FX Daily: Focus is on the new US Treasury Secretary

Besides expecting another round of positive US activity data, today's FX focus will be on the Senate confirmation hearing of Scott Bessent, Trump's nominee for US Treasury Secretary. He will be questioned about the dollar, tariffs, and the upcoming fiscal agenda. We don't think he'll disrupt the strong dollar stance just yet. Additionally, confidence is growing about a Bank of Japan rate hike next week, and Poland is setting rates today

Scott Bessent, Trump's nominee for US Treasury Secretary

USD: Bessent should keep the strong dollar theme alive

Global asset markets have enjoyed a positive 24 hours driven largely by the marginally sub-consensus US core CPI reading for December. US short-dated yields fell 10bp on the view that inflation is not getting any worse. However, sticky headline and core inflation near 3% YoY still cast doubt on the Fed's ability to cut this year and just 36bp of Fed easing is priced for 2025. ING's US economist, James Knightley, is starting to think that any easing now will be increasingly back-loaded. In terms of today's US data calendar, December retail sales are expected to remain strong. Last night's release of the Fed's Beige book noted that most of the Fed's 12 districts reported strong holiday sales, which exceeded expectations. Some are also thinking that the weekly initial claims figures are very low. So far, so dollar positive.

The highlight of the day, however, should be Scott Bessent's nomination hearing in front of the Senate Finance Committee. The session starts at 1630CET. He's going to be grilled about his views on various key topics, including the dollar, tariffs and fiscal sustainability to name a few. In pre-released remarks, he's said he wants to ensure the dollar remains the dominant reserve currency and that the 2017 TCJA tax cut be made permanent so there isn't a $4tr increase in taxes. On tariffs, in the run-up to the election, he's said that they are a useful negotiating tool. The *Economist* magazine describes Bessent as a "conservative mainstreamer" in one of the three blocs advising Trump – the other two blocs being "America firsters" and "tech tycoons". Over time, financial markets expect Bessent to apply a little restraint on America firsters when it comes to tariffs, but it is probably too early to expect those views to emerge today – especially since Trump last week was so quick to shoot down the *Washington Post* article suggesting a more measured approach to tariffs. We also wonder whether Bessent will comment much on how tariffs will contribute to balancing government finances. If tariffs are highlighted as a key tool, then the dollar could push back to the highs.

No doubt Bessent will be asked about the strong dollar. As discussed in this month's edition of FX Talking, the inflation-adjusted dollar index is now at its highest level since 1985. We doubt Bessent will want to go anywhere near the subject of a weaker dollar, although there is a chance he could discuss the need for trading partners to strengthen their currencies – that's the outside risk today. But that is a hard message to balance against the need for the dollar to remain the world's pre-eminent reserve currency.

On balance, we think the dollar can say bid today. However, DXY moves back towards 110 and could see some profit-taking ahead of Monday's event risk in the form of Trump's inauguration.

Chris Turner

EUR: Reluctant to unwind its under-valuation

A common theme running amongst FX strategists like ourselves is that EUR/USD has recently been undershooting levels normally suggested by short-term rate differentials. We run a short-term Financial Fair Value model. Other banks will have their own measures. The common theme is that most are saying rate differentials should justify EUR/USD closer to 1.05.

Yesterday provided a great opportunity for EUR/USD to rally. Two-year rate spreads narrowed 5bp on the 0.2% reading on core US CPI. Yet EUR/USD struggled to hold the rally to 1.0350. Not very impressive and perhaps represents a conviction view that the eurozone and the euro will underperform this year on weak growth and weak leadership in the region.

We also note that current speculative short positioning seems much more extreme in currencies like the Canadian, Australian and New Zealand dollars than it does in the euro. This suggests that EUR/CAD, EUR/AUD and EUR/NZD could all come lower if Trump does not deliver as aggressive a tariff package as some expect next week.

The strong dollar environment could push EUR/USD back to 1.0225/50 today. But we suspect that some buying may emerge there as investors lighten positions ahead of Monday's event risk.

Chris Turner

JPY: BoJ hike speculation continues to build

Another day and another set of source stories ahead of next week's Bank of Japan meeting. Today it was *Bloomberg* reporting that several officials felt a hike was likely. ING's economist covering Japan, Min Joo Kang, has been highlighting the risk of a January BoJ hike for a while – largely because the wage data has been coming in on the strong side. A 25bp hike in the policy rate to 0.50% is our call for next week.

Expectations of a BoJ hike (now priced at 80%) and perhaps fears of more FX intervention in the 158/160 area have helped the yen out-perform. Expect that to continue into next week's BoJ meeting. However, dips may exhaust in the 153/155 area. Our rates team expect US Treasury yields to stay firm all year and the risk of 5%+ 10-year yields over coming months should support $/JPY.

Chris Turner

CEE: Welcome relief after US numbers

Yesterday's meeting of the National Bank of Romania did not bring any surprises. Rates remained unchanged at 6.50% and the press release suggests an increase in the inflation forecast at the next meeting in February. Poland's inflation numbers brought some downward revision, which we think will be especially visible in weaker core inflation. This could bring a dovish shift in Friday's National Bank of Poland press conference. However, given the December style, the focus seems to be more on the longer term and therefore we will see a rather minimal impact. The NBP decision today should be a non-event with rates unchanged at 5.75% and attention turning to tomorrow's press conference.

CEE markets saw a significant relief after US inflation numbers yesterday, resulting in a strong rally in the rates and bond markets. The FX market was more muted but still EUR/HUF touched 410 for a while, the lowest level this year. Implications for the days ahead are more mixed though. We saw further tightening of rate differentials in Poland and the Czech Republic, implying weaker FX.

While EUR/CZK closed some of the gaps in the previous days, EUR/PLN continues to diverge. For EUR/CZK we keep an upward bias, following the direction of the rates market. Poland is more complicated and dependent on Friday's tone from the NBP governor. If the tone remains hawkish like in December, the PLN should stay supported, and the gap between rates and FX will close due to a sell-off in the rates market rather than the reverse. However, the NBP has been unpredictable in recent months and could surprise us again.

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