FX Daily: Big day for the Czech National Bank

Global FX markets are consolidating ahead of the next big input to the Fed tightening equation - US April CPI. Given that base effects should drag the annual rate lower, the focus will be on the monthly figures, with core inflation expected at a still high 0.4%. Elsewhere, we may find out today who is going to be the next Czech National Bank governor

USD: Higher core inflation should keep Fed tightening intact

Global FX markets appear a little calmer today, helped by some stability in Chinese asset markets. Despite the ongoing lockdown in Shanghai, Chinese equities are up over 2% today and the renminbi seems to have found some temporary support. Recall that the re-pricing of China's growth and asset markets over recent weeks has been a major contributor to commodity currency and emerging market FX weakness and a further support to the dollar. The current stability looks fragile, however. Until we see some major fiscal support coming through in China or policymakers adopt an alternative strategy to Covid (which seems very unlikely) the risks to USD/CNY remain skewed to the 6.80 area.

Another issue that has perhaps un-nerved some investors recently has been the stablecoin

TerraUSD 'breaking the buck'. As a stablecoin, it is in theory pegged to the dollar 1:1, but currently trades at 77 cents. Reportedly, it only has a market capitalisation of US$16bn, but developments here will be tracked closely for what, if anything, they mean for larger stablecoins such as Tether.

Tension in equity and credit markets earlier this week has seen pricing of the Fed tightening cycle cut by 10-15bp. Yet rhetoric from the Fed remains very hawkish. The message seems to be that the policy rate needs to be taken to neutral as quickly as possible and then the Fed will see if it needs to do more (not less) tightening. Feeding into that story will be today's US April CPI release. Headline year-on-year inflation may well be past its peak, helped by base effects and used car prices, yet the focus will still be on the core month-on-month figures. A still high 0.4% MoM core inflation increase is expected today. Unless that surprises at something like 0.2% MoM, we would expect the dollar to stay largely bid - or consolidate near the highs.

DXY could trade in a 103.20-104.00 range and barring a very soft CPI figure we see no reason for a sharp dollar sell-off.

EUR: ECB tightening expectations quite steady

We have seen lots of commentary from the European Central Bank over recent weeks, where the core message seems to have been a more hawkish one - managing expectations towards the first hike in July. Somewhat surprisingly, market expectations for ECB policy rate changes this year have been quite steady over recent weeks, with 85bp of hikes now priced in. We have a whole host of ECB speakers today, who will probably support that pricing. Yet we doubt EUR/USD derives much support until Fed tightening expectations falter - and that seems unlikely.

EUR/USD one month traded volatility is coming off its highs at 9% and points to a slightly more consolidative environment. 1.0500-1.0600 may be the near-term range. But with the EU moving ever closer to a full embargo on Russian energy - with negative implications for European growth - the 1.0500 floor in EUR/USD does not look particularly strong.

Elsewhere, we note today's agreed cash deal by Philip Morris to acquire Swedish Match for US$16bn. That is a big figure and we can but speculate that this was one of the reasons why the Swedish krona was so strong in April at a time when the rest of European FX was suffering. 10.50/10.60 levels in EUR/SEK may be more appropriate for the near term until European FX, in general, finds its footing.

GBP: Waiting on tomorrow's data dump

EUR/GBP is consolidating in a 0.8500-0.8600 range ahead of tomorrow's data dump - which includes 1Q22 GDP and March activity data. Expect further range trading, although politics is never far from sterling and could weigh on it at any time. Here UK-EU trade relations seem to be deteriorating again, with Downing Street threatening to unilaterally suspend parts of the Northern Ireland protocol. Doing so could spark an unwelcome trade war.

GBP/USD is consolidating after heavy losses. A technical correction could see 1.2500 (1.2600/1.2660 looks too far) before the bear trend resumes to drag GBP/USD to 1.20. That certainly looks the direction of travel over coming weeks and months.

CZK: A new central bank governor could be announced today

Here we are largely repeating what we wrote on Monday - because we think it is important. Czech media is saying that we could today hear the decision, taken by the Czech President, on the next governor of the Czech National Bank (CNB). EUR/CZK spiked on Friday afternoon after Czech media reported that the CNB dove, Ales Michl, would likely be the successor to outgoing governor Jiri Rusnok whose term ends in June. Given that the CNB has been one of the most hawkish central banks in the world over the last few years, this has naturally raised much uncertainty.

EUR/CZK volatility looks assured over the next two months as the existing hawks have one last chance to express themselves at the 22 June meeting. Yet, the Czech koruna may remain fragile on a potentially big shift in direction in the second half of this year. Confirmation today that Ales Michl will be the next governor could hit the koruna again and usher in a period of underperformance against the Polish zloty, where the local central bank may be taking the policy rate as high as 8.5% later this year.

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