Insights
Currency & Cash

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Currency Market Commentary

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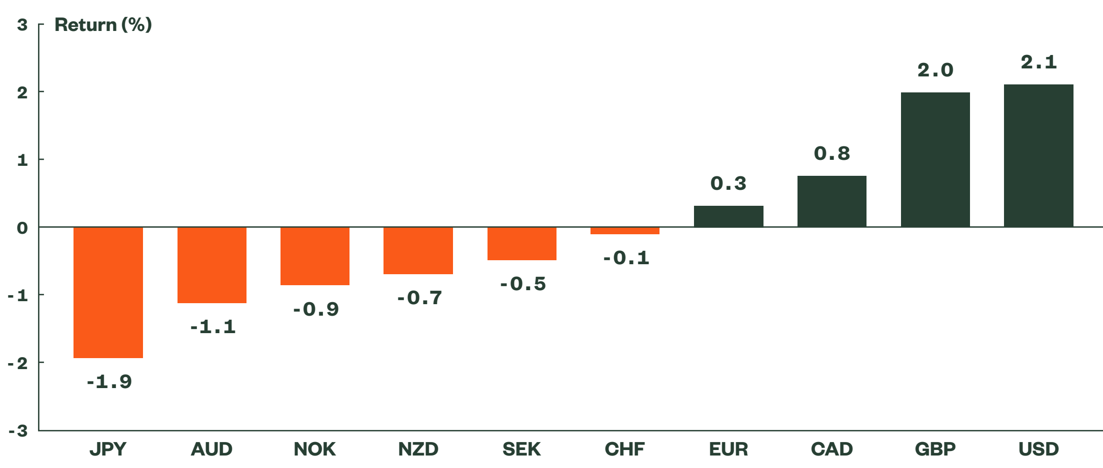
Summary of Views

Broad currency market behavior in January, or at least in the first half of January, is fairly easy to interpret. The moves across the G10 during the month had a negative 79% correlation to the moves in December.

We saw large moves in equities, rates and currency over the November–December based on the Goldilocks thesis — decent growth and disinflation will likely enable central bank policy easing alongside ongoing growth.

Figure 1
January 2024 Currency Return vs. G10 Average



Source: Bloomberg and State Street Global Advisors, as of 31 January 2024. **Past performance is not a reliable indicator of future performance.**

The optimistic soft-landing theme continued in January, but pockets of better-than-expected growth, a slower pace of disinflation and the sheer magnitude of the November–December market moves prompted a partial profit taking, thereby reversing the late 2023 price action. The US dollar and British pound won, while the ultra-rate-sensitive Japanese yen and the cyclically sensitive Australian dollar and Norwegian krone suffered. The pattern was similar to the bounce back in rates and the slight correction lower in equities, the opposite of the November–December moves.

Figure 2
January 2024 Directional Outlook

	Tactical Outlook	Strategic Outlook
USD	Up	Down
CAD	Down	Neutral
EUR	Neutral	Neutral
GBP	Down	Neutral
JPY	Up	Up
CHF	Neutral	Down
NOK	Down	Up
SEK	Down	Up
AUD	Down	Neutral
NZD	Down	Neutral

Note: All individual currency views in the table above are relative to the G-10 average.
Source: State Street Global Advisors, as of 31 January 2024.

Nearly all FX market returns occurred before 17 January, after which G10 currencies settled into a tight range. For perspective, the average absolute G10 currency return was 1.29% from 1–17 January. This sharply contrasted with the 0.26% return for the rest of the month, barely one-fifth of the early month price action. However, the directionless second half of the month was perhaps more informative about prospective currency behavior over coming months.

US growth once again came in well above expectations and the long-run potential. The US Federal Reserve (Fed) Chair Jerome Powell explicitly pushed back on the market pricing of a March rate cut. He also indicated clearly that the Fed is willing to ease policy even if the economy and labor market remain hot, as long as inflation continues to trend reliably down to the 2% target. On balance, this is good for the US dollar as developed markets' growth outside the US remains stagnant or at least well below their potential.

