

FX Daily: Divergence, divergence, divergence

Domestic developments in G10 are reinforcing the narrative of monetary policy divergence. Yesterday, lower-than-expected Canadian inflation reinforced our view of a June cut, while sticky UK services CPI and a hawkish RBNZ are boosting GBP and NZD this morning. The ECB appears to be sitting in the middle, with greater chances of a “hawkish” cut in June



➔ USD: Waller not as hawkish as it seemed

The dollar awaits any domestic input to make the first move, and domestic stories are taking centre stage. We are even more convinced the Bank of Canada will cut rates in June after lower-than-expected core inflation in April, while (as we discuss later in this note) easing expectations have been trimmed in the UK and New Zealand.

A few headlines from the Federal Reserve's hawkish-leaning member Chris Waller caught the market's attention yesterday. Those headlines have focused a bit more on the hawkish parts of his [speech](#), quoting that he graded the April CPI report “C+” and that at least three more months of inflation progress are needed to consider cutting rates. However, Waller also said that those three

good CPI reports are needed in the absence of significant weakening in the labour market, and that the April figures left him “hopeful that progress toward 2% inflation is back on track”. The overall message looked more centred around data-dependence than hawkish policy guidance.

Anyway, we should get a bit more clarity on the FOMC thinking in the May meeting minutes. While there should be evidence of increasing concern around the disinflation hiccups, Powell’s messaging seemed to denote a broad optimism on future price developments. Given the sub-consensus nonfarm payrolls and encouraging CPI were released after the meeting, comments from officials now should be more relevant than the minutes. Today, Raphael Bostic, Susan Collins, Loretta Mester and Austan Goolsbee are scheduled to speak, while on the data side, MBA mortgage applications and existing home sales are the only releases on the day. It looks more likely that the FX market will be impacted indirectly by the release of Nvidia’s quarterly results (expected after today’s US market close) than that data. We retain our neutral-to-slightly-bullish view on the dollar in the near term.

Elsewhere, New Zealand’s central bank kept rates on hold as expected overnight and struck an even more hawkish tone due to sticky services inflation. Policymakers discussed the possibility of hiking at this meeting and rate projections showed a slightly increased chance (60%) of another rate increase, with rate cuts from the current 5.50% only starting in 3Q25. The New Zealand dollar is significantly stronger this morning, and we think there is more upside room against other high-beta currencies as markets still price in more than one cut (34bp) by year-end. We now expect 25bp of easing by year-end in New Zealand, but the risks are skewed to no cuts at all.

Francesco Pesole

➔ ECB: Lagarde further endorses June cut

European Central Bank President Christine Lagarde sounded cautiously dovish in line with most comments from her Governing Council members in a speech yesterday. She claimed to be “really confident that we have inflation under control” and there is a “strong likelihood” rates will be cut in June if inflation remains encouraging. Markets are pricing in 24bp of easing for next month and are therefore disregarding more comments on the June meeting.

However, markets are slowly trimming rate cut expectations by year-end (now at -66bp) as the ECB communications have signalled some a cautious approach to future easing. Expectations are increasingly centred on a “hawkish cut” in June, with the focus on data dependency and still some emphasis on lingering upside risks to prices. If this proves to be the case, an idiosyncratic EUR decline would not be warranted. The dollar can indeed gain some more ground on higher rates and the divergence narrative with other central banks (not just the ECB), and ultimately take EUR/USD a few notches lower; but the case for a move back below 1.05 – which was very popular only a month ago – does not look strong. Crucially, the euro retains a decent fundamental position (e.g. the eurozone’s terms of trade), which would make a move towards parity increasingly unsustainable.

We still think EUR/USD can ease back to 1.08 in the near term, but our 3Q forecast remains for 1.10 as the Fed transitions to easing and the ECB broadly matches the market’s rate cut expectations. The only event in the eurozone today is another speech by Lagarde.

Francesco Pesole

➔ GBP: Stronger on slower disinflation

This morning, UK services inflation [came in at 5.9% for April](#), exceeding both consensus estimates (5.4%) and the Bank of England's projections (5.5%). Headline inflation slowed from 3.2% to 2.3% and core from 4.2% to 3.9%, but those were also above consensus and we know the BoE is mostly focused on the services price dynamics. Notably, rents surged, and other service categories also saw strong increases.

While this doesn't significantly alter the BoE's trajectory, it may prompt them to delay rate cuts for another month. Our base case remains a first rate cut in August.

Markets are understandably scaling back rate cut bets in the UK and the pound has jumped on the release. We had forecasted a move below 0.8550 in EUR/GBP at the start of this week, but we are seeing even more pressure on the policy-sensitive EUR/GBP. The pair may be on track to test the March lows at 0.8506, and we are marginally favouring some support at that level as opposed to another break lower. Our view beyond the short term remains positive on EUR/GBP as we see the ECB delivering a hawkish cut and the BoE cutting rates 100bp from August, but it now looks likely this strength will take some more time to show.

Francesco Pesole

⬆️ CEE: Data in Poland may support further gains for the zloty

Today begins a two-day series of Polish data. This morning we will see labour market numbers including wage growth, which have surprised rather to the upside in recent months and triggered some market reaction. We expect wage growth above market expectations this time as well. Industrial production will also be published, which should show a decline from the previous month but growth year-on-year. And also today we will see the PPI for April in Poland.

Yesterday's [meeting](#) of the National Bank of Hungary didn't bring too many surprises or impetus to the markets. The NBH cut rates by 50bp to 7.25% but we didn't learn much new regarding the June meeting. For now, we lean towards a 25bp rate cut but the odds are almost even with the 50bp alternative, which is also reflected in market pricing.

Poland's zloty and Hungary's forint continue to strengthen this week while the Czech koruna is steady and data in Poland today may support a view of no rate cuts this year and push EUR/PLN below 4.250.

Frantisek Taborsky

Author

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Frantisek Taborsky

EMEA FX & FI Strategist

frantisek.taborsky@ing.com

Chris Turner

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

chris.turner@ing.com

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