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Weekly Report

# Weekly FX Market Update


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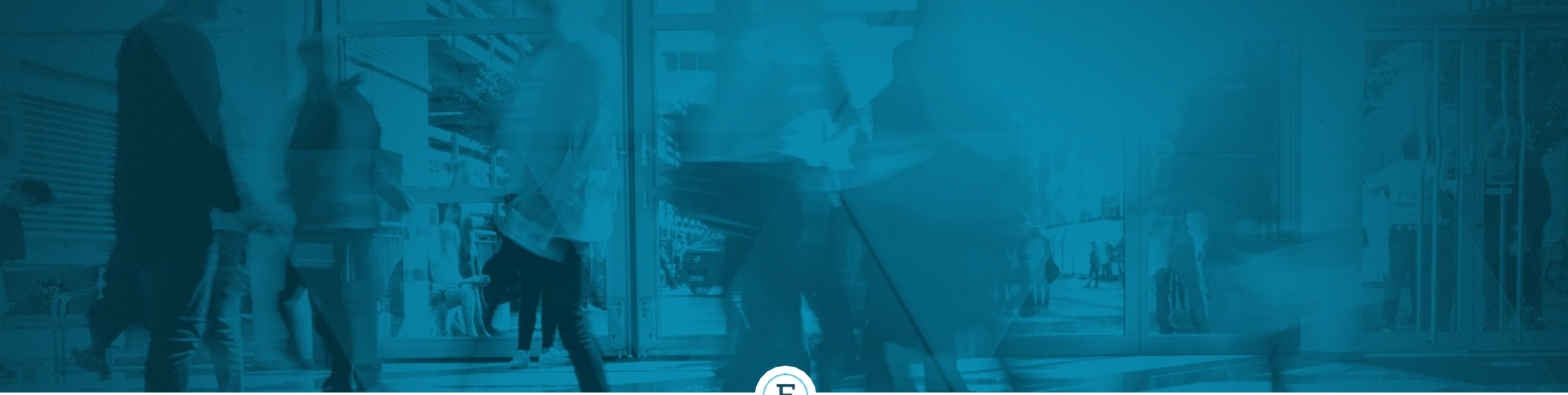


# European currencies sink, dollar soars as the news from Ukraine get grimmer

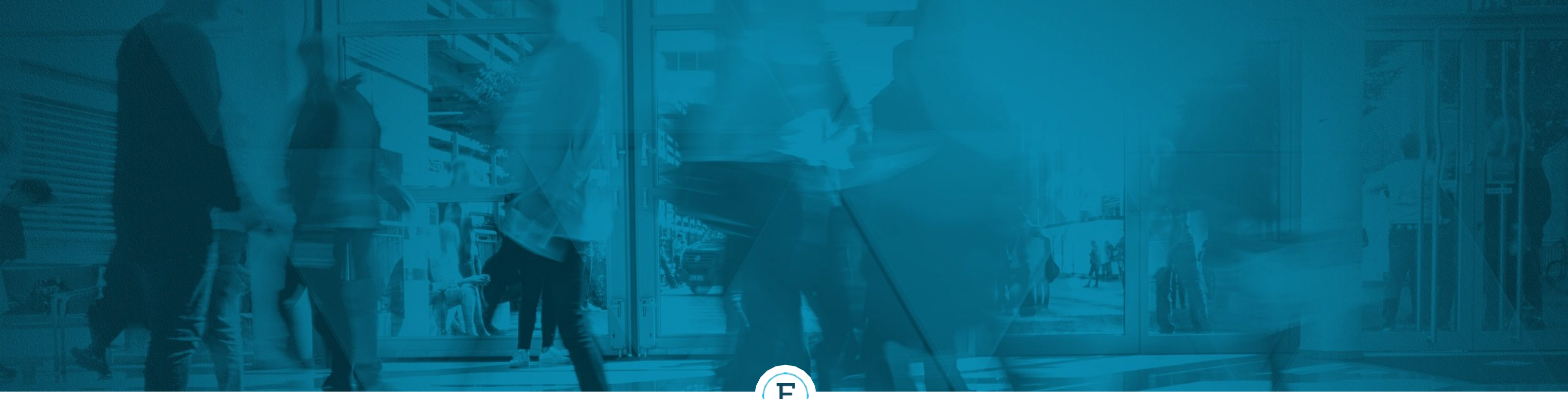
The worsening humanitarian and security crisis brought about by the Russian invasion of Ukraine continues to buffet financial markets.

There are volatile moves and a flight to safe havens everywhere, but European assets are being punished with particular severity, due to both geography and the continent's vulnerability to energy supply disruptions. The euro and the Swedish kroner were the worst performing currencies in G10, down approximately 3% and nearly 5% respectively. At the top of the rankings, we are not seeing the traditional safe havens, like the Japanese yen and the Swiss franc. Instead, soaring commodity prices worldwide have rewarded the currencies of commodity-exporting countries far from the war, such as the Australian and New Zealand dollars, the Colombian peso, and the Brazilian real, in a stark departure from previous bouts of risk aversion. On the other extreme, aside from the ruble, we are unsurprisingly seeing sharp moves downward of most Eastern European currencies, led by the Hungarian forint and the Polish zloty.