However, the willingness to cut rates with strong growth limits equity downside risk and the magnitude of the US dollar upside. Let us call it a well-supported range for the dollar. The more fragile environment outside the US keeps a lid on commodity demand expectations and raises local recession risk. We expect this to weigh on cyclically sensitive currencies, including the British pound. Despite indications that high inflation may keep the Bank of England (BoE) on hold for longer than most, any rally owing to tighter expected policy will likely be short-lived.

High rates with a shaky external balance and stagnating economy are not a recipe for currency appreciation. The yen continues to be one of our favorites as we approach an almost synchronized global rate-cutting cycle, but we may have to wait longer as the expected start of easing is pushed out.

Our longer-term view has not changed much. We see US dollar downside with the US losing much of its interest rate and growth advantage over the next 1–3 years leading to a sustained dollar bear market. The unsustainably high combined US fiscal and current account deficits should add to the dollar downside pressure. We recommend medium–long-horizon investors to position for a weaker US dollar now.

US Dollar (USD)

The US dollar gained 2.1% against the G10 average in January. After a dramatic two-month sell-off alongside falling yields and rising equity markets, the US dollar looked overextended to start the year. Positive surprises in non-farm payrolls, wage gains, the ISM manufacturing survey and factory orders during the first week of January triggered a reversal, sending US yields and the dollar higher.

Higher-than-expected Consumer Price Index (CPI) inflation on 11 January furthered the rally. On 16 January, Fed Governor Waller commented that the bank should be methodical and careful with rate cuts. That cautious tone, followed by a substantial upside surprise in retail sales the following day — +0.6% MoM vs. 0.3% expected — further supported yields and sent the dollar to its intra-month high.

From there, the rally stalled as growth data continued to impress but inflation-related data came in soft. Q4 gross domestic data (GDP) blew away expectations — +3.3% seasonally adjusted annual rate vs. 2% expected — but an unexpectedly soft GDP deflator, an broad measure of inflation, offset the impact of headline growth to leave the dollar up only 0.31% on the day.

The month-end saw the dollar fall back 0.54% on a downside surprise in the quarterly employment cost index for Q4 — 0.9% vs. 1% expected. It is not reflected in our reported US dollar return, which uses London close data, but the dollar recovered in the New York afternoon on month-end following the Fed meeting as Powell clearly pushed back on the idea of a March rate cut.

We have long held the view that the US dollar is likely to fall at least 10–15% over the coming years as US yields and growth fall back toward the G10 average, and the US grapples with high fiscal and current account deficits. For investors with a horizon of two years or more, we strongly recommend short US dollar positions; just look though this highly uncertain transition period.

For those with a shorter horizon, we believe the dollar will remain well supported in a range-trading environment at least over the next few months and is likely to press higher toward the top of its range into February. The US economy continues to impress, backed by excess consumer savings, rising real wages, and a fiscal deficit in excess of 6% of GDP — a recession-like level of fiscal support. Developed markets outside the US can best be described as mired in a stable stagnation. That broader global fragility and uncertainty regarding how long above-potential US growth can persist also help the US dollar, as they tend to diversify risky asset exposures, should US and global growth unexpectedly move toward recession.

Sounds like a great story; why do we not think the dollar will break out to new highs? The dollar is historically expensive. To become even more expensive as it did in 2022 and at times in 2023 required the combined catalysts of rising yields and some panic in equity markets. Fed Chair Powell has stepped away from the Phillip's Curve, meaning that the Fed does not need to see material economic and labor market weakness to cuts rates — only continued stable improvement in inflation moving toward the 2% target. This means that good economic news and a modest rise in yields need not precipitate fear in equity markets for now.

Similarly, if the amazing run of above-average US growth suddenly collapses, the Fed will very likely cut aggressively, sending rates lower. In other words, it appears that the ultra-high stock–bond correlation that amplified US swings is likely to weaken or even flip negative. That creates a higher probability that the US dollar faces conflicting macro drivers, which should keep it contained relative to the past couple of years.

Canadian Dollar (CAD)

The Canadian dollar gained 0.8% relative to the G10 average on the month. Tight monetary policy has clearly had a negative impact on economic activity, but there has been almost no progress on disinflation since June 2023. Monthly GDP figures from May to November 2023 show cumulative growth of –0.1%, while YoY trimmed mean CPI was down only 0.1% to 3.7% from May through year-end.

