Dr. Thomas Gitzel · Chief Economist

Our View on Currencies

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Dollar weakness continues

Will the weakness of the US dollar continue? This question is occupying the currency markets like no other. Following the announcement of new "reciprocal" tariffs by US President Donald Trump at the beginning of April, the US currency fell sharply. In recent weeks, some calmness has returned, and the dollar stabilized. However, the downward trend continued with the latest tariff threats against the EU.

The large US budget deficit (2024: 6.9% of GDP) and the resulting current account deficit (2024: 4% of GDP) are weighing on the greenback. Analysing historic data reveals that current account deficits of over 4% of GDP have always weakened the dollar - and this hurdle has just been crossed. Also, the US has become the world's largest foreign debtor.

The higher one country's liabilities to the rest of the world grow, the more difficult it is to receive new capital from abroad. Empirically, there is a very close correlation between foreign liabilities and the interest that has to be paid on government bonds. In other words, investors demand a premium.

For foreigners to continue to finance the budget deficit linked to the current account deficit, the price of US government bonds in dollars will have to fall. This is usually happening through currency devaluation or a fall in bond prices.

A drastic setback in the price of US government bonds would hardly be tolerated by the White House in view of the growing mountain of debt. The only likely reaction is therefore a devaluation of the US dollar. This is why further setbacks of the dollar could be on the agenda in the coming months.

Dr. Thomas Gitzel, **Chief Economist**

Our View on Currencies - Overview

Currency pairs

Our View on **EUR/USD**

1.10 – 1.20
Expected range
for 3 to 6 months

- Interest rate advantage of the dollar recedes
- New tariffs weigh heavily on the dollar
- Spreading US recession fears

- More ECB interest rate cuts than expected by the market could weigh significantly on the euro
- Dollar remains in demand as a safe haven in uncertain times

Dollar: Consider further devaluations

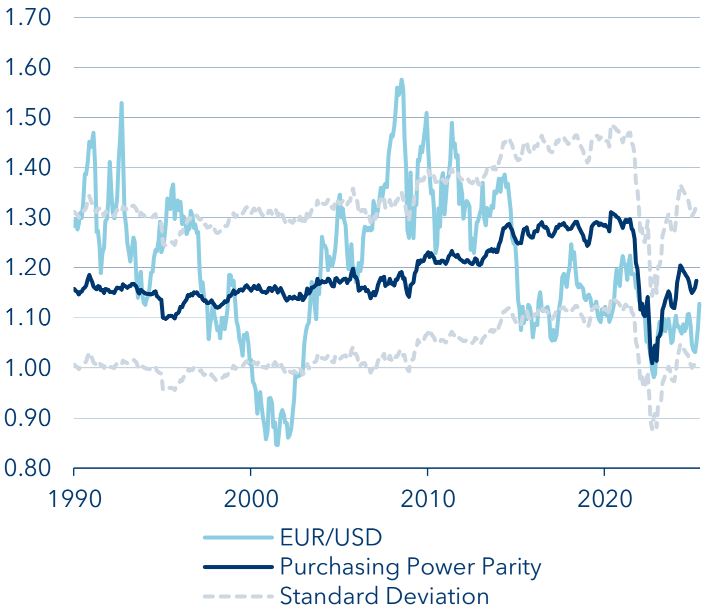
The euro rallied against the dollar. US tariff policy led to a loss of confidence towards the US. Investors favoured European assets, which also helped the euro. Following the dollar's significant losses, market technicals are now signaling a consolidation phase. We expect further dollar losses in the coming months. The trade-weighted US dollar is significantly overvalued and hence vulnerable to further losses in view of the persistently high trade deficit.

This deficit is accompanied by a record level of foreign debt - the higher the foreign liabilities, the more difficult additional financing becomes. Correcting these imbalances will require more attractive US investments, which will primarily be achieved by devaluing the dollar.

