

FX Daily: Global stabilisation

Markets are navigating much calmer waters after last week's action. The PBoC's efforts to stabilise the yuan are offering support for FX risk sentiment and hurting the dollar's momentum. The declining FX volatility may keep the yen pressured by funding demand for carry trades, making USD/JPY even more reliant on a move in USD rates



The current environment suggests a recovery in JPY remains strictly tied to US rates breaking lower

➔ USD: Yuan stabilisation continues

We had deemed last week's dollar rally as overdone given the relatively dovish Federal Reserve message, and we are not surprised to see the greenback decline at the start of this week. Amid a generalised calm after the central bank meetings last week and before the US PCE this Friday, many investors have kept an eye on China and FX policy from the People's Bank of China (PBoC) after a break above 7.20 last Friday in USD/CNY gave support to the dollar across the board. The PBoC fixed the yuan 0.1% stronger this morning, reinforcing the message it sent yesterday that currency stability remains a priority.

There are a couple of data releases to watch in the US today after a good Chicago Fed Activity index print, soft manufacturing figures (Dallas Fed index) and lower-than-expected new home sales yesterday. Durable Goods Orders for February are expected to rebound after January's decline, and the Conference Board consumer confidence is seen stabilising after printing 106.7 in February.

There are no scheduled Fed speakers today, but equity markets seemed to react negatively to yesterday's comments by Raphael Bostic, who reiterated his expectation for only one cut this year and stressed the risks of easing too early. Interestingly, the dollar did not benefit from the remarks, and we suspect that while a core PCE at 0.3% month-on-month (our call and consensus) on Friday shouldn't do much to encourage dovish bets, the dollar looks more likely to stabilise than stage another rally at this point.

The drop in FX volatility after last week's action is being helped by the PBoC's stabilisation of the yuan and should not help the yen, which remains the most popular funding currency for carry trades. Verbal interventions in Japan and the softer dollar momentum are helping a bit, but the current environment suggests a recovery in JPY remains even more strictly tied to US rates breaking lower. Our call remains bearish on USD/JPY moving forward, but in the very short term, the pair may retest the 152+ "verbal intervention" area.

Francesco Pesole

➔ EUR: ECB doves raise their voices

European Central Bank (ECB) doves are continuing to reiterate the message that consensus within the Governing Council is shifting to imminent easing. Fabio Panetta said recent weeks have seen growing support for rate cuts in the GC, and that inflation is moving closer to the ECB target. Chief Economist Philip Lane sounded optimistic that the normalisation in wages – a necessary condition for cuts – is proceeding and signalled that the ECB has made "good progress" on disinflation.

Despite more cautious messages by other ECB members in the past few days, there are clear indications that the Bank is prepared to cut rates this summer and that June remains the most likely meeting, as policymakers will want to see more convincing evidence on wages and inflation. Inflation numbers will be released in the next ten days in the eurozone, with the EZ-wide March CPI estimate released on 3 April. Barring major surprises, markets should continue to gain confidence about a June cut (21bp already in the price), meaning that the EUR may lag other currencies that have short positioning and/or have higher beta to sentiment once a dollar decline materialises. In our view, this can happen in the next month.

For this week, EUR/USD should be able to prevent much more pressure on the 1.0800 support and stabilise around or modestly above 1.0850.

Francesco Pesole

➔ GBP: Some speculation on a May cut

The GBP swap curve has recorded a moderate hawkish repricing since the start of the week, although it continues to signal a 25% implied probability of a rate cut by the Bank of England at the May meeting. That is a higher expected chance than for the Fed (also May), and the ECB (April).

When looking at the pricing for December, this is now very similar for the BoE (-76bp) and the Fed (-80bp), while ECB expectations remain more dovish (-97bp). In our view, however, markets are expecting too much easing in the eurozone. We expect 75bp. Meanwhile, we see the BoE cutting by 100bp and the Fed by 125bp by year-end. Since we forecast the USD decline to start materialising in the coming weeks, we see GBP/USD being supported. However, EUR/GBP, which is a mirror of the BoE-ECB rate expectation gap, may not re-explore the low 0.85's seen in February

and early March.

Francesco Pesole

➔ HUF: Better safe than sorry

The highlight of this week in the CEE region is the National Bank of Hungary's rate-setting meeting [today](#). Developments since the last meeting have been mixed and could again, in our view, justify a more cautious approach. We expect the central bank to deliver a 75bp cut to 8.25%, accompanied by some hawkish guidance on monetary policy strategy in the second quarter of 2024. The current account balance will deteriorate in the fourth quarter based on monthly statistics, possibly turning into a small deficit due to the slump in goods exports in December. The latest set of labour market data will be challenging to read. We expect strong wage growth to continue, with some deceleration due to base effects. On the other hand, we forecast employment data to deteriorate and the unemployment rate to rise, suggesting a further easing of labour market tightness.

In the FX market, we see HUF fairly balanced, or maybe even strengthening too quickly. However, if the NBH can deliver a hawkish message and bring some anchor to the current situation, it may unlock potential for HUF coming from a higher IRS curve. On the other hand, the situation remains fragile, especially going into the second quarter with the looming central bank law change, EU funds issues and the approaching EU and local elections. Therefore, we expect rather higher volatility today and we are neutral on the direction.

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