD / CAD	1.28	Positive	1.25	Positive	1.25
Asia	China	USD / CNY	6.37	Negative	6.50	Negative	6.50
	India	USD / INR	74.71	Neutral	76.00	Negative	78.00
Latam	Brazil	USD / BRL	5.35	Negative	5.50	Neutral	5.25
	Mexico	USD / MXN	20.77	Positive	19.70	Positive	19.00
EMEA	Russia	USD / RUB	76.13	Neutral	76.00	Positive	74.00
	South Africa	USD / ZAR	15.51	Positive	15.00	Positive	15.00
	USD Index	DXY	95.49	Neutral	96.25	Neutral	96.31

Source: Refinitiv - BNP Paribas WM

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