



FX Forecasts

April 2025

MONEX

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INTRODUCTION

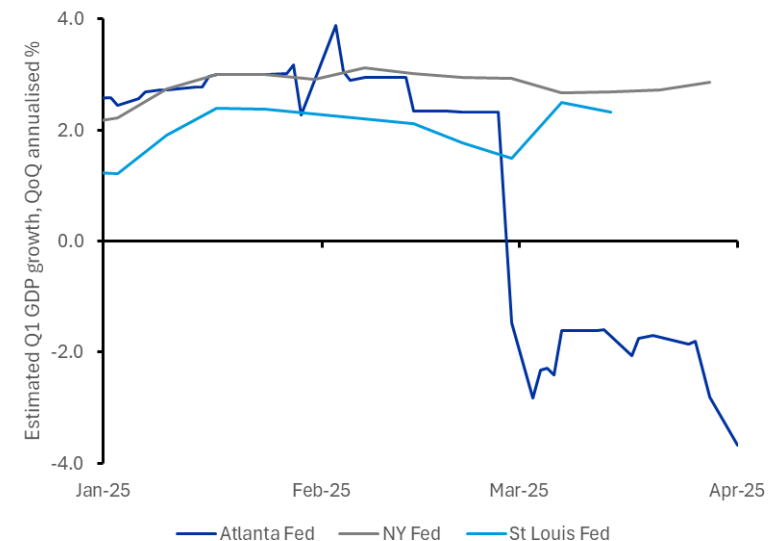
The dollar slipped notably lower through March, as market attention switched away from the greenback positive impact of rising tariffs to the growth negative impact of repeated tariff threats, and the broader impact of the new US administration's policies. Our view, however, remains that US growth fears are overstated. Whilst American economic exceptionalism may be dimming, it is not done yet, as evidenced by the lack of slowdown visible in hard data readings over the past month. Markets, meanwhile, continue to underestimate the non-growth impact of tariffs ahead of "Liberation Day" on April 2nd, when Trump is set to announce reciprocal import levies. The economic wisdom of such measures aside, our view remains that rising tariff barriers should favour the greenback on a relative basis. All told, we think conditions favour an acceleration in the dollar rebound that began mid-March as traders find growth fears assuaged and the impact of rising tariff barriers return to front of mind.

US growth fears remain overstated, but eurozone risks are underrated

Arguably the main story of markets over the past month stemmed from the rapid emergence of US recession fears, prompted by a sharp drop off in sentiment readings and in some forward-looking growth indicators. While this dynamic could have been expected to weigh on the dollar alone, it has been further exacerbated by resurgent European optimism, prompted by the announcement of several packages that promised to boost government spending with a specific focus on infrastructure and defence. This saw an erosion of the US exceptionalism story that has proven so dollar-supportive from both sides, contrasting weaker US activity expectations against the emergence of a potential growth competitor. It is also a story that we see as overblown, as noted across our recent commentary.

Looking first at the US, while it is true that sentiment readings have fallen sharply, these are strongly correlated with political viewpoint. Accounting for this, the recent fall in aggregate expectations appears to be driven primarily by Democrats, warning against the reliability of such measures as forward-looking growth indicators. Similarly, some nowcasts have registered large declines in recent weeks, with the Atlanta Fed GDPNow model most notable. This went from predicting 2.3% QoQ annualised Q1 growth in late February, to -2.8% in early March, a level around which the tracker continues to hover. This, however, has been largely driven by unusual flows of gold. Adjusting for this suggests that the economy is flatlining – admittedly not great, but likely not recessionary either.

