

FX Daily: Hard to turn any less bullish on USD

We might see some tentative signs of stabilisation in risk sentiment today, but we think that a number of USD-positive factors (hawkish re-pricing of Fed expectations, US debt-ceiling concerns and lingering Evergrande fears) will keep any dollar correction short-lived. Meanwhile, central bank speakers in Sintra may have an overall contained impact



➔ USD: Supported by multiple factors

The current market environment appears to offer the perfect combination of factors for a supported dollar. Inflation-related fears and higher yields dealt a blow to global equities, as US stocks faced their worst trading day since May yesterday. Any signs of recovery in risk sentiment during the Asian session overnight were held down by market concerns about another potential missed coupon deadline by Evergrande today (last week's deadline for a dollar interest payment was also breached), while Fitch cut the company rating again – now to one notch above default level.

Incidentally, the dollar has received an extra lift from rising USD short-end yield, as markets appeared to start aligning with the Fed's Dot Plot after having largely dismissed it as too hawkish last week. Today, Federal Reserve Chair Jerome Powell is on the list of central bank heads speaking at the European Central Bank forum in Sintra, as his future appears to be under question again after Senator Elizabeth Warren announced she will vote against his confirmation as Chairman.

Powell's comments should fall somewhere close to yesterday's tone at his Senate testimony and may not move the dollar significantly today. One thread investors should however remain highly focused on is the US debt ceiling standoff, as yesterday's comments by Secretary Janet Yellen about the risks of the Treasury running out of cash sooner than previously thought continued to pressure the already vulnerable bond segment. The latest news is not very encouraging in this sense, as the Democrats reportedly gave up on their plans to merge a proposal for a debt limit increase and the stopgap funding into the same bill. The uncertainty around the timing of debt-ceiling legislation may continue to unnerve debt markets that are already weighing inflation and tightening concerns. Ultimately, this should contribute to keep any dollar weakness caused by improvements in the risk environment as short-lived, in our view.

➔ EUR: Sintra may go down as non-event

The EUR was amongst the least hit currencies yesterday as a generalised risk-off environment mostly hit high-beta FX. To be sure, no particular support to the EUR is coming from the Sintra ECB Forum, as President Christine Lagarde reiterated her quite relaxed stance about inflationary pressures yesterday whilst warning against “overreacting” to any temporary price shocks.

Given the lingering dovish stance by the ECB, the FX impact of upside surprises to the eurozone's CPI numbers released between today and Friday (tomorrow we'll see Germany and France's numbers) may be quite limited. For today, some improvement in risk sentiment may offer some support to EUR/USD, but we think any rebound in the pair may lose steam around the 1.1750 highs seen last week.

⬆ GBP: Overstretched downside?

GBP sensitivity to global risk sentiment has continued to rise, and yesterday's sell-off in equities saw the pound underperforming the G10 commodity FX segment. Such downside pressure on GBP, however, does not appear to be linked to any re-pricing in the Bank of England rate expectations, which have remained broadly unchanged after the BoE meeting last week. Let's see today whether Governor Andrew Bailey will give markets reason to cement their hawkish views as he participates in Sintra's forum.

At the same time, it will be interesting to see how much weight is given by investors to the latest Brexit developments, after the UK limited access of French fishing boats by granting only 12 licences. The risks are that investors see any dispute on fishery as a signal of broader diplomatic/trade tensions between the EU and the UK, although that appears a bit premature for now.

All in all, we suspect the pound may have over-reacted to the risk-off environment yesterday, and unless Bailey gives us reason to doubt the current pricing on BoE tightening today, we could see GBP rebound more than other currencies to any sentiment stabilisation.

➔ SEK: Eyes on data, but Riksbank still far from changing tone

Like the EUR, the low-yielding Swedish krona appeared less vulnerable than other G10 currencies to the hostile risk environment. We'll keep an eye on some domestic factors possibly affecting SEK today. In particular, September's Economic Tendency Survey, which will be released along with consumer confidence data. Like in the eurozone, it will be worth monitoring how much of a drag on business confidence has been generated by the combination of supply disruptions and the spread of the Delta variant.

We'll also have two Riksbank speakers today (Bremán and Flóden). Markets are awaiting for any slight shift-away from the very dovish tone at the central bank, but our suspicion is that this tone will hardly change by end of the year. We think we'll continue to see EUR/SEK oscillate within a tight range (10.12/10.22) in the coming days.

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