

## FX Daily: Fed minutes keep dollar supported

Last night's release of the September FOMC minutes revealed a Fed intent on 'recalibrating' restrictive monetary policy. Certainly, there was no sense that the Fed was rushed into a 50bp rate cut. As the Fed notes, short-term rate differentials drive the dollar. And risks of a 0.3% MoM core September CPI release today can keep the dollar supported



### USD: Sticky CPI should keep the dollar supported

Reading through the September FOMC minutes, there seemed no sense of urgency from the Fed to get rates lower – even though it did cut by 50bp. More a sense that the inflation scare was over, unemployment was drifting higher and a risk management approach required a recalibration of policy. There were not any strong signals about how quickly rates would be cut to less restrictive levels and of course, the future pace of rate reductions would be data-dependent. Interest rate markets did not do much on the release of the minutes, with short-dated yields perhaps ticking up 2-3bp in the aftermath.

The reason markets did not do much is that we've already seen a considerable adjustment in short-dated US rates since late September. The Fed's terminal rate for this easing cycle has been repriced 50bp higher over the last few weeks. And short-dated yields have moved significantly in

the dollar's favour. EUR:USD two-year swap differentials have widened from 85bp to 130bp in about three weeks – no wonder EUR//USD is down towards 1.09.

The big question is, what is the trade from here? Can short-dated US rates rise much further from here? We suspect probably not. But we could find out today should US September CPI come in slightly above consensus at 0.3% MoM. That will not be a deal-breaker for a 25bp cut from the Fed in November but perhaps will give the Fed a little less leeway to pursue more aggressive easing. Additionally, later today we have two more Fed speakers in the form of Tom Barkin and John Williams, both seen as modest hawks.

As we [discussed here yesterday](#), the FX market is choppy due to stimulus measures from China and ongoing instability in the Middle East. Investors anticipate the Chinese Ministry of Finance will announce CNY2-4 trillion in new bond issuance this Saturday, which is supporting commodity currencies. However, the bearish flattening of the US yield curve remains a negative factor for these currencies.

DXY could make a bid for the 103.35 area should the US core CPI surprise on the upside today. Geopolitical uncertainty should also help the dollar.

*Chris Turner*

## ➔ EUR: ECB minutes in focus

EUR/USD remains under pressure for the reasons we discuss above. In focus today will be the release of the ECB minutes from the 11-12 September meeting when the ECB cut rates by 25bp but provided no forward guidance. Since then we've seen a terrible set of September PMI data across the region and ECB speakers have acknowledged dwindling inflation risks and increasing growth risks. Hence the market is now fully pricing 25bp rate cuts in October and December and keeping those EUR:USD swap differentials wide. It seems unlikely that today's release of the minutes can scale back expectations for an ECB rate cut next week – but let's see.

EUR/USD remains soggy. Technically it looks like it can break down to the 1.0800 area. But we're not sure US short-dated yields will be the trigger since these have come a long way quite quickly. What would be a trigger is higher energy prices and that's why tension in the Middle East could demand a greater risk premium of the euro.

*Chris Turner*

## ⬆️ CEE: Focus turning to inflation prints

This morning we have already received the September inflation figure for Hungary. Inflation dropped from 3.4% to 3.0% YoY (INGf: 3.0%, cons 3.1%, NBH: 3.1%). Although a further drop in inflation is positive news for the central bank, an October rate cut is still probably off the table given EUR/HUF levels and recent market volatility.

We will also see the September Czech inflation number later this morning. Our economists expect some increase from 2.2% to 2.4% YoY, which is in line with market expectations. Already the August number is 0.2pp above the central bank's forecast and the September deviation may be key to the CNB's next steps. As we discussed here on Tuesday, the inflation profile for the rest of the year is tricky given the base effect, and today's number should tell us more about the months ahead and a possible pause in the CNB's cutting cycle in December.

CEE currencies tried to find some ground yesterday for a second day. PLN and HUF continued to post modest gains while CZK stagnated. We should get more today given the inflation numbers in the region which could turn the market's attention to the local story. Although global risks remain, the market is visibly trying to get over it. However, global headlines indicating escalation conflict in the Middle East could again be a trigger for a sell-off. Otherwise, we remain slightly bullish on CEE FX, which should be further supported by high rate differentials, resulting from the recent sell-off in the rates market. Although EUR/CZK was the only one in the region to remain unchanged yesterday, today's inflation numbers could be a welcome boost for the CZK given the CNB's inflation forecast overshoot.

*Frantisek Taborsky*

## ➔ BRL: Poor performance

The Brazilian real is performing poorly. China's stimulus measures should have been a positive for the real, but instead USD/BRL is trading up towards the 5.60 area. Despite Brazil receiving a sovereign upgrade from Moodys recently, there are a few factors which could be explaining the real's underperformance.

One is the poor performance of President Lula's party in local elections at the weekend, which could prompt the government to spend more ahead of the next presidential election in 2026. The second is a factor we identified in our [US election preview](#), where 44% of Brazil's government debt is on floating rates and Brazil has the lowest share of long-term fixed debt in the region. Higher US bond yields are therefore a problem for Brazil.

Forthcoming rate hikes in Brazil should be enough to contain USD/BRL near 5.60, but the real outlook remains challenging.

*Chris Turner*

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