While the closely watched Atlanta Fed GDPNow model suggests that the economy will contract sharply in Q1, other trackers suggest a much more benign outlook



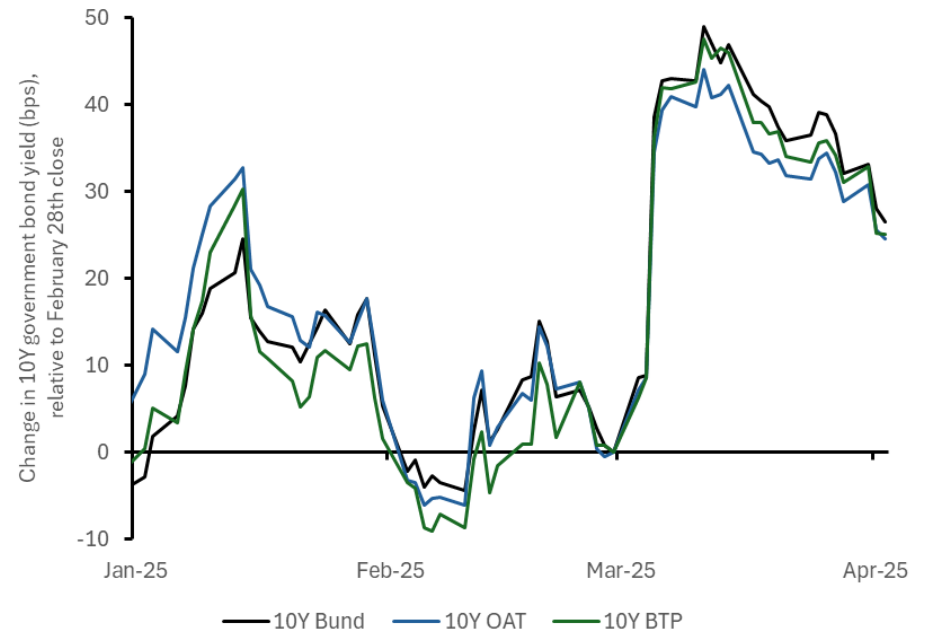
This also contrasts sharply with the New York Fed Staff Nowcast, which sees Q1 growth at 2.86% QoQ annualised as of writing, and a different nowcast from the St Louis Fed which sees GDP growth at 2.13%. This view is further bolstered by the hard data, which is yet to turn. Labour market readings remain solid, with 151k payroll gains in February, and an unemployment rate of 4.1%. Moreover, 4.0% YoY wage growth combined with core inflation of 3.1% points to inflation pressures much too hot for comfort at the Fed. And that is all before tariff impacts begin to push up prices, as is widely expected.

“So, while markets have turned increasingly bearish on US growth and dovish on the Fed, we continue to project no cuts in 2025, while recession risks look overblown in our eyes.”

Moreover, even as markets have soured on US growth, a pickup in expectations for the eurozone looks over-optimistic. In terms of the measures announced, headlines indicated up to 800bn in additional fiscal support across the EU primarily to fund re-armament, with 650bn euros from triggering national escape clauses in the Stability and Growth Pact, plus a further 150bn euros funded by collective borrowing. In addition, Chancellor-in-waiting Merz proposed and then passed a reform Germany’s debt break last month, exempting defence spending above 1% of GDP, whilst also establishing a 500bn euro fund for infrastructure investment. For context, the fund that accompanied Olaf Scholz’s much-feted Zeitenwende announcement totalled just 100bn euros.

Taking the debate around NGEU funds as a baseline, however, we suspect that initial optimism is likely to give way to disappointment in both implementation and effectiveness. Already, cracks are emerging around collective EU spending, whilst it has since emerged that headline figures initially quoted are indicative. We are also sceptical that Germany will be able to deploy its additional fiscal resources at speed, given the complexities of government procurement processes. Accordingly, our base case only embeds a meaningful growth uptick in 2026. Even so, the promise of increased spending has already translated into higher eurozone yields. This will prove a challenge to fiscal sustainability in other eurozone countries, while rising interest rates should also weigh on growth across the bloc. As such, this means a timing mismatch that is likely to prove a drag on activity in the coming months, even if the fiscal impetus from greater government spending eventually proves growth-supportive.