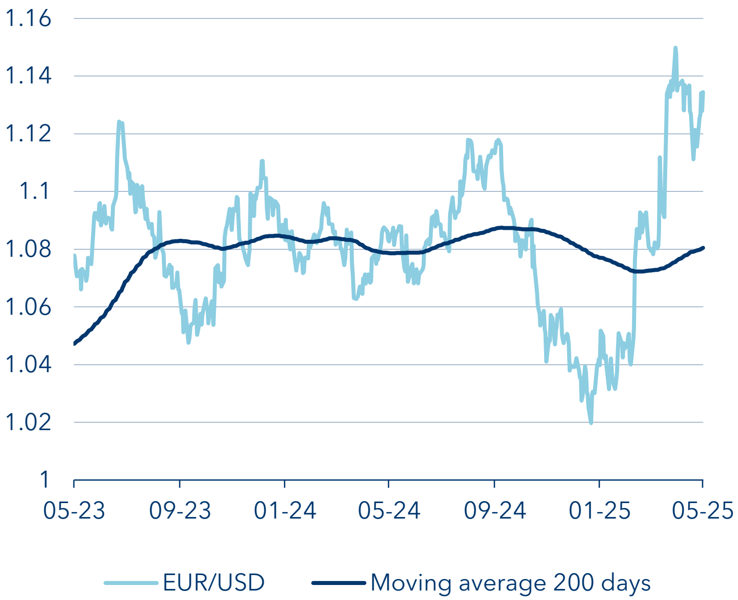
Our View on **EUR/USD**

1.10 – 1.20
Expected range
for 3 to 6 months

Purchasing power parity (producer prices; monthly data)



Technical view



Our View on **EUR/CHF**

0.92 - 0.98
Expected range
for 3 to 6 months

- SNB expected to cut interest rate to 0%
- ECB must act cautiously, price pressure in the services sector is high
- Market technique points to franc weakness

- A larger than expected interest rate cut by the ECB could weaken the euro
- Weakening of the euro against the franc due to a sudden flight to safety

Swiss franc shows slight weakness

The Swiss franc has depreciated slightly against the euro since the beginning of April. The temporary easing of the threat of US tariffs has made safe havens such as the franc less attractive. Short-dated Swiss government bonds are trading with a negative yield again. However, this did not significantly harm the franc. This shows that the interest rate differential is not the driving factor for the Swiss franc.

Despite the declining need for safety, the franc remains a safe haven during bouts of global uncertainty. We do not expect anything significant to change and the franc should therefore remain an extremely robust currency. We expect it to move sideways in a range between 0.92 and 0.98 over the next three to six months.

Our View on **EUR/CHF**

0.92 – 0.98
Expected range
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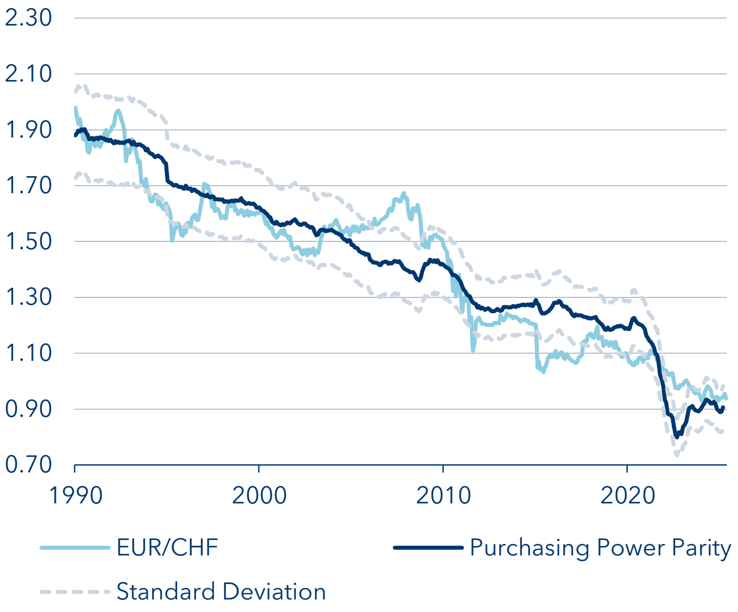
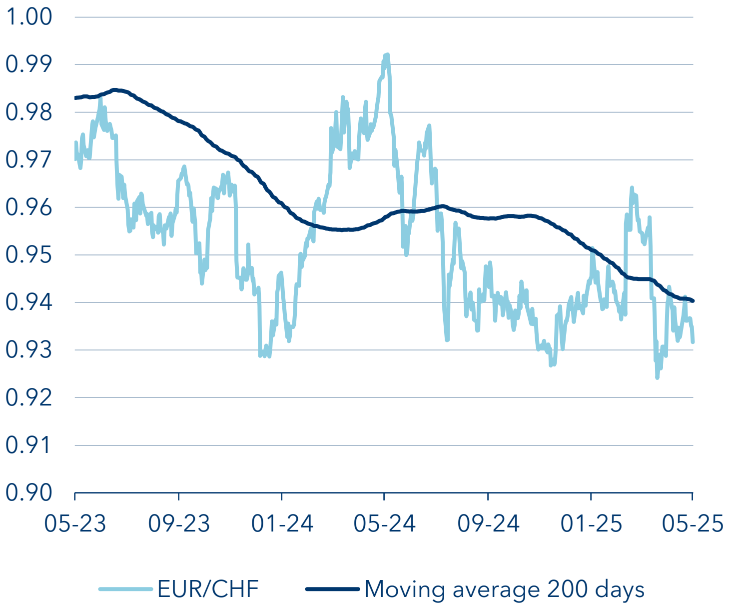


