

FX Daily: Dollar bulls undeterred

There has been little respite in the surge in energy prices. This story continues to play out in FX markets through two key channels: i) what it means for a country's terms of trade - i.e. exporters vs. importers and ii) what central banks are prepared to do about high inflation. The dollar looks well-positioned here.



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USD: Softer NFP did little damage to dollar rally

The world economy remains in the clutches of an energy price surge, where crude prices look to be following gas prices higher. As our team pointed out on Friday in relation to gas anyway - [there are no quick fixes](#). FX performance over the last week has largely fallen in line with the energy story. The outperformers have been the currencies of key energy exporters, Norway, Russia and Canada. While under-performing have been the energy importers of Japan, Turkey and Hungary.

Bouyed by the positive income shock of the energy rally, the central banks of Russia and Norway are some of the most hawkish in their peer group. And a good jobs number in Canada on Friday supports the view that the Bank of Canada could be joining them with a hike in 1H22.

On the subject of jobs, Friday's [headline NFP jobs miss](#) has done little to dampen Fed tapering/tightening expectations. For example, Dec 2023 Euro-dollar futures continue to break

lower consistent with the recent trend of the market re-pricing the US interest rate curve towards Fed projections in the September Dot Plots. This is dollar bullish. The dollar is also taking its cue from the sell-off in Treasuries, where a heavy auction schedule this week (\$58bn three years, \$38bn 10 years and \$24bn 30 years) may keep US yields supported.

This story of high inflation and how central banks react to it will be very much on the agenda in the week ahead. Wednesday sees US September CPI, expected at 5.3% YoY headline, 4%+ core. And Wednesday will also see the release of the September FOMC minutes - a meeting that was generally seen as hawkish.

US energy independence stands the US in good stead right now and a central bank ready to normalise policy should keep the dollar supported - especially against energy importers and central banks not prepared to react to higher prices - i.e. Japan and Turkey. USD/JPY is currently in the process of breaking some major resistance and the entrance of momentum funds could propel USD/JPY towards 115 multi-day.

DXY is consolidating below some major resistance at 94.50/70, but upside pressure should remain in place all week.

➔ EUR: Downside pressure should build

EUR/USD failed to enjoy much of a bounce on the soft US NFP figure - largely because the low number was seen more of a supply than a demand problem. But one would have thought that the gas surge and what it means for the manufacturing sector would be a negative for the EUR - given manufacturing's relatively high weight in Eurozone GDP.

So far the ECB seems unmoved on viewing high inflation as transitory. There are some ECB speakers today (e.g. Lane around 1400/1430 CET), but they seem in no mood to follow a bank, like the BoE, expressing concern in the potential permanence of inflation.

1.1500 remains very big support for EUR/USD and which may be tested on Wednesday on the release of US CPI/FOMC minutes. Trading may be subdued today for the US Columbus Day holiday.

⬆️ GBP: BoE sounds like it is gearing up for an early hike

Typically BoE monetary policy - and the UK economy - is seen falling between the US and Eurozone economic cycles. But currently strong speculation is building that the BoE will tighten ahead of the Fed. Two-year Gilt yields rose 7bp on Friday and should rise more today following weekend comments from BoE Governor Bailey effectively warning of second round effects from currently high inflation.

We do have BoE speeches later this week as well, but these are from the doves. We really need to see if the hawks have any problems with the aggressive, early pricing of the BoE rate hike cycle and so far that does not seem to be the case.

As we noted last week, we think an early BoE rate hike (even if it were later viewed as a policy mistake) would be positive for GBP in the short term. And the BoE story does seem to be trumping Brexit-related risk, where Wednesday should see a flurry of headlines as the UK-EU try to adjust the NI protocol.

0.8450/8470 looks a tough nut to crack on the EUR/GBP downside, but for those that like GBP,

GBP/JPY looks set to retest the 156 high.

➔ CZK: Domestic problems

The CZK has been strong and steady all year, backed by a very hawkish central bank. The market prices another 50bp hike from the CNB in November, following the surprise 75bp hike on September 30th. With energy prices surging around the world and Czech September CPI expected at 4.6% YoY today, it seems the CNB has been right to be cautious.

Yet part of the rationale for the 75bp hike in September was domestic demand pressure. The question is whether the announcement from Skoda last week, that it plans to reduce or completely shut down car production into year-end because of chip shortages, resonates with the CNB? Given the car industry's heavy direct and indirect role in the Czech economy we will need to monitor this story and whether it prompts a re-pricing of the CNB tightening cycle. We have a slight preference for EUR/CZK moving back to the 25.55 area.

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