The growth impact of increased spending will not be visible for some time, but higher yields will push up borrowing costs with immediate effect

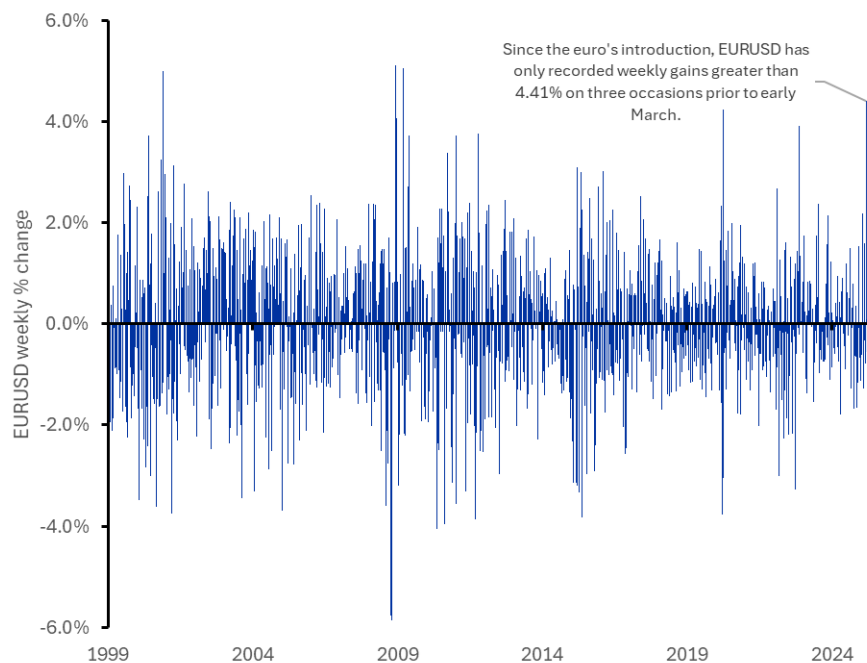


The euro’s rally through early March has few historic precedents

Despite our view on the fundamentals, the immediate market reaction to last month’s developments saw a rotation out of US assets with flows into the eurozone, prompting a sharp EURUSD uptick. In fact, since the euro was introduced, there are only three instances where the single currency posted a larger weekly gain versus the greenback than the 4.41% recorded in the first week of March. These came in December 2000, December 2008, and March 2009. By magnitude, a move of this size has only been exceeded on five total occasions including the aforementioned weeks, with two weekly falls greater than 5% both recorded in October 2008. And, despite a modest softening through mid-month onwards, EURUSD ended March above 1.08, 4.2% stronger than it began last month.

However, if our views on the fundamentals are correct, then this move higher for EURUSD is likely overdone, with the pair due a retracement lower in the coming month. In part, this should be supported by a moderation in growth expectations for Europe and recession fears in the US. But the more immediate catalyst for a reversal through early April likely comes from tariffs and tariffs threats.

The early March EURUSD rally represents the largest one-week gain for the pair in more than 15 years



Liberation day awaits

Front of mind for many as April gets underway, “Liberation Day” on April 2nd is the date when reciprocal US tariffs are expected to be unveiled. We have long been of the view that markets are underestimating the likely breadth, scope, and longevity of US tariffs. In fact, once including a 25% tariff on most auto imports due to start on April 3rd, America’s effective tariff rate now stands around 8%, up from just 2% before Trump took office. Yet this is a story that we think has been broadly overlooked by traders, with reaction across FX markets proving muted, and most dollar pairs pricing minimal tariff risk-premia.

And that is all before “Liberation Day” announcements take place. In terms of what we will be liberated from, uncertainty seems the most obvious. After months of speculation, administration officials will have to spell out more precisely what is meant by “reciprocal tariffs”. A broad spectrum of outcomes looks credible to us. We have seen a range of sell-side predictions in recent weeks, with most estimates for the rise in the effective tariff rate falling in the 5-25pp point range.

