

BBVA

ECB Foreign Exchange Contact Group

Review of recent markets
developments and outlook

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Rotation in asset demand has weighed on the USD

- The uncertainty stemming from the new US administration has undermined confidence, creating headwinds that are expected to have lasting structural repercussions, even if trade agreements emerge.

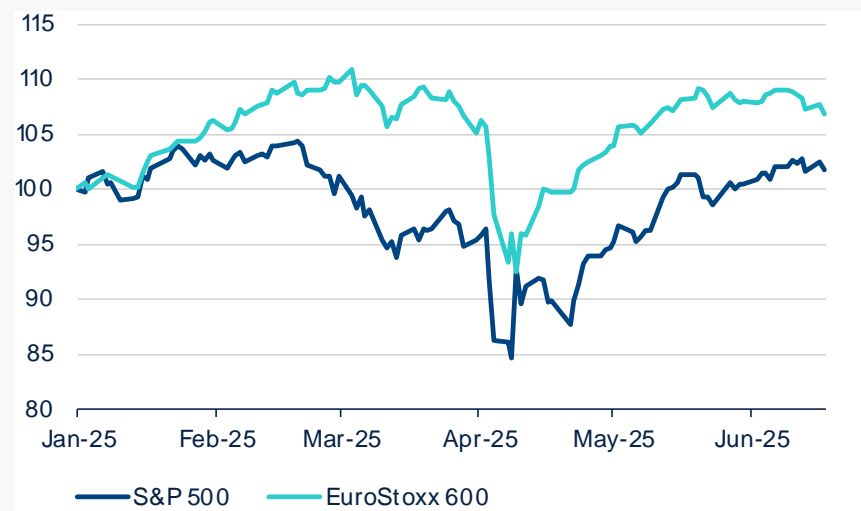
The breakdown in the correlation between the USD and interest rates has been driven by US uncertainty

Source: Bloomberg and BBVA FX Strategy



The relative performance of European equities vs. US equities highlights a rotation in capital flows (Jan25 = 100)

Source: Bloomberg and BBVA FX Strategy

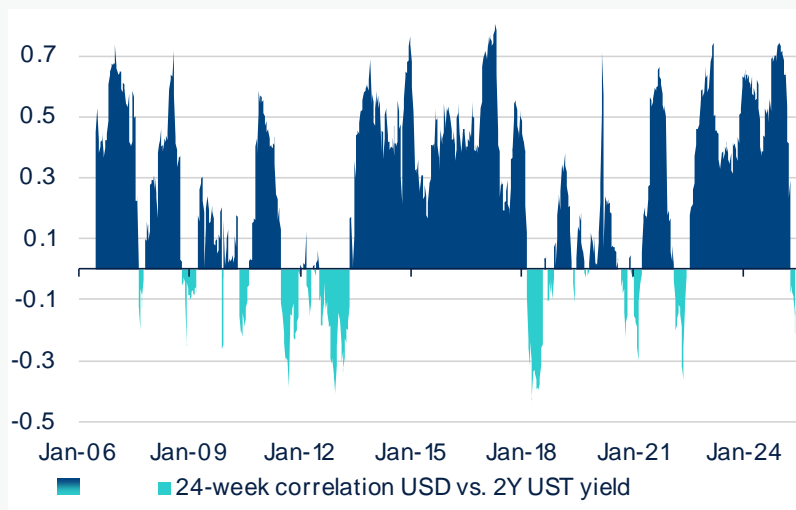


Shifting correlations underscore USD vulnerability

- The evolving correlation landscape reflects the broader impact of the new US administration and the sustained uncertainty it has introduced