This marks a complete stalling of the disinflationary process that brought the trimmed mean inflation from 5.6% to 3.8% in the year ending May 2023, freezes central bank policy and raises the probability that a recession may be necessary to fully tame prices — a difficult position for policy makers.

Consequently, almost all of January volatility in the Canadian dollar happened around inflation and policy news. In the few days following the upside surprise in inflation on 16 January that sent the dollar sharply higher and the dovish reaction to the Bank of Canada (BoC) meeting on 24 January.

The inflation surprise instilled expectations of a more hawkish central bank, hence the Canadian dollar appreciation, but by 24 January the governing committee removed the explicit warning of further rate hikes from the policy statement. This omission helped trigger a complete reversal of the inflation-led rally in the dollar. Later that day, Governor Tiff Macklem verbally warned of the risk of further rate hikes at the press conference, which along with better US data, a recovery in oil prices, and a rare positive GDP surprise — +0.2% MoM for November — helped the Canadian dollar regain some lost ground into month-end.

The Canadian dollar remains one of the lowest-ranked currencies in our short- and medium-term models. Rapid deceleration in growth, alongside weak and choppy commodity prices, suggests further dollar weakness. Resilient inflation and labor markets support the currency via tight monetary policy, but we believe that has a limit.

Weak growth coupled with high yields is not nearly as positive for the currency as the combination of strong growth and high yields. Furthermore, we believe that inflation will give way to the weaker economic conditions over coming quarters, likely resulting in a more rapid monetary easing cycle in Canada relative to the US and other countries. This risk appears to be underappreciated in current market pricing and suggests scope for near-term Canadian dollar weakness.

In the long term, looking through the weaker cyclical picture, the Canadian dollar looks more attractive as it is cheap in our estimates of fair value relative to the euro, the Swiss franc and the US dollar. Additionally, its long-term potential growth is poised to improve on an aggressive increase in immigration and substantial plans to invest in sectors such as green energy technology.

Euro (EUR)

The euro gained 0.3% against the G10 average in January, thanks to a steady rally during the first half of the month. Early-month economic data remained weak, with December purchasing manager's index (PMI) data stuck well below 50, signifying contraction and November retail sales, released on 8 January, contracting –0.3%.

The rebound in the euro appeared to be the result of the general wave of profit taking after its large November–December sell-off and was also likely helped by comments from European Central Bank (ECB) officials discouraging investor expectations of an early rate cut.

On 15 January, ECB Governing Council member Robert Holzmann went so far as to say that rate cuts were not guaranteed in 2024 at all. After reaching its peak of 1.21% on 19 January, the euro trended lower through the month-end. January composite PMI missed expectations on 24 January, while the ECB held rates steady. Meanwhile, ECB President Christine Lagarde pointed to the rate cuts beginning in the summer, but she did not explicitly push back on the potential for earlier cuts. Investors interpreted this as dovish and sold the euro.

We maintain a neutral view on the euro against the G10 average and a negative view on the US dollar and the Japanese yen. This is not a good environment for the euro, as the combination of ongoing European Union recession risk and expectations of ECB easing is likely to weigh on the currency.

The slowing pace of disinflation and robust labor market may keep the ECB on the sidelines until summer, but the case for a material easing cycle over the next 12–18 months is strong. That said, our models are not negative relative to the G10 average despite these euro-negative factors. We see similar risks across many G10 economies, and much negativity is already priced into the currency.

We will not go so far as to say there are green shoots, but it appears that investors may be overly pessimistic. As weak as it is, economic data has been coming in above expectations, on average — a factor our model views favorably against the G10 average.

British Pound (GBP)

The British pound rose 2.0% against the G10 average in January, almost outpacing the US dollar. Over the first couple of days, the global bounce in yields and reversal of outsized December moves pushed UK two-year yields up 13 basis points (bp) and the pound up 0.5%.