Technical view



Our View on **USD/CHF**

0.80 - 0.85
Expected range
for 3 to 6 months

- US economy under pressure from tariffs
- Interest rate advantage of the greenback fades
- Technical analysis signals a necessary consolidation

- The dollar is ahead when uncertainty is elevated
- The Swiss franc is fairly valued at levels of 0.80 and slightly below

Further Swiss franc appreciation limited

The Swiss franc appreciated sharply against the dollar at the beginning of April, reaching the lower end of our forecast range at 0.80. The signing of the first trade agreements between the US and the UK and China led to a brief respite on the financial markets, which eased the pressure to sell the dollar. However, the selling continued due to a new tariff conflict with the EU. However, from a technical point of view, a consolidation is possible. In addition, the franc is approaching its fair level against the dollar based on purchasing power parity. The high interest rate differential no longer plays a major role.

Short-dated Swiss government bonds are again trading at negative yields, but this has not stood in the way of the franc's appreciation. We expect the franc to move sideways against the dollar over the next 3 to 6 months.

Our View on **USD/CHF**

0.80 - 0.85
Expected range
for 3 to 6 months

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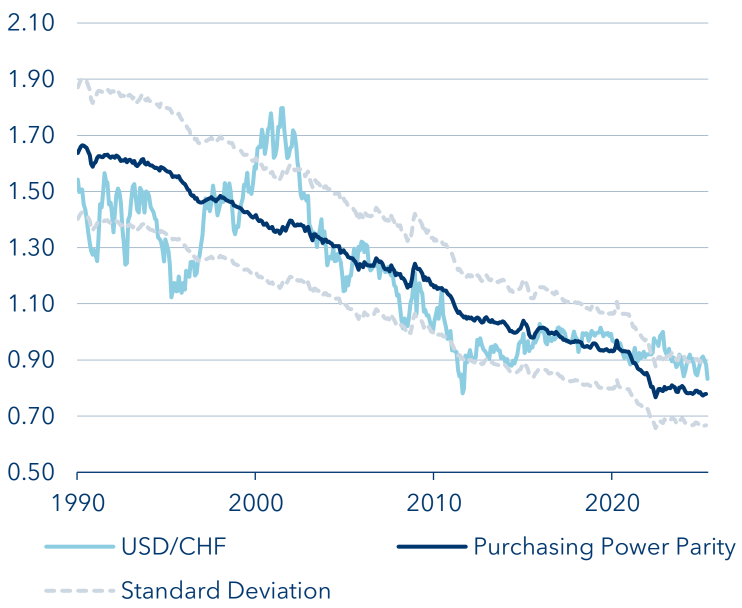

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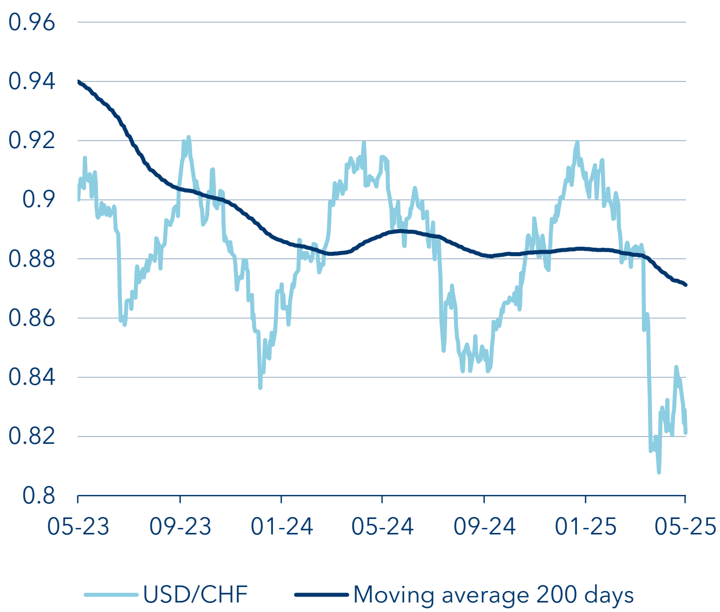