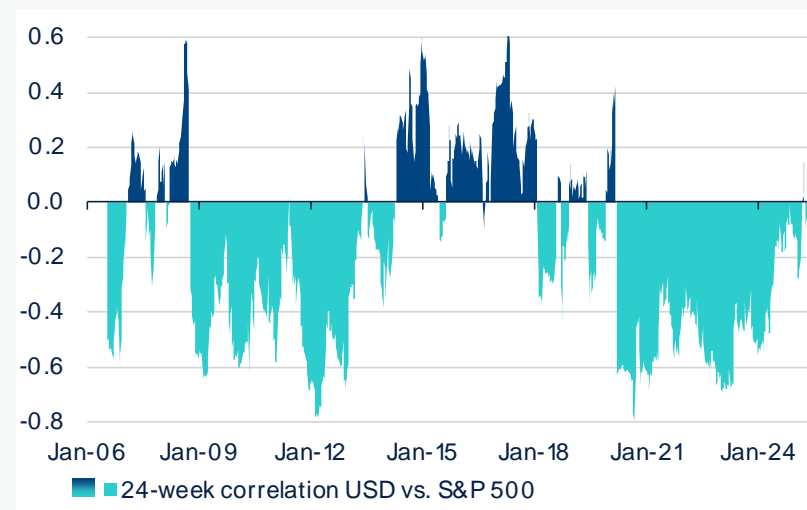
The trade war has been a primary catalyst behind the dislocation between the USD and interest rates

Source: Bloomberg and BBVA FX Strategy



The USD did not act as the main safe-haven in 1H25 although instability in ME have backed USD demand

Source: Bloomberg and BBVA FX Strategy

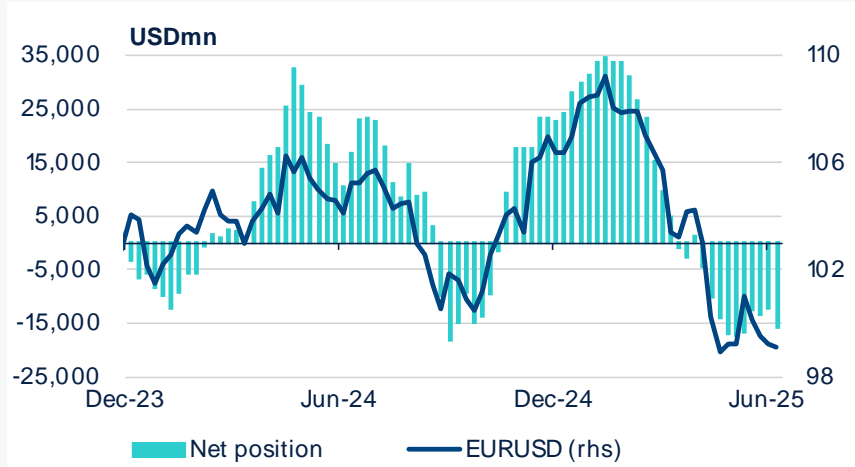


Speculative flows as a short-term key

- The shift in positioning, from a record net long in January to the multi-month net short peak reached in June, highlights declining investors confidence
- Bearish positions in the EUR tied to cyclical weakness and expectations of further rate cuts, gave way to bullish sentiment in 1H25 amid fiscal optimism and a more positive Eurozone outlook

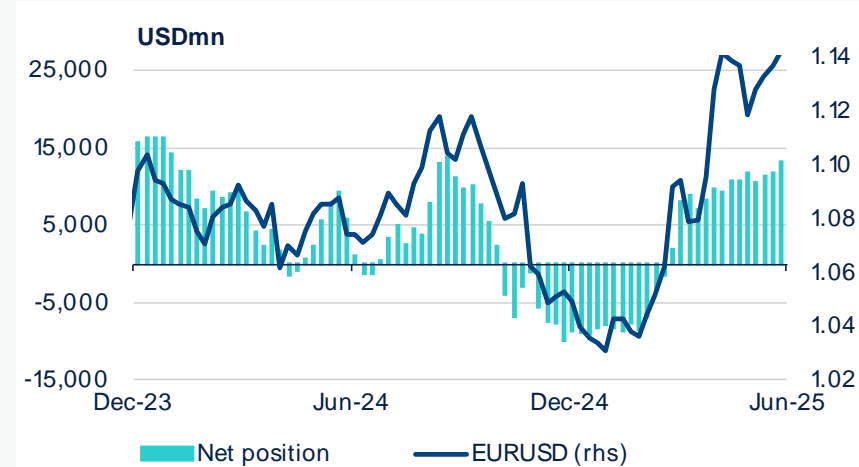
Non-commercial accounts exited long USD positions, triggering a sharp correction

