GLOBAL FX TRADER

Resolution Resolve

Our thoughts on USD, HUF, AUD & NZD, CHF, COP, and CAD

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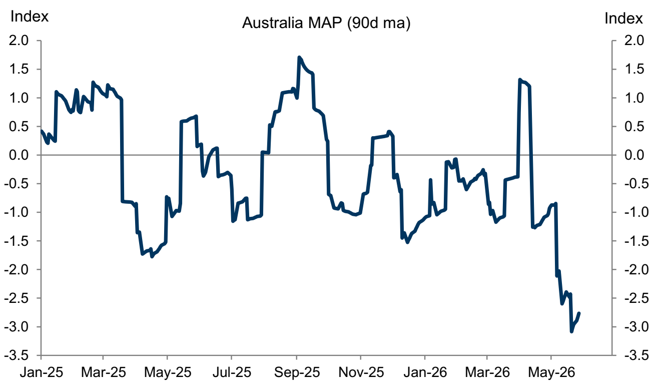
- **USD: Not just a case of open and shut.** The Dollar weakened over the course of the week on familiar drivers, including hopes of a US-Iran deal and steady CNY appreciation. Relative terms of trade continue to be a strong determinant of FX returns, and the FX market remains highly correlated and exceptionally stable. Leaning on these tendencies, we have highlighted a slate of crosses that we think are best to position for resolution or escalation, especially where it aligns with other fundamentals: those include ZAR, HUF, KRW and CLP in EM alongside SEK, NZD and GBP in the G10 space. That said, we see a number of hurdles for the broad Dollar to "snap back" to the overwhelmingly negative narrative that prevailed in January and February. We believe there are two important shifts affecting broad terms of trade simultaneously—an AI boom and an energy supply bust—which are both net positive for the Dollar and help explain why it is 1-1.5% stronger (depending on the index) on net since the beginning of March. The AI boom has helped restore foreign investor demand for Dollar assets that we think was a critical component behind last year's currency depreciation. Relatedly, it helps explain the divergent growth picture through easier financial conditions and stronger investment. Better growth outcomes and firmer inflation have pushed front-end rate differentials in the Dollar's favor in recent weeks. And we think that the growth impact of the energy shock is likely to impact FX returns for some time after the Strait begins to open; after more than three months with severely restricted flows, product shortages and elevated prices will likely continue to drive more divergent growth outcomes for some time. While we continue to see room for the Dollar to depreciate on more positive headlines, we think the overall picture should still lead to more divided Dollar performance ahead.
- **HUF: Unblocked**. There were two key developments in Hungary this week: the MNB meeting at which a June rate cut was signaled and the announcement that EUR16.4bn in EU funds had been unblocked. On the former, the central bank's press release noted a significant improvement in the inflation outlook, and Governor Varga stated that the decision to remain on hold was not unanimous. While these were dovish developments, the FX-specific commentary did not include pushback against HUF appreciation following the cut in the FX swap implied rate earlier this month. Instead, the positive inflation developments and

the ability to cut are framed in the context of a stronger HUF, leaving the currency as a key binding constraint to delivering cuts. In this context, the causation in the FX-rates relationship is driven by FX, and the correlation between FX and rate differentials is negative, which we have also found in our analysis. Hence, we expect an eventual MNB cutting cycle to have a limited HUF impact, in the context of the sustained decline in country risk. And, more broadly, we continue to think that a stronger Forint is key in lowering inflation to meet the Maastricht inflation criterion, and that depreciation risks should also be mitigated by the fulfillment of these criteria. Turning to the EU funds, the unblocked funds include EUR10bn from the Recovery and Resilience Facility funds (RRF), which had been in focus given the tighter deadline for disbursement by year-end, but also a portion of the Cohesion funds. We see this as a marginal positive relative to expectations that were more focused on a deal covering RRF funds only. These funds are worth over 7% of GDP and so represent a significant tailwind for external balances and growth. These funds, as we have shown before, can more than offset the impact of higher energy prices on the current account. Overall, we continue to see the asymmetry towards further HUF appreciation from here and maintain our short EUR/HUF trade recommendation with an initial target of 350.

