

# FX forecast update

November 14, 2008

## Time for change? Not yet

- We revised our FX forecasts in-between our regular forecast updates on 24 October; see [Revised FX Forecasts: G10 and EM](#). Most notably, we raised all our short-term USD forecasts and pencilled in more JPY and CHF strengthening, along with more SEK and NOK short-term weakness. As risk sentiment was deteriorating sharply and no obvious triggers for an end to this was in sight, we considered it likely that things could worsen further. The rapid rise in risk aversion has stopped – albeit remains at a high level – and the immediate drivers for further JPY and CHF appreciation have thus faded. Unfortunately we called off our predicted rise in EUR/GBP too early as we – in line with most other forecasters – underestimated the amount of negative news already priced into the pound at a time when sterling denominated assets were heavily sold off.
- **We remain guided by the dual themes of a financial crisis and a global recession.** Recent data has further confirmed the outlook of the global economy falling into recession and we do not expect global activity to begin to expand until H209. Key data will continue to be depressed and both household and business conditions are likely to worsen further as access to credit has been severely tightened. Demand for fiscal stimulus is increasing but implications for fiscal sustainability remains unsettled. We do not see a significant bettering of financial conditions before well into 2009 and it is still too early to dismiss the possibility of a new wave of financial distress. Accordingly, we still see support to the counter-cyclical currencies CHF, JPY and USD – especially in the short term. However, given the reduced systemic risk seen since our last forecast update, we have opted to pencil in less CHF and JPY strength, implying a higher USD/JPY and EUR/CHF forecast profile.
- **On the longer horizon – going well into 2009 – we anticipate financial conditions to improve gradually.** That is, despite global production likely to have slumped around 2-3%, governments likely to have presented new rescue packages, this time focused more on fiscal initiatives, additional private institutions probably de facto nationalised, and those countries most burdened by external deficits and financial distress likely to be under the wings of the IMF. We do not expect to see a sharp recovery in risk appetite but rather a slow and cautious normalisation leading to lower but still elevated risk premiums. Price formation will continue to be influenced by ill-functioning markets and likely also the beginning of increased regulation limiting the possibility of a repetition of the 2002-2007 years. We anticipate seeing the USD strengthening further, but the JPY and CHF losing steam.
- **Our most notable forecast change is for EUR/GBP.** We have revised our EUR/GBP forecast upwards across all horizons but have kept our bias for a stronger pound in the longer run. The Bank of England's recent massive rate cut of 1.5% and the subsequent readiness to cut rates to 'whatever level needed' have made us revise our base rate forecast downwards, see [BoE cuts 150bp – more to come](#). The fact that prospects for consumption, house prices and growth in general have turned even gloomier has convinced us that the pound will see no support in the near term. We believe however that the undervalued pound represents good value in the longer term and will benefit from a normalisation in risk sentiment, see [Is GBP still interesting after downbeat Inflation Report?](#)

## Exchange rate forecasts

	Spot	Forecast				Forecast vs forward outright, %			
		+1m	+3m	+6m	+12m	+1m	+3m	+6m	+12m
<b>Exchange rates vs EUR</b>									
USD	1.270	1.24	1.21	1.16	1.16	-2.2	-4.5	-8.4	-8.5
JPY	123.13	117	114	114	118	-5.1	-7.0	-6.5	-1.9
GBP	0.857	0.88	0.86	0.82	0.80	2.8	0.6	-4.1	-6.5
CHF	1.511	1.47	1.46	1.48	1.48	-2.5	-2.9	-1.2	-0.8
DKK	7.45	7.45	7.45	7.46	7.46	-0.1	-0.1	0.0	-0.2
NOK	8.81	8.70	8.50	8.40	8.20	-1.3	-4.0	-5.4	-8.1
SEK	10.02	10.10	9.80	9.70	9.50	0.7	-2.2	-3.2	-5.3
<b>Exchange rates vs USD</b>									
DXY	86.9	88.4	89.6	91.7	91.7	1.7	3.2	5.7	5.9
JPY	97.0	94	94	98	102	-3.0	-2.6	1.9	7.0
GBP	1.48	1.41	1.41	1.41	1.45	-4.9	-5.0	-4.5	-2.1
CHF	1.19	1.19	1.21	1.28	1.28	-0.3	1.7	7.8	8.3
DKK	5.87	6.01	6.16	6.43	6.43	2.2	4.6	9.2	9.2
NOK	6.94	7.02	7.02	7.24	7.07	0.9	0.6	3.3	0.6
SEK	7.90	8.15	8.10	8.36	8.19	3.0	2.4	5.7	3.6
CAD	1.22	1.26	1.28	1.28	1.26	3.3	5.0	5.0	3.5
AUD	0.66	0.64	0.62	0.61	0.61	-2.1	-4.9	-6.1	-5.5
NZD	0.56	0.55	0.53	0.51	0.51	-1.6	-4.6	-7.5	-6.1

