Currency Outlook

An OFXpert guide to key currencies and events to watch

The below key drivers are likely to impact investor risk sentiment and FX markets in December:

1 US dollar weakness and subsequent bond sell-off boosted the performance of most G10 currencies. AUD, NZD, GPB, EUR and JPY were primary beneficiaries.

2 The European Central Bank and Federal Reserve both seem to favour holding future interest rates, leading markets to price in an end to tightening cycles.

3 Poor economic data for multiple markets could mean further contraction for the European bloc and flat progress for the United Kingdom.

€ EUR Euro

The euro gained ground against the US dollar amid expectations that the US Federal Reserve was pausing rate hikes. With the Eurozone's economic challenges, eyes are on the ECB's upcoming interest rate decisions.

In November, the euro surged against the US dollar as markets became convinced that the US Federal Reserve (Fed) was done with its rate hiking cycle and would be entering a 'wait and see' period.

The EURUSD currency pair started November around US$1.05 but managed to break above US$1.10 on November 29th, its highest level since August.

The European Central Bank (ECB) looks to be holding rather than hiking interest rates. At present, many expect the ECB to be the first big central bank to loosen policy with many eyeing its March 7th or April 11th get-togethers most likely for when a reduction from 4.5% will be seen.

Eurozone inflation fell further than expected in November, with the Consumer Price Index (CPI) dropping to 2.4% from 2.9%, nearing its 2% target. With a flatlining economy, ECB President Christine Lagarde will likely be focused on energy prices over the winter and then hopefully look to ease policy in the Spring.

Many economic indicators continued to paint a picture of an economy slipping into recession with manufacturers across the bloc seeing a further contraction in output. One bright spark was the German Manufacturing PMI above forecast at 42.3, its fourth move in a row closer to the 50 level that divides contraction and expansion.

Looking ahead, the ECB's December 14th interest rate decision will be the main event of note. With no change in policy expected comments from ECB President Lagarde regarding the date of potential cuts will be closely eyed.

Expected ranges:

- **EURUSD 1.0500-1.1000**
- **EURGBP 0.8500-0.8725**

$ AUD Australian dollar

November saw a remarkable turnaround for the AUD, surging from October lows. Softening US data shifted market expectations, pricing in an end to the Federal Reserve's tightening cycle, benefiting the AUD.

After testing 2023 lows through October, the AUD rallied aggressively through November, bouncing off US$0.6270 and surging through US$0.6650 to mark fresh 3-month highs.

Softer US activity and inflation data, plus naturally tighter financial conditions have allowed markets to price-in an end to the Federal Reserve's (Fed) tightening cycle while adjusting expectations across the curve through 2024.

Markets expect inflation will continue to move toward the Federal Open Market Committee's (FOMC) 2% target without the need for further rate hikes, adjusting yield curves to price in a series of rate cuts beginning as early as March 2024.

US treasury yields have given up some 60 points over the last 4 weeks, driving a broad USD sell-off.

The AUD has been a primary benefactor of the USD correction. Given the pace and scale of the rebound to date, we expect further gains will be more measured. A theory evidenced after the December RBA policy meeting.

Having tested fresh highs at US$0.6690 on Friday, the AUD traded back below US$0.66 following the RBA decision to leave rates on hold. While the market had priced-in the decision, a dovish commentary accompanying the policy announcement helped take some of the wind from the AUD's sails.

Looking ahead, speculators and investors are still holding a USD net long position, suggesting potential downside risk should markets continue to swing toward a neutral USD setting. Fed policy guidance and expectations remain key in shaping the global rates backdrop and USD performance.

Expected ranges:

- **AUDUSD 0.6400-0.6800**

$ USD United States dollar

The US dollar was down in November, due to economic data indicating a slowdown. The uncertain economic outlook suggests a cautious approach amid potential fluctuations. All eyes are on central banks for any policy shifts.

November saw the US dollar on a downtrend against G10 currencies.

It's not difficult to guess what is driving the US dollar weakness: the latest economic data. For example, the US job market has entered a consolidation period with low rates of quitting, hiring, and layoffs, which is a move away from the "great reshuffle" of a high rate of quitting and hiring with a low rate of layoffs in 2021-2022.

Furthermore, the manufacturing sector's performance suggests that the US economy might be slowing down. Likewise, delinquent commercial real estate loans at US banks hit the highest level in a decade and auto loan delinquencies among subprime borrowers reached a near 30-year high a couple of months ago.

There was a slowdown in US retail sales growth for the first time in seven months, and a decrease in momentum for retail sales when adjusted for inflation. This deceleration suggests that consumers are tightening their spending habits.