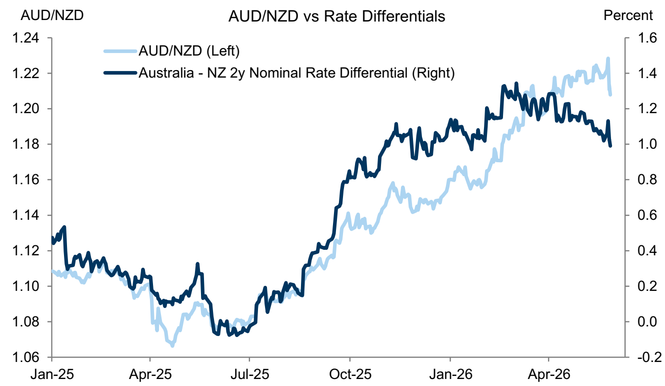
- **AUD & NZD: Unwinding road.** A few weeks ago we flagged scope for an unwind in AUD/NZD should the relative policy backdrop shift, the domestic data disappoint expectations, or the terms of trade backdrop become less supportive. The incoming news has been consistent with the first two of these three conditions and there has already been some reversal. The May RBNZ meeting and Australia inflation data this week added to the recent run of less constructive domestic news for AUD relative to NZD, driving AUD/NZD sharply lower. The RBNZ shifted in a decisively hawkish direction with three of the six committee members preferring a hike and all Committee members agreeing that increasing the OCR at upcoming meetings would likely be necessary. While our economists pulled forward their expectation for RBNZ hikes and now expect two hikes year in July and September (prior +25bp hikes in Dec26/Feb27/May27), they recently shifted their call for the RBA in the opposite direction, pushing back their call for a final 25bp hike from June to August. On the data front, Australia data has broadly disappointed (Exhibit 1). The softer April CPI report followed a soft Q1 inflation report. The April employment report was weaker than expected and consumer sentiment has deteriorated. That said, with energy prices still elevated the terms of trade backdrop has remained AUD supportive, and we think these opposing impulses—terms of trade on the one hand and domestic consideration on the other— have contributed to the stall in AUD/NZD's strong run over the past month. But with Australia–New Zealand rate differentials showing signs of having peaked (Exhibit 2), more hikes priced for the RBNZ this year than any other G10 central bank, stretched positioning, and NZD well positioned to benefit from "de-escalation", we think the impetus for a more meaningful correc cross is building. Clarity on a normalization in global energy flows w pressure in that direction, but at this juncture we think risk-reward i AUD/NZD is appealing from a relative data and policy perspective.

Exhibit 1: Australia data has broadly disappointed



Source: Goldman Sachs Global Investment Research

Exhibit 2: Australia–New Zealand rate differentials are showing signs of having peaked

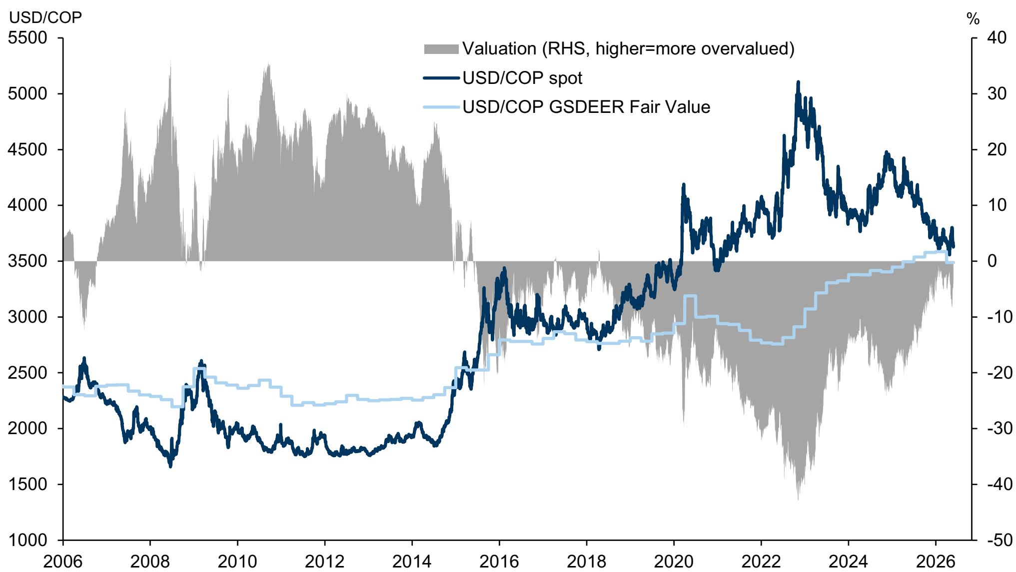


Source: Goldman Sachs FICC and Equities, Goldman Sachs Global Investment Research

