G10 FX Weekly

Group Economics
Macro & Financial Markets Research

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USD gains as Fed leaves door open for December hike

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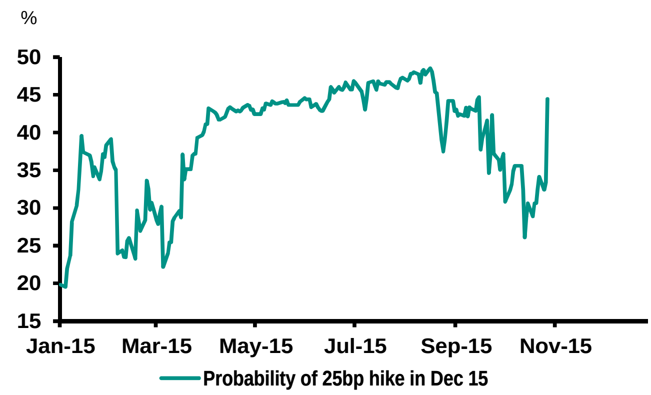
- **US dollar gains as December rate hike expectations rise**
- **Speculation of ECB stimulus weighs on the euro**
- **Australian dollar slides as RBA easing expectations increase**
- **RBNZ warns strong New Zealand dollar will trigger more rate cuts**

US dollar gains as December rate hike expectations rise

The US dollar (USD) gained across the board as the FOMC was more hawkish than expected. The FOMC appears to be less concerned about global developments. Our base scenario is that the Fed will wait until next year before raising interest rates, but the statement raises the probability of a December move. US economic data have softened recently. Meanwhile, it remains to be seen whether the pricing in of earlier Fed rate hikes negatively impacts sentiment, which could lead to a renewed tightening of financial conditions.

Probability of 25bp rate hike in Dec 15



Source: Bloomberg, Fed funds futures

Speculation of ECB stimulus weighs on the euro

The euro has weakened noticeably over the past few days. The ECB's signal that it will step up its monetary stimulus program in December has pressured the euro. Indeed we now expect the ECB to lower the deposit rate by 10bp to -0.3% later this year in December. In addition, it seems likely that the ECB will leave the door wide open to do more if necessary. This will depend on the strength on the euro. We also expect a 5bp cut in the refi rate, taking it to zero. We already expected the ECB to increase the size of its asset purchase program from EUR 60b a month to EUR 80b. The deadline of the QE program is also likely to be extended beyond September 2016. We have lowered our euro forecasts versus the US dollar and sterling to reflect our changes in the ECB call as we now also expect a deposit rate cut. Our new forecast for the end of this year for EUR/USD is 1.10. Our forecast for the end of 2016 remains unchanged at 1.00.

Australian dollar slides as RBA easing expectations rise

A weaker-than-expected inflation print in the third quarter has reinforced our view that the Reserve Bank of Australia (RBA) will resume its easing cycle on 3 November. This is not fully priced in by financial markets. Hence a weaker AUD to around 0.70 by the end of this year is expected. Looking ahead, weaker house price inflation, subdued wages will continue to weigh on non-tradable inflation. A weaker Australian dollar is also needed to boost tradable inflation. Indeed the risk has increased that the RBA may need to further ease monetary policy next year due to sub trend economic growth and weak commodity prices. Slower economic growth in China next year to 6.5% will remain a headwind to the Australian economy. We expect the AUD to decline to 0.62 by the end of 2016.

RBNZ warns strong NZD will trigger more rate cuts

We maintain our bearish view on the New Zealand dollar (NZD) and year end forecast of 0.64. We expect the Reserve Bank of New Zealand (RBNZ) to lower the Official Cash Rate (OCR) by 25bp to 2.50% later this year in December. The RBNZ has warned that the recent strength in the NZD if sustained would require more aggressive rate cuts in the future. As the current level in the NZD trade weighted index is more than 6% stronger than the RBNZ year-end forecast, intervention in the currency market to weaken the NZD is also a likely option for the central bank. Our 2016 forecast for the NZD/USD is 0.58.

ABN AMRO major currency forecasts

Changes in red/bold

	29-Oct	Q4 2015	Q1 2016	Q2 2016	Q3 2016	Q4 2016
EUR/USD	1.0961	**1.10**	**1.08**	1.05	1.00	1.00
USD/JPY	120.84	122	126	130	133	135
EUR/JPY	132.46	134	136	137	133	135
GBP/USD	1.5265	1.57	1.54	1.50	1.45	1.47
EUR/GBP	0.7181	**0.70**	**0.70**	0.70	0.69	0.68
USD/CHF	0.9895	1.00	1.02	1.07	1.14	1.15
EUR/CHF	1.0847	1.10	1.10	1.12	1.14	1.15
AUD/USD	0.7097	0.70	0.68	0.66	0.64	0.62
NZD/USD	0.6693	0.64	0.62	0.6	0.58	0.58
USD/CAD	1.3209	1.33	1.35	1.37	1.39	1.41
EUR/SEK	9.3323	9.50	9.50	9.50	9.50	9.50
EUR/NOK	9.3674	9.50	9.25	9.00	8.75	8.50
EUR/DKK	7.4577	7.46	7.46	7.46	7.46	7.46

Source: ABN AMRO Group Economics

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