Source: Bloomberg and BBVA FX Strategy



EUR positioning followed suit, turning bullish as fiscal prospects improved

Source: Bloomberg and BBVA FX Strategy



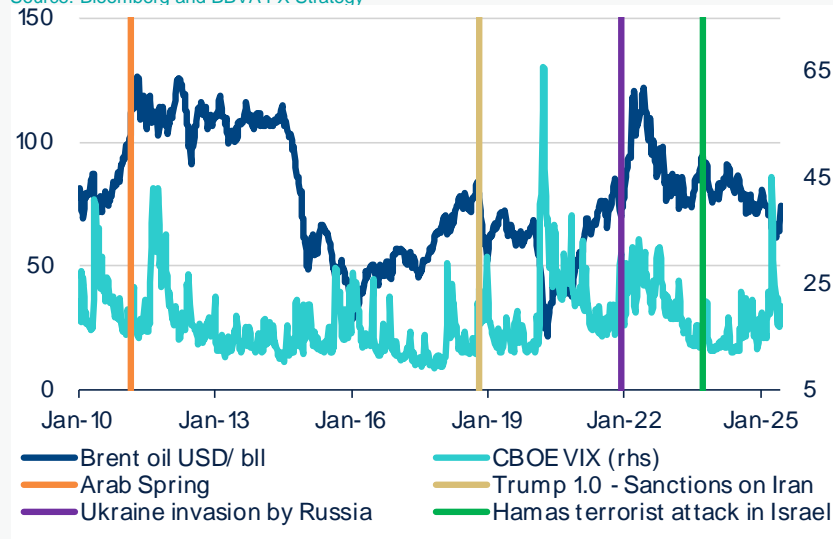
Middle East instability sparks volatility and inflation risks

“History doesn't repeat itself, but it often rhymes”

Mark Twain

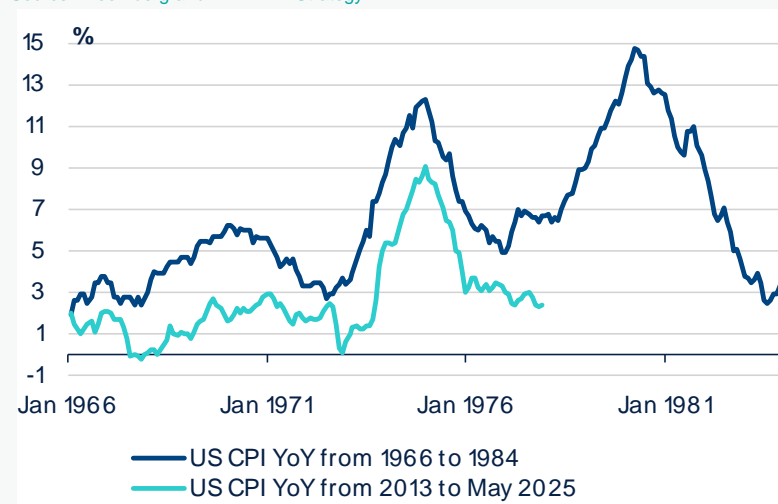
Geopolitical instability typically leads to heightened oil prices and increased market volatility

Source: Bloomberg and BBVA FX Strategy



From a macro standpoint, stagflation remains the key risk emerging from the regional instability

Source: Bloomberg and BBVA FX Strategy



Market consensus supports further USD weakness

Market consensus(%)