The uncertain US economic outlook does not guarantee an uninterrupted decline for the USD. Interestingly, this uncertainty could bolster the US dollar's status as a safe-haven currency. However, this trend could pause or extend into December and 2024, influenced by various factors, such as other central banks' assessments, because the US dollar's weakness hinges on domestic conditions and assessments made by other central banks regarding their own economies.

Expected ranges:

- **DXY 99-105**

$ SGD Singapore dollar

The SGD reached a 4-month high against the US dollar last month, boosted by lower US yields, strong economic indicators, and higher-than-expected inflation. A cautious tone from the Fed meeting in December could drive continued SGD strength.

The Singapore dollar traded to a four-month high in November off the back of lowering US yields. The USDSGD pair dropped to 1.3284 on November 28 and finished the month lower by -2.4%.

Last month also saw Singapore's Q3 GDP surprised to the upside, printing a result of 1.4% (quarter on quarter) versus a 1.1% forecast. Furthermore, Inflation in October rose to 4.7% (year on year) from 4.1%, beating the forecast of 4.5%. Core inflation moved up to 3.3% (year on year) from 3%. The SGD strengthened after the stronger-than-expected inflation figure.

In December, the SGD momentum is likely to be determined by the USD strength with the Fed meeting on December 13 and Fed officials have already been giving the market mixed signals. The Singapore dollar may find more support should the Fed become less hawkish.

Expected ranges:

- **USDSGD 1.3250-1.3550**

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Any questions?

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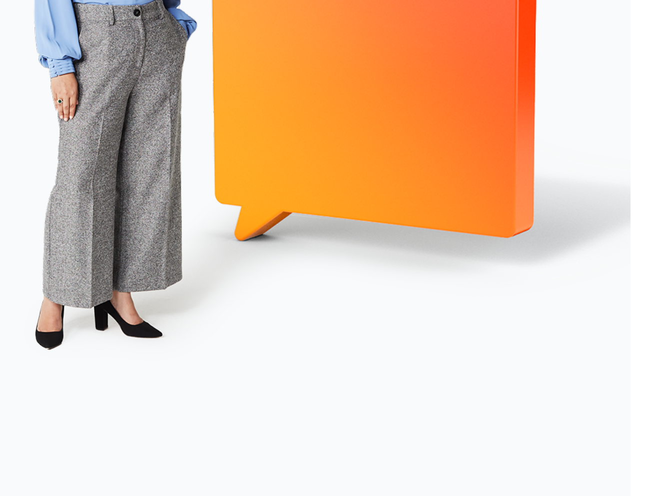

£ GBP Sterling

The pound soared against the US dollar in November, fuelled by the Bank of England's interest rate decision and broad dollar weakness. Mixed domestic data sets the stage for the BoE's December interest rate decision.

Throughout October, the GBPUSD currency pair traded in a narrow range, with it dipping as low as US$1.2035 on October 4 and remaining between US$1.21 and US$1.23 for most of the month.

At the November 2 policy decision, the Bank of England (BoE) held interest rates at 5.25%, their highest level in over 15 years. Those households remortgaging and hoping for a cut in rates early next year may be left disappointed as BoE Governor Andrew Bailey and other members of the Monetary Policy Committee seem to favour an extended period at 5.25% before any cuts are considered. This extended period of elevated rates may help support the pound's value unless there is a considerable downturn in UK economic health.

October's monthly GDP saw 0.2% growth compared to the previous reading of -0.6%. Retail Sales fell back by -0.9% when a more modest drop was eyed and the closely followed Services PMI came in at 49.2 showing that the sector that makes up around 80% of the UK economy is contracting slightly. Combined this paints a picture of an economy that will likely flatline at best for several months, however, it should be said that the economy has outperformed what many were predicting this time last year.

Expected ranges:

- **GBPUSD 1.2050-1.2425**
- **GBPEUR 1.13-1.16**

$ NZD New Zealand dollar

NZD surged in November, thanks to softening US data, a USD sell-off and a hawkish RBNZ statement further boosting its performance. Will the momentum last through December?

The New Zealand dollar outperformed through November, outpacing most key counterparts. After testing 2023 lows through October, the NZD rallied aggressively through November, bouncing off US$0.5790 and surging through US$0.62, to mark fresh 3-month highs.

Despite naturally tighter financial conditions, softer US activity and inflation data have allowed markets to price-in an end to the Federal Reserve's (Fed) tightening cycle while adjusting expectations across the curve through 2024.

US treasury yields have given up some 60 points over the last 4 weeks and while conditions are tighter than they were at the beginning of October, the correction in yields has fostered a broad USD sell-off.