“Based on recent commentary, we lean toward a more maximalist outcome, now expecting a rise in the effective tariff rate of 15-20pp, albeit with low conviction.”

Experience to date suggests a preference from the Trump administration to propose higher tariff rates at the outset, with these then used as a basis for negotiation. Indeed, recent indications from officials suggest that this approach is unlikely to change. What is different this time around is that so many more countries will be targeted, and with few apparent avenues to make concessions. This raises the risk that the barriers will remain much stickier than prior iterations levied on Mexico, Canada, and China. Albeit even in these instances, the tendency has been for tariff barriers to end up higher, despite some measures being pared back.

Flip-flop odds likely to induce some caution

It is this flip-flopping, however, that appears to have induced a degree of caution across markets. For now, the sentiment-negative impact of tariff uncertainty is flowing into soft-data readings – a dynamic most obvious in the US, weighing on growth expectations and the dollar. But the effect of actually increasing tariff barriers is not yet being meaningfully transmitted into market pricing – also, we think, as a consequence of tariff uncertainty.

“Traders appear to be holding fire until the size and scope of US tariffs become more apparent, and as such, are positioned by default for a relatively benign outcome on April 2nd.”

This leaves risks skewed toward a negative surprise and a stronger dollar as the uncertainty starts to clear. Albeit, given the prior history of flip-flopping and what is likely to be a fair degree of scepticism when it comes to tariff longevity, it may take some time for any changes to be fully priced in FX markets, a dynamic we expect to be a key theme through April.

FX VIEWS

USD

Stagflation nation

Despite rising market speculation throughout March, our macro base case continues to see US recession concerns as overstated. Indeed, we think this would be a major challenge to achieve, absent significant imbalances that are far from obvious at present - especially when considering the fiscal support implied by a federal government deficit projected to come in above 6% of GDP in FY 2025. That said, we still expect the American economy to slow over the coming year, as tariffs and policy uncertainty take their toll on growth. But this is also likely to be accompanied by a renewed rise in inflation. Early indications suggest firms are increasing prices in response to tariffs, while "Liberation Day" levies pose a further upside risk to that dynamic. In short, the US is rapidly becoming a stagflation nation, albeit not in a way that is likely to favour dollar downside, at least in the short term.

Indeed, we see a series of factors that suggest to us that the dollar remains cheap, all things considered. First, higher tariff barriers, even if they prove disruptive, should alter net capital flows in a manner that favours dollar strength. After all, tariffs should make it more attractive to produce domestically in the US, at the expense of imports.

Second, we see little chance that the Fed is able to look through the inflationary impact tariffs as "transitory", despite prior research to the contrary. This requires inflation expectations to remain well-anchored - far from apparent given the current inflationary stickiness, and the price growth dynamics of recent years. That leaves the Fed firmly in wait-and-see mode, meaning no interest rate cuts until there are clear signs of weakness in labour market. And, bearing in mind our view on US growth, we see this latter concern as still some way off.

"As such, we continue to look for no Fed rate cuts in 2025, in contrast to swap implied expectations that price three rate cuts through the remainder of the year."

Elsewhere, however, we suspect that conditions will pose much less of a dilemma for policymakers. Absent a one-for-one retaliatory response to US tariffs, the inflation impact outside the US should prove less pronounced. Growth, meanwhile, will still take a hit. And given our view that expectations for Europe specifically already look over-optimistic, we see a clear path to further policy easing as growth and inflation outside the US broadly underwhelms. The upshot is that expected growth and rate differentials

should widen in favour of dollar strength, if our base case for tariffs is met. Accordingly, we still expect the dollar to strengthen by close to 4% through Q2 as other economies readjust to the initial tariff shock, with the greenback then softening through the second half of the year as policy easing outside the US prompts a pick-up in economic activity.

