

FX Daily: BoJ hike and China tariff threat unwinding

The Bank of Japan delivered a well-telegraphed 25bp hike, but surprised markets on the hawkish side by materially raising its inflation forecasts. We expect two more hikes this year which can pave the way for a stronger JPY outlook. In other news, Trump surprised by saying he'd rather not hit China with tariffs, adding short-term pressure on the dollar



- At the World Economic Forum in Davos, President Trump said he'd rather not hit China with tariffs

📌 USD: Trump scales back China tariff threat (for now)

Donald Trump's address in Davos yesterday included most of the threats related to implementing his America First vision – something markets are becoming accustomed to. Comments on oil prices and interest rates seemed to attract more headlines. Trump said OPEC should increase production to allow a decline in oil prices, which led to another leg lower in oil prices which have been under pressure since touching multi-month highs last week. The new administration plan is to drive down energy costs and by extension interest rates.

Trump also said that he will discuss with Federal Reserve Chair Jerome Powell his view on rates “at the right time”, which probably suggests the government's pressure shouldn't be felt just yet when the FOMC meets next week. As discussed in our [Fed meeting preview](#), we expect a decision to hold rates steady next week will not be the trigger of another round of USD longs unwinding.

Overnight, the dollar did however take a hit as Trump surprisingly told Fox News he'd rather not impose tariffs on China. This seems to feed into the growing sense that Trump is underdelivering on protectionism compared to pre-inauguration remarks, and that ultimately some of those tariff threats may not materialise as long as some concessions are made on trade.

We would not be entirely surprised if Trump's next comments on the matter point in the opposite direction. But barring that, the dollar momentum may remain soft today. On the data side, watch for US S&P Global PMIs today – expectations are for a small recovery in the manufacturing index – and home sales data (the latter for December).

Francesco Pesole

📈 EUR: 1.050 now looking feasible

January's preliminary PMIs for the eurozone are released this morning, and consensus is looking for a slight improvement in the manufacturing figure from 45.1 to 45.4, with the composite number expected to flatten just below the 50 contraction line. With external uncertainty staying high and the prospects of European Central Bank cuts already factored in, the case for a rebound in the eurozone's business confidence in the short term is not very compelling. This should ultimately allow the ECB to stick to the plan of taking rates towards 2% this year.

President Christine Lagarde delivers remarks in Davos today after having reiterated the guidance for gradual cuts earlier this week. That echoed what we have heard from other ECB members – even the more hawkish ones – and next week's expected rate cut should be accompanied by a similar message that may just leave the market unfazed.

EUR/USD has received another small boost from Trump's seemingly benign comments on China tariffs. The risk premium (i.e. short-term undervaluation) in EUR/USD has been halved from 3% to 1.5% since 9 January. We are not convinced that the gap will be entirely closed given lingering uncertainty about Trump's trade hostility against the EU. But unless PMIs disappoint today, that China headline overnight has likely paved the way for testing 1.0500 in the coming days.

Francesco Pesole

📈 JPY: Hawkish BoJ hike

The Bank of Japan [hiked rates](#) by 25bp this morning, in line with market expectations and consensus. Markets are still assessing Governor Kazuo Ueda's press conference as we write, but the reaction in the yen to the whole event signals a hawkish surprise, primarily related to the upward revision in headline and core CPI forecast projections.

Policymakers now expect 2.4% inflation (up from 1.9%) in 2025 and the BoJ added that it will "continue to raise the policy interest rate and adjust the degree of monetary accommodation", echoing the language used in the July statement. Some previous remarks by Ueda on potentially delaying the hike if markets proved too volatile following Trump's inauguration have been clarified, with the statement highlighting that "markets have been stable on the whole".

USD/JPY briefly traded below 155.0 this morning before paring back some losses as Ueda delivered a rather cautious tone at the press conference. He gave no indication about the timing for the rate hike or the pace of further tightening. Two-year JPY swap rates are up only modestly to 0.74%, signalling there is still room for a hawkish repricing down the line to help the yen. We now expect

two more hikes in May and October this year, which would help the yen counter the generalised dollar strength and keep some pressure on USD/JPY into the 155.0 mark.

Francesco Pesole

📈 CEE: February CNB rate cut seems like a deal done

In the Czech Republic, consumer confidence for January will be released and we could potentially hear more from the Czech National Bank before the blackout period begins on Thursday next week. On Wednesday, we heard from CNB board member Jan Prochazka confirming that the February meeting may see a resumption of the cutting cycle after a pause in December, which is our forecast. However, it is important to recall that Prochazka was one of the two members who voted for a cut against the consensus in December. So it would be good to hear a dovish tone from other board members as well, but a rate cut in February seems very likely unless January inflation, released on the day of the meeting, surprises to the upside significantly.

In line with expectations, the Central Bank of Turkey cut rates again by 250bp to 45% [yesterday](#). As expected, the post-meeting statement suggests further rate cuts supported by disinflation. While inflationary risks persist in the near term, relatively high real rates and recent tightening in loan growth caps should keep disinflation from continuing. We expect 25.5% inflation and a 27.5% policy rate at the end of 2025 with risks skewed to the upside. USD/TRY remained essentially unchanged leaving investors with a fat carry, however, we expect the lira to return to its usual trajectory of managed nominal depreciation after two days of stability.

The CEE region continued its swift rally yesterday with Poland's zloty leading gains. EUR/PLN touched 4.210 yesterday, a new low, and it looks like momentum may lead to a test of 4.200 soon. Although valuations are pointing to significantly higher levels, the narrative and market positioning support a stronger PLN. Thus, after breaking key 4.250 levels, we see EUR/PLN gapping down with short positions closing and flipping into new longs. Of course, the National Bank of Poland's hawkish tone supports a stronger PLN, but we do not see a similar mood in the rates market. We believe another EUR/PLN move down to 4.200 would lead to profit-taking after such a big move in a short period and we should see stabilisation higher.

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