On 4 January, a surprisingly strong and expansionary services PMI — 53.4 vs. 50.9 prior and 52.7 expected — further boosted two-year yields by 0.09% and the pound by 0.33%. Upward momentum continued following a better-than-expected November GDP report — +0.3% MoM — released on 12 January. A weak employment report on 16 January threatened to derail the pound's uptrend, with a 24,000 reduction in payrolled employment and a deceleration in average weekly earnings to 6.5% from the prior 7.2%.

However, the next day, December core inflation surprised higher — 5.1% vs. 4.9% expected — led by outsized services inflation. Yields and the pound once again jumped higher. From there, the currency largely went sideways through month-end on mixed data. Retail sales were notably weak, but January preliminary services PMI once again surprised to the upside.

Our factor models remain neutral to slightly negative on the pound versus the G10 average, but are quite negative on the yen and the US dollar. As the economy stagnates, disinflation persists and the constraining effects of the high fiscal and current account deficits loom, we perceive downward risks for the pound.

However, in the very short term, those downside risks are partly offset by a few factors. We see similar risks across most G10 economies and currencies, resulting in a relative tactical pound outlook only slightly negative against the G10 average.

In addition, the UK's economic stagnation is proving to be surprisingly stable, meaning the risk of falling off a cliff into recession has proven limited. We also see the Bank of England facing greater constraints on easing policy as inflation rose higher than in most G10 economies and the disinflation process is not as far along, which may provide the pound some temporary, though low-quality, yield support.

Our long-term valuation model has a more positive pound outlook. It is particularly cheap against the US dollar and the Swiss franc. Nevertheless, it is important to temper upside expectations, as low productivity growth and high inflation are pushing fair value lower. The fair value of the pound to the US dollar has fallen from 1.55 to 1.42 since May 2022.

Based on breakeven inflation expectations and recent trend productivity differentials, fair value will trend down to at least the mid-1.30s over the next few years. Despite this trend, the pound, currently trading in the mid-1.20s, remains materially cheap, even if fair value trends down as expected.

Japanese Yen (JPY)

The yen was the worst-performing currency in the G10 during January, down 1.9% vs. the average. This was classic yen behavior — rising global yields and rising global equity markets provide a doubly negative impulse to the currency, with the bounce-back in yields being the more significant driver.

After the initial rebound in global yields during the first half of the month drove the yen lower, they moved sideways into month-end and the yen stabilized. Local data and news had little impact. The Bank of Japan (BoJ) met on 23 January and kept all policy settings unchanged, while retaining dovish language. There was no hint of exiting the negative interest rate policy (NIRP), but markets had largely priced out an early 2024 NIRP exit in December, so it had little impact.

Our models maintain a positive view on the yen relative to the G10, but retain a negative view versus the US dollar, given the high US interest rates and a strong relative growth. Q1 2024 may be quite volatile, but we see risks skewed toward a broad yen recovery in 2024 as yields peak and turn lower, while below-trend global growth (maybe only returning to trend in the US) should increase the chance of periods of volatility in risky assets. The increased likelihood that the BoJ exits NIRP by mid-year is also supportive, though the magnitude of potential BoJ rate increases is tiny compared to the scope for rate cuts across the rest of the G10.

We believe foreign interest rate policy will remain the bigger driver of yen. To that end, the much better-than-expected performance of the US economy and resultant delay of the first rate cut are likely to keep the yen on the weak side longer than previously expected.

Swiss Franc (CHF)

The franc was little changed in January, down by −0.1% versus the G10 average. The currency jumped on 8 January following a higher-than-expected core CPI print for December — 1.5% vs. 1.4% expected — though that remains well below the 2% upper end of the Swiss National Bank's (SNB's) target band.

However, the strength in the US dollar, the euro, and the global yields into mid-month erased the gains on the relatively low-yielding franc. SNB President Thomas Jordan then sent the franc into negative territory following comments from Davos on 18 January, pointing to the disinflationary effects of the expensive currency. Subsequently, last month's weakness in the euro helped the franc recover much of its loss in the final week of the month, resulting in a finish that was nearly unchanged.