A surprisingly hawkish RBNZ policy statement on November 29th helped ensure the NZD outpaced other majors, enjoying gains against the AUD, Euro, GBP and Yen. The question now is, can the NZD extend the recovery through the end of the year? Given the pace and scale of the rebound to date, we expect further gains will be more measured. A theory evidenced in the correction to back below US$0.62 in the week starting December 4th.

Looking ahead, market analysis shows that speculators and investors own more USD than they owe, suggesting there is more downside risk for the USD should markets continue to swing toward a neutral USD setting.

If the market continues to prepare for an end to the Fed tightening cycle, the NZD should consolidate recent moves and track within a higher trading range through the end of the year.

Expected ranges:

- **NZDUSD 0.60-0.64**

¥ JPY Japanese yen

In November, the yen reached a 3-month high against a weaker US dollar. Despite the market thinking otherwise, BoJ officials suggest no immediate easing policy change, tying JPY's fate to USD strength in December.

The Japanese yen rallied to a near 3-month high on November 27, off the back of a weaker US dollar. The USDJPY pair traded under the 150 level for most of the last month, moving away from intervention levels.

Despite a lack of a central bank meeting in November, Bank of Japan (BoJ) officials Adachi and Nakamura made comments on the policy stance. They do not think it's time to discuss ending the easing yet and Nakamura said they "can't say when policy will be adjusted". This may be supported by the fact that Q3 preliminary GDP in Japan contracted by 0.5% (seasonally adjusted quarter on quarter) but other economic indicators disagreed. However, Japan's national CPI in Oct edged higher to 3.3% from 3.0% prior and labour cash earnings year on year in September rose as well from 1.1% to 1.2%.

Therefore, the strengthening momentum of JPY would be largely dominated by USD strength in December and it may find more support if the Fed turns dovish. Furthermore, at the time of writing, the market is pricing a higher chance for Japan to exit negative rates territory as early as this month, giving more room for the yen to rally.

Expected ranges:

- **USDJPY 143-148**

$ CAD Canadian dollar

In November, the Canadian dollar weakened against most G10 currencies. The Bank of Canada's dovish tone reflects concerns over economic factors, influencing monetary policy decisions.

The Canadian dollar fell against all G10 currencies except the US dollar, which beat it by 2.3% in November.

Canada is demonstrating a heightened sensitivity to interest rates compared to the United States. This has implications for monetary policy decisions in Canada. The Bank of Canada (BoC) kept its overnight rate at 5% for the third consecutive time, and they are becoming more dovish on their market message. For instance, they took out the reference to the labour market being on the "tight side." The BoC has also deleted the phrase "inflationary risk has increased" from their statement.

The impact of stringent monetary policies in Canada is becoming more apparent as business fixed investment declines. Meanwhile, companies indicate that labour shortages are improving, and employment is hovering around neutral levels; the weakening job market introduces potential downsides to forecasts for spending and overall economic growth.

Many Canadian households face mortgage resets in 2024 under higher rates; the spending surge in Canada in November is viewed as temporary, signalling an imminent need for further financial caution. Governor Macklem from the BoC said two weeks ago that tighter monetary policy "is working, and interest rates may now be restrictive enough to get us back to price stability."

Technically speaking, the USDCAD bounced at the beginning of December from a 1.35 handle; however, 1.36 and 1.37 are strong resistance levels, which might make this pair trade in this range for the rest of December.

Expected ranges:

- **USDCAD 1.3400-1.3700**

$ HKD Hong Kong dollar

In late November, the Hong Kong dollar hit a 4-month high before retracing some gains. Despite fluctuations, it closed the month down slightly. December's direction hinges on Fed interest rate signals.

The Hong Kong dollar traded to a four-month high in late November before erasing some of the gains by month end. The USDHKD started the month at 7.8239, fell to a 4-month low at 7.7861 on November 27, yet managed to trade back up to 7.7104 and finished the month down by only 0.2%.

On November 2, the Hong Kong Monetary Authority (HKMA) kept its base rate unchanged at 5.75%, in line with the Fed's rate hike pause decision the day prior. However, the HKMA said HKD interbank rates "might remain high for some time". Hong Kong's interbank offered rate (HIBOR) was on one way up last month – one-month HIBOR rose from 4.8756% to 5.1167% and 3-month HIBOR increased from 5.2263% to 5.6105%.

In December, the HKD is likely to edge higher against the USD but within a reasonable range should the market become clearer about the future interest rate paths for the Fed.

Expected range:

- USDHKD 7.8000 - 7.8300

Expected ranges:

- **USDHKD 7.8100-7.8400**