

FX Daily: Dollar rebound shouldn't have long legs

A benign 0.2% MoM core PCE print today could be enough for the dollar to start giving back some of this week's gains, which in our calculations are a bit overdone. EUR/USD should make it back above 1.170 (even as early as today), although markets need to remain sanguine on geopolitical risks



⬇️ USD: PCE can halt hawkish repricing

We discussed [yesterday](#) how we didn't see evidence that the dollar rebound was driven by geopolitics, and it appeared more like USD bears were setting a higher bar to justify the expensive dollar selling. Strong US data yesterday all but confirmed that tendency, sending short-dated USD swap rates and the dollar higher.

Here's a round-up of those market-moving data. The third release of 2Q GDP revised growth higher from 3.3% to 3.8%, with personal consumption looking much healthier at 2.5% (previous revision 1.6%). But what probably mattered even more was the second consecutive drop in initial jobless claims, from 232k to 218k, well below the 227k one-year moving average. The picture there

couldn't be more different from two weeks ago, when claims had spiked to 264k, a print that is looking increasingly like a fluke. Finally, durable goods orders surprisingly rose 2.9% MoM in August, and home sales figures were also better than expected.

The dollar hadn't had such a slew of good data in a while, and positioning squeezes likely helped the move. But we think more good news is needed to keep the dollar going, and we see substantial risks of a correction today after a USD rally that looks slightly overdone according to our model. The trigger could be August's personal income/spending or core PCE, which we expect at 0.2% MoM, in line with expectations. That could be enough to bring the pricing for December Fed easing back into the 40-45bp area (now 39bp). We expect DXY to ease back below 98.0 into next week's payrolls.

Francesco Pesole

📈 EUR: Room to recover, barring geopolitical risks

We estimate the short-term fair value for EUR/USD at 1.180 after the moves in rate differentials this week. The two-year swap rate gap has now widened in favour of USD by almost 15bp since 11 September, but at 120bp remains some 40bp narrower than two months ago.

As discussed above, our baseline view is for the dollar to give back some gains, and we think a return above 1.170 can happen as early as today. One risk, aside from any more US data strength, is that markets take rising geopolitical tension in Europe more seriously. NATO said yesterday that it is ready to shoot down any Russian planes violating its airspace.

On the data side today is eurozone inflation expectations for August, with the ECB expected to publish figures that show a modest slowdown.

Francesco Pesole

📈 JPY: Inflation cooldown not helping

The yen has been one of the biggest losers this week due to its sensitivity to any hawkish repricing in the USD curve. Not helping the JPY's case overnight were some lower-than-expected Tokyo CPI data. The headline reading slowed from 2.6% to 2.5% versus expectations of 2.8%, and the core measure excluding fresh food and energy surprisingly dropped to 2.5%, the lowest since March.

Market pricing for an October Bank of Japan hike is around 14bp, and today's data may prevent hawkish bets from building up for now. But we favour some unwinding of this week's dollar strength and the yen should be a main beneficiary of markets re-cementing expectations for two Fed cuts by year-end.

Our view is for any exploration above 150.0 to be relatively short-lived, with still ample downside room for the pair.

Francesco Pesole

➡ CEE: Relaxed end to a busy week

Today's calendar in CEE does not have much to offer after the meetings of the National Bank of Hungary and the Czech National Bank over the past few days. Next week, we should again get

more local stories with Polish inflation as the highlight. Yesterday, we heard from another MPC member, Ireneusz Dabrowski, that the National Bank of Poland is ready to cut rates, but it will be a cautious process. We believe that we will see one more rate cut this year at the October or November meeting, depending on next week's inflation figures.

In the Czech Republic, we also had the opportunity to hear from Deputy Governor Eva Zamrazilova yesterday, who expanded on the governor's press conference after Wednesday's decision to leave rates unchanged. Clearly, the main inflationary problem for the CNB is wage growth and the price of services, including housing. Although negotiations with unions on wage growth for state employees are not progressing, the CNB sees wage growth heading above forecast, which, according to the deputy governor, is creating further inflationary pressures.

FX remains relatively stable, but we still see signs of global pressure to weaken. The continuation of the USD rally is clearly negative news for the CEE complex in general, which may threaten heavy long positioning, especially in the HUF market. Given the absence of local news today, global factors will remain the main driver.

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