Predicting the outcome for this week's ECB meeting Thursday is more difficult than ever, as the central bank is faced with a massive stagflationary risk on top of preexisting burgeoning price pressures. US February inflation data is also released on Thursday, which should make for a very volatile trading day in the EUR/USD currency pair. Obviously, the main focus for financial markets in general will remain the headlines out of the Russian invasion, with particular attention being paid to any sign of a ceasefire that could send risk assets temporarily higher.

## CZK

The Czech koruna was one of the worst-performing currencies last week, selling off by 3.4% against the euro. At one point, the currency fell to its weakest level since April but was still outperforming regional peers, Polish zloty and Hungarian forint. Part of it could be due to differing fundamentals, with Czechia having arguably the best among peers making it a regional 'safe haven'.

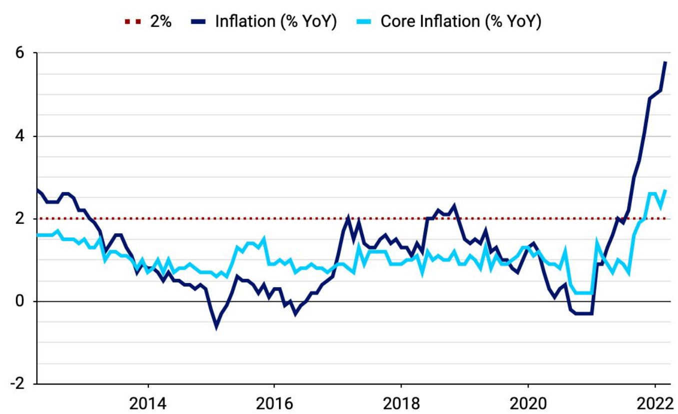


Importantly, as the National Bank of Poland, the Czech National Bank turned words into action and confirmed on Friday it has intervened in the FX market. We think such interventions are likely to continue if the pressure on the exchange rate remains and it's particularly hard to say if it's going to be the case considering the fast-moving pace and uncertainty over the Russia-Ukraine war. As a sidenote, Thursday will see a release of Czechia's inflation data which may show price growth finally crossing the double-digit barrier.

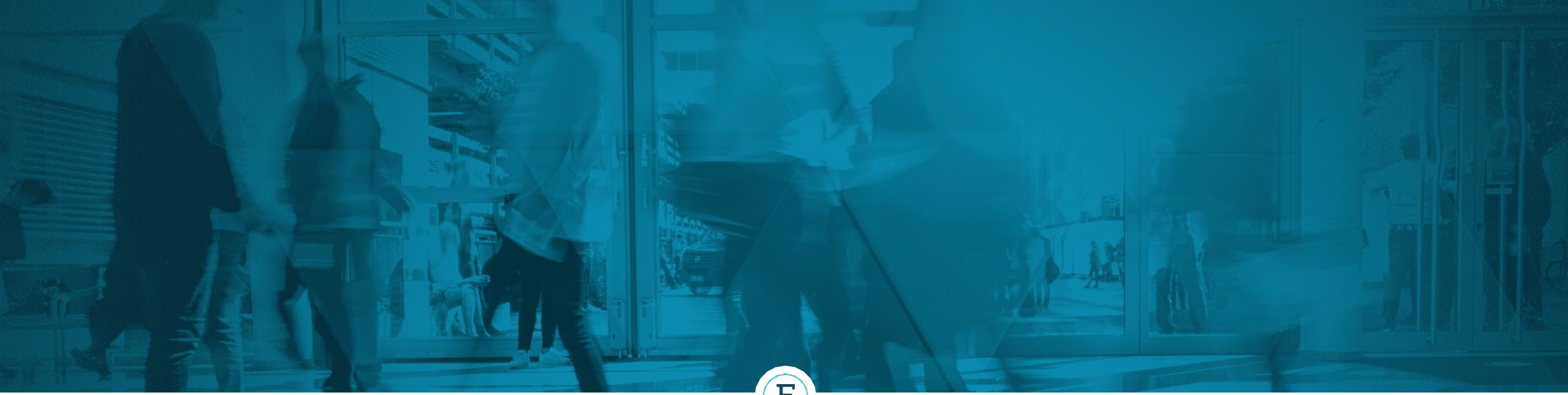
## EUR

The inflation report for February was of course completely overshadowed by the terrible news from Ukraine, but it still deserves mention. It was yet another upward surprise, showing strength both in the headline number and the core one, confirming that price pressures were already becoming widespread even before the stagflationary shock of the war. The ECB reaction is expected to be dovish, delaying the removal of accommodation that we had previously expected this week. However, any such delay will have to be more than compensated with additional tightening later on, if the ECB is serious about keeping inflation expectations in the Eurozone well anchored. For now, it does seem the path of least resistance for the common currency is down.

Figure 1: Inflation in the Eurozone (2012 - 2022)




Source: Bloomberg Date: 07/03/2022



## USD

The payroll report out of the US also failed to have the impact it would have had in normal conditions, but nevertheless, it confirmed the booming state of the US job market. Strong job creation came hand in hand with surprisingly mild wage pressures, though we would hold judgement till next month given the high volatility that these numbers have presented on a month-on-month basis. Chair Powell's testimony to Congress was relatively sanguine about the war impact on the US economy, which is self-sufficient in energy terms and relatively isolated from the conflict. Powell made it clear that the rate-hiking process has not been derailed and the first 25 bp are coming in March. The contrast with the ECB's apparent dovishness is stark and explains the tumble we saw in the EUR/USD exchange rate.

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