FX Monthly Report

February 2023

sucdenfinancial.com

FX Monthly Report

Published by:
Sucden Financial Limited
February 2023

Research Desk
research@sucfin.com

Press Enquiries
press@sucfin.com

Authors:

Geordie Wilkes
Head of Research

Daria Efanova
Research Associate

Daniel Henson
Deputy Head FX

Nimit Khamar
FX Desk Broker

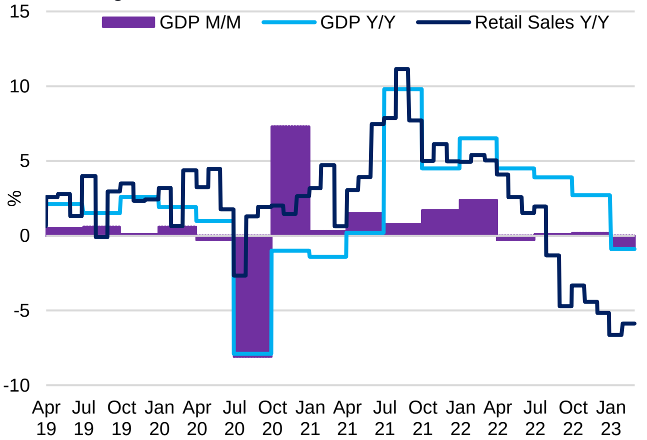
Chris Husillos
FX Desk Broker

Scandinavia Focus

Sweden

GDP Y/Y & M/M vs Retail Sales Y/Y

PPI has started to fall, but CPIF is stubbornly high. However, M/M data is falling for CPIF.



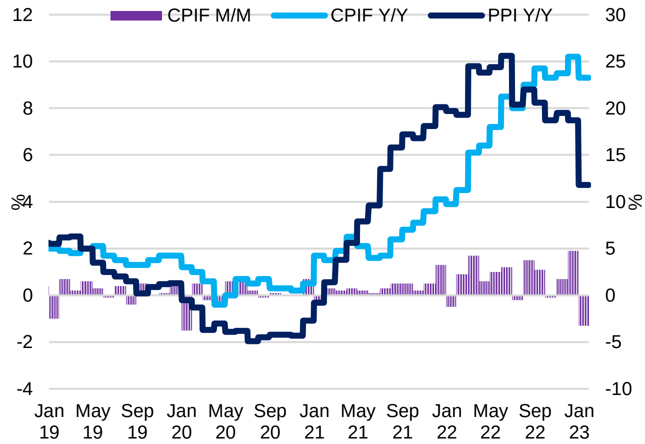
Source: Statistics Sweden

The Riksbank increase rates by 50bp in their February meeting, bringing interest rates to 3%. While CPIF inflation was softer in January at 9.3% Y/Y, down from 10.2% Y/Y in December. The issue is that core inflation increased, with food inflation contributing to higher data point for the 14th time in a row. Core inflation was 8.7% a three-decade high, with 90% of the consumer basket above 2%, one bright spot was that electricity prices were down M/M. The higher core inflation reading has prompted strength in SEK, the implied rate change is 40bps for the April meeting. Economic data will dictate if the market prices in 50bp in the coming weeks. But on February 15th, the implied rate change was 23bps, this highlights the increased hawkishness of traders over the last week following the inflation release.

The unemployment rate has increased, in the month to January 7.6%, up from 6.9% Y/Y. This presents a worry that stagflation could creep into the economy as growth declines, costs, and unemployment rises. This is not the case at this moment, but we continue to look at the data, consumer confidence, and retail sales. These data points are released in the coming days and may indicate the resilience of the consumer. However, if consumers are purchasing using debt, this would be detrimental to the economy. The January manufacturing PMI is contractionary at 46.3 but increased from the previous month of 45.9. The employment part of the survey has weakened to the lowest level since the summer of the pandemic.

Sweden CPI Y/Y vs M/M & Retail Sales Y/Y

PPI has started to fall, but CPIF is stubbornly high. However, M/M data is falling for CPIF.

