

FX Daily: Bracing for volatility

There are some important data to watch today: the Employment Cost Index in the US, GDP in the eurozone and CPI in France. We think the dollar can stay broadly supported into tomorrow's FOMC, but the euro could outperform other G10 currencies on the back of rebounding inflation. In the Czech Republic, we will see the last numbers before Thursday's CNB meeting



The dollar may stay broadly supported going into tomorrow's FOMC meeting

USD: Some support going into the Fed meeting

European data and global risk sentiment drove G10 FX dynamics yesterday. A weak start to the week for risk assets kept the dollar supported, especially during the US session, and signalled some market cautiousness ahead of multiple risk events: the FOMC tomorrow, ECB and Bank of England on Thursday, and US payrolls on Friday.

Today, the last few pieces of US data before the Fed decision will be watched quite closely. Particular interest will be on the Employment Cost Index (ECI), which is expected to have eased from 1.2% to 1.1% in the fourth quarter. This is a key input in the Fed's policy equation, and we could see investors shift between pro-hawkish/dovish positions ahead of the FOMC if the ECI surprises on either side. [Our view for tomorrow](#) is that the Fed still has an interest in hanging on to a hawkish rhetoric and pushing back against speculation of an early peak and – above all – rate hikes in 2023. The net result for the dollar may be positive.

The US calendar also includes the Conference Board Consumer Confidence index – which may have rebounded in January – and the Dallas Fed Services index.

We think the dollar can hold on to yesterday's gains going into the FOMC meeting, and high-beta currencies could remain key underperformers in a risk-off environment. Volatility looks likely to pick up quite markedly during the remainder of the week.

Francesco Pesole

➔ EUR: Inflation headaches before ECB meeting

European rates markets had to deal with a surprising acceleration in [Spanish inflation](#) yesterday, which reinforced expectations of multiple 50bp hikes by the ECB. At the same time, the growth picture seems to have deteriorated, as Germany recorded [negative growth in the fourth quarter](#). Eurozone-wide GDP figures will be released today, and are expected to show a 0.1% quarter-on-quarter contraction. However, it seems more likely that CPI figures out of France this morning will have a bigger impact on the euro. After all, a rebound in inflation is a more concerning development for the ECB than soft growth data which were heavily impacted by energy prices.

In the section above, we discussed how the dollar may stay broadly supported going into the FOMC meeting. The euro, however, may show more resilience than other G10 peers (especially high-beta currencies) given the shift in the inflation narrative in the eurozone which can surely fuel ECB hawkish speculation. EUR/USD may hover around the 1.0850 handle until tomorrow's FOMC.

Yesterday, we published [our scenario analysis](#) for this week's ECB meeting: the recent hiccups in communication have heightened the risk that markets have lost some trust in President Christine Lagarde's guidance. Investors may keep tracking data (EZ-wide CPI data are released tomorrow) more closely than they track Lagarde's remarks, and the ECB meeting may not have a big impact on the euro after all.

Our commodities team just [revised their gas price forecasts](#), now expecting TTF to stay below 80 EUR/MWh throughout 2023. This is a bullish scenario for eurozone sentiment and the euro in the medium term.

Francesco Pesole

⬇ GBP: Standing by before 'super Thursday'

There are no key data releases in the UK before Thursday's [Bank of England](#) meeting. Markets are currently pricing in 46bp (our call is for 50bp) at this meeting and an additional 25bp in March. We expect a broadly neutral impact on the pound, and GBP/USD moves may be mostly dictated by the FOMC reaction.

EUR/GBP may hold below 0.8800 until "super Thursday" (ECB and BoE meetings), although inflation figures in the eurozone mean the balance of risk is tilted to the upside for the pair.

Francesco Pesole

➔ CEE: Czech economy pulled down again by automotive

Today in the region we will see the first estimate of GDP for the fourth quarter of last year in the

Czech Republic. We expect a 0.8% QoQ decline, below market expectations. This would confirm a shallow recession in the Czech economy. Looking ahead, the outlook for the first quarter of this year also does not look good despite better numbers across the region and from the eurozone. Yesterday, the Czech Republic's largest carmaker announced production cutbacks at some of its factories due to chip shortages. The news comes just a week after the country's third-largest manufacturer made the same announcement. This marks the beginning of difficult times for the industry, which is mainly driven by the automotive sector. The situation is dangerously reminiscent of the end of 2021 when chip shortages and automotive production curbs dragged the industry into its biggest slump since the Covid-19 lockdowns. This may also be a piece of the puzzle for the [Czech National Bank \(CNB\) meeting](#) this week, however we will have to wait a few months for proof in hard data. For the koruna, a weaker economic number could be a trigger to correct recent gains and return to 24.00 EUR/CZK.

We also see interesting developments in Hungary following the downgrade of the country's sovereign rating. The weakening of the forint that we mentioned yesterday did not materialise and, on the contrary, the currency ended roughly unchanged at the end of the day. It confirmed that the strengthening of the forint is not short-lived and its strengths are of a more permanent nature. In the long term, we expect further strengthening. For now, we see yesterday's market reaction as a possible clearing of long positions while attracting new buyers and consolidating around 390 EUR/HUF.

Frantisek Taborsky

Author

Frantisek Taborsky

EMEA FX & FI Strategist

frantisek.taborsky@ing.com

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Chris Turner

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

chris.turner@ing.com

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