

FX Focus

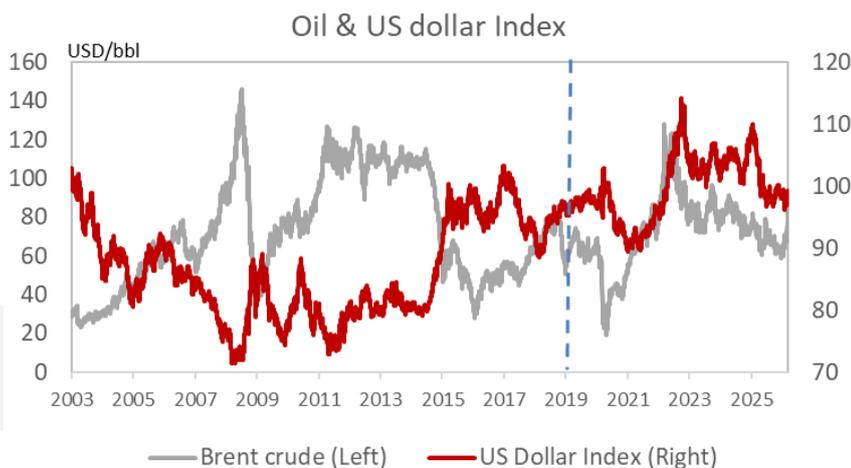
USD in the Crossfire

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- Geopolitical flare-ups and oil shocks lifted safe haven demand and magnified the divide between energy exporters and importers, offering the USD support for now.
- Artificial intelligence (AI)-driven equity rotations and the Supreme Court’s tariff ruling weighed on USD sentiment, though AI-driven long-term productivity upside could still anchor high USD valuation.
- If our base case of no Hormuz blockade prevails, stronger non-US growth points to USD softness, with cyclicals leading gains. JPY stays capped by BoJ dovishness, while resilient exports keep CNY on an appreciation track.

After a soft January, the USD’s performance has been more mixed. Geopolitical tensions have moved sharply to the forefront after US and Israeli strikes on Iran prompted retaliatory attacks across the region. Oil spiked before retreating to just above USD80/bbl – still not high enough to threaten global growth, though a sustained rise through mid-year would elevate stagflation risks.

New USD-oil relationship means the assets are no longer inversely correlated



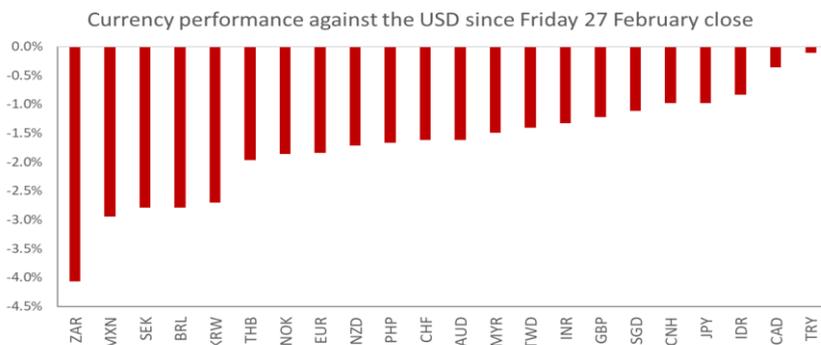
Source: Bloomberg, OCBC Group Research

FX markets reacted in classic risk-off mode following the Middle East escalation: safe haven currencies outperformed, and energy exporters were favoured over importers. This backdrop broadly supported the USD, which also drew strength from the US’ status as a net energy

exporter since 2019 and the world’s largest LNG exporter from early 2026.

Despite its safe-haven reputation, the CHF underperformed as elevated Swiss National Bank intervention risk kept investors cautious. CAD – given its net energy exporter status -- also held up better than most G10 currencies, benefiting from positive spillovers of higher oil prices. By contrast, currencies of energy-importing economies in Asia and Europe weakened. EM FX faced the sharpest pressure as rising volatility triggered deleveraging, accelerating unwinds of crowded carry trades such as BRL, MXN and ZAR.

Currency moves reflect not just oil exporter-versus-importer divide, risk-off risk-on but also intervention risks and deleveraging pressures



Source: Bloomberg, OCBC Group Research

AI-related equity rotations and the recent Supreme Court tariff ruling also influenced currency sentiment. The AI narrative triggered selling in US tech stocks and raised concerns over private credit vulnerabilities, weighing on the USD through equity underperformance. Longer-term effects remain uncertain: productivity gains from AI could ultimately reinforce US growth and support a high USD valuation.

Relative ex-US equity outperformance driven by AI disruption narrative a drag on the USD



Source: Bloomberg, OCBC Group Research

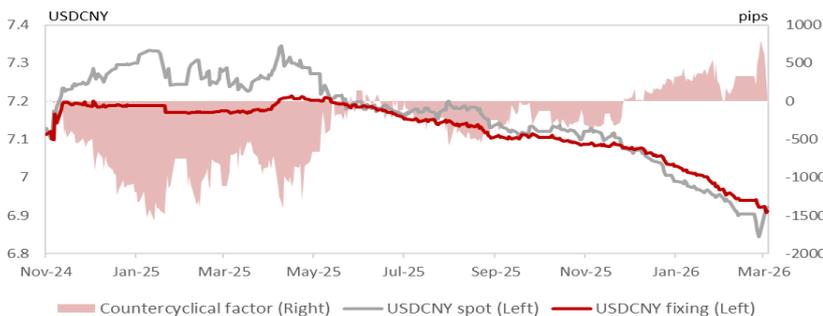
The Supreme Court’s rejection of IEEPA-based tariffs removed a layer of legal uncertainty but left refund questions unresolved. President Trump’s shift to alternative tariff authorities keeps effective tariff rates largely intact, explaining the muted USD response. Importantly, these alternative tools are less discretionary, reducing the “tariff on/off” volatility seen in prior cycles.

The USD has recovered from the “Greenland shock,” but with no Hormuz blockade in our base case – keeping oil on track toward the low-USD60s/bbl by year-end – its upside still looks limited. Persistent US policy uncertainty leaves the dollar with modest downside, supporting our unchanged end-2026 EURUSD forecast of 1.23, driven more by USD softness than EUR strength. Even so, firm US growth should cap the scope of any sharper USD decline. A genuine USD reversal would require a clear reacceleration in US growth momentum – something still missing for now – though early signs of labour market stabilisation could pave the way for a 2027 recovery.

Our base case remains intact: AI-disruption narratives, tariff uncertainty and geopolitical oil shocks are unlikely to derail improving US and global growth, especially with fiscal support strengthening into 2026. Better non-US growth provides room for USD weakness, particularly against cyclicals such as AUD, NZD, ZAR and BRL once the oil volatility subsides.

While EUR lacks a compelling undervaluation story, JPY and CNY do not. Yet reports of Prime Minister Takaichi’s reluctance toward further Bank of Japan (BoJ) hikes — and the nomination of two dovish-leaning Board members — reinforce a dovish impression that restrains JPY upside. By contrast, China’s resilient exports continue to place upward pressure on the CNY, creating positive spillovers across Asia FX. The CNY appreciation trend should persist, even as authorities aim to moderate its pace via a stronger counter-cyclical factor in fixings and by removing the FX forward sales reserve requirement.

The CNY appreciation trend should persist, even as authorities aim to moderate its pace



Source: Bloomberg, OCBC Group Research

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