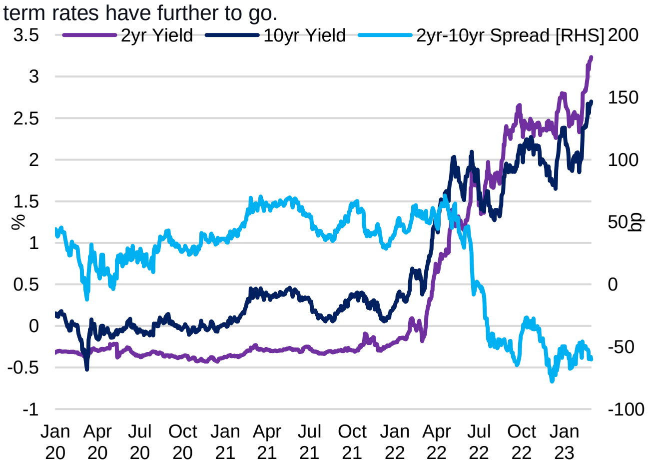


Source: Statistics Sweden, Riksbank

The housing market in Sweden is cause for concern, as rates have decreased demand for houses due to mortgage rates. Sweden house prices are down 16% in the past year, and this is expected to decline to 20% in the coming months. With rates rising, there is little respite for those on a variable industry, transaction volumes were down 27% Y/Y in January, down 14% Y/Y. This presents downside to economy in the near term, with Q4 GDP expected to be 2.5% Y/Y but only up 0.6% Q/Q, we expect growth to remain lacklustre in the near term.

Swedish Yield Curve

The spread between 2yr-10yr yields show an inversion, and near-term rates have further to go.



Source: Bloomberg, Swedish Government

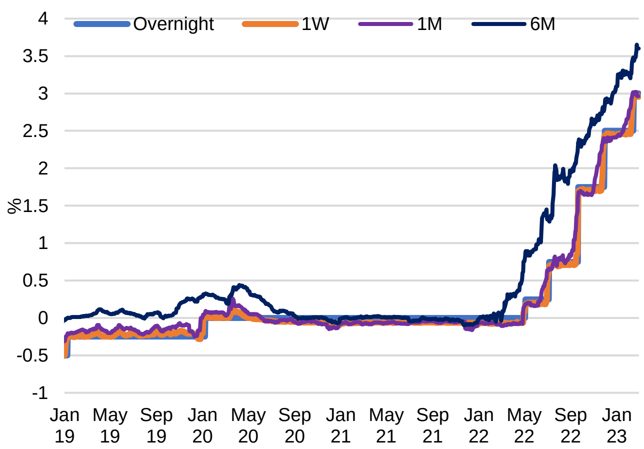
USDSEK has firmed because of the hawkish stance from the Riksbank, However, the trend has been that inflation has remained sticky, suggesting the banks will keep rates higher for longer, and terminal rates will be higher than previous expectations. This is why the USD index has rallied in recent weeks, but USDSEK has firmed in recent sessions. The range is still intact, and that is likely to be the trade until the Fed stop raising rates, and traders start betting on USD weakness. The movement in currencies shows it is still a rates trade, but the fundamentals for the Swedish economy are not as strong as the USD, which could see SEK struggle to gain ground.

STIBOR has shifted higher at the back end of the curve, with 6-months at 3.447%, but the middle of the curve between 1-month and 3-month has softened. The yield curve is inverted with the 2yr at

3.13% and the 10yr at 2.64%. This inversion is expected to widen in the coming months as short-term rates rise, but longer-term growth expectations fall. The upwardly sticky inflation could limit the curve inversion.

STIBOR Curve

The interbank facility deposit rate has risen sharply in recent weeks.



