

FX Daily: Buying into the US slowdown

FX markets are reasonably quiet during this lull in the US data calendar. We had been expecting more of a Fed pushback against this drop in US rates, but Fed speakers seem quite equivocal. This has left US rates at the lows and investors seemingly starting to buy into the US slowdown - a mild dollar negative. Look out for many central bank speakers today



Jerome Powell will speak as a panelist at an IMF conference later today

📉 USD: Soft US rates undermine the dollar

Looking across asset markets the mood appears to be one of investors buying into the US slowdown. US rates remain at recent lows and there has been no concerted pushback from the Federal Reserve, yet, on this easing of financial conditions. Instead, we seem to be getting a core message from the Fed that the US labour market is moving better into balance - which can take some steam out of wage growth and broader inflation. Far from reversing last week's big drop, US money market rates priced two to three years out remain at their lows and 75bp off their peaks seen in mid-October.

This view that the Fed cycle may have turned seems to be showing up in the bond market too, where the long end is in demand again. Last night's \$40bn 10-year Treasury auction went OK (there is a 30-year auction later today) and data released overnight suggested Japanese

investors stepped up their purchases of Treasuries during September's sell-off - buying \$22bn that month. We also note that Brent oil trading down to the lows at \$80/bbl is a mild dollar negative.

The argument against expecting the dollar to soften further is probably that something like 4.50% on the 10-year Treasury yield is the lower end of a new 4.50-5.00% range. Equally, money markets may struggle to price short-term rates below 4.00% over the next few years. Let's see.

For today, the focus will again be on Fed speakers. Raphael Bostic (dovish) and Tom Barkin (hawkish) discuss the merits of survey evidence at 15:30CET. More focus will probably be on Jay Powell's speech at the IMF - but that does not take place until 20:00CET. In terms of data, the focus will again be on the weekly jobless and continued claims numbers, where any spike could hit the dollar - hinting at signs that the US labour market is finally turning.

We have a mild preference today that the dollar can drift lower, with DXY heading back down to 105.00.

Chris Turner

➔ EUR: Germany gets criticised (again) by the US Treasury

EUR/USD is enjoying a brief foray above 1.0700 - enjoying the reprieve of a day without terrible German data. Investors do not seem to be listening to the threat of one last European Central Bank rate hike, where instead 80bp+ of easing is priced in 2024. We doubt ECB speakers today will move the needle on EUR/USD and the best hope of slightly higher spot prices probably comes from the US weekly claims data.

Separately, we note with interest the release of the [US Treasury's semi-annual report on the FX market](#). Remember, this is a report for a weak dollar environment and designed to shine a light on those trading partners not allowing orderly appreciation in their currencies and potentially intervening - or manipulating their currencies for trade gain. The US Treasury is now no longer interested in Switzerland - which is now selling not buying FX. But by nature of its large trade surplus with the US, Germany remains on the US Treasury's Monitoring List. In what is a familiar refrain now, the US Treasury questions why Germany is still seeking fiscal surpluses when activity is so weak - an implicit criticism of Germany's business model of dining out on foreign demand.

For today, let's see whether EUR/USD can test decent resistance at 1.0765. Support is set at 1.0650/60.

Chris Turner

⬆️ PLN: NBP keeps rates unchanged despite expectations

The National Bank of Poland (NBP) [left rates unchanged yesterday](#) despite market and survey expectations. The market is repricing expectations, particularly at the short end of the curve upward, resulting in bear flattening. Higher rates at the short end are positive news for the zloty. EUR/PLN dipped to 4.430 after the decision but later returned to 4.440. We remain positive on PLN. Rates repricing in our view will continue today and current rate differentials already indicate EUR/PLN should be trading more like 4.420. However, the key today will be the NBP governor's press conference which should show what was behind the surprise decision to hold rates and what to expect next. We believe rates will remain unchanged in December as well, but next year is still a question mark given the inflation profile.

Frantisek Taborsky

MXN: Banxico should remain hawkish

Banxico announces its rate decision later today. Survey respondents unanimously expect unchanged rates at 11.25%. That makes a lot of sense given the difficult external environment that [recently interfered with Chile's easing cycle](#). Equally, we think Banxico will be more than happy to keep the 600bp policy rate premium over Fed rates - a position that has kept USD/MXN relatively stable, reduced implied volatility and contributed to the peso's attractiveness for carry trade strategies.

Additionally, Banxico will be wary of the Mexican government's loosening of fiscal policy into next year's election cycle. It is almost as if the AMLO administration failed to spend big during the pandemic (unlike Brazil) and kept its fiscal powder dry for the election cycle.

Loose fiscal and tight monetary policy is normally a very positive environment for a currency and this is why we think USD/MXN will be trading comfortably below 17.00 into 2024.

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