FX Daily: Fed cancels the free lunch

European FX markets will today be monitoring how US asset markets react to the news that the Fed will not be renewing its Bank Term Funding Program. US regional banks will be in focus here. Elsewhere, the focus will be on what should be a decent 4Q23 US GDP figure and central bank meetings in the eurozone, Norway, Turkey and South Africa

USD: Let's see how the US regional banks do today

FX markets continue in their slightly risk-averse mode, where some of the investors' favourite high-yield currencies - such as the Mexican peso and the Hungarian forint - remain under some pressure. This is despite global equity markets doing reasonably well. In short, we continue to see a very mixed investment environment and one in which conviction views can be dangerous.

Looking ahead today, there are two US themes to focus on. The first is the Federal Reserve's announcement last night that its Bank Term Funding Program (BTFP) would end as scheduled on 11 March. And effective immediately, banks will be charged the rate paid on Fed reserve balances (around 5.40%) rather than the prior one-year USD OIS +10 bp (around 4.88%) to borrow money from the facility. This cancels the free lunch of banks borrowing at the BTFP and parking it at the Fed. The question is how US regional bank equity prices react to this news today. We presume that the Fed has a good handle on this such that these regional banks do not come under stress again. But let's see how this group trades today and whether it ushers in a new, potentially risk-off tone in US markets.

The second focus is the 4Q23 US GDP data. We are looking at an above-consensus 2.5% quarter-on-quarter annualised figure. Consensus is now 2.0%. In theory that should be dollar-positive, but not necessarily risk-negative because the price data is far more important to the Fed right now. On that topic, Friday sees the December core PCE deflator (expected at a subdued 02.% month-on-month), while 13 February remains a major day for calendars in the release of the January CPI figure and the 2023 annual CPI revisions.

Given also the event risk of the US quarterly refunding on Monday as well as the CPI release on 11 February, we doubt investors will want to commit much capital just yet. Instead, then, we think rangebound trading is the order of the day, with little follow-through should the dollar look particularly bid or offered. 102.75-103.75 looks the near-term DXY range.

Chris Turner

EUR: Lagarde will try to hold the data dependency line

As Francesco Pesole discusses in our ECB Cheat Sheet, President Christine Lagarde will try to avoid being drawn into any pre-commitment over a summer rate cut. In theory then, if she can avoid this and leave markets with a sense that the European Central Bank is truly data-dependent, short-term euro interest rates could nudge a little higher and support FX pairs like EUR/USD and EUR/CHF. For reference, the market still prices 17bp of ECB rate cuts for the 17 April meeting, whereas our team only sees the easing cycle starting in June once the ECB has a better understanding of the spring wage round. We would say that the ECB event risk (statement 14:15CET, press conference 14:45CET) proves a mild upside risk to EUR/USD - but the carpet could be pulled from under the euro should President Lagarde somehow convey the message that the policy rate will be getting cut in the summer after all. 1.0850-1.0950 looks the EUR/USD range, with outside risk to 1.0980/90 should the ECB pushback against easing expectations prove surprisingly effective.

Elsewhere Norges Bank announces rates today. The policy rate was hiked to 4.50% in December - so it would seem far too soon for Norges Bank to embrace any idea of easing. However, the Norwegian krone has been suffering a little this year as the backup in market interest rates has hit the risk environment. In all, we suspect EUR/NOK needs to trade a little longer in this 11.35-45 range.

Chris Turner

CEE: FX looking for hard ground

The calendar in the region is basically empty today but it seems that financial markets can find their own entertainment without it. CEE assets continue in higher volatility mode. After Tuesday's sell-off, Local currencies found some ground yesterday. From our perspective, we continue to see the Czech koruna as the most stable in this risk-off environment. Positioning was already short before the sell-off and the CZK seems to be firmly anchored to rates, which are not going anywhere for now thanks to the CNB's cautious approach. Therefore, we continue to see the 24.700-800 range as an anchor for EUR/CZK.

Poland's zloty remains the only currency supported by higher market rates, improving the interest rate differential. On the other hand, market positioning here supports more selling pressure. Moreover, the political situation has only temporarily calmed down, in our view, and we are likely to see more noise in the near term. Therefore, we expect to see 4.400 EUR/PLN levels again soon - rather next week than this.

However, the key now will be mainly EUR/HUF, which is moving up fast ahead of next week's National Bank of Hungary meeting. We expect a 100bp cut on Tuesday but a still-weak forint is the risk to our call. We see 390 as a pain threshold where NBH will start to be more cautious and 395 as a hard stop for a 100bp rate cut and switch to the previous 75bp pace. We turned negative on HUF before the start of this sell-off due to FX and rate divergence, discussed here earlier. But now we believe this gap has closed in the last few days and the pressure on HUF should stop. However, the risk-off sentiment and long positioning is a clear risk here, which may further threaten the forint.

Frantisek Taborsky

TRY: The final CBT hike

The Central Bank of Turkey (CBT) is today expected to conclude its tightening cycle with a 250bp rate hike - taking the one-week policy rate to 45.00%. We presume the CBT will retain the language that it can hike again if necessary. For reference, the Turkish lira is one of the very few emerging market currencies with positive total returns against the dollar this year. With cross-market volatility low, it looks like investors are keen to take on Turkish foreign currency risk and try to receive rates. We tend to cautiously favour these strategies too.

Chris Turner

Authors

Chris Turner
Global Head of Markets and Regional Head of Research for UK & CEE
chris.turner@ing.com

Frantisek Taborsky
EMEA FX & FI Strategist
frantisek.taborsky@ing.com

Francesco Pesole
FX Strategist
francesco.pesole@ing.com