MONEX | USA

CURRENCY OUTLOOK

April 2024

IN BRIEF

What Happened

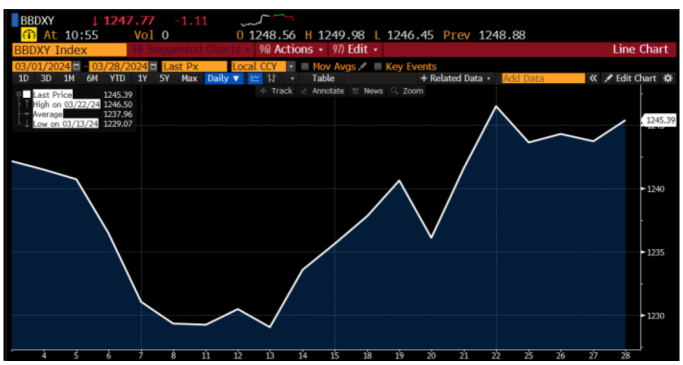
- The U.S. Dollar lost some momentum, but managed a 0.3% bump for March in what was a tale of two halves
- After initially reaching its strongest levels since mid-January, the Euro collapsed, losing 0.4% for the month
- Japanese Yen plummeted to record lows regardless of the Bank of Japan's first interest-rate hike in 17 years
- Although Banxico cut interest rates, the Mexican Peso climbed to its best point against USD since end of 2015
- The Swiss National Bank became the first among the G-10 to reduce borrowing costs joining other regions in jumping ahead of the Fed in loosening monetary policy

Monex USA's View

- Data-dependent Fed will need evidence of a weaker economy, lower prices, to hold "dot-plot" plans intact
- Record-highs for equity indices will be tested as the globe copes with conflict and infrastructure issues
- A new round of central bank policy divergence could keep Buck afloat after late-March gains
- FX-intervention from the Bank of Japan, if triggered, is likely to bring along more volatility to currencies
- China's attempts to reinforce the Yuan will have no impact unless the economy starts impressing and influencing others

IN FOCUS

BDXY: March Madness? Buck faced some swings, but it all culminated in March "flatness"



(Bloomberg Dollar Spot Index graph showing how the start point of the month almost matched its end)

The U.S. Dollar is up 1.9% for Q1 following the end of speculation of a more "dovish" Fed policy

- December talk made it seem like markets were convinced the Federal Reserve was ready to begin an era of lowered interest rates
- As explained in previous write-ups, without economic issues, there is no argument for cuts
- Chairman Jerome Powell and other officials will need to weigh the consequences of not acting at all
- The narrative has changed from expecting a "soft landing" to wondering when we will land. Turbulence ahead

THE VIEW — No clarity on cutting rates keeps U.S. Dollar buoyant

Markets did not predict the gap between global and American progress

Things were supposed to slow down. While true that the Federal Reserve's tightening cycle achieved disinflation and the desired cooldown in prices, the American economy is thriving while others are figuring a way out of contractions across many variables. Currently, global central banks have decided to lend a helping hand in fueling growth by ditching a policy of interest-rate increases to combat inflation, deemed mostly effective, but an obstacle to fomenting business activity.

While others decrease their toll on the economy in order to have a more accommodative financial environment, the Federal Reserve is taking its time in assessing just how much the American economy requires any type of reprieve as the year goes on. At the time of writing, odds of a rate cut at the Fed's June meeting changed from around 66.0%, the average throughout March, to just 55.0% when the second quarter arrived.

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March started with a lot of anticipation over guidance from central banks as meetings were considered pivotal to providing some direction. While no one thought the Fed would make a case for a cut sooner than June, investors and traders wanted reassurance that officials would maintain their plans to cut interest rates by at least 75 basis in 2024. The Dot-Plot was left unchanged, much to the immediate satisfaction of markets.

Additionally, the press conference held by Fed Chairman Jerome Powell also informed markets of plans to stop "quantitative tightening," the shedding of assets held in the Fed's balance sheet. Though there was no indication of a return to buying sovereign bonds, the announcement established a will by Fed officials to prevent further contractionary monetary policy impact.

What was peculiar about the timing of the Fed's gathering is that it occurred in between two dramatic central-bank decisions: the Bank of Japan's historic hike to get interest rates above negative territory the day prior and the Swiss National Bank's first reduction among the G-10 economies the day after. As seen in the Bloomberg Dollar Spot Index graph above, a rally developed in the Buck's favor for the last two weeks of March, marking the end of all central banks working in tandem.

Days before the BOJ's momentous decision, the leading automobile firm Toyota boosted the Yen's value with a report that it would agree to the highest wage increment in 25 years. Furthermore, inflation looking to have advanced convinced most traders that the central bank would be pushing the case for starting a round of borrowing cost increases.

As seen now, the Yen failed to appreciate following the "dovish hike," with BOJ members frustrating those hoping for a schedule of more raises. While satisfied with being able to get away from rates below zero, the committee thought it would be appropriate to wait-and-see how indicators progress and did not provide any possibility that they will continue on this "hawkish" path. BOJ also voted to keep quantitative easing as a tool. We are now potentially going to witness FX intervention as JPY levels reach fresh lows not seen since 1990.

Over in Switzerland, the SNB determined that the fight against inflation is over while the need for promoting exports is seen as crucial. By lowering its benchmark rate, officials explained they want to see more competitiveness for Swiss products while also fostering depreciation of the Swiss Franc. Consequently, the currency is now trading near its weakest value since November.

Down in neighboring Mexico, the effects of "Near-shoring" have made for a story of economic steadiness and wage growth. Manufacturing as well as Industrial Production remain expanding and oil prices are rising from the supply woes caused by violence away from our hemisphere. Since there is not a lot of economic pain, the interest-rate cut by Banxico, the central bank, came and went without inflicting losses to the Mexican Peso. The "hawkish cut" ultimately did not come accompanied with clear plans for more cuts ahead.

The mix of policy sentiment has made the Dollar a more attractive asset, backed not only by high interest rates of return, but also an economy that does not seem to be heading downward. Non-Farm Payrolls advancing more than expected and Consumer Price Index stubbornly hanging high in comparison to Q4 are making it likely the Fed will make two moves instead of three reductions as it has currently on its radar.

Only one other major central bank meeting risk event will occur this month as The Bank of Canada will meet on April 10th. With less than a 10.0% chance of a cut happening, one would be a shock to markets and surely hurt "Loonie" in a significant way. Other monetary talk will be guided by economic data as well as well as the dangers lurking worldwide.

China started off March with great news as exports figures topped forecasts with resurgence in global demand. The global recovery narrative, however, has not been enough to topple the Buck as economies try to balance between stimulus and keeping prices from going back to pandemic levels. Q1 was excellent for equities, but advancement in tech as well as in the defense industry will face challenges. After terrorism in Moscow and escalation in the Middle East, the Buck could enjoy a prolonged period of good fortunes unless risk-appetite somehow deters further improvement.

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