

FX Daily: Good news seems priced into the dollar

The market reaction to higher US inflation on Tuesday was muted, suggesting a lot of good news has already been priced into the dollar and US Treasuries



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⬇️ USD: A lot of good news seems to be priced in

Despite the upside surprise to US CPI yesterday, the reaction in markets was contained and to some extent surprising – a lower US dollar and lower US Treasury yields. This likely indicates that US inflation and growth stories are in large part priced in, the market doesn't expect the Federal Reserve to overreact and with the [USD positioning now close to neutral](#) (vs meaningful shorts at the start of the year) this suggests less scope for a USD rebound, particularly as it screens expensive against most G10 FX based on our short term valuation measures. The well received 30y US Treasury auction yesterday also provided a case in point. As vaccination in Europe is set to gain pace and eurozone activity is poised to level up with the US in the second half of the year, the less diverse and more synchronised recovery should weigh on the USD.



EUR: Recovering as USD is losing steam

As USD upside is losing steam, we are observing an EUR/USD uptrend. We expect EUR/USD to move above 1.20 on a persistent basis this quarter as the eurozone economy starts to catch up with the US. In Sweden, all March CPI inflation measures are expected to rise, but the Riksbank will look through this as the increase is driven by temporary factors and CPI should move lower again in 2H21.

📈 GBP: The Haldane resignation effect to be short-lived

Sterling sold off yesterday in response to the news of the resignation of Bank of England Chief Economist Andy Haldane. Although a big hawk, his departure shouldn't alter the pound's prospects for the coming months as no imminent BoE tightening was on the table (like for the Fed, it is a story for 2023). The fact that the market pricing of the BoE policy path was largely unchanged yesterday provides a case in point. Plenty of bad news now seems to be priced into GBP (EUR/GBP trades 1.3% overvalued based on our short-term valuation model) and with the UK vaccination programme powering ahead, GBP should recover in coming weeks.

➡ CEE: Back to fundamental price action after the positioning driven moves

In the Central and Eastern European FX space, we continue to observe diverging price action between the Czech koruna on the one hand, and the Polish zloty and Hungarian forint on the other. After heavy CZK underperformance late last week, the currency rebounded meaningfully yesterday while PLN and HUF weakened. We see the latest CZK outperformance as justified by the stronger fundamental outlook (mainly on the monetary policy front), with CZK weakness late last week being driven more by positioning (i.e. profit taking) – the same is true for PLN and HUF, but from an overcrowded shorts perspective (vs longs for CZK). We look for more CZK strength in the weeks and months to come (targeting EUR/CZK 25.50), while HUF should experience some tough months ahead due to the challenging CPI outlook. We also favour the Romanian leu for carry purposes and its limited weakening potential from here.

Author

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

chris.turner@ing.com

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

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