Note: GBP, AUD and NZD are denominated in local currency rather than USD

## FX Research

John Hydeskov	G10	+45 45 12 84 97	johy@danskebank.dk
Kasper Kirkegaard	G10	+45 45 13 70 18	kaki@danskebank.dk
Stefan Mellin	SEK	+46 8 568 805 92	mell@danskebank.se
Sverre Holbek	Option strategies	+45 45 14 88 82	holb@danskebank.dk
Thomas Andersen	Hedging strategies	+45 45 12 84 96	tpa@danskebank.dk
Klaus Ikast	Technical analysis	+45 45 12 84 99	kik@danskebank.dk
Kim Cramer Larsson	Technical analysis	+45 45 12 85 01	kimn@danskebank.dk

*This report has been prepared by Danske Research, which is part of Danske Markets, a division of Danske Bank. Danske Bank is under supervision by the Danish Financial Supervisory Authority.*

*Danske Bank has established procedures to prevent conflicts of interest and to ensure the provision of high quality research based on research objectivity and independence. These procedures are documented in the Danske Bank Research Policy. Employees within the Danske Bank Research Departments have been instructed that any request that might impair the objectivity and independence of research shall be referred to Research Management and to the Compliance Officer. Danske Bank Research departments are organised independently from and do not report to other Danske Bank business areas. Research analysts are remunerated in part based on the over-all profitability of Danske Bank, which includes investment banking revenues, but do not receive bonuses or other remuneration linked to specific corporate finance or debt capital transactions.*

*Danske Bank research reports are prepared in accordance with the Danish Society of Investment Professionals' Ethical rules and the Recommendations of the Danish and Norwegian Securities Dealers Associations.*

### **Financial models and/or methodology used in this report**

*Calculations and presentations in this report are based on standard econometric tools and methodology. Documentation can be obtained from the above named authors upon request.*

### **Risk warning**

*Major risks connected with recommendations or opinions in this report, including a sensitivity analysis of relevant assumptions, are stated throughout the text.*

### **First date of publication**

*Please see the front page of this research report.*

### **Disclaimer**

*This publication has been prepared by Danske Markets for information purposes only. It is not an offer or solicitation of any offer to purchase or sell any financial instrument. Whilst reasonable care has been taken to ensure that its contents are not untrue or misleading, no representation is made as to its accuracy or completeness and no liability is accepted for any loss arising from reliance on it. Danske Bank, its affiliates or staff, may perform services for, solicit business from, hold long or short positions in, or otherwise be interested in the investments (including derivatives), of any issuer mentioned herein. The Equity and Corporate Bonds analysts are not permitted to invest in securities under cover-age in their research sector. This publication is not intended for retail customers in the UK or any per-son in the US. Danske Markets is a division of Danske Bank A/S. Danske Bank A/S is authorized by the Danish Financial Supervisory Authority and subject to limited regulation by the Financial Services Authority (UK). Details on the extent of our regulation by the Financial Services Authority are avail-able from us on request. Copyright (C) Danske Bank A/S. All rights reserved. This publication is pro-ected by copyright and may not be reproduced in whole or in part without permission.*