Underlying US inflation remains sticky even before tariff impacts are felt, leaving market implied Fed easing expectations looking far too aggressive to us



EUR

Coming down off the highs

Despite the euro's strong start to March, we do not expect this upside to prove durable. Fundamentals suggest that a pullback for the pair is likely before a more sustainable EURUSD rally plays out in the second half of the year. Europe has likely seen peak stimulus fuelled optimism, and our macro base case sees sentiment turning less supportive for the euro moving forward, contrasting with US growth concerns that we see as overstated. Further solid data prints should assuage US recession fears and prompt a paring back of Fed easing bets, helping the dollar to retrace some recent losses. Meanwhile, tariffs are still coming and remain a EURUSD negative factor on balance.

"Absent another surprise, this should keep EURUSD tracking lower, with the pair having already cooled more than 1.5% off its mid-March high. We look for the pair to bottom out around 1.03 at the end of Q2."

Further out though, continued ECB policy easing, combined with the building effects of fiscal support, should begin to translate meaningfully into an improvement in activity, particularly toward year-end. Under our baseline forecast, this implies a slow grind higher for the EURUSD from mid-2025 onwards, projecting the pair at 1.10 over a 12-month time horizon.

GBP

Underwhelming

While we remain long-term sterling bulls, we were surprised by the pound's surprising resilience through March. The Chancellor broadly underwhelmed with her Spring Statement, while tariff risks on the horizon pose a further downside risk. With this in mind, we are doubling down on our call to turn tactically bearish on GBPUSD, expecting the sterling to broadly track the euro lower over the course of Q2. That leaves GBPUSD to bottom out at 1.23 around mid-year under our central expectations.

This is, admittedly, at odds with our prior view that sterling should outperform the euro given the UK's relative insulation from the impact of tariffs. But having now seen the content of the Spring Statement, we now see little chance that the Chancellor manages to stay within her borrowing rules. A further rise in Gilt yields between the OBR closed its forecast window and the Spring Statement has already wiped out around half of the Chancellor's £9.9bn in headroom. Tariffs should do the rest by weighing on growth. As the UK's constrained fiscal space becomes apparent, this should weigh on sterling. Similar recent periods have seen the pound notably

underperform, though in this case, we expect it to see the pound broadly track the euro lower in the short-term, even despite a recent tariff-induced decline in the typical sterling sensitivities to cross-currency moves.

JPY

Still set to outperform

We continue to expect the yen to appreciate as 2025 wears on, underpinned by further BoJ policy tightening, haven demand in the face of heightened global economic uncertainty, with these first two dynamics compounded by growing repatriation flows. While this is in keeping with our prior forecasts which see USDJPY sinking to 130 over a 12-month horizon, we have tweaked our short-run projection to the upside, reflecting recent price action. We now expect USDJPY to trade at 147 by month-end. This would still leave the yen to outperform the dollar, but by less than we expected last month, a result of our updated expectation for the relative timing of the crystallisation of US tariff risks, and the BoJ's next policy meeting which takes place on May 1st.

CAD

Only a temporary reprieve

The loonie remains a standout amongst G10 FX given the Canadian economy's sizeable exposure to US trade. It was therefore surprising to see USDCAD end March trading around 1.43 – roughly 1% stronger than it began the month. This is despite further tariffs looming large as a threat, with Trump's April 2nd deadline arguably more consequential for Canada than any other economy. We think this highlights market complacency when it comes to US trade risks, expecting the pair to rally sharply in the coming months, topping out at 1.50 in our baseline forecast.

In part, these expectations are fuelled by our view on the dollar and the US economy. But the Canadian side of the equation is just as consequential. A significant rise in tariff rates, as has been proposed, would almost certainly tip the Canadian economy into recession while only shaving a fraction off US growth. Not only would growth differentials widen under such a scenario, but we would expect rate differentials to follow suit. Despite BoC Governor Macklem's non-committal stance in recent commentary, we expect the downside growth impact to dominate any upside pressure on inflation from higher tariff barriers.