We are negative on the franc over the strategic horizon, but have a rare neutral signal over the tactical horizon against the G10 average — still tactically negative versus the US dollar and Japanese yen. The franc is the most expensive G10 currency per our estimates of long-run fair value; growth data remains soft; inflation stable well within target ranges; and aside from the yen, the franc has the lowest yields in the G10. The monetary policy outlook is also likely to continue to shift toward easing in first quarter as indicated by Jordan's comments. With the real trade-weighted franc near 30-year highs, any further strength could easily induce the SNB to intervene to weaken the franc. Such a shift is likely to provide a catalyst for the highly overvalued franc to begin a reversion toward our estimate of its longer-term fair value.

However, we also likely need to see stabilization and early signs of recovery in the world economy outside of the US to fully unlock franc weakness; hence the neutral signal. In other words, our shift from negative to neutral is not so much a function of improvement in Swiss fundamentals as it is a deterioration in fundamentals outside of Switzerland and the US.

Norwegian Krone (NOK)

The krone lost 0.9% against the G10 average in January. It was extremely choppy and largely beholden to volatility in oil and equity markets. On four occasions, the krone rapidly dropped 0.8–1.0% and three times it rapidly recovered back to flat for the month, forming a true saw-tooth pattern.

The final of these moves resulted in a drop of 0.9%, leaving it underwater for the month. On 2 January, there was a sharp unwind of December returns and a 1.49% fall in Brent crude prices, causing the top-performing krone to fall 0.78%. Oil bounced back, as did the krone, over the next two days.

On 8 January, Saudi Arabia cut crude prices, pushing Brent down by 3.35% on the day and the krone back down by 0.92%. As oil gradually recovered that loss, the currency followed suit. The sharp drop in equity prices from the 15–17 January once again sent the krone to its lows, down by −0.88% month-to-date. It languished at those levels until a near 5% rally in oil prices and a rebound in equity markets prompted a recovery in the krone back to flat for the month.

The Norges Bank held policy and outlook steady at its meeting on 25 January, with little impact to the currency. However, another downdraft in oil prices during the last few days of the month and a disappointing Norwegian retail sales reported on 26 January appear to have triggered a final sell-off of the currency into month-end.

The more vigilant Norges Bank and the reduced krone sales are clear positives. However, our short- and medium-term models remain negative on the krone due to weak oil price trends and disappointing growth data. Even the relative tightening of the Norges Bank's monetary policy outlook has had limited impact beyond the near term.

The Norges Bank may hold off on rate cuts longer than other central banks, but tepid growth data and a steady disinflation suggest a steady policy easing later this year and into 2025.

Our short-term value model suggests that the krone's strength over recent months has substantially outpaced its fundamentals even after the modest January correction. Going forward, we also think it prudent to be cautious on the global risk sentiment and its impact on the krone. Any general slowing of global growth led by the US later this year will likely increase recession fear and result in periods of greater equity market volatility and subdued oil prices, both of which are consistent with a weaker krone, or at least limited upside.

In the long term, the outlook is positive. The krone is historically cheap relative in our estimates of fair value and is supported by steady potential growth.

Swedish Krona (SEK)

The krona fell throughout January, ending down 0.5% against the G10 average. It had been the top-performing G10 currency in November–December and was subject to some profit-taking early in the month as the US dollar, the euro, and other late 2023 underperformers rebounded.

Better-than-expected November GDP released on 10 January — +0.2% MoM vs. –0.6% expected — provided temporary relief for the currency. However, comments from Riksbank Deputy Governor Jansson once again pressured the currency lower, as he stressed that he is convinced that interest rates have peaked and inflation is on its way down. Although the higher-than-expected December inflation reported on 15 January should have been supportive, the currency faced pressure from weak equity markets and rising risk aversion on 15 and 17 January, making recovery difficult.

The krona sank to its low for the month during that time, where it stayed until a rally in the last few days of the month before a late-month rally. There was not an obvious cause for that rally. In fact, fourth-quarter GDP disappointed and December retail sales came in below zero on 29 and 30 January. Most likely, the krona's strength was due to some squaring of short positions in anticipation of the Riksbank meeting on 1 February.

Our short-term value model is strongly negative on the currency, as it estimates that the recent strength in the krona is not justified by economic data. The modest 0.5% loss in January was not enough to cure that undervaluation given the ongoing weakness in growth data and the dovish Riksbank.

