

FX Viewpoint

Currencies
Global

USD, EUR, and NZD: Geopolitics and rates

- ◆ The USD is likely to remain range-bound over the near term amid geopolitics
- ◆ The EUR appears to lack a clear directional path
- ◆ The RBNZ’s hawkish hold has buoyed the NZD, while global risk sentiment dominates

The US and Iran have reached a tentative deal to extend a ceasefire by 60 days, pending President Trump’s signoff; the deal would require Iran to remove all mines from the Strait of Hormuz within 30 days (Bloomberg, 29 May). But, unless there is a clear resolution to the Middle East stalemate, **the USD is likely to extend its recent sideways trend and remain range-bound over the near term.** The geopolitical impasse is allowing other factors, alongside energy prices, to play a larger role in FX.

With the Middle East stalemate, the USD is likely to trade sideways over the near term

Key theme: Interest rate differentials

Over the coming weeks, interest rate differentials are likely to be the primary market focus. **The Federal Reserve (Fed) is still shifting from dovish to more hawkish,** whereas this transition is already largely priced in for Europe. This should help underpin the USD (Chart 1) but may not be sufficient on its own to trigger a sustained USD rally.

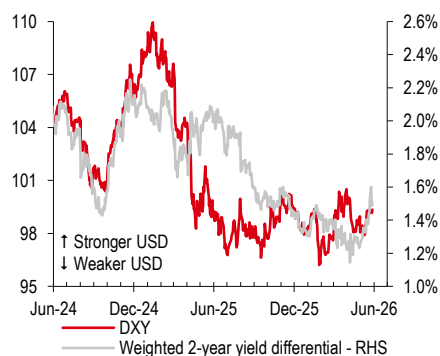
Interest rate differentials are likely to gain market attention

EUR: Limited scope for a standalone move

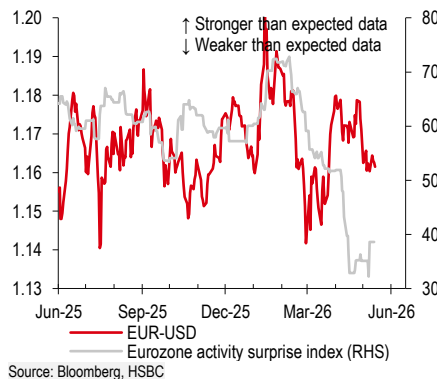
With a steady USD as the backdrop, there appears to be limited scope for a sizeable, EUR-specific move. Markets are pricing in around 60bp of the European Central Bank (ECB) hikes by year-end (Bloomberg, 28 May). However, with **growing signs of weaker activity** (Chart 2), it may be difficult for the ECB to deliver a path that is materially more hawkish than current expectations. **The EUR reaction to a less hawkish ECB is uncertain** – markets may favour growth support or reprice lower on carry considerations, but the balance of risks is to the downside for now.

With limited EUR-specific catalysts, the EUR is unlikely to break out decisively, though risks are tilted to the downside

1. US Dollar Index (DXY) and its interest rate differential



2. EUR-USD and Eurozone activity surprise index



NZD: Policy expectations and risk sentiment

The NZD is now in focus after the Reserve Bank of New Zealand (RBNZ) held rates at 2.25% on 27 May in a finely balanced decision, with a hawkish signal via a higher projected rate path (including a 25bp hike in 3Q26, at least one in 4Q26, and a gradual rise towards 3.3% by 4Q28). **Our economists expect RBNZ tightening to begin in 3Q26,** followed by another hike in 4Q26, and three additional increases, taking the policy rate to 3.50% by 3Q27. Market pricing is more hawkish, with around three hikes fully priced in by end-2026 (Bloomberg, 28 May). Beyond rates, the **NZD should remain highly sensitive to global risk sentiment** over the near term.

The RBNZ’s balanced hold and hawkish guidance have supported the NZD

Disclosure appendix

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