- **CHF: Stairway to haven.** Over the past two months we have argued that the repercussions of the energy shock should apply steady downward pressure on EUR/CHF. The Franc's safe-haven properties are particularly relevant in geopolitical, inflationary, and downside European growth shocks, and the ongoing conflict has elements of all three. The shift in the SNB's intervention bias meanwhile has been key in capping any haven-based gains for the Franc so far, but we think a reacceleration in domestic Swiss inflation should be enough to shift that bias back to a neutral setting and uncover those haven benefits. This is the main angle through which we will be watching the SNB's upcoming meeting on June 18, with headline CPI already running above the Bank's most recent Q2 projection, and consensus expecting a further increase in next week's May report. This path to looser SNB FX management is central to our expectation for further CHF outperformance in the months ahead, but several important risks remain. First and foremost, EUR/CHF carry-to-vol is close to post-2015 highs, weakening risk-reward in outright downside positions. Second, we find evidence that gold's shifting correlation to risk is spilling over to the Franc and is likely to continue to be a source of idiosyncratic vol for the Franc via its terms of trade linkages. And third, we think a re-rating of Swiss growth on a passing of the country's June 14 population cap referendum would pose modest downside risks for the currency, though option market pricing for the event is understandably light.
- **COP: Going in strong.** The first round of Colombia's presidential election will take place this weekend on May 31. In the run-up, after a large energy price driven rally previously, COP moves have been primarily driven by election-related factors including the BanRep's consensus-building on-hold decision and the last poll before the election suggesting that right-leaning candidate Abelardo de la Espriella would win in the second round on June 21. Overall, left-leaning Ivan Cepeda appears well-positioned to advance to the runoff, with the main uncertainty for this weekend being which of the right-leaning candidates will also advance. In that context, COP is likely to take direction from the share of votes on the right vs. the left in gauging the likely winner of the June runoff. The signal from polls has become noisier due to changing electoral laws, which leaves greater scope for surprises in either round and thus greater FX volatility. When considering potential COP moves under different

election outcomes, we think it is important to note that the Peso's undervaluation signal has eroded over time and USD/COP now screens close to fair value (around 3500) on our GSDEER model (Exhibit 3). This contrasts with a large undervaluation signal ahead of the 2022 presidential elections. To be sure, the COP appreciation trend can be explained by various factors including (i) declining external balance vulnerabilities (especially relative to 2021-2022), (ii) the BanRep's decisive hiking cycle, which has left local rates bearing a greater share of the inflation and fiscal risks, and (iii) the broader risk and carry-supportive backdrop. Nevertheless, it means that this starting point of COP strength points to asymmetric risks into the election, with scope for a larger move in the event of a less market-friendly outcome.

Exhibit 3: COP screens close to fair value currently, whereas it was deeply undervalued in the run-up to the 2022 election



Source: Goldman Sachs FICC and Equities, Goldman Sachs Global Investment Research

- **CAD: USD/CAD and The USMCA Review.** USMCA negotiations have mostly flown under the radar, but the July 1 deadline is drawing closer, and we recently noted that increasing trade policy uncertainty could be a more meaningful headwind to CAD in the months ahead. While USMCA would remain in effect if negotiations extend past the deadline, we think markets will continue to grapple with a USMCA exit as a credible risk given the process the last time around. We expect ongoing talks will likely proceed bilaterally with US-Canada talks proving more difficult, mirroring the original USMCA process and the 2025 fentanyl-related tariffs. We find that negotiations with Canada have generally been more contentious than those with Mexico (Exhibit 4) and that USD/CAD tends to rise when trade tensions escalate. However, we find markets price limited trade-specific premium beyond standard cyclical drivers in our GSBEER models. We attribute this limited premium to the BoC's incorporation of trade policy uncertainty—and consequent adverse impacts on activity— into its reaction function, both in 2018 and more recently such that trade shocks more durably impact the USD/CAD via rate differentials, rather than as a sustained premium over traditional cyclical drivers. We also find that increasing trade tensions affected CAD in low-delta options, with less impact on realized or implied ATM volatility consistent with stronger demandor protection against policy-driven tail risks (Exhibit 5). Overall, we see three key market implications. First, USMCA negotiations are likely to be more strained with Canada and therefore a more important driveror CAD than MXN. Second, elevated trade uncertainty should weigh on CAD perormance by potentially deterring investment and keeping the Bank of Canada on the more dovish end of the central bank spectrum. Third, while trade policy uncertainty has historically had less impact on implied ATM or realized volatility, we see value in low-delta USD/CAD options as the deadline approaches.