The Riksbank met on 1 February as we wrote this note and took a clear dovish tilt, suggesting earlier and perhaps greater rate cuts over coming quarters. The ongoing Riksbank reserves hedging program likely provided support to the krona over the past few months, but that program is nearing its end.

Eventually, though maybe not in the next several months, Swedish and global inflation will be under control and the economy will begin a more durable recovery. Once that happens, the historically cheap krona has substantial room to enjoy a broad-based appreciation back toward its long-run fair value on a sustained basis. Until then, we maintain a negative bias.

Australian Dollar (AUD)

The Australian dollar fell 1.1% against the G10 average in January, making it the second worst performer for the month. Shaky global equity markets and the rebound in US yields pushed the Australian dollar steadily lower through 15 January.

During that time, positive local data appeared to have little impact, such as a slight uptick in composite PMI and a notable beat in November retail sales reported on 8 January.

Similarly, the negative data, such as the downside surprise in November CPI released on 9 January, also had little impact. A large negative surprise in Australian employment on the 17 January — with a loss of 65,000 jobs compared to an expected gain of 15,000 — likely had a negative impact, although it is hard to discern given the sharp downturn in global equities and sell-off of high-beta currencies that day.

After 17 January, recovering equity markets and commodity prices lent support, but only enough to send the Australian dollar sideways, not enough to materially retrace the early-month loss. In part, this is due to a soft finish at month-end following weaker-than-expected December retail sales on 29 January and a surprise drop in fourth-quarter CPI reported on 30 January.

Our models continue to see medium-term risks tilted to the downside for the Australian dollar on tepid commodity prices, underperformance of Australian equity markets, and the recent downside inflation surprise. However, the signal has improved for a number of reasons and is only slightly negative.

Our growth sub-signal has turned positive on a relative basis and we do not expect the Reserve Bank of Australia (RBA) to ease monetary policy as rapidly as in the EUor North America in 2024.

In addition, the cheap Australian dollar suggests many of these negative factors are priced into the currency. Furthermore, we also expect stabilization in Chinese growth following recent fiscal and monetary stimulus, although investors are currently reacting poorly to announcements of Chinese stimulus and likely need to see the positive impact before it spills over to support the dollar.

In the longer-term, the Australian dollar outlook is mixed. It is cheap against the US dollar, the British pound, the euro, and the Swiss franc, with potential for appreciation, but it is relatively expensive against the yen and the Scandinavian currencies. Here, the Chinese story is less positive as we see a structural downtrend in Chinese growth, as well as a rotation toward domestic consumption and higher-value-added industries, which is likely to gradually reduce the growth rate of Australian commodity export demand.

New Zealand Dollar (NZD)

The New Zealand dollar fell 0.7% against the G10 average in January. The pattern was similar to that of the neighboring Australian dollar, characterized by a general downtrend during the first half of the month as the US dollar bounced back from its late 2023 losses and the equity market rally stalled.

Weak credit card spending, building permits, and manufacturing PMI also cast a shadow on the New Zealand growth outlook. However, the New Zealand dollar held up better in the second half of the month compared to the Australian dollar following a large upside surprise in fourth-quarter non-tradeable inflation reported on 23 January — +1.1% QoQ compared to +0.8% expected. The combination of positive inflation data and the rebound in global equity markets paved the way for the dollar to rally into the month-end.

We are negative on the New Zealand dollar over the near term. Slow growth, choppy commodity prices, and the weak external balance — the current account is –7.5% of GDP — more than offset any benefit of high yields even after the upside inflation surprise in January. However, the current market focus on the start and extent of monetary easing cycles may help provide some near-term support. Markets expect New Zealand to begin its easing 1–3 months later than most G10 central banks and cut less; this seems a reasonable expectation. As a result, the New Zealand dollar is likely to remain the highest-yielding G10 currency through 2024.

In the longer term, our New Zealand dollar outlook is mixed. Our estimates of long-run fair value suggest that it is cheap versus the US dollar and the Swiss franc and has ample room to appreciate, but is expensive against the yen and the Scandinavian currencies.

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