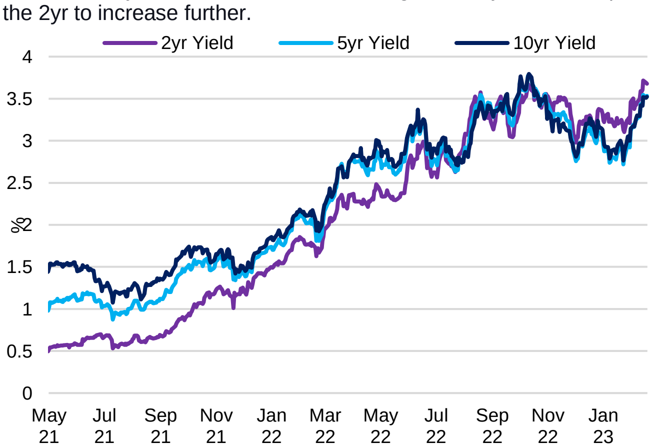
Source: Swedish Benchmark Facility

Norway

The Norges Bank kept their interest rate unchanged at 2.75% in January, however we expect rates to be increased to 3% in March. Global inflation has started to slow, but in Europe levels are still high. Freight rates have declined sharply and are at pre-pandemic levels, this highlights weaker trade, especially from China, and lower supply side costs. While the demand-pull side of inflation is weaker, borrowing costs, food prices, and rents are keeping CPI readings high. Energy costs are reducing costs for households, gas prices are significantly lower than forecasts in 2023. CPI was 0.2% M/M in January, and 7% Y/Y, with CPI underlying at 6.4% Y/Y.

Norway Yield Curve

The inverted yield curve indicates a slowing economy, and we expect the 2yr to increase further.

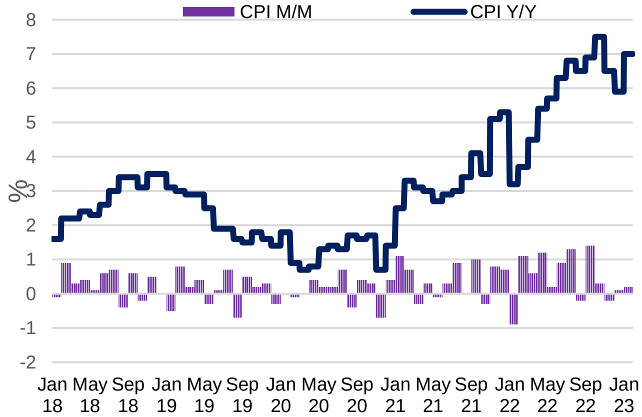


Source: Norges Bank

In Norway, this has benefitted the economy with higher-than-expected activity. GDP in Q4, including the offshore industry, was 0.8% Q/Q. This increased the probability of rate hikes from the central banks. Growth in Q4 was underpinned by strong household consumption at 5.9%, spending on services grew at 1.1%, and GDP for 2022 reached 3.8%. The unemployment rate trend was 3.4% in January, unchanged from the previous month. The unemployment rate is 1.9%, which is still historically low, and the new job vacancies has declined, and we expect some upside to unemployment in the coming months. Credit indicators growth was 5.3% Y/Y, marginally below the previous reading of 5.5%. Lower credit growth during high consumption is positive for the economy. Average earnings have been stronger in recent quarters at 4.4% Y/Y for Q4 2022. Consumer confidence for Q1 was -36.5, which is marginally better than the previous month at -36.8.

Norway Inflation

M/M data shows slowing inflationary pressure but CPI is still high.

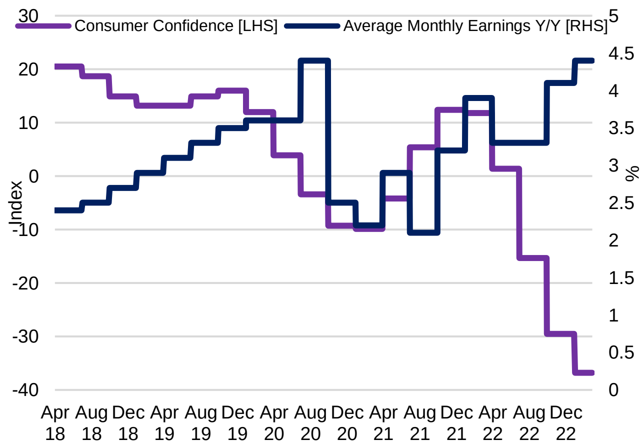


Source: Statistics Norway

Trade is robust for Norway, and was at NOK102.8bn, which historically is high, but it is significantly below last year's high of NOK231.87bn, when oil prices reached $120/bl. Oil prices are marginally softer, and the expectation that Chinese consumption will increase. Oil demand could be capped by the slower economy growth, but prices are forecast to edge lower as the surplus is intact. The EIA forecast prices will average $83.63/bl for brent, the more hawkish Fed will trigger gains in the USD.