Our View on **GBP/USD**

1.32 – 1.40
Expected range
for 3 to 6 months

- The pound is significantly undervalued against the dollar
- British government moves closer to the EU again
- Weaker US economic data weigh on the dollar

- Brexit reduces potential growth, which argues against a significant appreciation of the pound
- The pound remains under pressure due to relatively high inflation

Pound also shines

The pound appreciated sharply. This shows that tariff debates are damaging the dollar, which was the opposite at the beginning of the year. The US is suffering a loss of confidence. Meanwhile, the British economy showed its strong side in the first quarter and grew unexpectedly strongly by 0.7% compared to the previous quarter. A trade deal concluded with the US is also a positive factor. However, these positive factors will not help the pound to appreciate further.

After significant gains, the signs are pointing to consolidation for the time being. In terms of purchasing power parity, the British currency remains massively undervalued (see left chart, next page). In the long term, further price gains could therefore be on the agenda. However, this would require not only a strong pound, but also a sustained, broad-based weakness of the dollar.

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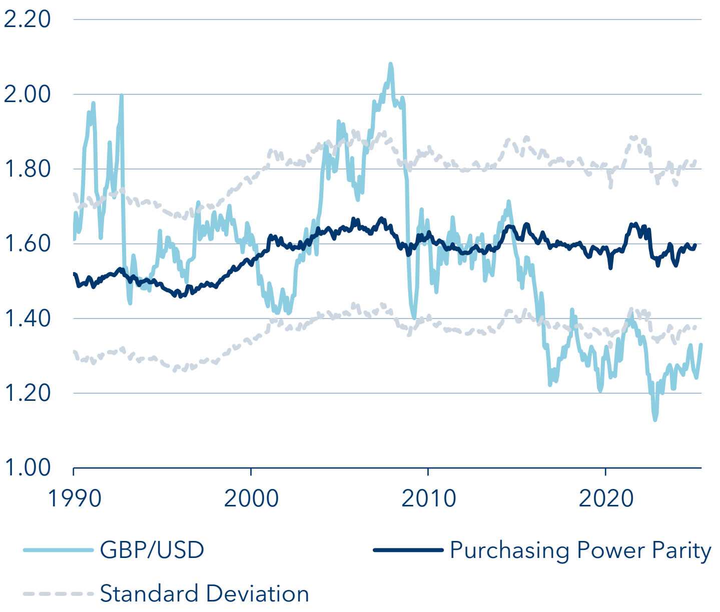

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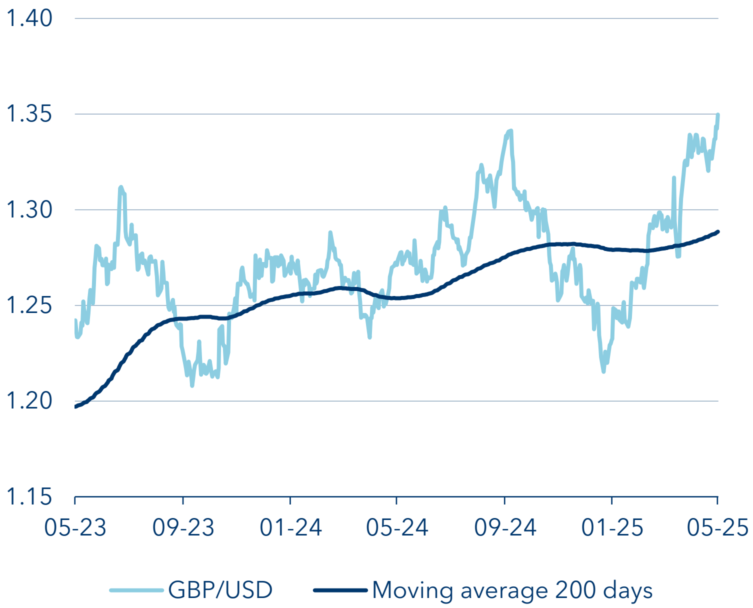

