Market Watch

USD/CHF remains under pressure

Summary

Event: The Swiss Franc has strengthened significantly in recent days, despite policy rates being cut to zero, as the US Dollar weakness and safe-haven demand takes hold.

Market reaction: USD/CHF fell below 0.79 on 1-Jul while EUR/CHF held in a tight range between 0.93-0.94.

Investment strategy: A short-term rebound in USD/CHF is expected as excessively bearish USD positioning unwinds. Initial resistance is at 0.8060, subsequent resistance is at 0.8200. Beyond the next few weeks, though, downward pressure on USD/CHF is likely to persist amid a weak USD, deflationary pressures in the Swiss economy and bouts of safe-haven demand. Next support is at 0.7770.

More broadly, carry trades – a strategy where investors borrow in a currency with low rates and invest the proceeds in a currency with higher rates – are likely to remain under increasing pressure as the USD stays weak and the rate gap slowly narrows. The market focus is likely to shift towards more idiosyncratic opportunities, such as currently low HKD rates.

Understanding the drivers

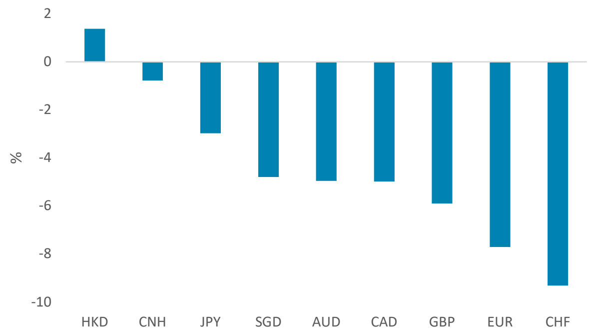
CHF strengthens despite the SNB's best efforts. The Swiss economy continues to face deflationary pressures, pushing the Swiss National Bank (SNB) to cut rates to zero. Nevertheless, the CHF has continued to strengthen against the US Dollar because (i) the US Dollar has weakened broadly against most major currencies, (ii) markets currently view the CHF as a safe haven from US trade policy uncertainty, and (iii) negative inflation means real (net-of-inflation) yields offer some support despite zero nominal rates.

Currency strength overwhelms low borrowing costs. The CHF has gained over 10% against the USD since the start of Q2, overwhelming its c.4% borrowing cost advantage that has made it a popular funding currency for carry trades.

Weak USD the biggest challenge to the carry trade. As the first chart illustrates, carry trades that aimed to own USD-denominated assets while taking advantage of low funding costs in other currencies faced significant losses given USD weakness. Over Q2 2025, for example, long USD carry trade returns (spot + interest rates) were highest when funded in HKD and lowest when funded in CHF. Strategies funded in JPY – another favoured low-rate funding currency – performed less poorly than CHF, but still resulted in negative returns. Strategies funded in some major Asian currencies fared better.

CHF resilience more than outweighed its low rates amid a weak USD in Q2 this year

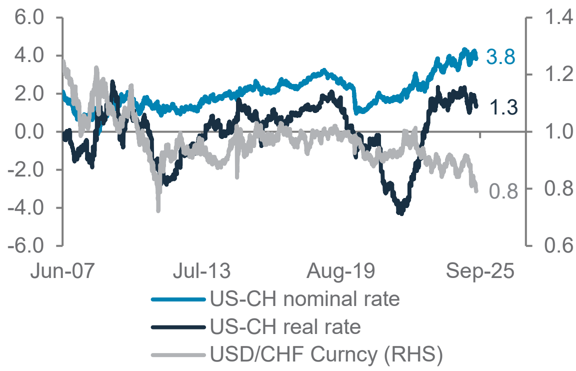
Performance of carry strategies that are long the USD and funded by each of the following currencies over Q2 2025



Source: Bloomberg, Standard Chartered

USD/CHF has fallen more than what rate differentials alone (nominal or real) would suggest

USD/CHF vs. interest rate differentials



Source: Bloomberg, Standard Chartered

What does this mean for investors?

A USD/CHF rebound is likely to be short-lived. After a move of the kind witnessed in Q2, it is tempting to conclude USD/CHF is set for a rebound.

Technicals argue a short-lived rebound over the next 2-4 weeks is possible – short-USD investor positioning has turned excessive and is ripe for a reversal while USD/CHF technical indicators (RSI) similarly argue the pair is oversold. In the next 2-4 weeks, this points to a rebound towards initial resistance at 0.8060. Secondary resistance is at 0.8200. However, the lack of long-term support means that a subsequent test of support at 0.7770 is expected.

USD/CHF rebounds lack long term support. A sustained rebound, or a stabilisation around current levels, is likely to require one or more of the following events to occur:

(i) **The SNB intervenes, either verbally or directly. This appears unlikely without a firm US-Swiss trade deal and Fed-SNB coordination.** Even in such a scenario, though, we would be mindful that, historically, one-sided FX market interventions have usually resulted in a temporary, rather than permanent, impact on the underlying currency pair.

(ii) **The Fed goes on an extended pause, or raises rates.** Such an outcome is likely if our risk scenario of higher-than-expected inflation were to play out, though it is not clear whether USD/CHF-supportive rate differentials or USD/CHF-negative safe-haven demand would dominate in such a scenario.

(iii) **A reversal of the De-Dollarisation debate.** It remains difficult to make a case for significant USD/CHF upside in the face of a weak (or weaker) US Dollar. A reversal of the de-dollarisation debate would likely mean a much better-than-expected outcome on trade deals in Q3.

On balance, we see the chances of such scenarios to be low. Hence, we see a poor risk/reward in being bullish USD/CHF beyond very short-term trades.

Carry trade focus to shift to more idiosyncratic opportunities

The risk/reward of new carry trades is arguably poor in a weak USD environment. A combination of a weak USD and safe-haven demand for low-rate currencies makes carry trade strategies less rewarding. While new pairings of high carry and low-rate currencies are likely to eventually emerge, for now the focus is likely to shift to more idiosyncratic opportunities.

Unusually low HKD rates one such example. Despite its pegged range to the US Dollar, short-term rates in HKD remain unusually low, likely a result of excessive HKD liquidity. While history shows us this is unlikely to last once markets return to equilibrium, several reports have highlighted the persistence of this unusually wide gap in HKD and USD rates.

Low volatility currencies another possible focus. As we pointed out in our last Market Watch on carry trades (see *Time to reduce FX risk*, 21st April 2025), currencies with relatively low volatility are likely to become more attractive to carry traders looking for funding alternatives, even if they do not have the lowest borrowing costs. Many Asian currencies may rank relatively high on this combination of metrics.

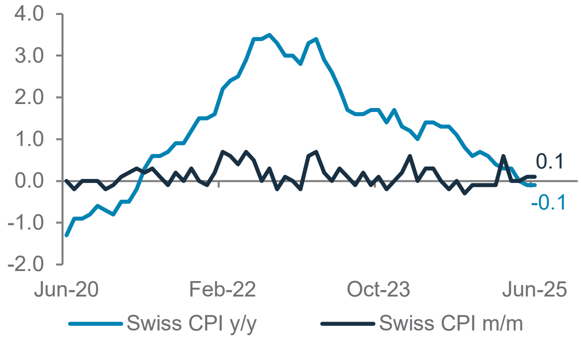
SNB focus is expected to be as much on EUR/CHF as USD/CHF, especially if it considers intervention

EUR/CHF

Source: Bloomberg, Standard Chartered

Swiss inflation has fallen steadily since 2023 and is currently just below 0% y/y

Swiss CPI y/y and CPI m/m



Source: Bloomberg, Standard Chartered

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