

FX Daily: A week of key inflation tests

We expect an above-consensus 0.4% core PCE read on Thursday, which should support the dollar this week. Eurozone inflation numbers will also be in focus. We expect a decline in the core rate below 3.0%, but there are risks of an upside surprise. In Japan, inflation may fall below 2.0% and hit the yen, while the RBNZ should resist the temptation to turn dovish



➔ USD: One (last?) week of strength

As discussed in our recent monthly [FX Talking](#) update, US disinflation-linked trades are facing mounting obstacles which are keeping the dollar at reasonably strong levels, despite the consensus view that the greenback will ultimately capitulate on Fed rate cuts later this year. Our call has been for dollar resilience to last at least until the end of February, in line with our view that January PCE figures will come in on the strong side.

The release of the PCE deflator on Thursday is one of the key highlights in the US calendar this week, and our economics team forecast an above-consensus 0.4% month-on-month core read on the back of insurance, medical and portfolio management fees inflation boost. Personal consumption figures may come in softer than expected, but other activity indicators like the Conference Board Consumer Confidence and the ISM manufacturing should inch higher. Today,

new home sales figures are in focus.

All in all, we expect this last week of February to encourage less aggressive bets on Fed easing. Market pricing is falling between three and four rate cuts by year-end, with a move in June 80% priced in. We see USD rates receiving one – potentially final – round of support on the back of strong PCE figures and the dollar to have a good week. Our outlook beyond the short-term remains bearish on the dollar as we think markets are underestimating the size of Fed easing.

Elsewhere in the developed space, the Reserve Bank of New Zealand announces policy and releases new projections on Wednesday. As discussed in our [New Zealand macro update](#), the impact of rising net immigration is looking increasingly inflationary, and the slower than expected deceleration in non-tradeable CPI may discourage the RBNZ from delivering a clear dovish pivot as it keeps rates unchanged this week.

In Japan, Tokyo's CPI numbers for January (released overnight) are expected to show both headline and core inflation moving to 1.9%, falling under the 2.0% Bank of Japan target for the first time since March 2022. This may well prompt markets to price out a June hike and add buying pressure to USD/JPY beyond the 150.90 February highs and potentially testing the 151/152 November highs.

Francesco Pesole

➔ EUR: Lagarde speaks ahead of Friday's CPI

Our economists forecast the eurozone's CPI numbers on Friday to come in line with consensus: 2.5% headline and 2.9% core rate. A drop in core inflation below 3.0% may prompt European Central Bank doves to raise their voices, but the consensus within the Governing Council appears directed at waiting for early-2024 wage data before taking steps to ease policy. Incidentally, risks are probably skewed towards a stronger CPI reads in parts of the euro area, like France, where energy taxes are being reintroduced.

As discussed in the section above, we expect a good week for the dollar thanks to a strong PCE on Thursday. Before then, EUR/USD may struggle to find much sense of direction and keep hovering around the 1.0800 gravity line.

One event to watch today is ECB President Christine Lagarde participating in a plenary debate in the EU Parliament. Politicians generally put pressure for an earlier untightening of financial conditions, but Lagarde may not derail much from her hawkish tone before seeing February's CPI numbers.

Francesco Pesole

➔ GBP: BoE speakers in focus

The week is very quiet in the UK data-wise, and the focus will be on a few Bank of England speakers. As discussed recently, the BoE has – unlike the ECB – let the data do the “hawkish” talking, and recent comments from Governor Andrew Bailey and others have tended to endorse market rate cut expectations. At the moment, the Sonia curve embeds around 70bp of easing by year-end.

Today, BoE Chief Economist Huw Pill will give a speech along with Deputy Governor Sarah Breeden.

Both are generally seen as neutral members, making any policy comments particularly interesting. Later this week, Dave Ramsden and the arch-hawk Catherine Mann are also scheduled to speak.

We see downside risks for GBP/USD as PCE inflation data in the US could help the dollar, with the pair potentially testing the 1.2530 14-February low. EUR/GBP will be affected by today's speech from Lagarde and eurozone CPI data on Friday. Here, we expect some stabilisation around the 0.8550 mark.

Francesco Pesole

➔ CEE: Data confirming weak region performance

The calendar for this week should be less busy than previous days. Today, the calendar is basically empty. The Hungarian National Bank is scheduled to meet tomorrow. We expect the pace of rate cutting to accelerate from 75bp to 100bp, which would mean a rate cut to 9.00%. On Wednesday in the Czech Republic, we will see January PPI. Thursday will see the release of final fourth-quarter GDP in Poland, which grew 1.0% year-on-year according to the flash estimate. We expect the number to be confirmed but we will see a decomposition of growth.

We will see the same numbers in the Czech Republic on Friday, and we will also see the state budget result for February. Speaking of which, Fitch upgraded the rating outlook from negative to stable last Friday, as we expected, because of the improved fiscal outlook. We will also see PMI numbers across the region on Friday, which are likely to reaffirm the worse outlook for the industry. We will also keep an eye on politics this week. The Hungarian parliament will vote today on Sweden's admission to NATO. Tomorrow the V4 group will meet in Prague. We'll also likely learn the presidential candidate in Hungary this week.

EUR/PLN broke the 4.310 level on Friday, which has been a hurdle for some time, following positive news on the unlocking of EU money. This was also supported by a fall in core rates supporting PLN. However, with core rates moving down slightly ahead of the end of CEE trading, we are likely to see local rates catching up with core rates today, reversing Friday's FX gains. So the question is whether or not the EU story proves more supportive of PLN for now. We think it is more likely to do so despite heavy long positioning in PLN. Even so, we will see the first pullback to or above 4.310 today and more gains later.

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