

## FX Daily: Hard to argue with the strong dollar

Another day brings another set of data to support further Fed tightening. That should be the main story with the release of US personal income data and the core PCE deflator for May. Barring a data surprise, the only threat to the strong dollar story comes from quarter-end rebalancing flows – which could generate some dollar selling at key fixings



### 📈 USD: Strong data goes head-to-head with rebalancing flows

The dollar remains reasonably well bid after US data releases yesterday prompted another jump up in US yields and firmed up calls for a 25bp hike from the Federal Reserve in July. The economy grew a revised 2% quarter-on-quarter annualised and initial claims dropped back sharply, leaving the market with the impression that the Fed still has more work to do.

Dollar strength emerged across the board yesterday. The key flash point remains USD/JPY. It seems the Bank of Japan is readying intervention above 145 – just as it did last September. News of intervention at either the London or New York open would not be a surprise, and would probably be worth 200 pips maximum before the dollar turned higher again. On the subject of intervention, the Swiss National Bank (SNB) releases first quarter FX intervention figures. In the fourth quarter of last year, it sold around CHF22bn as it sought to strengthen the Swiss franc. A net sale of FX is expected today, although it may be a little smaller after the SNB probably bought FX during the

banking crisis in March when EUR/CHF was under pressure.

Back to today. May's core PCE deflator is expected at a firm 0.3-0.4% MoM, consistent with the Fed's view that core inflation is not falling quickly enough. That should keep US rates and the dollar firm. The challenge today will be month and quarter-end portfolio rebalancing flows. The outperformance of US equity benchmarks over the last month and quarter could generate some dollar selling, particularly around the 17CET WMR fix. We prefer to see rebalancing as more of a risk to a preferred view that the dollar stays strong given what seems a clear macro story.

DXY could edge up to the 103.65 area unless fixing flows take their toll.

*Chris Turner*

## ⬇️ EUR: Sticky Eurozone CPI can provide some support

Following inflation data releases across Europe over the last few days, the June Eurozone core inflation rate is expected at 5.5% YoY today – a rise from 5.3% in May. The data may nudge market pricing towards a 25bp hike from the European Central Bank in both July and September. Currently, the market only prices a combined 37bp rate increase over those two meetings. A hawkish ECB is providing the euro with some resistance to a hawkish Fed, although two-year EUR/USD swap differentials have still widened back out to 120bp in favour of the dollar.

With yield curves still heavily inverted around the world and the Chinese economy continuing to misfire, this is not the best environment for the pro-cyclical euro. EUR/USD can drift back towards the 1.0825/45 area on the day and it is increasingly looking as though we could see a 1.07-1.10 range for a large part of the third quarter this year.

Elsewhere, [the Riksbank 25bp hike and increase in the pace of quantitative tightening](#) have failed to provide lasting support to the Swedish krona. However, we note with interest the Riksbank's plans to currency hedge 25% of its FX reserves. We hope to publish more on this later today, but it does seem a confident move from the Riksbank that it expects the undervalued krona to recover in the medium term.

*Chris Turner*

## ➡️ GBP: Steady as she goes

Sterling is consolidating and must be enjoying support from implied short-dated yields over 5%. We made the point in last week's [Bank of England](#) review that the FX hedging costs were now very painful for foreign investors in the UK Gilt market – a factor that could help sterling.

There is little on the UK calendar today, so strong US data could briefly tip GBP/USD back to the 1.2550 area, where we expect it to find support.

*Chris Turner*

## ⬆️ CAD: Business Outlook Survey to provide a lift

The Canadian dollar has been one of the better G10 performers this year and, like the Mexican peso, is buoyed by a healthy risk-adjusted yield. On the subject of yields, the market is split on whether the Bank of Canada needs to push ahead with its tightening cycle in July. The Bank of

Canada (BoC) policy rate is now 4.75%.

One important input into the BoC's decision will be today's release of the quarterly [Business Outlook Survey](#). This will help the BoC better understand both business inflation expectations but also the environment for corporates to be able to push higher prices onto consumers. With Canada's unemployment rate still relatively low by historical standards, corporates may still see opportunities to push on higher prices or restore profit margins. Let's see.

In general, we expect the Canadian dollar to continue to perform well (as should the Mexican peso) and today's outlook survey could help to see the Canadian dollar withstand US dollar strength better than some.

*Chris Turner*

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