Source: Bloomberg

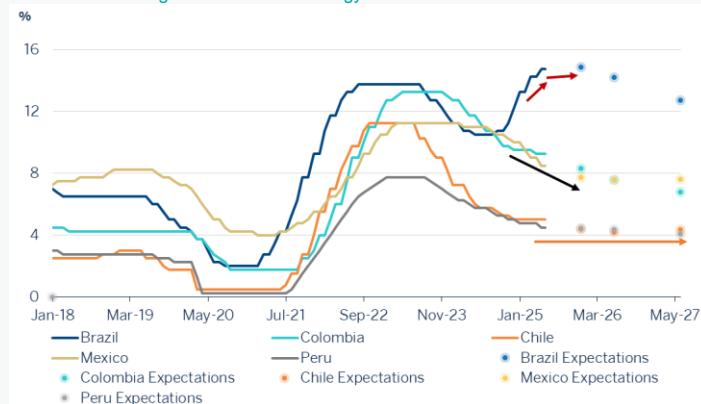
	Q3 25	Q4 25	Q1 26	Q2 26	2026	2027	2028
EURUSD (June25)	1.15	1.15	1.17	1.18	1.2	1.19	1.18
EURUSD (December24)	1.04	1.05			1.08	1.08	1.12
USDJPY (June25)	142	140	138	136	135	130	122
USDJPY (December24)	146	145			140	136	126
GBPUSD (June25)	1.35	1.36	1.37	1.37	1.38	1.39	1.37
GBPUSD (December24)	1.27	1.28			1.29	1.31	1.36
USDCHF (June25)	0.82	0.82	0.82	0.81	0.82	0.84	0.88
USDCHF (December24)	0.9	0.89			0.9	0.88	0.88
USD INDEX (June25)	98.8	97.6	96.7	96	94.4	94	93.5
USD INDEX (December24)	106.7	106.1			102.2	100.1	97.9

LatAm FX has recovered amid USD weakness

- **Momentum shifts** – LatAm currencies have seen large swings. 2024 was weak, early 2025 saw recoveries, while April saw renewed weakness amid the latest tariff tantrum. Since then, LatAm FX has recovered the April losses and more, in several cases setting multi-month highs. Part of this is due to USD weakness as global investors look to diversify exposure away from USD, even if LatAm FX is not necessarily the obvious choice as a diversifier from USD.
- **Valuations less favourable** – The gains in 2025 have unwound some of the more extreme short positioning and undervaluations.
- **Emerging Asia are likely still more at risk.** They may face tariffs directly or suffer from spill-overs as China. Asia seems more exposed given the latest tariff focus on China.
- **Differentiation** – Each LatAm currency has had its own issues, or at least differing exposures to the various concerns across LatAm. These include concerns regarding global growth (China and the US in particular), fiscal sustainability, and US policy shifts (tariffs in particular).

Monetary policy cycles remain divergent

Note: Market pricing used except for Colombia and Peru which use survey data
Source: Bloomberg and BBVA FX Strategy



LatAm FX has recovered tariff tantrum losses – and in some cases even more, reaching multi-month highs

