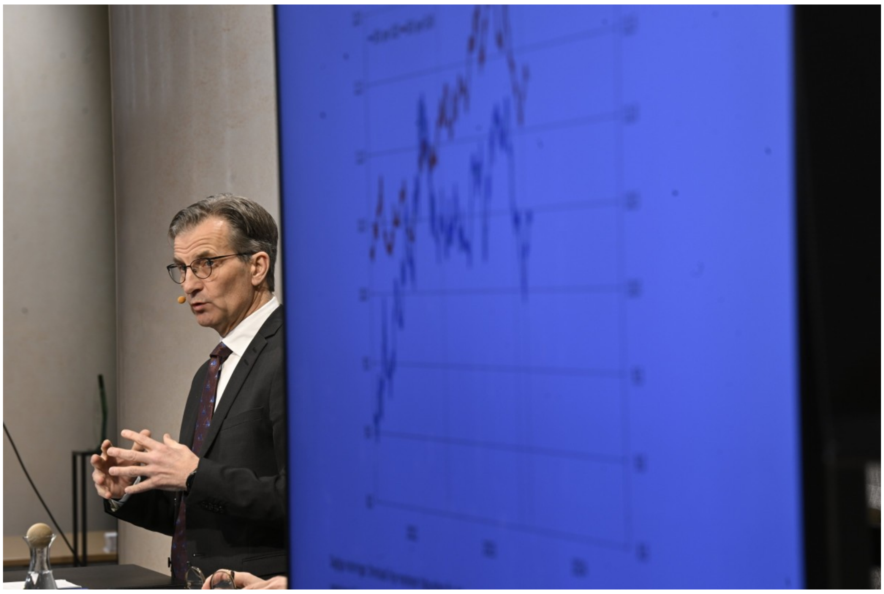
FX Daily: EUR/USD presses top of medium term range

In quiet trading conditions, the dollar is staying soft and EUR/USD is heading towards the top of an 18-month trading range. The FX options market suggests momentum is with EUR/USD. In the continued absence of US data today, the focus will be on a 25bp rate cut from Sweden's Riksbank and the Central Bank of Turkey keeping rates at 50%



Today we should see the Riksbank cutting rates by 25bp to 3.50%. Pictured: Riksbank Governor Erik Thedeen

USD: Going with the flow

In quiet markets, the dollar is edging gently lower. The big question over the next week is whether the dollar is just drifting to the bottom of the medium-term range and will soon rebound, or whether we are about to see the start of an important downside break-out. When it comes to the speculative community, positioning in both EUR/USD and USD/JPY looks now to be around flat – meaning investors are waiting for the next big thing.

As we discuss below, we prefer to run with the dollar bear trend for the time being as the Fed prepares the market for its first cut in September. Additionally, we would re-iterate that dollar price action has been quite poor and it is notable to see DXY trading under the 5 August low, while two-year US swap rates (now 3.82%) are still some 40bp above the levels seen in early August. True, we have seen a strong rebound in equity markets and there is no need to price dramatic easing from the Fed – but if so, then the dollar should be doing a lot better than it actually is.

Given the prospect of some downside revisions to the US employment picture when the Bureau of Labour Statistics releases some provisional benchmark revisions tomorrow, we expect the dollar to stay on the soft side. 102.15/102.25 may well now cap DXY rallies and we have a bias towards 101.

Chris Turner

EUR/USD: FX options markets suggests some active buying

EUR/USD continues to grind higher without much news. At the heart of the story is whether EUR/USD will break out of an 18-month trading range, which has largely contained EUR/USD between 1.05 and 1.11. The FX options market suggests that – at least over the next month – the bias is with the upside. The one-month risk reversal – the price of a EUR/USD call option over an equivalent put option – is moving deeper in favour of euro calls. This is happening when implied volatility is rising, suggesting active buying of euro call options.

The eurozone calendar remains very light today and does not pick up until Thursday's PMI releases. However, we do get to see the eurozone monthly (June) current account data today. This is now running close to a €30bn surplus per month (euro positive) compared to the €30bn monthly deficits seen in 2022 – and a big driver of EUR/USD weakness that year. On that subject, lower oil prices on the back of a potential Middle East peace deal are good news for EUR/USD. 1.1040/1050 should prove intra-day support for EUR/USD and we see the 1.1110/1140 as big medium-term resistance – a break of which would be big news.

Elsewhere today we should see the Riksbank cutting rates by 25bp to 3.50%. The market thinks there is a small chance of a 50bp rate cut. Our team continues to expect that the Riksbank will point to at least two further rate cuts later this year given the economy has been hit hard by higher rates and now that inflation expectations have fallen back under 2%. We do not think EUR/SEK has to rally too much on the rate cut. And unless the Riksbank surprises with a 50bp rate cut today, our bias is that the softer US rate environment can carry EUR/SEK down to the 11.30 area.

Chris Turner

CHF: A rare speech from the SNB

We do not often hear from him, but at 1130CET today outgoing Swiss National Bank President Thomas Jordan delivers a speech. We suspect he will be dovish given that the SNB has been under some pressure from local exporters to deal with the strong Swiss franc. Additionally, a technical move from the SNB yesterday also points to the dovish side, or at least an adjustment to ensure that dovish policy is properly filtering through Swiss money markets. Yesterday, the SNB cut the threshold factor on the remuneration of sight deposits, meaning that more of the banking sector's CHF sight deposits would be subject to a discount factor. EUR/CHF nudged a little higher on the news.

Any progress on Middle East peace talks could see EUR/CHF edge a little higher. However, as we discussed in our EUR/CHF update published yesterday, we think a lower global interest rate environment will see EUR/CHF trading in a 0.92-0.95 range later this year.

Chris Turner

CEE: CBT to stay hawkish until inflation expectations fall

Currencies in the region opened the week on the positive side but closed almost unchanged. HUF, despite a closed local market yesterday and today, showed openness to follow Friday's rate move up and we thus like to maintain a bullish bias here for the days ahead with EUR/HUF heading lower towards 390 ahead of next week's National Bank of Hungary meeting.

Across the rest of the region, we are rather neutral with expectations of Polish data tomorrow which could add more momentum to the PLN market. However, PLN rates are gradually climbing higher, which should at least keep the current strong PLN levels after rallying in the last two weeks. If this trend in the rates space holds, we think there is potential to open the door for another leg of the rally in FX for EUR/PLN heading lower below 4.260, but the economic data is rather mixed and Wednesday's releases may point in the opposite direction.

Today on the calendar we have the Central Bank of Turkey meeting. In line with expectations, we expect rates to stay unchanged at 50%. Although inflation has finally shown a downward turn in the last month, we expect the first rate cut in Turkey only in November. At the last press conference, Governor Karahan reiterated his commitment to leaving rates unchanged until inflation expectations are trending towards the central bank's projected inflation trajectory. On the other hand, inflation has surprised to the downside in the last two months and markets are moving to the dovish side with FX-implied yields pointing to a central bank rate of around 43%, below our economists' forecast.

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