

## FX Daily: Debt ceiling deal lifts sentiment, with Asian FX even getting a boost

European FX markets are opening up to a better risk environment. This looks to be a function of both the US debt ceiling deal making it through Congress and a more relaxed Fed. Even Asian currencies are rallying. Whether this week marks an important turnaround for the dollar remains to be seen, but today's US NFP job data should have a big say



### ⬇️ USD: Dollar bias looks lower unless NFP comes in strong

Thursday proved somewhat of a turnaround session for the dollar. News that the Federal Reserve was preparing to skip a hike at the June meeting plus later progress on the debt ceiling deal saw the DXY sell off 0.8%. Whether this marks an important reversal for the dollar will largely be down to whether US activity data, particularly US price data, allows the Fed room to breathe – i.e. to reflect on the 500bp of tightening so far – without being rushed into further hikes. The latter largely drove dollar pricing and bearish risk sentiment last month.

As ING's Chief International Economist, James Knightley, [discusses here](#), today's US NFP data will have a major say in determining whether the Fed hikes in June or not. For FX, we would say that an on-consensus +195k increase in jobs, a 3.5% unemployment rate and a 0.3% month-on-month increase in hourly earnings would not be enough to shift the needle from the view that the Fed pauses in June and the dollar can stay gently offered.

We also note a slightly better environment coming through in Asia overnight. USD/CNH has reversed recent gains, the Hang Seng is up 4%, as is iron ore – suggesting Chinese pessimism may have run far enough for the time being. A close in USD/CNH today near the week's low of 6.07 could mark an important reversal and set the scene for a recovery in the commodity currency complex. Here we note speculation is growing of another Reserve Bank of Australia hike next week, following a large increase in the national minimum wage and some positive first quarter capex data released yesterday. AUD/USD could recover further.

High dollar deposit rates will stop the dollar from selling off too quickly, but unless the May NFP surprises on the upside we would say today's DXY bias lies towards the 103.20 area. Take a look at [ING's latest monthly update](#) – it looks at where we could get our forecasts wrong.

*Chris Turner*

## ➔ EUR: Some welcome relief on inflation

[Eurozone May inflation fell more than expected yesterday](#), EUR:USD two-year swap differentials stayed wide, but EUR/USD rallied. Probably helping EUR/USD was a mildly positive re-assessment of global growth prospects on the view that late-cycle inflation may not be as severe after all, and central banks may not have to tighten a lot further and deepen recessions. On the subject of the ECB, read our latest [eurozone update](#) from Peter Vanden Houte, where we are in line with market pricing of two further 25bp rate hikes from the ECB.

As above, today's US data will have a big say in determining whether this week's EUR/USD low of 1.0635 was significant. As we have been saying here over the last few weeks, we have expected the 1.05-1.07 area to mark the base in the second quarter, so let's see whether we get much of a rally from here. EUR/USD could press the 1.0810/20 area if NFP does not come in too hot, with outside risk to 1.0865.

*Chris Turner*

## ➔ JPY: Turnaround from 140?

USD/JPY has reversed from a high near 141, largely on the back of shrinking expectations that the Fed would hike in June. That is now priced with a 25% probability rather than a 70% probability attached to it last month. We have noted that the current environment should continue to see interest in carry trade strategies – where the Japanese yen scores poorly. However, USD/JPY looks overvalued relative to the terms of trade story – which is much better for the yen than a year ago.

In addition, there is still the risk that the Bank of Japan surprises on 16 June by further normalising its Yield Curve Control policy. That would be a yen positive. And thus it would not be a surprise to see speculator investors trying to re-position short USD/JPY above 140 – even if such a strategy has already proved painful this year.

*Chris Turner*

## ⬇ SEK: Still in troubled waters

EUR/SEK has marginally eased back from the 11.68/11.69 highs, largely on the back of some improvement in risk appetite. But Scandinavian currencies continue to lie at the bottom of the G10 scorecard, and recent domestic news out of Sweden did not offer many reasons to turn less

bearish on the krona. The Riksbank released its bi-annual financial stability report yesterday, sounding the alarm on commercial real estate and encouraging exposed firms to strengthen their balance sheets. The overall assessment of the Swedish banking sector's health – especially during the period of distress in the US and Switzerland – was rather positive, even though the structural exposure of lenders to the troubled property market means multiple vulnerabilities may emerge. Speaking on this topic, Riksbank Governor Erik Thedeen said that the commercial real estate risks will not affect monetary policy decisions.

On the data side, manufacturing PMIs for the month of May came in sharply lower than expected, at 40.6. That marked a sharp divergence with hard data that instead surprised on the positive side last week, when first-quarter GDP figures showed a relatively solid 0.6% quarter-on-quarter growth after the 0.5% contraction in the fourth quarter of last year.

In practice, domestic data are not having a very material impact on SEK moves at the moment, and we mostly stress them from the perspective of what those can imply for future monetary policy decisions by the Riksbank. The krona is being driven by risk sentiment at the moment but is clearly retaining a bearish bias that – in our view – is primarily attributable to the Riksbank's dovish tilt at the April meeting.

[As discussed in this note](#), picking a top for EUR/SEK in this environment is hard. The highest-ever intra-day level is 11.79, and unless we see a few consecutive sessions of risk-sentiment improvement in FX, new historic highs in the pair may be reached. The Riksbank's options to counter this bearish pressure on the krona remain, for the moment, quite limited.

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