

FX Daily: Data versus Powell, round two

The dovishly-perceived testimony by Fed Chair Jerome Powell last week shifted all attention to US data. The first input, US jobs data, raised more concerns on data quality than answering questions on the labour market. We expect a 0.3% MoM core CPI this week, which remains inconsistent with a cut before June and can offer the dollar some support



Federal Reserve Chair
Jerome Powell

➔ USD: Inconclusive payrolls, focus turns to CPI

Federal Reserve Chair Jerome Powell's Congress testimony last week left markets with a dovish aftertaste. Reiterated (albeit cautious) optimism about the disinflation path and claims that the Fed is "not far" from cutting rates wrong-footed most investors who were likely bracing for a more hawkish tone on the back of resilient data. The resulting shift in FX positioning against the dollar was an example of what we'll see once data eventually endorses rate cut expectations.

We recently discussed how sticky US data depressed FX volatility by leaving markets without a sense of direction. Ultimately, a divergence in rate expectations for the Fed or the rest of the developed world is needed to revamp FX volatility on a sustainable basis. Cautious, inflation-focused central bankers need (by extension) conclusive data evidence to start cutting. So, despite the cautiously dovish Powell and European Central Bank President Christine Lagarde opening the

door to a June cut last week, data remains overwhelmingly central for FX.

Friday's US payrolls probably raised more questions on data quality than providing answers on the actual state of the jobs market. As discussed by our US economist [here](#), it is understandable markets weren't fooled by the strong headline print (275k). There were 167k downward revisions in the past two months, meaning the actual employment gains were just above 100k. This is yet another example of how unreliable data has been lately. Incidentally, job gains were primarily concentrated in industries not typically associated with a strong economy like retail, manufacturing and construction. There are plenty of indications from other surveys – including the household survey, used to calculate unemployment – that the jobs market is cooling off.

The inconclusiveness of payrolls puts more emphasis on February CPI figures, which will be released tomorrow. We expect a 0.3% MoM core print, which remains inconsistent with the Fed's inflation targets and suggests easing is not imminent. This week's US calendar also includes February's retail sales and industrial production, as well as the University of Michigan surveys. The Fed is already in the blackout period for the 20 March meeting.

We expect inflation figures to put a stop to the dollar decline this week. The shifts in FX positioning last week no longer justify an exacerbation in USD downward pressure unless key data starts to turn in favour of Fed easing. There is a non-negligible risk that part of the USD losses driven by Powell's testimony are unwound this week.

Francesco Pesole

➔ EUR: Eyes on post-ECB comments

This will be a quiet week for eurozone data. The only highlight is January's industrial production data, which should not move the market much. We'll be more interested to hear what ECB members have to say after Thursday's meeting, especially on whether June is indeed a reasonable target for the first rate cut and the conditions that need to be met on the wage and inflation side. Austria's Robert Holzmann (a hawk) is speaking today. We'll hear from Isabel Schnabel, Pablo Hernández de Cos, Luis de Guindos, Philip Lane and others later this week.

We must reiterate that EUR/USD is trading around the top of the range that is consistent with a still depressed short-term rate differential. The EUR:USD 2-year swap rate gap has not moved much since the start of March, staying around 125bp, and we need to see a clearer convergence of USD and EUR rates to justify continued support beyond 1.1000.

We see some downside risks this week for EUR/USD, and a correction could take it back to the 1.0850-1.0900 area. However, our call for a first rate cut in June by both the ECB and the Fed can still argue for a higher EUR/USD, as the Fed should ultimately deliver a larger easing package.

In other EUR-crosses, EUR/JPY may well test the 160.0 level this week as a revision in fourth-quarter GDP showed Japan dodging a recession (even though consensus was for a stronger read), which should keep part of the market betting on a rate hike by the Bank of Japan on 19 March. As of this morning, 6bp of tightening is priced in for March, 9bp for April and 10bp for the June meeting. JPY can stay supported this week, but is heading towards a potential cliff edge next week as March hike expectations may prove premature.

Francesco Pesole

➔ GBP: Key data tests for the strong pound

The pound's strong momentum is set to face a key challenge tomorrow as the UK releases its jobs report. Wage growth figures – especially in the private sector – will be watched very closely as they now represent the second most important input for the Bank of England after services inflation. Later in the week, we'll also see the UK's January GDP report, February's retail sales and the BoE's inflation attitude survey.

EUR/GBP dived on Friday and is trading close to the 0.8500 lows. Back in February, the pair's exploration of the 0.8500 area was very short-lived and followed by a sharp rebound. The 2-year swap rate gap between EUR and GBP is close but not as wide as it was then, currently at -143bp. Unless UK data surprises on the strong side, we doubt EUR/GBP can fall much further from these levels.

Francesco Pesole

➔ CEE: Inflation figures across the region

February inflation in the Czech Republic will be published today. We expect a further decline from 2.3% to 2.1% year-on-year, which would confirm the stability of inflation near the central bank's target. This would be well below the Czech National Bank's forecast of 2.8%, maintaining the same deviation as in January. Inflation and industrial production will be published on Wednesday in Romania and the central bank will publish minutes in Hungary. For inflation here, we expect a small decline from 7.4% to 7.1% YoY.

On Friday, February inflation in Poland and industrial production in the Czech Republic will be published. We expect inflation in Poland to fall from 3.9% to 3.3% YoY. Outside the economic calendar, it is worth mentioning Wednesday's start of the Czech National Bank's blackout period. Unusually, it starts a day earlier and we can therefore expect more statements from the board in the first half of the week. We expect a further acceleration in the pace of CNB rate cuts from 50bp to 75bp at the March meeting.

In the FX market, we remain positive on PLN and neutral on CZK. However, the HUF should be the main focus again this week. Friday's inflation numbers and global developments supported HUF, which also suggests higher market rates and interest rate differentials. However, the current political noise does not seem to be over and we expect the pressure on a weaker HUF may continue. We see EUR/HUF more around 396 and suspect the market will want to see the 400 level hit before turning bullish on HUF assets again.

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