All this, however, remains unchanged from our longstanding loonie base case. But these latest forecasts have seen us marginally upgrade our expectations for USDCAD, despite the pair underperforming our prior forecasts. Underpinning this change – a Canadian general election on April 28th. The Liberals have made a remarkable comeback since Mark Carney

took power, albeit we are not convinced that this is a loonie-positive dynamic. Carney's popularity stems, in part, from the hard line he has taken on US tariffs. That reduces the odds of ultimately reaching a favourable compromise, leading us to expect greater loonie softness in the coming months.

CNY

Make or break

The lack of CNY weakness year-to-date has been somewhat surprising to us. Despite the US increasing tariffs on China by 20% over recent months, greater than the total rise seen over the entirety of Trade War 1.0, the yuan has actually appreciated against the dollar since Trump took office - a sharp contrast to the significant depreciation seen during the prior round of trade hostilities. Therefore, while we have rolled forward our forecasts for another month, April is likely to be make or break for our longstanding call for CNY weakness.

“Key to our call remains a view that Chinese authorities will ultimately use the FX channel to partially offset the impact of rising tariff barriers.”

Granted, this has not happened to date, with the Chinese response remarkable in terms of restraint. That said, we also thought some of the rhetoric out of the Two Sessions that took place last month was notable. To us, there appeared to be a hardening in the language coming from some Chinese officials, suggestive that they may be starting to run out of patience with the Trump administration. We suspect that frustration will only intensify following another round of tariffs on April 2nd.

With this in mind, we expect to see more forceful pushback from China over the coming month, including via the yuan, which remains tightly controlled by the PBoC. While a sharp USDCNY move higher looks unlikely given this latter fact, a slow and steady grind higher for the pair remains among the more likely options to retaliate against US tariffs in our view.

Forecasts

Currency Pair	1-month (30 th April 2025)	3-month (30 th June 2025)	6-month (30 th September 2025)	12-month (31 st March 2026)
G10				
EUR/USD	1.05	1.03	1.05	1.10
USD/JPY	147	145	140	130
GBP/USD	1.26	1.23	1.26	1.33
USD/CHF	0.90	0.90	0.90	0.88
USD/CAD	1.47	1.50	1.48	1.45
AUD/USD	0.62	0.61	0.60	0.60
NZD/USD	0.56	0.56	0.55	0.55
USD/SEK	10.4	10.8	10.3	9.5
USD/NOK	10.8	11.1	10.6	9.8
DXY	106.5	108.1	105.8	100.7
Emerging Markets				
USD/CNY	7.35	7.50	7.65	8.00
USD/INR	86.5	88.0	90.0	93.0
USD/SGD	1.35	1.37	1.39	1.40
USD/ZAR	18.8	19.3	19.5	20.0
USD/TRY	38.0	38.0	40.0	42.0
USD/PLN	4.00	4.13	4.10	3.91
USD/HUF	386	395	386	364
USD/CZK	24.0	24.8	24.1	22.7
USD/BRL	5.90	6.20	6.40	6.50
USD/MXN	20.8	21.2	21.5	22.0
Euro Crosses				
EUR/GBP	0.83	0.84	0.83	0.83
GBP/EUR	1.20	1.19	1.20	1.21
EUR/CHF	0.95	0.93	0.95	0.97
EUR/CAD	1.54	1.55	1.55	1.60
EUR/SEK	10.9	11.1	10.8	10.5
EUR/NOK	11.3	11.4	11.1	10.8
EUR/TRY	39.9	39.1	42.0	46.2
EUR/PLN	4.20	4.25	4.30	4.30
EUR/HUF	405	407	405	400
EUR/CZK	25.2	25.5	25.3	25.0
EUR/BRL	6.20	6.39	6.72	7.15

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