Exhibit 4: Negotiations with Canada have generally been more contentious than those with Mexico

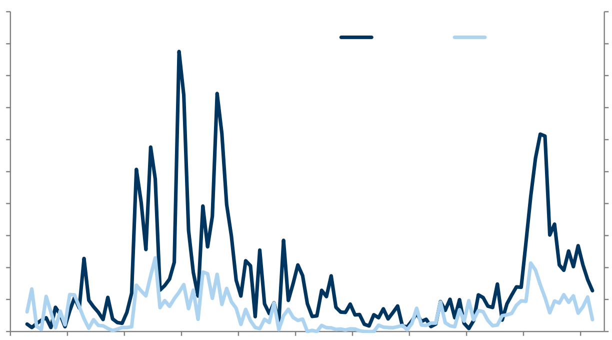


Exhibit 5: Increasing trade tensions affected CAD in low-delta options

Global FX Forecasts

	Current Spot	3-Month Horizon		6-Month Horizon		12-Month Horizon	
		Forward	Forecast	Forward	Forecast	Forward	Forecast
G10							
EUR/$	1.17	1.17	1.14	1.17	1.18	1.18	1.20
£/$	1.34	1.34	1.33	1.34	1.34	1.34	1.33
AUD/$	0.72	0.71	0.72	0.71	0.73	0.71	0.74
NZD/$	0.59	0.60	0.60	0.60	0.61	0.60	0.62
$/CAD	1.38	1.37	1.36	1.37	1.34	1.36	1.32
$/CHF	0.78	0.78	0.78	0.77	0.76	0.75	0.76
$/NOK	9.25	9.27	9.30	9.29	8.98	9.32	8.75
$/SEK	9.25	9.21	9.65	9.17	9.15	9.08	8.75
$/JPY	159	158	160	157	158	155	155
EMEA							
$/CZK	20.8	20.8	21.5	20.8	20.7	20.8	20.2
$/HUF	304	305	311	306	297	307	288
$/PLN	3.63	3.63	3.77	3.63	3.60	3.64	3.54
$/RON	4.50	4.52	4.52	4.54	4.39	4.58	4.38
$/RUB	73.07	73.07	80.0	75.13	85.0	79.31	90.0
$/UAH	44.3	45.4	44.0	46.8	46.0	49.4	48.0
$/TRY	45.86	50.14	48.0	54.85	50.0	64.51	54.0
$/ILS	2.82	2.81	3.00	2.81	3.05	2.79	3.10
$/ZAR	16.24	16.36	16.50	16.48	16.00	16.74	15.75
$/NGN	1376	1412	1325	1451	1300	1526	1250
Americas							
$/ARS	1410	1489	1500	1579	1600	1780	1800
$/BRL	5.04	5.15	4.90	5.26	5.00	5.47	5.00
$/MXN	17.32	17.45	17.75	17.58	18.00	17.86	18.00
$/CLP	891	890	920	890	900	891	860
$/PEN	3.41	3.43	3.40	3.44	3.35	3.47	3.30
$/COP	3640	3723	3600	3809	3700	3987	3750
Asia							
$/CNY	6.78	6.72	6.80	6.67	6.70	6.59	6.50
$/HKD	7.83	7.81	7.80	7.79	7.80	7.76	7.80
$/INR	95.70	96.96	97.00	97.94	96.00	99.66	96.00
$/KRW	1494	1490	1460	1486	1440	1479	1420
$/MYR	3.98	3.97	3.90	3.96	3.80	3.94	3.70
$/SGD	1.28	1.27	1.28	1.26	1.25	1.24	1.24
$/TWD	31.4	31.5	31.5	31.6	31.0	31.6	30.5
$/THB	32.70	32.51	34.00	32.39	33.50	32.06	33.00
$/IDR	17789	17947	17000	18056	17100	18266	17200
$/PHP	61.63	61.78	62.00	62.03	61.00	62.49	61.00
Euro Crosses							
EUR/GBP	0.87	0.87	0.86	0.87	0.88	0.88	0.90
EUR/CHF	0.91	0.91	0.89	0.90	0.90	0.89	0.91
EUR/NOK	10.78	10.84	10.60	10.90	10.60	11.01	10.50
EUR/SEK	10.78	10.77	11.00	10.76	10.80	10.73	10.50
EUR/CZK	24.28	24.35	24.50	24.41	24.40	24.53	24.20
EUR/HUF	355	357	355	360	350	363	345
EUR/PLN	4.23	4.24	4.30	4.26	4.25	4.30	4.25
EUR/RON	5.25	5.29	5.15	5.33	5.18	5.41	5.25
EUR/RUB	85.1	85.5	91.2	88.2	100.3	93.7	108.0

