

FX Viewpoint

A resilient USD

- ◆ The broad USD is likely to remain strong, supported by relatively high US yields and slow global growth
- ◆ We no longer look for the CAD to strengthen against the USD, and now think a sideways move is the more probable path
- ◆ USD-JPY may have a modest recovery in 2H24, but will probably consolidate for now

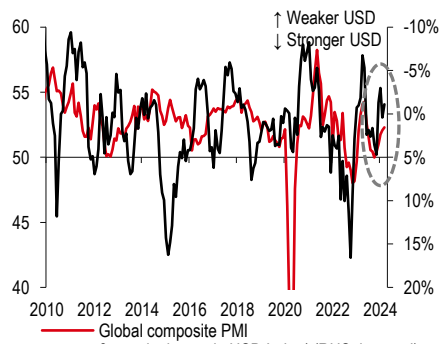
We see the broad USD remaining strong through the course of the year. Central to this view is the belief that the Federal Reserve (Fed) would lower its policy rate gradually, with **relatively high US yields providing support**. **Slow global growth should also support the counter-cyclical USD**.

However, one recent development could challenge our USD view, **as there are some signs of improvement in global trade and growth** (Chart 1). In particular, if there is additional evidence that global growth is gaining traction, then this will be a headwind to the USD. That being said, **it remains unclear whether, for example, an inventory adjustment is happening or something more meaningful is occurring**. For now, we believe that the USD can shake it off, believing the currency can manage further resilience ahead.

We expect the USD to remain resilient...

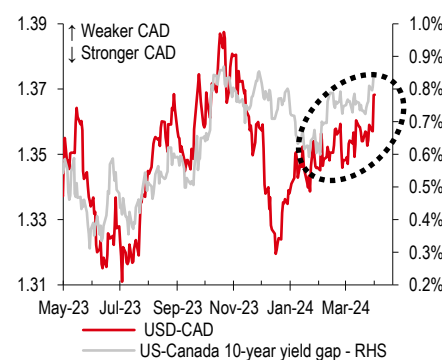
...as it is still uncertain whether improvement in global growth is sustainable

1. The global PMI has tilted higher, but the USD has also reflected this



Note: *USD Index is derived from an equally weighted G10 FX basket.
Source: Bloomberg, HSBC

2. USD-CAD has been following its yield differentials recently



Source: Bloomberg, HSBC

As for the CAD, we now think that it is unlikely to strengthen against the USD. USD-CAD does not appear to be out of line with its yield differentials (Chart 2). **The CAD has also become less responsive to its traditional drivers**, including constructive risk appetite (as suggested by the rally in global equities) and higher oil prices. All things considered; **we now think a sideways move is the more probable path**.

We no longer look for the CAD to strengthen against the USD

Another currency pair that is likely to consolidate for now is USD-JPY. **Carry trade activities** funding out of the JPY and outflows related to the Nippon Individual Savings Account (NISA) programme¹ have been putting upward pressure on USD-JPY and trying **Japan's Ministry of Finance's tolerance**. But when some of the underlying variable changes later this year, for example, when the Fed starts to cut rates, the JPY is likely to see a modest recovery.

We still expect a modest JPY recovery, albeit with a delay

¹ With effect from 1 January 2024, investment limits for NISA (which provides capital gains tax exemptions) were raised by 2-3 times (to JPY3.6m per year and JPY12-18m in total).

Disclosure appendix

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