FX Daily: Climbing the wall of worry

FX markets have opened the week on a steady footing, buoyed by a strong end to last week from equities and appearing to shake off a slightly lower-than-expected growth target from China. This week's focus will very much be on central bankers and activity data - the highlights being Jay Powell's testimony (Tuesday and Wednesday) plus US jobs growth (Friday)

USD: How strong is the US economy and what will the Fed do about it?

After a few weeks where US price data has taken centre stage, this week will all be about activity data and Fed speak. On the activity side, Friday's release of February US jobs data should shed light on whether January's +517,000 surge was an aberration powered by seasonal adjustment factors or a genuinely strong number. Our US economist, James Knightley, tends to favour the former interpretation - although conviction levels are low. Running up to Friday's job data will be Wednesday's release of JOLTS and ADP data - again providing insights as to whether tight conditions in US labour markets are starting to ease.

The other US highlight this week will be testimony to the Senate (Tuesday) and House (Wednesday) from Federal Reserve Chair Jerome Powell. He will be testifying on the Fed's semi-annual monetary policy report which was released on Friday. The market will be interested to hear what he thinks about re-accelerating the pace of hikes to 50bp from 25bp (+30bp is priced for the 22 March meeting) and any indication on what the terminal rate might be. Recently, we have been writing that an upward revision to the Dot Plots on 22 March will discourage investors from aggressively re-establishing dollar short positions.

This week also sees central bank policy meetings in Japan, Australia, Canada, and Poland. Of these, the Reserve Bank of Australia (RBA) is the only one expected to hike rates (+25bp). However, Friday's Bank of Japan (BoJ) meeting will prove interesting as will tomorrow's release of Japanese wage data for January. Another widening of the BoJ's 10-year JGB target band on Friday would be a big surprise and drag USD/JPY lower.

What does this all mean for the dollar? In today's session, the dollar has not found too much support from a slightly lower-than-expected Chinese growth target for 2023 at 5.0% (5.5-6.0% had been expected). Equally, equities continue to hold up quite well despite last week's big rise in bond yields and are providing a little support to pro-cyclical currencies. In all, we suspect it is another range-bound week for the dollar, where DXY continues to trade in a 104.00-105.50 range and local stories can win out.

Chris Turner

EUR: ECB helps build the 1.05 EUR/USD floor

European Central Bank speakers continue to point to a 50bp hike at the 16 March meeting as being a done deal. The market then prices a further 150bp of tightening by year-end - which looks a little aggressive. Still, the tough ECB talk has kept the EUR:USD interest rate differential supported at the short end of the market and firmed up the 1.05 support zone for EUR/USD this month. We think EUR/USD probably ends March in the 1.07/1.08 area.

For today, the eurozone focus will be on January retail sales and the March Sentix Investor survey. Improvements are expected for both, although may not move markets. We also have ECB Chief Economist, Philip Lane, speaking in Dublin at 11 CET. He has recently shifted over to the hawkish side and it is probably too early for him to push back against the market's pricing of the ECB deposit rate at 4.00%. EUR/USD probably trades well inside a 1.0600-1.0700 range today.

Elsewhere in Europe, Switzerland sees February CPI. The market expects some deceleration from January's firm readings. Any upside surprise could pressure EUR/CHF in its latest 0.9900-1.0000 range.

Chris Turner

GBP: Steady sterling this week

This week it is hard to find a UK catalyst for sterling to break out of recent ranges. We doubt any further progress on the Windsor Framework deal is worth much more to sterling. And having heard from Bank of England big hitters (Andrew Bailey and Huw Pill) last week, we doubt that this week's BoE speakers make much of a dent in market pricing of the BoE cycle. Activity data for January looks like it could come in on the softish side, although the services sector will be in focus following the recent jump in the services PMI reading.

In all, EUR/GBP should trade well within a 0.8800-0.8900 range, while GBP/USD will be bounced around on this week's big inputs from the US events calendar.

Chris Turner

CEE: Inflation numbers leave no room for rate cuts

A busy calendar awaits us this week in the CEE region. Today, we start with labour market data in the Czech Republic, key for the Czech National Bank, and retail sales in Hungary. On Tuesday, industrial production for January will be released, which should confirm a weakening economy. On Wednesday, we will also see February inflation in Hungary, as the first number within the CEE region. We expect only a slight drop from 25.7% to 25.4% year-on-year, in line with market expectations, but also slightly higher core inflation. Later on, we will see the decision from the National Bank of Poland. In line with the market, we expect interest rates to remain unchanged. However, the main focus will be Governor Adam Glapinski's press conference a day later. The central bank will also publish a new forecast. While inflation was lower than expected in January, core inflation remains high. So the question will be how the governor's tone will change since the last forecast and whether he will officially announce the end of the hiking cycle or mention a possible rate cut later this year. We then move to the Czech Republic on Friday, where industrial production and inflation data will be published. CPI, in our view, fell slightly from 17.5% to 16.9% YoY, above the market and CNB forecasts.

In the sovereign rating space, Fitch maintained a negative outlook for the Czech Republic on Friday. In Hungary, Moody's again did not publish a rating review as it did in September, which means that the outlook and rating remain unchanged, and presumably, the agency is waiting further for developments in the negotiations between the Hungarian government and the European Commission regarding access to EU money.

On the FX side, global conditions for the CEE region remain mixed. The US dollar will hamper EM currencies, on the other hand, gas prices broke 45 EUR/MWh on Friday indicating a further rally in the Hungarian forint and Czech koruna. February inflation data should be a boost to both currencies, confirming the current hawkish market pricing, leaving no room for early rate cuts. On the other hand, a dovish NBP may bring pain to the Polish zloty. Thus, it will be key to watch for indications of a first rate cut during the governor's press conference on Thursday. The Czech koruna could retest levels below 23.40 EUR/CZK and the Hungarian forint below 375 EUR/HUF. However, the Polish zloty should test weaker levels above 4.740 EUR/PLN again.

Frantisek Taborsky

Authors

Chris Turner
Global Head of Markets and Regional Head of Research for UK & CEE
chris.turner@ing.com

Frantisek Taborsky
EMEA FX & FI Strategist
frantisek.taborsky@ing.com

Francesco Pesole
FX Strategist
francesco.pesole@ing.com