Note: Spot values are as of Thursday's close.

See dynamic table here (or click image above): https://publishing.gs.com/content/themes/fx-forecasts.html

Source: Goldman Sachs Global Investment Research

Return Forecasts & Valuations

	Current Spot	Forecast: 12-Month Return (%)				GSDEER			GSFEER			Average Estimate	PPP*
							Misalignment			Misalignment			
		Spot	Carry	Total	NEER	Estimate	Bilateral	Trade-Weighted	Estimate	Bilateral	Trade-Weighted		
G10													
EUR/$	1.17	3.0	-1.4	1.5	2.3	1.20	-3%	8%	1.18	-1%	1%	1.19	1.52
GBP/$	1.34	-0.8	0.2	-0.6	-2.5	1.22	10%	23%	1.30	4%	6%	1.25	1.50
AUD/$	0.72	3.3	0.8	4.1	0.2	0.81	-11%	11%	0.72	-1%	7%	0.78	0.70
NZD/$	0.59	4.5	-0.7	3.7	1.5	0.68	-12%	4%	0.62	-4%	1%	0.65	0.67
$/CAD	1.38	4.4	-1.4	3.0	3.6	1.21	-12%	-7%	1.34	-2%	0%	1.27	1.17
$/CHF	0.78	3.4	-3.9	-0.6	1.6	0.85	8%	16%	0.800	2%	4%	0.83	0.92
$/NOK	9.25	5.8	0.7	6.5	3.5	6.62	-29%	-22%	8.92	-4%	-3%	7.54	8.87
$/SEK	9.25	5.7	-1.8	3.8	3.1	7.44	-20%	-11%	8.99	-3%	-2%	8.06	8.26
$/JPY	159.2	2.7	-2.9	-0.2	0.5	93	-41%	-32%	140	-12%	-6%	112	93
EMEA													
$/CZK	20.84	3.3	-0.4	2.9	1.1	25.3	21%	29%	20.8	0%	1%	23.5	15.8
$/HUF	304	5.8	1.0	6.9	3.8	329	8%	15%	329	8%	8%	329	261
$/PLN	3.63	2.4	0.4	2.8	0.9	3.92	8%	16%	3.7	2%	3%	3.84	2.43
$/RON	4.50	2.9	1.7	4.7	--	--	--	--	5.25	17%	16%	--	--
$/RUB	73.1	-18.8	8.5	-11.9	-20.5	76.52	5%	22%	75.94	4%	4%	76.29	40.15
$/UAH	44.26	-7.8	11.7	3.9	--	--	--	--	--	--	--	--	--
$/TRY	45.86	-15.1	40.7	19.5	-15.3	32.42	-29%	-27%	45.51	-1%	2%	37.66	29.15
$/ILS	2.82	-9.1	-0.9	-9.9	-9.9	3.55	26%	40%	3.03	8%	6%	3.34	4.70
$/ZAR	16.2	3.1	3.1	6.3	0.7	13.01	-20%	-11%	15.4	-5%	-3%	13.98	18.40
$/NGN	1376	10.1	10.9	21.0	--	--	--	--	--	--	--	--	--
Americas													
$/ARS	1409.6	-21.7	26.3	4.6	-23.1	--	--	--	--	--	--	--	--
$/BRL	5.04	0.8	8.5	9.3	0.1	4.22	-16%	-3%	5.18	3%	9%	4.61	5.28
$/MXN	17.32	-3.8	3.2	-0.8	-5.0	19.51	13%	21%	17.23	-1%	2%	18.60	20.29
$/CLP	891	3.6	0.0	3.6	2.2	660	-26%	-13%	830	-7%	-2%	728	787