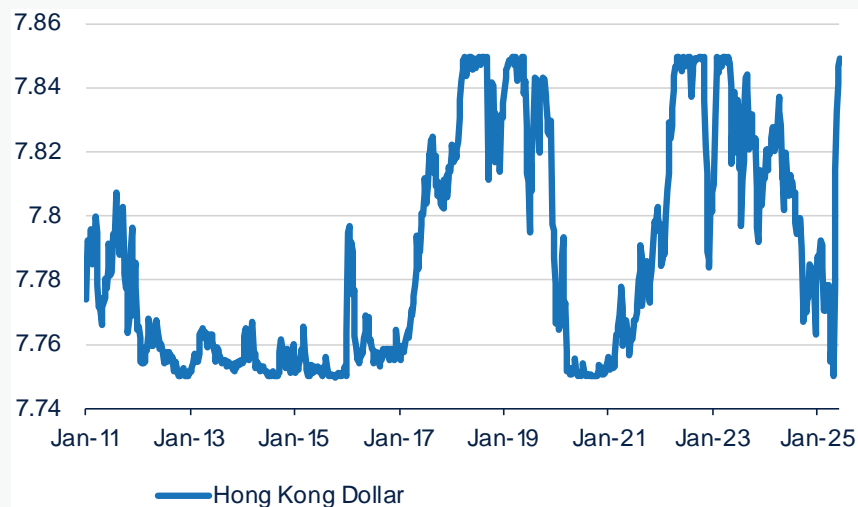
Source: Bloomberg and BBVA FX Strategy



Asian FX reaction to US trade policy

The HKD reached the upper end of the intervention band, but a formal regime change remains unlikely

Source: Bloomberg and BBVA FX Strategy

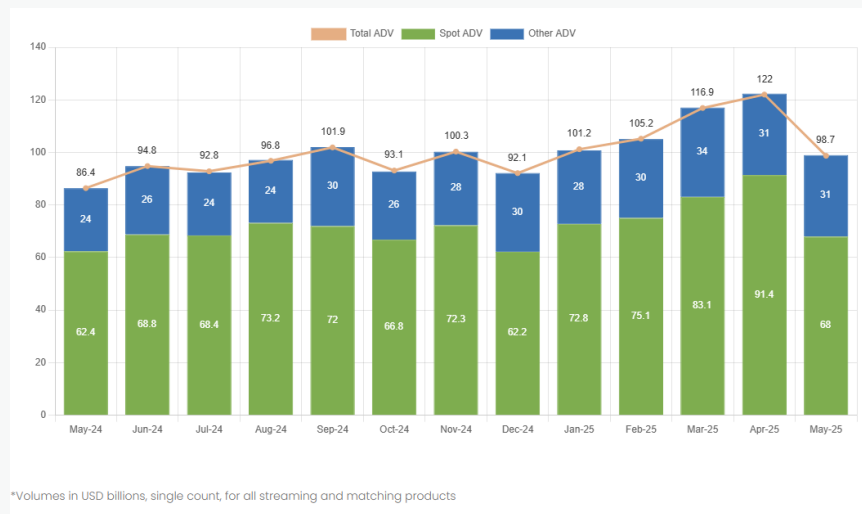


- The HKMA has actively sought to prevent a confidence crisis in the currency peg
- Hong Kong's significant trade exposure to China leaves it vulnerable to the 145% tariff regime, with trade-related activity amounting to approximately 320% of GDP
- The external balance remains strong, with a current account surplus of 13% of GDP in 4Q25
- The territory's net international investment position stands at 514% of GDP, substantially higher than the broad money supply
- Given historical precedent, Hong Kong SAR may follow a trajectory similar to the late 1990s, with the currency peg remaining internal adjustment

FX volumes dip in May but remain strong in 2025

FX Spot Stream Monthly Volumes

Source: FX SpotStream



Other Venues

May average daily volumes

- **LSEG FX:** USD 110Bn spot (-18.5% MoM / +18.3% YoY)
- **EBS:** USD 67Bn spot & NDFs (-25% MoM / +25.2% YoY)
- **360T:** EUR 32.7Bn spot (-17.4% MoM / +24.3% YoY)
- **CLS:** USD 2.254 Tn all products (-11.3% MoM / +11.4% YoY)

Questions and talking points

1. How does the recent escalation of the conflict in the Middle East impact currency markets?
2. Outlook and key volatility triggers for 2H25?
3. Further downside for USD and continued EUR strength tied to EU fiscal stimulus and portfolio inflows in 2H25?
4. EM carry trades to remain in vogue?
5. GENIUS Act recent approval by US Senate. Thoughts?

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