Consumer Confidence & Average Monthly Earnings Y/Y

Consumer confidence has fallen despite higher earnings, inflation is persistently high which continues to damage confidence.



Source: Finance Norway, Statistics Norway

Currency View

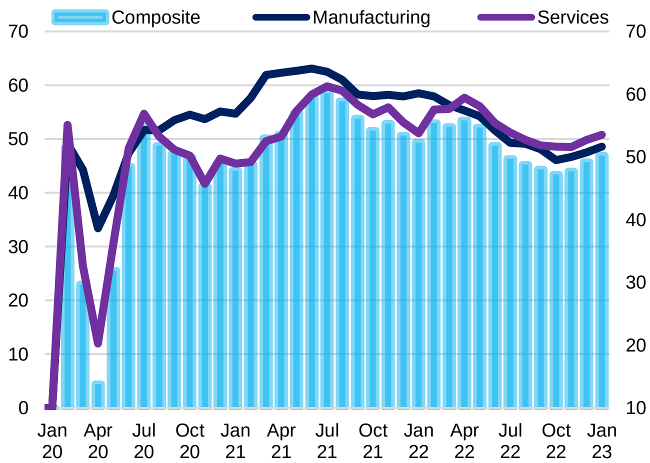
In the near term, we expect to see the USD rally as the market prices in more rate hikes. The implied rate change is 30bps for March, and 56bps change until May (approximately 30bps and 25bps), respectively. The terminal rate is little changed for the US, but higher rates for longer are entrenched in the economy, and this could cap growth. The US economic data, continues to show resilience, another boon for the USD against SEK, and NOK. However, the long-term trend is still in a period of consolidation, but we expect USDSEK and USDNOK to test the upper ranges, especially if PCE is stronger than expected the Fed inflation gauge. Rate cuts are not priced in for 2023 and stand at 63% for January 2024, even when this approaches, the rate differential will be important. As the Fed will have a higher rate (5.2%-5.3%) to cut from compared to Norway which currently stands at 2.75%, at the time of writing.

Desk Comments

Euro

European PMIs

European PMIs have edged higher in recent months but can this be sustained.



Source: S&P Global Platts

Headline inflation in the eurozone continued to ease after energy prices declined further but the core inflation numbers remain elevated and will remain significantly above the ECBs 2 % target for an extended period. A 50bp rate hike is priced at the next meet with a terminal rate currently projected at 3.75%. Lagarde recognises the upward inflation pressures, so the risk remains of more tightening and an upward revision in line with other G8 economies.

The 10 yr German yields moved above 3% for the first time in over a decade. The 2-to-10-year segment inverted meaning the market is expecting inflation to be under control in the longer term.

We expect EUR to remain in a tight range in the near term but remain cautious of any big misses in macro data. EUR should also benefit on positive headlines to the Northern Ireland protocol as an agreement is close.

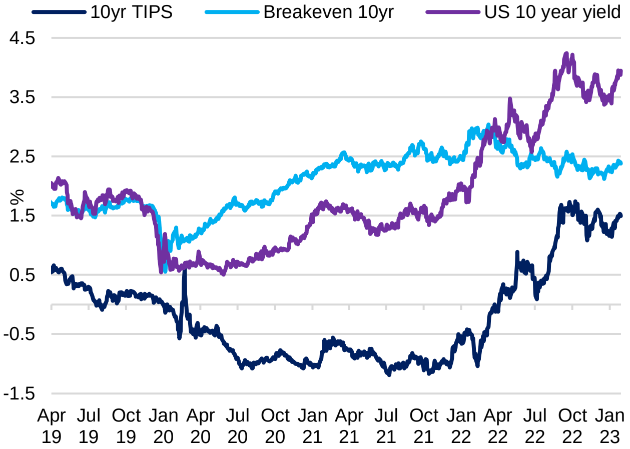
USD

The Fed raised rates by 25 basis points in Feb spurring a rally in the USD after chair Jerome Powell indicated a hawkish rhetoric leading to treasuries rising to multiple month highs. Minutes showed Fed expect further increases would be required to bring inflation down to their 2% target. There is increased sensitivity to a hawkish signal helping the USD strengthen against all G10 currency.

With data showing US inflation still running hot, coupled with the labour market remaining tight; terminal rates are about 50 basis points higher (5.38% at time or writing) compared to start of month, with expectations for rate hikes into Q3.

