

FX Daily: Dollar rally overdone despite December's cut in doubt

EUR/USD has dropped significantly more than what the swing in rate differentials can justify. So, while a December Fed cut has clearly decreased in probability, there are downside risks for the greenback ahead of today's payrolls. A bad payroll print could prompt FX intervention on USD/JPY, which has kept marching towards 160



The dollar remains soft ahead of a busy week for data and policy meetings

⬇️ USD: Dollar has gone too far

Stock markets cleared the key hurdle of Nvidia's earnings release yesterday. While the S&P500 is still down in November as valuation concerns are seemingly on the rise, yesterday's strong earnings are offering relief to global risk sentiment and helping the high-beta G10 segment stabilise.

The recent risk-off move lent the dollar some safe haven support, but USD crosses remain primarily an extension of Fed expectations. Two factors drove them to the hawkish side yesterday, with pricing for December having now dropped to just 7bp.

First, the BLS announced that the November jobs report – alongside an October payroll estimate (without unemployment) – will be published on 16 December. That is after the 10 December Fed meeting.

The second factor is hawkish Fed minutes, which were released yesterday. At the October meeting, several FOMC members were against the decision to cut rates, and many expected a hold in December. This confirms that Powell's hawkish presser was representative of a good chunk of the Committee.

Our call so far has been that jobs data would justify a December cut, but the change in the data release schedule makes it a much harder call now. The balance is swinging in favour of a hold as the higher bar set by the FOMC for a cut may not be met by today's payrolls, which are, incidentally, outdated (September figures) and lacking unemployment data. Consensus is 54k, and while the risks are probably on the downside for the dollar today given the recent hawkish repricing, we'll probably need to see a very soft print to convince the FOMC to cut without having seen the October and November releases.

Looking into year-end, our bearish call on the greenback is intact, although dollar weakness may only fully materialise in the second half of December, after jobs data releases. Before then, the balance of risks is on the downside for the dollar, whose rally has overshot what our short-term valuation model suggests and the stabilisation in equities can lift some support.

USD/JPY has continued to rally and at 157-158 is now clearly in intervention territory. However, our view remains that Japanese officials prefer to intervene after a USD-negative event, like they did in July 2024. If today's payrolls prove to be bad, we could see an intervention in USD/JPY.

Francesco Pesole

EUR: Drops below 1.150 unsustainable for now

Our EUR/USD model returns a short-term undervaluation of 2%. That means that the drop in the pair has materially exceeded what the changes in the rate differential and other market drivers can justify. That, along with what was discussed in the USD section above, means that the balance of risks is still tilted to the upside in the near term.

We think EUR/USD can make brief explorations below 1.150, but for those to be sustainable, we'd need either a broader hawkish re-rating (due to strong US data) or some negative news affecting the euro.

Our year-end 1.18 target remains unchanged anyway, even though the pair may struggle to trade sustainably above 1.160-1.1650 until mid-December.

Francesco Pesole

GBP: Budget risk premium to stay

Today, we should hear from the opposing sides of the Bank of England's MPC spectrum as Catherine Mann (hawk) and Swati Dhingra (dove) are both scheduled to speak.

Yesterday's UK CPI report was not too remarkable, with hawks likely pointing to rebounding food inflation and doves to the multi-month moderation in services inflation. But as Huw Pill said earlier this week, the December decision hangs in the balance. The doves need one defection to push a cut through: we think a restrictive UK budget next week and upcoming data will be enough.

The pound is trading with a moderate risk premium that appears likely to remain in place until the

Budget announcement on 26 November, as the government's U-turn on income tax hikes has added a layer of uncertainty and unnerved bond investors. Our year-end target remains 0.88 for EUR/GBP, as the risk premium may well abate after the Budget, but we expect part of it will be replaced by dovish repricing.

Francesco Pesole

CEE: Another promise of peace supports the region's currencies

The National Bank of Hungary meeting on Tuesday did not bring much news, but a few details are worth mentioning. The central bank delivered a hawkish message as expected, and it seems that elevated inflation expectations remain the main concern. On the other hand, it was the first chance for the governor to comment on the recent increase in the public finance deficit for this year and next. However, the governor avoided any comment, which can be taken as a dovish sign here.

However, the market's attention was taken yesterday by headlines that the US government is working on a new draft peace agreement between Ukraine and Russia. Although we do not have much evidence of progress in the negotiations, for the markets, it is a signal of a higher probability that we will move in this direction. This is good news for CEE currencies, which reacted in the usual order, with HUF leading the gains and PLN second, with CZK less affected. Although the market will primarily follow the US job data today, it can be assumed that the Ukraine-Russia story will continue in the background and may bring further gains if we see signs of progress.

EUR/HUF thus gets another impulse to test new lows, and it seems that the forint has more room to rally as the main beneficiary of this story within the CEE region. After yesterday's break of 382, the route to 380 is open. However, today's direction will be driven by US data and EUR/USD in our view.

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