Our View on **EUR/SEK**

10.00 – 11.00
Expected range
for 3 to 6 months

- High current account surplus and healthy public finances counter the weakness of the SEK
- Declining commitment of the ECB in the fight against persistently high inflation would weaken the euro

- Currently still unfavourable environment for high-beta currencies such as SEK
- Technical counter-reaction to be expected after the recent SEK appreciation

Impressive SEK rally

For a short time, it seemed as if the Swedish krona was gaining momentum for significant appreciation. However, it ended at 10.80 against the euro. Further appreciation would require a general change in sentiment on the currency markets. For this to happen, the dollar would have to show further weakness, or the euro would have to continue to gain strength in return. The Swedish krona can benefit disproportionately in phases of broad euro strength. This has recently been the case, and this phenomenon has also been regularly visible in the past.

If more foreign capital reaches Europe, this draws investors' attention to Sweden. Due to its lower liquidity, the much smaller currency compared to the eurozone reacts significantly to these capital flows. For the time being, the usual sideways movement of the Swedish krona against the euro is likely to dominate.

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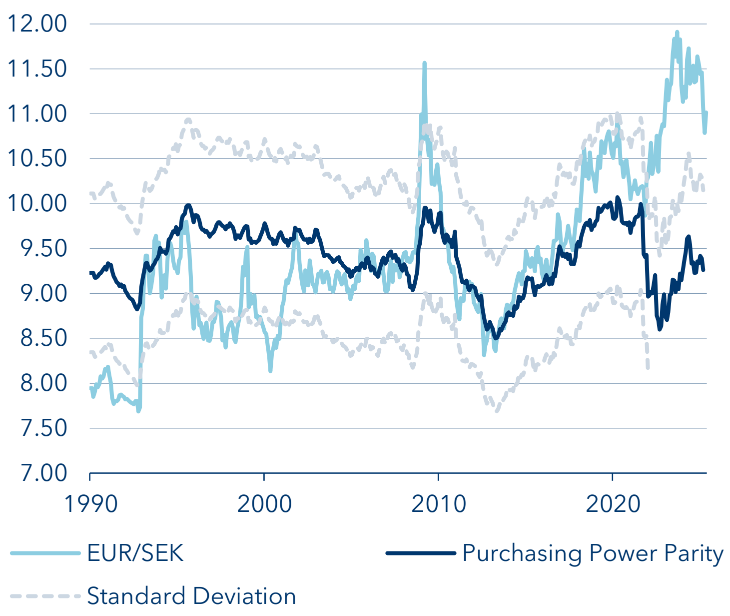

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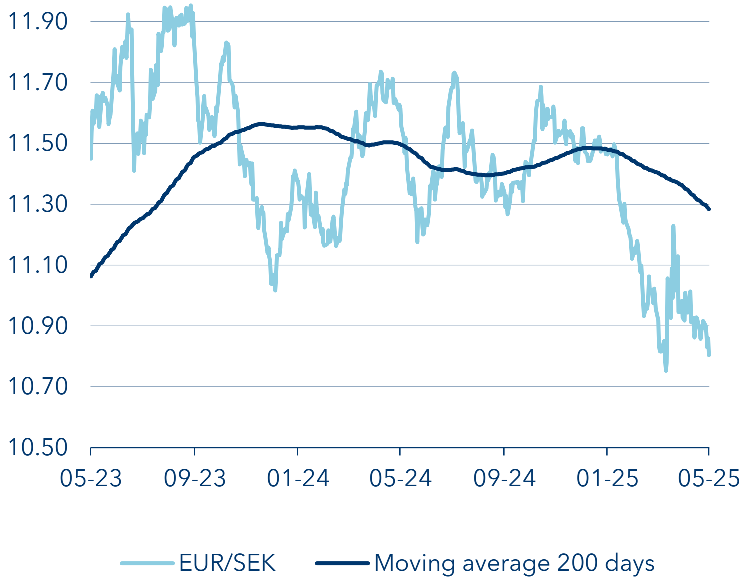

Authors and Disclaimer

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On Purchasing Power Parity: The Purchasing Power Parity (PPP) describes that a product costs the same in two countries as long as it can be traded without restrictions and the transaction costs are negligible. The relative PPP used here is based on producer price indices and assumes that the prices of the products change by the same amount, taking into account the exchange rate, but that the price levels may differ.

Source: Bloomberg