$/PEN	3.41	3.5	1.7	5.2	2.3	2.79	-18%	-7%	2.98	-13%	-11%	2.87	4.24
$/COP	3640	-2.9	9.5	6.3	-3.8	3487	-4%	9%	3823	5%	7%	3621	3298
Asia													
$/CNY	6.78	4.2	-2.8	1.4	2.7	5.02	-26%	-17%	5.89	-13%	-10%	5.37	5.82
$/HKD	7.83	0.4	-1.0	-0.5	-2.8	6.95	-11%	10%	6.67	-15%	-7%	6.84	5.85
$/INR	95.70	-0.3	4.1	3.8	-1.9	85.79	-10%	-2%	86.97	-9%	-6%	86.26	57.50
$/KRW	1494	5.2	-1.0	4.2	3.2	1166	-22%	-6%	1161	-22%	-17%	1164	929
$/MYR	3.98	7.5	-1.0	6.5	4.6	3.27	-18%	-1%	4.02	1%	8%	3.57	1.95
$/SGD	1.276	2.9	-2.6	0.2	-0.2	1.36	7%	26%	1.30	2%	8%	1.34	0.57
$/TWD	31.42	3.0	0.7	3.7	0.0	24.9	-21%	-2%	26.1	-17%	-12%	25.4	13.2
$/THB	32.70	-0.9	-1.9	-2.8	-3.7	30.60	-6%	15%	33.83	3%	10%	31.89	18.82
$/IDR	17789	3.4	2.7	6.2	0.6	14101	-21%	-5%	15947	-10%	-3%	14840	10885
$/PHP	61.63	1.0	1.4	2.4	-1.8	58.87	-4%	17%	63.29	3%	11%	60.64	52.56
Euro Crosses													
EUR/GBP	0.87	-3.7	1.6	-2.1	-2.5	0.99	14%	23%	0.91	5%	6%	0.95	1.01
EUR/CHF	0.91	0.4	-2.4	-2.1	1.6	1.01	11%	16%	0.94	3%	4%	0.98	1.40
EUR/NOK	10.78	2.7	2.1	4.8	3.5	7.93	-26%	-22%	10.49	-3%	-3%	8.96	13.46
EUR/SEK	10.78	2.7	-0.4	2.2	3.1	8.92	-17%	-11%	10.58	-2%	-2%	9.59	12.54
EUR/CZK	24.28	0.3	1.0	1.3	1.1	30.33	25%	29%	24.47	1%	1%	27.99	24.02
EUR/HUF	355	2.8	2.4	5.1	3.8	394	11%	15%	387	9%	8%	391	396
EUR/PLN	4.23	-0.5	1.8	1.3	0.9	4.70	11%	16%	4.4	3%	3%	4.57	3.68
EUR/RON	5.25	-0.1	3.1	3.1	--	--	--	--	6.18	18%	16%	--	--
EUR/RUB	85.1	-21.2	9.9	-11.2	-20.5	91.8	8%	22%	89.4	5%	4%	90.8	--
Addendum													
USD	--	-1.1	-2.0	-2.9	-2.2	--	--	15%	--	--	4%	--	--

Note: USD returns average of all other currencies (except ARS, NGN and UAH) with opposite sign; *EM estimates adjusted for per capita income. Spot values as of Thursday.

See dynamic table here (or click image above): https://publishing.gs.com/content/themes/table.html?criteriaKey=1k2HGqqS2h

Source: Goldman Sachs Global Investment Research

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Reg AC

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