

FX Daily: Dollar bulls take control

The 0.4% MoM print for the March core CPI reading has wiped out expectations of a June rate cut. This will probably prove quite frustrating for the Fed, although, as they have been saying recently, strong growth gives them the luxury of patience. What it does mean is that trading partners may still push ahead with rate cuts, and that's dollar-positive



📈 USD: CPI delivers stronger dollar and tighter financial conditions

Yesterday's release of the [March US CPI data](#) continued the run of strong/above consensus US inflation and activity data. Last week, we were talking about the dollar being at the crossroads given that the market was pricing 75bp of 2024 easing – the same as the Fed median Dot Plot. Well, those high CPI figures have now seen the market take a decisive turn in favour of the stronger-for-longer camp. And Fed easing expectations have been pared back to just 42bp for this year. The terminal rate for this easing cycle continues to creep us as well. It is now priced at 3.75% in four years' time. That looks pretty high in terms of a neutral policy rate, but investors won't argue with it until some softer data comes through.

The high US CPI figures probably have two clear implications for FX markets. The first is that it will

generate policy rate divergences as trading partners will still try to push ahead with easing cycles to address domestic disinflation and growth needs. Notably, we are looking for a [dovish ECB statement and press conference today](#). And yesterday's Bank of Canada meeting means the BoC is [holding open a door for a June rate cut](#). The prospect of widening policy differentials can only help the dollar. The second is the implication that short-term rates will probably be higher globally (or at least Rest of World easing cycles will not be as deep as they could have been). This will generate greater restraint on the global economy and be another negative factor for growth-sensitive currencies. As we have noted previously, bearish flattening of the US yield curve (as seen yesterday) is bad news for the commodity currencies, and it was no surprise to see this community bearing the brunt of yesterday's losses.

Today's March US PPI data will probably deliver more of the same. High readings in the medical and insurance components of the PPI data will point to a likely 0.3% MoM March core PCE reading on 26 April. Recall this is the Fed's preferred inflation gauge and will likely prove the nail in the coffin of a June rate cut.

DXY broke to six-month highs yesterday, and 106.00 looks the next likely target.

The FX market is now also on Bank of Japan FX intervention watch. One month USD/JPY volatility surged after USD/JPY burst through 152 yesterday. And the market will now be expecting BoJ FX sales somewhere between current levels and 155. Recall that the BoJ sold around \$70bn of FX in intervention episodes in September and October 2022.

It's worth adding here that Dmitry Dolgin [published an update](#) on the de-dollarisation story yesterday. As we suspected in publications last year, it looks like the de-dollarisation process remains an exceptionally slow one.

Chris Turner

📌 EUR: ECB lines up the June cut

All eyes today are on the ECB policy rate announcement at 14:15 CET and President Lagarde's press conference at 14:45 CET. As outlined in ING's [ECB Preview](#), we are expecting the ECB to show more confidence in its scope to cut interest rates. A 25bp rate cut in June is surprisingly only 82% priced, and the recent, US-inspired climb in short-term rates around the world means that only 70bp of ECB easing is expected this year. We look for 75bp, with probably risks for more - rather than less - easing. Looking at the forward ESTR curve, the market prices terminal rates for this ECB cycle at around 2.3% - which seems fair.

The prospect of the Fed doing nothing this year and the ECB cutting has pushed two-year EUR/USD swap rate differentials close to 160bp in the dollar's favour - the largest gap since December 2022. EUR/USD was trading closer to 1.05 at that point. Clearly, the near-term bias for EUR/USD is lower, and unless President Lagarde delivers some surprise reticence to ease policy today, it looks like the 1.0700 February low is going to come under heavy pressure.

EUR/USD will probably not be helped by geopolitics either, where the increasing risk of a retaliatory strike from Iran or its proxies against Israel will only push crude oil prices further ahead and damage the euro's terms of trade again.

Chris Turner

➔ CEE: US numbers shuffle the cards but the result is the same

Yesterday's inflation in the Czech Republic did not **bring** too many surprises. The headline number was 2.0% YoY, as expected by the market. However, core inflation (2.7%) seems to be falling a bit slower than expected. We also saw inflation in the rest of the region this morning. In Romania, inflation fell from 7.2% to 6.1% YoY, slightly below market expectations, which should be enough for the NBR to start cutting rates in May. In Hungary, inflation also fell from 3.7% to 3.6% above market expectations. Here, we have a meeting in two weeks, where we think the discussion will be between a 50 and 75bp rate cut, with a preference for a rather larger move due to the inflation profile and strong HUF at the moment.

US inflation numbers shuffled the cards in the region significantly. However, for now, it seems that lower EUR/USD is offset by higher CEE rates, and FX should not be affected much as a result. Therefore, we continue to retain our bias that the CZK is undervalued. With inflation not surprising to the downside, we expect EUR/CZK may re-couple with rates again to close the gap from recent weeks, which would imply a move below 25.30. On the other hand, the return of the local story to Hungary - lower inflation and more rate cuts - should return EUR/HUF higher towards 395. PLN tested new stronger levels again yesterday, and especially after the US numbers, we believe that for now, the rally is over, and EUR/PLN should move up to 4.280 in the near term despite us remaining positive on PLN in the medium term.

Frantisek Taborsky

⬆️ MXN: The Teflon peso

The Mexican peso continues to perform exceptionally well. One might have thought that higher US rates would have shaken out some crowded plays in the high-yield peso - but no. We have been discussing this internally and are wondering whether higher US rates mean that Banxico will keep its policy rate higher for longer - thereby cementing the peso's high-yield status.

We do think that the real trade-weighted peso is now at some super-strong levels that could elicit a Banxico response - either from a faster easing cycle or more directly through some kind of FX programme. The issue, however, is that Mexican Presidential elections take place on 2 June. and Banxico may not want to address the strong peso before this. Additionally, some locals are saying that Banxico may choose to avoid back-to-back rate cuts at the May 9th meeting - again, given the proximity of the election.

Our view on the peso this year has been that it will substantially outperform its forward curve (correct) but perhaps would not deliver continued nominal appreciation (incorrect). Consensus sees USD/MXN ending the year around 17.00 - we see it somewhere in the 16.50/17.00 region. However, a correction from current levels may not come until presidential elections are out of the way.

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