10yr TIPS vs 10yr Breakeven vs 10yr Yield

Yields have further to climb following upwardly sticky inflation.



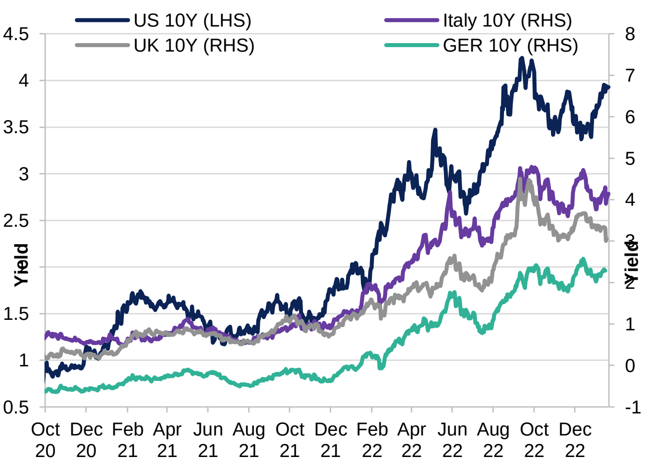
Source: Federal Reserve

We believe the recent hawkish rhetoric and strong data has now been priced in and further significant re rating of terminal rate is looking increasingly unlikely in the coming months. This does not necessarily mean dollar will start shifting lower as increased risk of recession amid prospect of higher rates and inflation. Hence, we expect the dollar to continue to be supported into Q2 as market participants seek to safety of the dollar especially given the yields on offer. Market focus over the next month will likely be on equity markets and VIX index as market participants look for change in risk sentiment rather than movements in the rate market.

GBP

US, UK, Italian, Germany, 10yr Yields.

Yields in the UK and Italy are falling, but the US has kicked on.



Source: Bloomberg

The British pound has continued to perform well, buoyed by better-than-expected data. UK PMI beat forecast and showed business activity is picking up sharply leading to projections of the UK avoiding a recession and GDP to grow by 0.1% in Q1. Inflation has continued to decline and will likely fall further due to a global fall in energy prices. However, there are plenty of reasons for the BOE to be on alert. There are concerns of food supply shortages due to the adverse weather in Spain and North Africa and the constraints on producing locally during the winter months. Moreover, the labour market is a bigger concern with companies boosting pay at the quickest rate on record. Average weekly earnings excluding bonuses was up to 6.7% from 6.5% this month. As a result, we have seen a lot of two-way flow in GBP. The MPC is divided on how much more action is needed to contain price pressures. We expect further small hikes in the near-term to allow the effects of previous rate hikes to come through the economy.

Technical Analysis

GBPUSD

GBPUSD has broken below the ascending triangle mentioned in last month's report. Breakout target could see GBPUSD pull back to 1.1388 and then 1.1237. Support along the way will be around 1.1842 and 1.1645. On the upside, a break above 1.2450 area which has held 3 times now could lead to further correction up to 1.2759 (61.8% fib) white down trend.

EURUSD

EURUSD failed to close above the 50% Fib level and has retraced back forming support around 1.0533. On the upside, while the uptrend (black line) and support around 1.0466 hold then expect market to retest the 50% fib line. A close above the 50% fib retracement could see EURUSD climb up towards 200week MA / 1.1213 (61.8% fib). Next resistance level beyond there comes in at 1.15. On the downside, a weekly close below 38.2% fib could see the market pull back towards 50% fib of the recent move up, with a break below signalling a deeper pull back to 1.0108 and parity level.

Disclaimer

United Kingdom
Sucden Financial Limited
Plantation Place South
60 Great Tower Street
London
EC3R 5AZ

Tel: +44 (0)20 3207 5000
Email: info@sucfin.com

Hong Kong
Sucden Financial (HK) Limited
Unit 1001, 10/F
Li Po Chun Chambers
189 Des Voeux Road Central
Hong Kong

Tel: +852 3665 6000
Email: hk@sucfin.com

USA
Sucden Futures Inc.
156 West 56th Street
12th Floor
New York, NY 10019
United States

Tel: +1 212 859 0296
Email: ny@sucfin.com

sucdenfinancial.com